



Case Western Reserve Law Review

Volume 50 | Issue 2

1999

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Recommended Citation

William J. Carney, *The Legacy of "The Market for Corporate Control" and the Origins of the Theory of the Firm*, 50 Case W. Res. L. Rev. 215 (1999)

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THE LEGACY OF “THE MARKET FOR CORPORATE CONTROL” AND THE ORIGINS OF THE THEORY OF THE FIRM

William J. Carney[†]

INTRODUCTION

This Symposium celebrates the whole of Henry Manne’s contribution to scholarship and to education. I nearly said “legal” scholarship and education but that would have been too narrow, as the articles in this Symposium will demonstrate. While we celebrate the impact of Manne’s work on a broad universe, I would be ungrateful if I did not say a few words about Manne’s impact on my own work and life, for it is considerable, and I owe him a great debt. I graduated from law school when *The Nature of the Firm*¹ was the only work, other than Berle and Means,² that attempted to apply economic analysis to the corporation. Whether one characterizes *The Nature of the Firm* as tautological or as an important description, one certainly could not characterize it as a theory of the firm.³ I never encountered

[†] Charles Howard Candler Professor, Emory University School of Law. I am grateful to Henry Manne for conversations concerning the origins of his ideas and the development of the papers discussed herein. I also thank Fred McChesney for his encouragement to take this paper in a slightly different direction than he and Professors Butler and Macey originally contemplated. The indulgence of one’s colleagues is appreciated. Particular thanks are due to Will Haines of the Emory Law Library for his help with citation studies in the social science literature. Because this paper is not intended to be a review of the literature on the theory of the firm, I have made no attempt to list all the contributions to this literature. Aside from the small body of work that preceded Professor Manne’s I have included only seminal articles that followed his path-breaking work. I have similarly omitted references to important works of economic history that examine the development of firms, such as ALFRED D. CHANDLER, *STRATEGY AND STRUCTURE: CHAPTERS IN THE HISTORY OF THE INDUSTRIAL ENTERPRISE* (1962).

¹ R.H. Coase, *The Nature of the Firm*, 4 *ECONOMICA* 386 (1937).

² See ADOLF A. BERLE & GARDINER C. MEANS, *THE MODERN CORPORATION AND PRIVATE PROPERTY* (1932).

³ Oliver Williamson characterizes *The Nature of the Firm* by saying that “[t]ransaction costs are appropriately made the center piece of the analysis, but these are not operationalized in a fashion that permits one to assess the efficacy of completing transactions as between firms and markets in a systematic way.” OLIVER E. WILLIAMSON, *MARKETS AND HIERARCHIES: ANALYSIS AND ANTITRUST IMPLICATIONS* 3 (1975). In an article published after Williamson, Coase agreed with this description. See R. H. Coase, *The Nature of the Firm: Influence*, 4 *J.L. ECON. & ORG.* 33, 35-36 (1988). Steven Cheung argues that it is not tautological: “Generality in the extreme renders an argument tautological, whereas a total lack of general applicability renders an argument ad hoc. Testable implications are to be found somewhere in between . . .” Steven N. S. Cheung, *The Contractual Nature of the Firm*, 26 *J.L. & ECON.* 1, 4 (1983).

Coase's work in law school, although Berle and Means lay just beneath the surface in all teaching about corporate law. After eleven years of private practice, I entered teaching in 1973, still blissfully unaware of the economic analysis of anything other than antitrust.⁴ I had the good fortune to attend Manne's summer camp in 1975, and Manne and his program changed my scholarly career.⁵ I can see the change in my choice of subjects to investigate, and in the way I examine them. Whatever the quality of my efforts, it is far better and more interesting than it would have been without Henry and his work.

The other part of Henry's gift has been his friendship. Henry has embraced everyone he has encountered who is seriously interested in ideas. I was fortunate enough to have been his colleague at Emory for a few years. Those years were, in hindsight, the most exciting my institution has enjoyed to date. The intellectual environment created by Henry during those years was exhilarating, and sometimes exhausting. Henry attracted the best and the brightest to Emory at that time: Fred McChesney, Jon Macey, Dave Haddock, Peter Aranson, Roger Meiners and Jesse Markham.

But Henry created excitement for a broader group as well, and the purpose of this Article is to examine his impact on our learning about corporate governance. Part I describes the world before Henry Manne when, as I mentioned, there were only two works applying economic analysis to corporate law. Berle and Means described a world familiar to a generation of readers of the antitrust literature—a world of monopolies, oligopolies, administered prices, and consumer exploitation. Managers were autonomous, conceding only "satisfactory" returns to powerless shareholders. The firm was a black box of little interest to most economists.⁶ Only lawyers cared about corporate law, and they did so without benefit of economic analysis. Part II describes how Manne's work changed all of that. It recast the paradigm, perhaps as much for industrial organization analysis as for the theory of the firm. We may still be too close to this shift to be able to see its full magnitude, but I will attempt to outline it as best I can. My assigned topic is the market for corporate control, and this is the title of Manne's most famous article. I am going to argue that relatively too much attention has been given to that one article. It is only part of an enterprise during the 1960s that outlined the modern theory of the firm—a pioneering effort for which Manne has received too

⁴ Just prior to attending the Economics Institute for Law Professors in 1975, I came across *ECONOMIC POLICY AND THE REGULATION OF CORPORATE SECURITIES* (Henry G. Manne ed., 1969).

⁵ Among the distinguished teachers that year were Harold Demsetz and Armen Alchian, along with Manne.

⁶ A good description of what the author calls the "textbook orthodoxy" of this approach appears in Sidney G. Winter, *On Coase, Competence, and the Corporation*, 4 J.L. ECON. & ORG. 163, 164-65 (1988).

little credit. Part III undertakes a brief examination of the evidence of the importance of these articles, through citation counts.

I. THE SCHOLARLY WORLD BEFORE HENRY MANNE

A. *The Economics Literature*

Berle and Means set the intellectual table for the "higher criticism" of corporate law for an entire generation. They described a world in which large corporations became oligopolists, with the presumed ability to earn monopoly rents.⁷ Corporate managers took advantage of the collective action problems facing shareholders to insulate themselves from accountability. These managers, possessing monopoly power to set prices and independence from capital markets through retained earnings, were able to pay shareholders a "sufficient" amount to satisfy them, while retaining the residual benefits of control for themselves.⁸ Berle and Means confused management control with large shareholder control, and argued that control was a "corporate asset," belonging either to the corporation or to the shareholders as a group.⁹ Oddly enough, there were the seeds of a different paradigm in the book, but they were ignored. Berle and Means described stock markets as semi-strong form efficient, but failed to explore the implications of that observation.¹⁰

Ronald Coase wrote *The Nature of the Firm* in 1937.¹¹ Oliver Williamson has characterized this as the beginning of transaction cost economics, and has written that "the state of transaction cost eco-

⁷ BERLE & MEANS, *supra* note 2, at 45.

⁸ *Id.* at 342-44.

⁹ This notion was implicit rather than fully spelled out by Berle & Means. They argued that the value of "control" arises out of the ability of the stockholder to dominate "property which in equity belongs to others." *Id.* at 244. Discussing a New York lower court decision where a judge declined to dismiss a suit to capture a control premium for the corporation or all of the shareholders, the authors said "it apparently involved too great a leap into the dark for the New York court to say that the power going with 'control' is an asset which belongs only to the corporation; and that payment for that power, if it goes anywhere, must go into the corporate treasury." *Id.* Development of the legal argument that control was a corporate asset was undertaken later in, Adolf A. Berle, Jr., "Control" in *Corporate Law*, 58 COLUM. L. REV. 1212 (1958).

¹⁰ BERLE & MEANS, *supra* note 2, at 293-94. Note the negative tone about the high expectation of fraud in corporate statements to the market:

"The more respectable exchanges, at least in recent years, have required a certain amount of continuous disclosure by the corporation; such material permitting an appraisal Naturally much of what is disclosed is not necessarily true; and much of what is true never reaches the market; the ideal situation—that of constant running disclosure of all information bearing on value being of course necessarily unattainable. It can, however, be approximated; and it certainly is true that the mechanisms of dissemination are so well developed that any facts bearing on values can become common market property almost instantaneously."

Id.

¹¹ Coase, *supra* note 1.

nomics in 1972 was approximately where Coase had left it in 1937.”¹² Williamson was wrong; perhaps because he cited none of Manne’s works, although he was writing in 1988.¹³ Williamson explained that what remained to be done after Coase was to identify the factors responsible for cost differences among transactions, and to align transactions with governance structures in a discriminating way.¹⁴ Manne had already engaged in precisely this kind of work in 1967.¹⁵ Williamson argued that one of the distinctive features of transaction cost economics is its focus on post-contractual behavior. He further points out that where a bidder wins a Demsetzian auction for monopoly privileges,¹⁶ where no specialized investments are incurred, the winner realizes no advantage over non-winners because of the non-winners’ potential competition.¹⁷ This, of course, is a precise description of Manne’s contribution to the Berle and Means paradigm: markets for managers and markets for corporate control provided potential competition for managers of firms with market power.

Coase’s pathbreaking article defined the margin between firms and markets. Some of the literature that extended Coase’s work asked what causes the use of firms rather than markets. Alchian and Demsetz suggested that the necessity for team production played an important role.¹⁸ Klein, Crawford, and Alchian suggested that the existence of specific assets explained the development of many firms.¹⁹ Cheung argued that we don’t know exactly what a firm is,

¹² Oliver E. Williamson, *The Logic of Economic Organization*, 4 J.L. ECON. & ORG. 65, 65 (1988) (citations omitted).

¹³ In addition to ADAM SMITH, AN INQUIRY INTO THE NATURE AND CAUSES OF THE WEALTH OF NATIONS 700 (Edwin Cannan ed., 1976), quoted *infra* note 103, agency costs were noted, as well as the principal solutions of monitoring and incentive contracts, in JOHN STUART MILL, 1 PRINCIPLES OF POLITICAL ECONOMY 390 (Revised ed. 1900):

“Management, however, by hired servants, who have no interest in the result but that of preserving their salaries, is proverbially inefficient, unless they act under the inspecting eye, if not the controlling hand, of the person chiefly interested: and prudence almost always recommends giving to a manager not thus controlled, a remuneration partly dependent on the profits; which virtually reduces the case to that of a sleeping partner.”

Id.

¹⁴ Williamson, *supra* note 12, at 66. An enlightening account of the development of transaction cost economics and its contribution to the theory of the firm appears in Oliver E. Williamson, *The Modern Corporation: Origins, Evolution, Attributes*, 19 J. ECON. LITERATURE 1537 (1981).

¹⁵ Henry G. Manne, *Our Two Corporation Systems: Law and Economics*, 53 VA. L. REV. 259 (1967) [hereinafter *Two Corporation Systems*] (outlining a dual theory of corporations).

¹⁶ See generally Harold Demsetz, *Why Regulate Utilities?*, 11 J.L. & ECON. 55, 57-58 (1968).

¹⁷ Williamson, *supra* note 12, at 77.

¹⁸ Armen A. Alchian & Harold Demsetz, *Production, Information Costs, and Economic Organization*, 62 AM. ECON. REV. 777 (1972).

¹⁹ Benjamin Klein et al., *Vertical Integration, Appropriable Rents, and the Competitive Contracting Process*, 21 J.L. & ECON. 297 (1978).

but that it isn't vital to know.²⁰ To this day, defining the firm remains difficult, apparently with much work to be done before economics provides a full explanation of the existence, size, and shape of firms.²¹ Other contributors examined why different firms took distinct shapes.²² Neither of these areas was Manne's project; rather, he assumed the existence of firms, and examined the exogenous forces that constrained their managers and directors.

The notion of agency costs—first introduced in Berle and Means, although they did not cast the issue in those terms—was central to Manne's work. But rather than model the problem or suggest contractual and monitoring solutions, as Jensen and Meckling did,²³ Manne examined the market forces that would cause managers to offer these contractual arrangements.

Armen Alchian provided an excellent contemporaneous account of the early work on the theory of the firm up to 1965.²⁴ The literature showed that managers would seek non-pecuniary benefits at the expense of shareholders—a claim not different from that of Berle and Means—but accomplished with more rigorous proofs and empirical evidence.²⁵ It also formalized models that predicted that managers would seek larger firm size, regardless of profits, because higher managerial compensation is associated with larger size.²⁶ Williamson's 1963 article demonstrated the strong hold of the managerialist tradition: he argued, like Berle and Means, that managers sought only a "satisfactory" level of profits. Williamson recognized, however, that sometimes managers might seek higher levels of profit, either for

²⁰ Cheung, *supra* note 3, at 3.

²¹ See, e.g., Harold Demsetz, *The Theory of the Firm Revisited*, 4 J.L. ECON. & ORG. 141 (1988); Williamson, *supra* note 14, at 1539.

²² Eugene F. Fama & Michael C. Jensen, *Separation of Ownership and Control*, 26 J.L. & ECON. 301 (1983) [hereinafter Fama & Jensen, *Ownership and Control*]; Eugene F. Fama & Michael C. Jensen, *Agency Problems and Residual Claims*, 26 J.L. & ECON. 327 (1983) [hereinafter Fama & Jensen, *Residual Claims*].

²³ Michael C. Jensen & William H. Meckling, *Theory of the Firm: Managerial Behavior, Agency Costs and Ownership Structure*, 3 J. FIN. ECON. 305 (1976); see also Williamson, *supra* note 14, at 1541 (identifying CHESTER I. BARNARD, *THE FUNCTIONS OF THE EXECUTIVE* (1938) as containing an early discussion of the use of incentives to align agents' interests with those of the enterprise).

²⁴ Armen A. Alchian, *The Basis of Some Recent Advances in the Theory of Management of the Firm*, 14 J. INDUS. ECON. 30 (1965).

²⁵ *Id.* at 31-32 (citing GARY BECKER, *THE ECONOMICS OF DISCRIMINATION* (1957) and Armen A. Alchian & Reuben A. Kessel, *Competition, Monopoly and the Pursuit of Pecuniary Gain*, in *ASPECTS OF LABOR ECONOMICS* 157 (Nat'l Bureau Committee for Economic Research 1962)).

²⁶ *Id.* (citing ROBIN MARIS, *THE ECONOMIC THEORY OF 'MANAGERIAL' CAPITALISM* (1964), Thomas Mayer, *The Distribution of Ability and Earnings*, 42 REV. ECON. & STAT. 189 (1960), and OLIVER E. WILLIAMSON, *THE ECONOMICS OF DISCRETIONARY BEHAVIOR: MANAGERIAL OBJECTIVES IN A THEORY OF THE FIRM* (1964)).

professional and psychic satisfaction or to produce a larger source of managerial rents.²⁷

There are two contemporary suggestions of the constraints imposed by markets on the discretion of managers. In 1962, Alchian and Kessel suggested that even monopolists—who prior writers thought were not subject to constraints from competitive product markets and thus possessed total discretion—were subject to constraints from the capital markets.²⁸ In 1964, Oliver Williamson identified competitive product markets as a constraint on management's opportunistic behavior.²⁹ Williamson cites Scitovski's work suggesting a budget constraint for owner-managers³⁰ that anticipates Jensen and Meckling's later work. However, Williamson does not suggest the extensions to the agency setting developed by Jensen and Meckling.³¹

In 1965, Mosen and Downs visited the same agency problem that Williamson described in his dissertation, published in 1964.³² But Mosen and Downs doubted the effectiveness of markets in policing agency costs, because of stockholder ignorance, both about the alternative opportunities available to any single firm and the particular circumstances it faced.³³ Manne's work shows a much greater awareness of the developing notions of stock market efficiency and its effect on controlling managers than did the work of contemporary economic writers.

This pre-Manne literature lacked any sense of effective limits on the power of managers. If shareholders were content to receive just "satisfactory" returns, with managers appropriating the economic rents, and perhaps even the quasi-rents (a term not yet created, but

²⁷ See Oliver E. Williamson, *Managerial Discretion and Business Behavior*, 53 AM. ECON. REV. 1032, 1035 (1963).

The existence of satisfactory profits is necessary to assure the interference-free operation of the firm to the management. Precisely what this level will be involves a complicated interaction of the relative performance of rivals, the historical performance of the firm, and special current conditions that affect the firm's performance. Management, however, will find it desirable to earn profits that exceed the acceptable level. For one thing, managers derive satisfaction from self-fulfillment and organizational achievement, and profits are one measure of this success.

Id.

²⁸ Alchian & Kessel, *supra* note 25, at 160; see also GARY S. BECKER, *THE ECONOMICS OF DISCRIMINATION* 38 (1957).

²⁹ WILLIAMSON, *supra* note 26, at 2.

³⁰ *Id.* at 18-19 (citing T. Scitovski, *A Note on Profit Maximization and Its Implications*, 11 REV. ECON. STUD. 57 (1943)).

³¹ Jensen & Meckling, *supra* note 23, at 305.

³² R. Joseph Mosen, Jr. & Anthony Downs, *A Theory of Large Managerial Firms*, 73 J. POL. ECON. 221 (1965). These authors note that their article was written independently of, OLIVER E. WILLIAMSON, *THE ECONOMICS OF DISCRETIONARY BEHAVIOR: MANAGERIAL OBJECTIVES IN A THEORY OF THE FIRM* (1964), although some of the analysis is similar. See Mosen & Downs, *supra*, at 222 n.3.

³³ *Id.* at 225.

implicit in this literature) for themselves, why did shares persist? Why weren't firms financed entirely with bonds? Conventional economic analysis, entering the 1960s, offered no convincing answer to these questions.

B. The Legal Literature

Berle and Means' view of shareholders as powerless led legal scholars in two directions. The optimists took the path of "corporate democracy," that with a little regulation, shareholders could be empowered, and could wrest control away from management.³⁴ The pessimists concluded that shareholder democracy couldn't work, and wondered if giving shareholders the franchise at all was worth the trouble.³⁵ In essence, the pessimists conceded that managers were indeed the residual claimants, and shareholders merely bondholders.³⁶

The view of corporate managers was not a happy one, an understandable view given this model. Without using the terms, corporate managers were seen as the residual claimants on the firm's income stream. At the same time, this was viewed as illegitimate. In a positive sense, this was the world Berle and Means had described, but Berle and Means, or at least Berle, was more normative than positive. From Berle's point of view this wresting of property rights away from shareholders was illegitimate, and needed to be cured. In the meantime, legal scholars decried the high compensation received by corporate officers, an exercise that continues in many circles to this day.³⁷ The Baker and Cary casebook from which I was taught at the beginning of the 1960s, selected the American Tobacco case as an example of unaccountable executives receiving bloated bonuses.³⁸ Bayless Manning recited a complaint that management's self-determined compensation was so "unduly high" that it misallocated resources, by giving "the business corporation an overpowering bargaining advantage in the national competition for talented manpower—an advan-

³⁴ See, e.g., Mortimer M. Caplin, *Shareholder Nominations of Directors: A Program for Fair Corporate Suffrage*, 39 VA. L. REV. 141 (1953).

³⁵ See, e.g., Bayless Manning, Book Review, 67 YALE L.J. 1477, 1485-87 (1958) (reviewing J.A. LIVINGSTON, *THE AMERICAN STOCKHOLDER* (1958)).

³⁶ If they had been correct, the consequences for American capitalism would have been dire, because managers, holding undiversified portfolios, would probably not have taken the risks shareholders were willing to bear to restructure corporations in the 1980s and 1990s to meet the challenges of changing technology and international competition. Because American law imposed fiduciary duties on managers, there would have been constraints on managers' ability to capture all rents produced by the firm that would have prevented them from acting like owner-managers.

³⁷ Michael Jensen and Kevin Murphy have argued (1) that corporate executives appear to be underpaid, and (2) it doesn't matter very much if executives are overpaid, but it matters greatly *how* they are paid. See Michael C. Jensen & Kevin J. Murphy, *CEO Incentives: It's Not How Much You Pay, But How*, HARV. BUS. REV., May-June 1990, at 138.

³⁸ See RALPH J. BAKER & WILLIAM L. CARY, *CASES AND MATERIALS ON CORPORATIONS* 492 (3d ed. 1959) (discussing *Rogers v. Hill*, 289 U.S. 582 (1933)).

tage which government, schools, the military and other essential social service institutions cannot hope to match."³⁹ The academic literature of the late 1950s and early 1960s saw the sale of control of corporations as an opportunity for a new management team to steal from the stockholders.⁴⁰

During the 1950s, and even earlier, major regulatory efforts were made to cure this perceived "problem" of shareholder impotence and managerial power.⁴¹ Proxy reforms to allow shareholders to use management's proxy materials were proposed and adopted by the SEC.⁴² Yet observers were puzzled; nothing much changed, despite massive amounts of new regulation. Bayless Manning, one of the pessimists, summed this up in 1958:

In 1932, Berle and Means vivisected the modern corporation. They found a virtually omnipotent management and an impotent shareholdership. A quarter century of unparalleled law reform intervenes. In 1958, Livingston surveys the lot of the shareholder in a reformed world - a world of SEC regulation, extensive disclosure requirements, elaborate proxy machinery, Stock Exchange self-discipline, corporate Good Citizenship, People's Capitalism and Corporate Democracy. His finding? A virtually omnipotent management and an impotent shareholdership. The finding itself will not surprise many readers. But a book demonstrating that twenty-five years of reform have not appreciably changed the situation inescapably raises the question whether we have been on the right track for the last two and a half decades.⁴³

The legal literature had its own internal contradictions. While corporate managers were unfaithful stewards of shareholders' wealth, they were, at the same time, good corporate citizens with a sense of social responsibility that led them to make resource allocations with

³⁹ Manning, *supra* note 35, at 1484.

⁴⁰ CASES AND MATERIALS ON CORPORATIONS, *supra* note 38, contains a section on transfers of control. *Id.* at 590. The discussion contains a "Note on Problem of Equal Opportunity, Price or Realization," and contains only two cases: *Gerdes v. Reynolds*, 28 N.Y.S.2d 622 (N.Y. Sup. Ct. 1941), a corporate looting case, and *Perlman v. Feldman*, 291 F.2d 173 (2d Cir. 1955), which appears to be a corporate opportunity case that contains sweeping language about fiduciary duties of controlling shareholders. There is no mention in this section of any value that might be created through transfers of control. *Id.*

⁴¹ See, e.g., FRANK D. EMERSON & FRANKLIN C. LATCHAM, *SHAREHOLDER DEMOCRACY: A BROADER OUTLOOK FOR CORPORATIONS* (1954); LEWIS D. GILBERT, *DIVIDENDS AND DEMOCRACY* (1956).

⁴² The proxy rules first adopted in the 1950s were adopted in part to promote shareholder democracy. See Dennis S. Karjala, *Federalism, Full Disclosure, and the National Markets in the Interpretation of Federal Securities Law*, 80 NW. U. L. REV. 1473, 1491-92 (1986). See generally Caplin, *supra* note 34.

⁴³ Manning, *supra* note 35, at 1485.

the public good in mind. Berle himself made this argument in 1954,⁴⁴ after noting that in his earlier famous debate with Professor Dodd he had argued that managers should be responsible exclusively to shareholders.⁴⁵ At its root, all this literature suffered from one huge flaw—it gave no account of any serious constraints on corporate managers. Managers were viewed as possessing virtually complete discretionary power over firm assets. Logically, it would follow that they were also the claimants on the residual cash flows of the firm. Stockholders, content with a “satisfactory” return, were in effect no different than holders of risky debt. They would never receive any extraordinary returns, a claim at odds with common observations.

At the same time that corporate managers were vilified as unaccountable to shareholders, corporate raiders were frequently viewed as villains who were simply out to loot and pillage target corporations, and seize the perquisites of management for themselves.⁴⁶ There were proposals to restrict sales of control blocks of shares.⁴⁷ The irony of criticizing those who sought to displace unaccountable managers was lost on a generation of scholars, who saw this process as replacement of one unaccountable management team with another and possibly greedier team.⁴⁸ Rostow was almost alone in recognizing the paradox of these attitudes.⁴⁹ He noted that critics bemoaned

⁴⁴ ADOLF A. BERLE, JR., *THE 20TH CENTURY CAPITALIST REVOLUTION* 169 (1954) (acknowledging that corporate powers are held in trust for the community, despite Berle's earlier position that those powers are held in trust for shareholders).

⁴⁵ A. A. Berle, Jr., *Corporate Powers as Powers in Trust*, 44 HARV. L. REV. 1049 (1931); E. Merrick Dodd, Jr., *For Whom Are Corporate Managers Trustees?*, 45 HARV. L. REV. 1145 (1932); A. A. Berle, Jr., *For Whom Corporate Managers Are Trustees: A Note*, 45 HARV. L. REV. 1365 (1932); E. Merrick Dodd, Jr., *Is Effective Enforcement of the Fiduciary Duties of Corporate Managers Practicable?*, 2 U. CHI. L. REV. 194 (1935).

⁴⁶ See, e.g., William D. Andrews, *The Stockholder's Right to Equal Opportunity in the Sale of Shares*, 78 HARV. L. REV. 505, 509 (1965); Eugene V. Rostow, *To Whom and for What Ends is Corporate Management Responsible?*, in *THE CORPORATION IN MODERN SOCIETY* 46, 46 (Edward S. Mason ed., 1960). In fairness, Rostow's characterization seems more descriptive of the received wisdom than of his own views. Manning describes proxy contests as “[l]argely irrelevant to issues of corporate policy, fought out between rival cliques competing for personal control of the corporate treasury and the elixir of corporate office.” Manning, *supra* note 35, at 1488.

⁴⁷ See, e.g., Berle, *supra* note 9, at 1219; Richard W. Jennings, *Trading in Corporate Control*, 44 CAL. L. REV. 1, (1956).

⁴⁸ Manne raised this issue in 1967 and suggested that the pejorative term “raider” was misleading. He stated: “Unhappily, it is difficult to think of a mellifluous word with a happy connotation for what these unsung heroes do. Indeed the most accurate term might be ‘corporate garbagemen,’ since they clean up the messes left by the regular corporate householders. Anyone for ‘corporate redeemer?’” Henry G. Manne, *Cash Tender Offers for Shares - A Reply to Chairman Cohen*, 1967 DUKE L.J. 231, 236-37 n.14 [hereinafter *Cash Tender Offers*].

⁴⁹ But Rostow was not entirely alone. One writer argued as early as 1952 that purchasers of control may see the possibility of “increased profits from innovations in product or in production or merchandising policies.” Comment, *Sale of Corporate Control*, 19 U. CHI. L. REV. 869, 871 (1952). Another argued that purchases of control might as easily be motivated by the chance to improve management and increase firm value, and that a rule of equal opportunity for all shareholders to sell at a premium would reduce the number of such sales. See Wilber G.

the lack of shareholder activity, and posed an issue for which there was as yet no systematic explanation: "It is hard to imagine what canon of the capitalist ethic could be considered violated by the decision of the investor to buy corporate stock in order to vote it."⁵⁰ Rostow then asked a question that resulted from the current wisdom, coupled with distaste for corporate raiders and shareholders' derivative suits: "Whatever its past, has [the modern corporation] become a free collectivity, divorced in its business life from significant public or private control, save the will of the small group which happens to have inherited its management?"⁵¹

In Rostow's view, then, the result of the Berle and Means era was a recognition that the shareholder franchise did not appear useful; that transactions in control were frowned upon and likely to be treated as illegal; and that derivative actions were unlikely devices to hold managers accountable because they, too, were deemed socially unacceptable.⁵² Rostow was concerned that the end result of this view of corporations was acceptance of a form of socialism, where unaccountable managers operated corporations not with a view toward maximizing profits, but toward maximizing social welfare in some manner that he properly described as "bewildering balderdash."⁵³

At the end of this era, wise observers such as Bayless Manning realized that the old paradigms had served us badly.⁵⁴ He suggested that not only was shareholder democracy a failed paradigm, but that it might be useful to think about eliminating shareholder voting altogether as a misleading illusion, and rely instead on the Wall Street Rule and derivative suits.⁵⁵ Manning charged that corporate law's intellectual structure had rotted away so that it contained nothing but wind, and had ceased to be a field of intellectual effort.⁵⁶ In this criti-

Katz, *The Sale of Corporate Control*, 38 CHI. B. REC. 376, 379 (1957). The latter article contains an extraordinary discussion of what sharing rules shareholders might choose *ex ante*. See *id.* at 378-90. The article anticipates the discussion of this issue in Frank H. Easterbrook & Daniel R. Fischel, *Corporate Control Transactions*, 91 YALE L.J. 698, 700-03 (1982).

⁵⁰ Rostow, *supra* note 46, at 48.

⁵¹ *Id.* at 50.

⁵² *Id.* at 48-49.

⁵³ *Id.* at 63.

⁵⁴ Manning, *supra* note 35, at 1489 (noting that "the tenets of Corporate Democracy have served us little The reason is not hard to find. In looking to the shareholder franchise for management supervision, we have been trying to design remedies for a make-believe world rather than a real one."). For the last best articulation of the old paradigms, see generally THE CORPORATION IN MODERN SOCIETY (Edward S. Mason ed., 1960) [hereinafter Mason].

⁵⁵ Manning, *supra* note 35, at 1490-93.

⁵⁶ Bayless Manning, *The Shareholder's Appraisal Remedy: An Essay for Frank Coker*, 72 YALE L.J. 223, 245 n.37 (1962). I have previously written, "[a]s a law student studying corporation law [in the early 1960s], I found the subject unsatisfying, because it seemed to have little content beyond the Chancellor's *ex post* views of fairness." William J. Carney, *The ALI's Corporate Governance Project: The Death of Property Rights?*, 61 GEO. WASH. L. REV. 898, 953 (1993). This article provides a more complete explanation of the reasons for my dissatisfaction.

cism he was joined by Manne in 1962.⁵⁷ While Manning was correct, it remained for Manne to add content to the study of corporate law, and for him to restore it as a field of intellectual effort.

II. THE CONTRIBUTION OF *MERGERS AND THE MARKET FOR CORPORATE CONTROL* AND ITS COMPANIONS

By 1962, corporate law and jurisprudence was ready for a new paradigm. In the following five years, Henry Manne created the paradigm that has dominated discourse about the firm and corporate law for the remainder of the century, and shows every prospect of a long and vital life in the next. While the title of this article suggests that it focuses on only one of Manne's articles,⁵⁸ that is misleading. One cannot view *Mergers and the Market for Corporate Control* outside the immediate context of Manne's other contributions.⁵⁹ The context was an outpouring of intellectual creativity never seen before, and unlikely to be seen again, in analysis of the theory of the firm. It began in 1962 with *The "Higher Criticism" of the Modern Corporation*,⁶⁰ continued with *Some Theoretical Aspects of Share Voting* in 1964,⁶¹ *Mergers and the Market for Corporate Control* in 1965,⁶² and concluded in 1967 with two articles: *Our Two Corporation Systems: Law and Economics*,⁶³ and *Cash Tender Offers for Shares - A Reply to Chairman Cohen*.⁶⁴ I say "concluded" because at this point Manne had essentially outlined most of the concepts that we now think of as constituting the theory of the firm and had described the role of corporate law.

The curious part of my study is how one of these articles, *Mergers and the Market for Corporate Control*, stands out compared to the others. It is the nineteenth most frequently cited "law review" article of all time, even though it was published in an economics journal, rather than a traditional law review.⁶⁵ That makes it the most cited corporate law article of all time, and the third most cited law and economics article.⁶⁶ Only two other corporate law articles made the top

⁵⁷ Henry G. Manne, *The "Higher Criticism" of the Modern Corporation*, 62 COLUM. L. REV. 399, 430 (1962) [hereinafter *The Higher Criticism*].

⁵⁸ Henry G. Manne, *Mergers and the Market for Corporate Control*, 73 J. POL. ECON. 110 (1965) [hereinafter *Corporate Control*].

⁵⁹ Henry G. Manne, *Some Theoretical Aspects of Share Voting: An Essay in Honor of Adolf A. Berle*, 64 COLUM. L. REV. 1427 (1964) [hereinafter *Theoretical Aspects*]; *Two Corporation Systems*, *supra* note 15; *Cash Tender Offers*, *supra* note 48.

⁶⁰ *The Higher Criticism*, *supra* note 57.

⁶¹ *Theoretical Aspects*, *supra* note 59.

⁶² *Corporate Control*, *supra* note 58.

⁶³ *Two Corporation Systems*, *supra* note 15.

⁶⁴ *Cash Tender Offers*, *supra* note 48.

⁶⁵ See Fred R. Shapiro, *The Most-Cited Law Review Articles Revisited*, 71 CHI.-KENT L. REV. 751, 768 (1996).

⁶⁶ *Id.* at 767-68.

100, showing the unpopularity of our subject with law review editors.⁶⁷ Manne's other articles that I've mentioned do not appear on this list, although they also make signal contributions to the theory of the firm and the role of corporate law.

Let me begin by listing some of the major contributions Manne made in this brief period. As a preface, Manne brought positive social science to a field dominated by the normative preaching of both law professors and a significant number of judges of the time. First, the notion of shareholders as specialists in passive risk-bearing originated with Manne.⁶⁸ This passivity in turn explained why then-conventional notions of shareholder activism, through the ballot and the proxy fight, were misguided in their prescriptions. Second, Manne was aware of the problem of agency costs, and how these costs were imposed on shareholders. But rather than urge new legal rules to constrain agents, he recognized the role of financial incentives—even insider trading profits—to motivate agents. Third, he recognized the wisdom of judicial restraint in monitoring management and the uses of the derivative suit. Fourth, he recognized that control was an asset, although in a very different way than Berle and Means saw it. Finally, he recognized the value of corporate law as a series of default rules, and the potential need for very different such rules for public and close corporations.

A. *Positive Social Science*

The Higher Criticism was a challenge to the entire intellectual structure that proceeded from Berle and Means' work. It noted Berle and Means' argument that managers became independent from both shareholders and capital markets through retention of earnings, and that Lintner's work had rejected this claim.⁶⁹ Berle and Means predicted that earnings retention would lead to greater control of national wealth by giant corporations, which Lintner's work disproved.⁷⁰

More importantly, perhaps, *The Higher Criticism* introduced economic reasoning to legal discourse in a way that Berle and Means failed to do. For example, Berle and Means argued that managers of monopolies could hire capital with a "fair return," while retaining monopoly profits for themselves or dissipating rents through indolence, empire-building, and similar tactics. Manne noted that monop-

⁶⁷ *Id.* at 767-71 (listing Frank H. Easterbrook & Daniel R. Fischel, *The Proper Role of a Target's Management in Responding to a Tender Offer*, 94 HARV. L. REV. 1161 (1981) as the 24th most-cited law review article and William L. Cary, *Federalism and Corporate Law: Reflections upon Delaware*, 83 YALE L.J. 663 (1974) as the 49th most-cited law review article).

⁶⁸ *The Higher Criticism*, *supra* note 57, at 406 n.20.

⁶⁹ *Id.* at 400-01 (citing John Linter, *The Financing of Corporations*, in Mason, *supra* note 54, at 166).

⁷⁰ *The Higher Criticism*, *supra* note 57, at 401.

oly profits would be capitalized in share prices, providing a one-time windfall and normal returns in competitive capital markets.⁷¹

The beginnings of a theory of agency costs can be found in *The Higher Criticism*, where Manne argues that where managers can retain rents because of the high costs of proxy fights to replace them, firms with a separation of ownership and control will be less profitable than firms controlled by owner-managers.⁷² *The Higher Criticism* also introduced the idea that shareholders specialized in passive risk-bearing.⁷³ Indeed, *The Higher Criticism* concluded that there was at the time no detailed exposition of an economic theory of the modern corporation, and that reform of corporate law should proceed slowly until a theory was developed.⁷⁴

There is one other aspect of Manne's work that Fred McChesney has noted that is worth repeating and expanding.⁷⁵ By the standards of law professors, and even to some extent those of economists, these articles are brief. They have relatively few footnotes. *Mergers and the Market for Corporate Control* is eleven pages long, with 34 footnotes. *Some Theoretical Aspects of Share Voting* is eighteen pages long, with 43 footnotes. *The Higher Criticism* goes on for thirty-three pages and 100 footnotes, making it the monster in the group. *Our Two Corporation Systems* covers 25 pages and 35 footnotes, and *Cash Tender Offers for Shares - A Reply to Chairman Cohen* covers 22 pages and 55 footnotes. The average law review article that I read generally goes on for fifty or more pages, with perhaps 200 footnotes. Unlike most of his contemporaries, Manne was not citing to precedent for his arguments; he was creating theory. He was treading where none had gone before; there was, in one sense, no one to cite. After the completion of these articles, there were indeed articles to cite. We all stand on the shoulders of giants, and Henry Manne is one of those giants.⁷⁶

⁷¹ *Id.* at 402-04.

⁷² *Id.* at 405-06. Monsen and Downs should also be given credit for anticipating Jensen and Meckling's dichotomy between owner-operators and widely dispersed owners, three years after *The Higher Criticism*. See Monsen & Downs, *supra* note 32, at 223.

⁷³ *The Higher Criticism*, *supra* note 57, at 406 n.20.

⁷⁴ *Id.* at 430-432.

⁷⁵ Fred S. McChesney, *Manne, Mergers and the Market for Corporate Control*, 50 Case W. Res. L. Rev. 245, 252 (1999).

⁷⁶ Lest I be guilty yet again of using a felicitous phrase without attribution, this one is attributed to Sir Isaac Newton. See ROBERT K. MERTON, ON THE SHOULDERS OF GIANTS 31 (1965) (quoting letter from Isaac Newton to Robert Hooke).

B. *The Role of Shareholders*

1. *Shareholders as Specialized Risk-Bearers*

The notion of shareholders as specialized risk-takers was first introduced in 1962 in *The Higher Criticism*.⁷⁷ It was not elaborated in this article, because Manne only used it to reject the Berle and Means complaint about the separation of ownership and control, by responding that shareholders weren't specialized in monitoring or exercising control. Manne complained that the proponents of corporate democracy had never explained the justification for that goal.⁷⁸ It wasn't until he had worked his way through the collective action problems facing shareholders and transactions involving voting that he returned to analyze the role of shareholders in *Two Corporation Systems*, in 1967. According to Manne, the financing of large ventures through public markets and the concomitant dispersion of ownership necessitated centralized management.⁷⁹ Here he engaged in a pioneering exploration of the role of limited liability. He explained first that limited liability flowed inevitably from public ownership, since unlimited liability would be impracticable for small investors, and would deter them from investing at all.⁸⁰ In view of the later literature, one wishes he had said "passive investors," or "dispersed investors," but the point is clear enough, given what he had already said about the collective action problems of shareholders in earlier articles. Manne also pointed out that unlimited liability would result in uneven collection from shareholders and high costs of collection.⁸¹ Consequently, it was cheaper to shift the risk of non-collection to creditors who can adjust prices they charge the corporation to compensate for the risk they assume.⁸² These ideas were not explored again for many years, and then only to elaborate and refine the ideas Manne first expressed in 1967.⁸³ Manne was not concerned about a failure of protection for tort victims under such a regime, before the emergence of mass torts, because of what we would now call the safety net of social services-unemployment compensation, workers' compensation, and

⁷⁷ *The Higher Criticism*, *supra* note 57, at 406 n.20.

⁷⁸ *Id.* at 408.

⁷⁹ *Two Corporation Systems*, *supra* note 15, at 260-61.

⁸⁰ *Id.* at 262.

⁸¹ *Id.*

⁸² *Id.* at 262-63.

⁸³ See, e.g., Aubrey L. Diamond, *Corporate Personality and Limited Liability*, in LIMITED LIABILITY AND THE CORPORATION 22 (Tony Orhnia ed., 1982); Frank H. Easterbrook & Daniel R. Fischel, *Limited Liability and the Corporation*, 52 U. CHI. L. REV. 89, 90-91 (1985); Henry Hansmann & Reinier Kraakman, *Toward Unlimited Shareholder Liability for Corporate Torts*, 100 YALE L.J. 1879, 1880 (1991). For a review of this literature generally, see William J. Carney, *Limited Liability*, in ENCYCLOPEDIA OF LAW & ECONOMICS, <<http://encyclo.findlaw.com/lit/5620.htm>>.

bankruptcy priorities.⁸⁴ The discussion of the importance of liquidity to public investors in this article was not entirely original, but nonetheless an important part of a systematic explanation of the role of the public shareholder.⁸⁵

At the same time, *Two Corporation Systems* offered the first systematic explanation of the role of owners in close corporations. Manne noted the likelihood that shareholders in these firms bring particular skills or services to the firm, and thus do not expect to play a passive role.⁸⁶ Because of their reliance on each other and their anticipation of an active role, free transferability is the antithesis of this relationship, just as in the partnership.⁸⁷ All of this was developed more fully by Fama and Jensen, but the foundation was in place.⁸⁸

Berle and Means had alluded to the ability of controlling shareholders to cause the corporation to engage in self-dealing, typically in mergers or asset sales, at the expense of the remaining shareholders.⁸⁹ Manne recognized that conflicts among shareholders might develop naturally and innocently because of conflicting goals, and recognized the importance of liquidity as an exit device where corporate policy changed in ways that no longer suited shareholders.⁹⁰ Squeeze-out techniques such as withholding dividends were also recognized. More importantly, *Two Corporation Systems* recognized the importance of minority shareholder veto power in close corporations as protection against majority overreaching.⁹¹ This presaged the development of "shark repellent" defenses against abusive takeout mergers in the public corporation at a time when the two-tier takeover bid was in its nascent stage.⁹²

2. The Collective Action Problems of Shareholders

Without detailing the collective action problems of shareholders, Manne introduced the subject as a worthy one for study in *The Higher*

⁸⁴ *Two Corporation Systems*, *supra* note 15, at 263. For a discussion of the problems raised by modern concerns about tort liability, see Hansmann & Kraakman, *supra* note 83; David Leebron, *Limited Liability, Tort Victims and Creditors*, 91 COLUM. L. REV. 1565 (1991); Alan Schwartz, *Products Liability, Corporate Structure, and Bankruptcy: Toxic Substances and Remote Risk Relationship*, 14 J. LEGAL STUD. 689 (1985). See generally Carney, *supra* note 83.

⁸⁵ *Two Corporation Systems*, *supra* note 15, at 263-65; see also BERLE & MEANS, *supra* note 2, at 283-85.

⁸⁶ *Two Corporation Systems*, *supra* note 15, at 278-79.

⁸⁷ *Id.*

⁸⁸ Fama & Jensen, *Ownership and Control*, *supra* note 22; Fama & Jensen, *Residual Claims*, *supra* note 22.

⁸⁹ BERLE & MEANS, *supra* note 2, at 271-74.

⁹⁰ *Two Corporation Systems*, *supra* note 15, at 263-64.

⁹¹ *Id.* at 281, 283.

⁹² For a description of these shark repellents, see generally William J. Carney, *Shareholder Coordination Costs, Shark Repellents and Takeout Mergers: The Case Against Fiduciary Duties*, 1983 AM. B. FOUND. RES. J. 341 (1983).

Criticism in 1962. He simply noted Anthony Downs' work in public choice, and suggested that its reasoning might have applicability for the study of shareholder behavior and the market for managers.⁹³ This was expanded in 1964 in *Some Theoretical Aspects of Share Voting*, in which Manne noted that vote-selling takes place in politics, and that more open vote-selling might maximize welfare, citing Downs as well as Buchanan and Tullock's then-new book.⁹⁴ Manne wrote the article in the face of received wisdom that all vote-selling was against public policy, but it was not too many years before the Delaware courts examined the subject more carefully and rejected a per se rule against vote-buying, recognizing its potential for increasing aggregate welfare.⁹⁵ Manne went on to explore the costs shareholders face in proxy fights, providing the first complete account of why corporate democracy of the kind advocated by disciples of Berle and Means was a doomed idea. He spelled out the information costs facing shareholders in order to make intelligent decisions in a proxy fight between competing management teams.⁹⁶ More importantly, Manne developed the notion of rational apathy of shareholders, who could rationally free-ride on the efforts of others to obtain and use information, unlike the political arena, where voters must defend themselves against wealth transfers.⁹⁷

In 1965, Manne expanded this discussion in *Mergers and the Market for Corporate Control* to include a look at the free rider problem facing shareholders willing to undertake the expense of a proxy fight. Manne used this as a way of showing why acquisitions of control through stock purchases were a more likely corrective device for mismanagement, because they allowed a buyer to internalize more of the gains from a change in control.⁹⁸ He also noted that proxy fights may be discouraged at the margin by the increased costs imposed by SEC regulation—one of the first attempts to look at the costs of SEC regulation.⁹⁹

In *Some Theoretical Aspects of Share Voting*, Manne argued that the information problems facing shareholders were largely scale problems, and that they represented a market opportunity for entrepreneurs who could analyze information and realize economies of scale by selling the analysis to many shareholders.¹⁰⁰ While he an-

⁹³ *The Higher Criticism*, *supra* note 57, at 431 n.100 (citing ANTHONY DOWNS, AN ECONOMIC THEORY OF DEMOCRACY (1957)).

⁹⁴ *Theoretical Aspects*, *supra* note 59, at 1427-29 (citing JAMES BUCHANAN & GORDON TULLOCK, THE CALCULUS OF CONSENT (1962)).

⁹⁵ *Schreiber v. Carney*, 447 A.2d 17 (Del. Ch. 1982).

⁹⁶ *Theoretical Aspects*, *supra* note 59, at 1440.

⁹⁷ *Id.* at 1441-42. The idea of rational apathy of voters originated in DOWNS, *supra* note 93, at 4-6, 260-76.

⁹⁸ *Corporate Control*, *supra* note 58, at 114-15.

⁹⁹ *Id.* at 115.

¹⁰⁰ *Theoretical Aspects*, *supra* note 59, at 1442-43.

anticipated that brokers would be the logical sellers and that small shareholders would be their customers, it worked out somewhat differently. During the restructuring of the 1970s and 1980s, brokers sold information about firms to potential bidders for control. More recently, because of the growth of retirement plans, institutional ownership, and the development of advisory services to institutions on shareholder issues, informational intermediaries other than brokers have developed to produce and sell information to large investors.¹⁰¹ With the development of indexing, institutional investors no longer devoted resources to stock picking, and have instead turned their analysis to corporate governance issues in ways that could not have been anticipated twenty-five years ago. But Manne was correct; it took scale economies to make voting work, and to give some vigor to the proxy.

While Manne may not have said everything there was to say about a theory of shareholder behavior in this article, he said enough that no one really attempted to return to this area for over fifteen years. Robert Clark wrote his article describing the sale of votes in 1979, and Frank Easterbrook and Daniel Fischel treated the subject in 1983.¹⁰² Both articles built upon Manne's earlier insights.

C. The Agency Cost Problem

Agency costs have been noted since Berle and Means, or more accurately, since Adam Smith.¹⁰³ *The Higher Criticism* addressed this "problem" by noting that there is a competitive market for manage-

¹⁰¹ The Investor Responsibility Research Center (IRRC) is a non-profit research group that has conducted substantial research on institutional investor responses to anti-takeover devices such as unequal voting stock, limits on special shareholders' meetings, elimination of ability to act by written consents, adoption of a classified board, authorization of blank-check stock, and anti-greenmail provisions. See JEFFREY W. BERSHACH, VOTING BY INSTITUTIONAL INVESTORS ON CORPORATE GOVERNANCE ISSUES IN THE 1990 PROXY SEASON ii (1990). The Council of Institutional Investors, an organization that advises many of the largest institutional investors, has issued a list of the twenty-five worst corporate investments. See Kevin G. Salwen, *Institutions Are Poised to Increase Clout in Boardroom*, WALL ST. J., Sept. 21, 1992, at B1. Institutional Shareholder Services, Inc. advises and/or votes for more than 250 institutional investors, primarily in the United States but also some institutions in Canada, the United Kingdom, and Australia. See Howard Sherman, Commentary, 21 BROOK. J. INT'L L. 79, 80 (1995); see also Jayne W. Barnard, *Shareholder Access to the Proxy Revisited*, 40 CATH. U. L. REV. 37, 83 n.287 (noting that "[s]hared cost research is available through groups such as the Council of Institutional Investors, IRRC, Analysis Group, Inc., and Institutional Shareholder Services, Inc").

¹⁰² Robert C. Clark, *Vote Buying and Corporate Law*, 29 CASE W. RES. L. REV. 776 (1979); Frank Easterbrook and Daniel Fischel, *Voting in Corporate Law*, 26 J. L. & ECON. 395 (1983).

¹⁰³ "The directors of such companies, however, being the managers rather of other people's money than of their own, it cannot be well expected that they should watch over it with the same anxious vigilance with which the partners in a copartnership frequently watch over their own Negligence and profusion, therefore, must always prevail, more or less, in the management of the affairs of such a company." SMITH, *supra* note 13, at 700.

ment positions, evidenced by proxy fights; indeed, the presence of monopoly power in the market for managers was too far-fetched to be considered.¹⁰⁴ The article also argued that firms suffering the costs of separation of ownership and control would be forced to compete with firms controlled by owner-managers, perhaps presaging the formalization of this relationship by Jensen and Meckling fourteen years later.¹⁰⁵ The Business Judgment Rule was explained in *Two Corporation Systems* as being justified not because it reduced risk for directors, which could be compensated through higher directors' compensation, but because of the relative competence of directors and judges.¹⁰⁶ It was also described as a rule of procedure, rather than a substantive rule, which has become more apparent since the article appeared.¹⁰⁷ The nature of the derivative action as the tool of choice for judicial regulation of directors' misbehavior was explained by contrasting it with direct actions by shareholders. These shareholder actions could be multiple, and could provide for preferred recoveries for those acting first—the justification later offered for bankruptcy proceedings.¹⁰⁸

D. Monitoring Management

While Berle and Means identified the agency cost problem, Manne was the first to describe the role markets played in monitoring and controlling these costs. He introduced the now familiar trilogy: the market for products, the market for managers, and the market for corporate control, each as playing a part in controlling these costs.

The Higher Criticism was the first to recognize the role that product markets would play in constraining managers. Manne noted that where managers were capable of extracting rents from investors because of the high cost of proxy fights, management-controlled firms must compete with firms controlled by owner-managers. Such firms could operate at lower costs, thus affecting the profits of management-controlled firms.¹⁰⁹

The Higher Criticism also introduced the concept of a market for managers. The article spoke of owners of firms as purchasing management services, and rejected the notion of a monopolized market for managers as far-fetched.¹¹⁰ Manne declined to develop a theory of "a management industry . . . here; suffice it for the moment to say that

¹⁰⁴ *The Higher Criticism*, *supra* note 57, at 404-05.

¹⁰⁵ *Id.* at 405-06; Jensen & Meckling, *supra* note 23.

¹⁰⁶ *Two Corporation Systems*, *supra* note 15, at 270-72 (explaining the evolution and uses of the business judgment rule).

¹⁰⁷ *Id.* at 271-72.

¹⁰⁸ *Id.* at 272-73.

¹⁰⁹ *The Higher Criticism*, *supra* note 57, at 405-06.

¹¹⁰ *Id.* at 404.

there is such an industry and that individuals and groups of individuals compete for the prizes that are offered the successful contenders."¹¹¹ Like Berle and Means, Manne recognized that high costs of competing for management positions created entry barriers. Like Jensen and Meckling, Manne observed that if the marginal costs of eliminating an agency cost exceed the marginal cost itself, no change would occur.¹¹²

E. The Market for Corporate Control

Mergers and the Market for Corporate Control was the natural culmination of Manne's writing and thinking on the role markets played in constraining managers. John Lintner wrote an article in 1959 testing Berle and Means' predictions, which were that through retention of earnings, independence from capital markets and market power, large corporations would continue to grow and control a greater percentage of the nation's wealth.¹¹³ Lintner found the evidence rejected this and the other predictions of Berle and Means.¹¹⁴ Lintner provided evidence that managers were responsive to changes in the cost of capital, which was what "would be expected if management were under rather effective constraints to respond to the allocative mechanisms of the outside markets for funds."¹¹⁵ Lintner also showed that capital was seeking investments in industries with higher profits.¹¹⁶ In short, capital markets were behaving as if investors had good information about the quality of management. Manne was certainly the first legal academic to recognize the importance of the emerging work about the constraints imposed on managers by capital markets, as he did in *The Higher Criticism*. Citing Lintner's work, Manne noted that shareholders were primarily interested in having managers maximize profits, and that stock prices reflected the success of their efforts.¹¹⁷

In 1962 *The Higher Criticism* introduced the notion that weak management that caused profits to decline would also cause share prices to decline, which would in turn attract outsiders as buyers because of the votes attached to the shares.¹¹⁸ These buyers would in turn use the votes they had purchased with their shares to seek better

¹¹¹ *Id.* at 405.

¹¹² *Id.*

¹¹³ Lintner, *supra* note 69.

¹¹⁴ *Id.* at 176, 189-90.

¹¹⁵ *Id.* at 187.

¹¹⁶ *Id.* at 189.

¹¹⁷ *The Higher Criticism*, *supra* note 57, at 401-02.

¹¹⁸ *Id.* at 410-11, 420. In 1965, Monsen and Downs recognized that the threat of takeovers would constrain extraordinarily poor management, without citation to Manne's work. Monsen & Downs, *supra* note 32, at 226. This appears to be the second recognition of the power of the market for corporate control.

management and the rewards of higher earnings and stock appreciation.¹¹⁹ In this first article, Manne had made the critical linkage between share voting and share transferability, which he would develop more fully in 1964 and 1965.¹²⁰

In 1964 *Some Theoretical Aspects of Share Voting* first developed the notion that there were positive returns to acquiring voting control of firms, and that these returns come from improved management.¹²¹ Manne described shares as consisting of a bundle of rights—one being the investment and the other being the right to vote. He noted that the value of the share vote rose as the value of the share itself declined from poor management, and that the difference represented the control premium that outside management teams would be willing to pay for control.¹²² He first described the holdout problem facing a bidder for control, and concluded that a bidder would not require 100% of the shares as a condition for a tender offer, anticipating Grossman and Hart's important contribution by fifteen years.¹²³ Because of the veto power possessed by target management in mergers and their consequent ability to capture part of the control premium, he predicted that shareholders would receive smaller control premiums in mergers than in tender offers,¹²⁴ a prediction later borne out by empirical studies.¹²⁵ It was this 1964 article that first introduced the phrase, "the market for corporate control."¹²⁶

But it was *Mergers and the Market for Corporate Control* that gained the most attention in this remarkable series. The article was written as an antitrust article, but it achieved fame as a corporate law article.¹²⁷ In one sense the article represents an extension of the failing-firm defense in antitrust; that little competitive harm is threatened from the horizontal acquisition of a failing firm. Early on it rejected the received wisdom: "Take-overs of corporations are too expensive generally to make the 'purchase' of management compensation an attractive proposition."¹²⁸ The returns from acquiring control, Manne argued, were from improving management. Improving management would, in turn, increase cash flows that would be capitalized by the

¹¹⁹ *The Higher Criticism*, *supra* note 57, at 411-12.

¹²⁰ *Id.* at 413.

¹²¹ *Theoretical Aspects*, *supra* note 59, at 1430-31.

¹²² *Id.* at 1431-33.

¹²³ *Id.* at 1434; Sanford J. Grossman & Oliver D. Hart, *Takeover Bids, the Free-Rider Problem, and the Theory of the Corporation*, 11 BELL J. ECON. 42, 42-43 (1980).

¹²⁴ *Theoretical Aspects*, *supra* note 59, at 1437-38.

¹²⁵ Michael C. Jensen & Richard S. Ruback, *The Market for Corporate Control: The Scientific Evidence*, 11 J. FIN. ECON. 1, 11-13 (1983) (comparing target shareholder returns in tender offers and mergers).

¹²⁶ *Theoretical Aspects*, *supra* note 59, at 1444.

¹²⁷ *Corporate Control*, *supra* note 58, at 112 ("The emphasis will be placed on the antitrust implications of this market, but the analysis to follow has important implications for a variety of economic questions.")

¹²⁸ *Id.* at 113.

market.¹²⁹ Remarkably, the article predicted leveraged buyouts, noting that any gains from efficient management could be leveraged through borrowed funds, "although American commercial banks are generally forbidden to lend money for this purpose."¹³⁰ It took development of other sources of funds—notably junk bond markets and non-bank institutional lenders—for this leveraging to flower two decades later.

The article examined the arguments against control premiums that stemmed from Berle's claim that control was a corporate asset.¹³¹ Manne acknowledged the burgeoning literature on the subject in the late 1950s that argued for a sharing of any control premiums received. Reducing the amounts received by those presently holding control would, of course, reduce the number of transactions in control, and thus the efficiency of the market for corporate control as a curative device.¹³²

In the context of mergers, Manne recognized the value of the veto power held by managers over this form of takeover, and the likelihood that this veto would encourage side payments to management to persuade it to allow shareholders to accept a premium for their shares.¹³³ This observation has obvious implications, of which we all became acutely aware later on. First, if managers can extract a part of the economic rents available to shareholders in a target corporation, returns to target shareholders in mergers should be smaller than in tender offers. Later evidence has borne this out. Second, if changes of control are efficient and are furthered by management acquiescence, how much power should target-management possess in order to extract part of the gains? The struggles of the Delaware courts in attempting to delineate how much corruption is too much in this setting have occupied corporate lawyers for the past fifteen years. But the outline of the problem has been present for the last 34 years.

The article reiterated and fleshed out Manne's description of other tools to control management and agency costs, but the most important contribution of this article was its description of the market for corporate control as a serious constraint on management misbehavior. As Manne wrote:

Only the take-over scheme provides some assurance of competitive efficiency among corporate managers and thereby affords strong protection to the interests of vast numbers of

¹²⁹ *Id.*

¹³⁰ *Id.*

¹³¹ *Id.* at 116 (citing BERLE & MEANS, *supra* note 2, at 244, and Berle, *supra* note 9, at 1212).

¹³² *Corporate Control*, *supra* note 58, at 116-17.

¹³³ *Id.* at 117-118.

small, non-controlling shareholders. Compared to this mechanism, the efforts of the SEC and the courts to protect shareholders through the development of a fiduciary duty concept . . . seem small indeed.¹³⁴

Manne proceeded in 1967 to explain how markets for corporate control utilized information. In *Cash Tender Offers for Shares—a Reply to Chairman Cohen*, he focused on the costs of production of valuable information about mismanagement of firms.¹³⁵ If regulation were to require disclosure of a bidder's private information, it would reduce the gains from its production and thus deter wealth-creating takeovers. In responding to SEC Chairman Cohen's argument that shareholders should be on an equal informational footing with bidders, Manne wrote, "[i]t is hard to conceive of a sentence which packs more misunderstanding of how markets in general function and in particular how the market for corporate control functions."¹³⁶ These were words hardly designed to win friends and influence people in the Washington bureaucracy or the halls of Congress. Then, as now, Washington has been able to ignore hard truths.

F. The Role of Corporate Law

Our Two Corporation Systems was the first article to provide a defense of a system of competition among the states for chartering revenues. In a footnote, Manne observed both the permissive and uniform nature of state corporation laws and noted that "[a]lthough this process has generally been criticized in the literature, it has probably saved our corporate system from a substantial dose of undesirable state regulation."¹³⁷ No one returned to this theme until Ralph Winter's article in 1977.¹³⁸ Manne created the intellectual case for a permissive corporate law; again, a case that had not previously been articulated in economic terms, if at all. Most corporate legal academics of the time seemed embarrassed by the system that had developed.¹³⁹

Manne tells much of the story of the development of corporate law as a story of efficient common-law judges wisely exercising re-

¹³⁴ *Id.* at 113.

¹³⁵ *Cash Tender Offers*, *supra* note 48, at 232.

¹³⁶ *Id.* at 241.

¹³⁷ *Two Corporation Systems*, *supra* note 15, at 270 n.20.

¹³⁸ Ralph K. Winter, Jr., *State Law, Shareholder Protection, and the Theory of the Corporation*, 6 J. LEGAL STUD. 251 (1977). More recent evidence provides evidence of the interest group provisions, principally those benefiting labor and creditors, that have been avoided through competition for chartering business. See William J. Carney, *The Political Economy of Competition for Corporate Charters*, 26 J. LEGAL STUD. 303, 304 (1997).

¹³⁹ See, e.g., William L. Cary, *Federalism and Corporate Law: Reflections Upon Delaware*, 83 YALE L.J. 663 (1974); Ernest L. Folk, III, *Some Reflections of a Corporation Law Draftsman*, 42 CONN. B.J. 409 (1968).

straint in attempting to regulate the public corporation. Part of the restraint was in protecting the transferability of shares to allow the function of a market for corporate control.¹⁴⁰ A more important restraint, however, was shown in the development of the business judgment rule, which Manne correctly described as essentially a procedural rule to confine courts to relatively objective determinations of process, rather than more intrusive and subjective decisions of what constitutes reasonable care.¹⁴¹ The enabling nature of corporate statutes was seen not as the product of the visible hand of legislatures, but of competitive forces mentioned above.¹⁴² The result, he observed, was that there were few mandatory provisions left in corporate law. Indeed, he anticipated some later commentary about the triviality of corporate laws for public corporations¹⁴³ when he noted that the advent of these permissive provisions had not led to radical change in public corporations. Manne asserted that, "[o]ne is almost tempted to suggest that the large corporation system could and would function substantially as it does if there were almost no state corporation statutes beyond provisions for incorporation."¹⁴⁴

At the same time, Manne recognized the unsuitability of laws governing public corporations for closely held firms. Noting the specificity of resources that participants in closely held enterprises bring to the firm and their desire to participate in control, Manne anticipated the work of Fama and Jensen about the characteristics of these firms.¹⁴⁵ He recognized that the failure of courts in this area was in their application of the norms for public corporations to these firms. Manne further noted that this deficiency stemmed from their failure to recognize the very different economic functions performed by shareholder in public and close corporations.¹⁴⁶

III. THE LEGACY OF THE MARKET FOR CORPORATE CONTROL

The contributions in this Symposium are testimony to the impact Henry Manne's work has had on our times. My assigned task is to say something useful about the impact of *Mergers and the Market for*

¹⁴⁰ *Two Corporation Systems*, *supra* note 15, at 270.

¹⁴¹ *Id.* at 271-72.

¹⁴² *Id.* at 260 (Manne believes that "[t]o attribute the success of the modern corporation specifically to law and lawyers is a professional conceit which will not bear scrutiny"). *Id.* (citation omitted).

¹⁴³ See Bernard S. Black, *Is Corporate Law Trivial?: A Political and Economic Analysis*, 84 Nw. U. L. REV. 542 (1990).

¹⁴⁴ *Two Corporation Systems*, *supra* note 15, at 284.

¹⁴⁵ *Id.* at 278. See generally Fama & Jensen, *Ownership and Control*, *supra* note 22, at 301.

¹⁴⁶ *Two Corporation Systems*, *supra* note 15, at 282. Ayres later raised the question of whether common law judges were really as good at finding efficient solutions as earlier writers, notably Manne and Posner, thought, in view of this failure. See Ian Ayres, *Judging Close Corporations in the Age of Statutes*, 70 Wash. U. L.Q. 365, 369 (1992).

Corporate Control. Simply by describing the intellectual contribution he made with these five articles published over five years, I hope that I have fulfilled my charge. It would be unfair to focus simply on these five articles as the extent of his contribution during that period. He also published his book on insider trading, which stirred an immediate furor beyond anything these five articles started.¹⁴⁷

In examining the legacy of *Mergers and the Market for Corporate Control*, I have thus far tried to provide a qualitative account of the intellectual importance of Henry Manne's work, simply by recounting his observations and theories. Anyone conversant with academic literature in law, economics, or finance over the past two decades will recognize the importance of these ideas.

A. Manne and the Law Professors

In this part, I will attempt to add a quantitative aspect. *Mergers and the Market for Corporate Control* was, as I noted earlier, number nineteen on the all-time hit list of most cited law review articles, with 384 cites.¹⁴⁸ It is difficult to say something objective about the importance of this and the other articles I have described. The hit parade ranking is one way. I lack both the research skills and the will to engage in a search as thorough as that of Professor Shapiro, so my results are much more limited. In a search I conducted on LEXIS on February 12, 1999, I found the following frequency of citation for these articles, set forth in Table 1:

Table 1
Frequency of Citation in Law Journals

<i>The 'Higher Criticism' of the Modern Corporation</i>	9 cites
<i>Some Theoretical Aspects of Share Voting</i>	49 cites
<i>Mergers and the Market for Corporate Control</i>	214 cites
<i>Our Two Corporation Systems: Law and Economics</i>	66 cites
<i>Cash Tender Offers for Shares - A Reply to Chairman Cohen</i>	8 cites

¹⁴⁷ HENRY G. MANNE, *INSIDER TRADING AND THE STOCK MARKET* (1966); see also Jonathan R. Macey, *Securities Trading: A Contractual Perspective*, 50 CASE W. RES. L. REV. 269 (1999). For commentary on Macey, *supra*, see Michael P. Dooley, *Comment from an Enforcement Perspective*, 50 CASE W. RES. L. REV. 319, 319-20 (1999); David D. Haddock, *Academic Hostility and SEC Acquiescence: Henry Manne's Insider Trading*, 50 CASE W. RES. L. REV. 313, 314-15 (1999); Richard W. Painter, *Insider Trading and the Stock Market Thirty Years Later*, 50 CASE W. RES. L. REV. 305, 306 (1999); Robert B. Thompson, *Insider Trading, Investor Harm and Executive Compensation*, 50 CASE W. RES. L. REV. 291, 292 (1999).

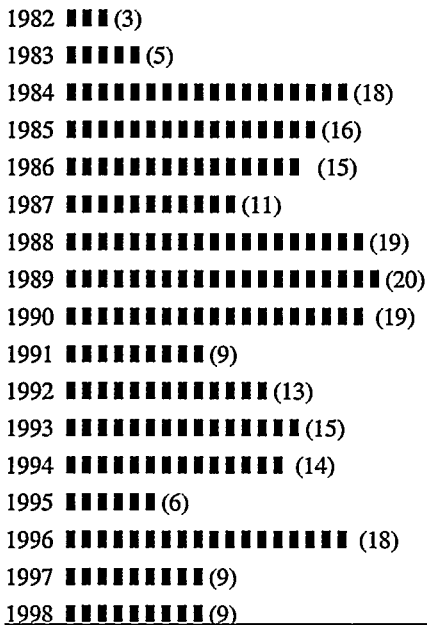
¹⁴⁸ See *supra* note 65 and accompanying text.

I searched the phrase "market for corporate control" in the Law Review library of LEXIS, and obtained 787 hits. This demonstrates several points. First, the phrase has entered our legal vocabulary in a most pervasive way. Second, legal writers aren't very good about acknowledging sources. If Manne's article had been cited each time the phrase was used, it would have moved into fourth place on Shapiro's all time hit parade.

I then asked whether *Mergers and the Market for Corporate Control* had legs: was it just a flash in the pan that soared into visibility for a short time when hostile takeovers were dominating the popular business press? My research suggests that it has remained an important resource for any legal writer investigating mergers and acquisitions. I looked at the timing of citation of *Mergers and the Market for Corporate Control* on LEXIS, and found a remarkably steady stream of citations. I found no citations before 1982, which is pretty much the beginning of the LEXIS law review data base. This study may understate the frequency of citations in the early years, because law reviews were still coming into the data base, but it represents the best one can do with this resource. Figure A presents those results:

Figure A

Frequency of Citation of *Mergers and The Market for Corporate Control*, by Year



Number of citations

I then tried a qualitative approach. *Mergers and the Market for Corporate Control* was described as “seminal” in 29 law review articles, while others described it as “pioneering” or the “first.” *Some Theoretical Aspects of Share Voting* was described in those terms only once that I could locate, and *Our Two Corporation Systems* was described as “seminal” twice. One article, citing all of the articles I’ve discussed, stated that “[t]he prime mover in focusing the attention of legal scholars on the economic constraints on corporate management was, of course, Professor Manne.”¹⁴⁹ In their casebook, Gilson and Black refer to the article as “groundbreaking,” and describe Manne as having “‘invented’ the market for corporate control.”¹⁵⁰ My own casebook simply reprints most of the article.¹⁵¹ That is the best evidence of my personal view of its importance.

The last question I asked about the law review literature was why *Mergers and the Market for Corporate Control* was so much more cited than four other seminal articles which were an integral part of the same project, and which make equally important contributions to our understanding of the economic forces that shape the firm. I looked at the possibility that the article was introduced to law professors by other authors who published in traditional law journals. It seems obvious that there must have been some authors who learned about the article not from systematic reviews of the economics journal literature but from citation in law reviews. I explored the possibility that Manne’s article would frequently be cited in the same footnote with an article that cited it. Easterbrook and Fischel’s article on management’s role in takeovers was the most likely suspect, since it was 24th on the all-time list of most frequently cited articles, and appeared relatively early in the flood of articles on the subject in the 1980s. This combination, however, was cited only five times. Indeed, there were only 25 incidents of citation of Manne’s article with another in a single footnote.¹⁵² I concluded that this approach would not help tell the story of why this article received so much more attention than the four other worthy candidates.

One possible explanation for the dominance of one article over the others is timeliness. *Mergers and the Market for Corporate Con-*

¹⁴⁹ Dennis S. Karjala, *Federalism, Full Disclosure, and the National Markets in the Interpretation of Federal Securities Law*, 80 NW. U. L. REV. 1473, 1492 n.83 (1986).

¹⁵⁰ RONALD J. GILSON & BERNARD S. BLACK, *THE LAW AND FINANCE OF CORPORATE ACQUISITIONS* 370, 1400 (2d ed. 1995).

¹⁵¹ WILLIAM J. CARNEY, *CASES AND MATERIALS ON MERGERS AND ACQUISITIONS* 34 (2000).

¹⁵² There were three joint citations in footnotes with three other articles: Eugene F. Fama, *Agency Problems and the Theory of the Firm*, 88 J. POL. ECON. 288 (1980); Daniel R. Fischel, *Efficient Capital Market Theory, The Market for Corporate Control and the Regulation of Cash Tender Offers*, 57 TEX. L. REV. 1 (1978); and Michael C. Jensen & William H. Meckling, *Theory of the Firm: Managerial Behavior, Agency Costs and Ownership Structure*, 3 J. FIN. ECON. 305 (1976).

trol was written at the beginning of the era of hostile takeovers. Because they were spectacular financial events, they quickly attracted the attention of political entrepreneurs in Congress, which enacted the Williams Act within three years after the appearance of this article. Manne's article had joined issue with those who argued, as did Senator Harrison Williams, that corporate raiders were "white-collar pirates" and looters who engaged in "industrial sabotage."¹⁵³ Manne's article contained a testable hypothesis, and economists proceeded to provide evidence that rejected the looting hypothesis and did not falsify his displacement of the inefficient management hypothesis. A massive body of evidence now shows dramatic wealth gains for target company shareholders.

In contrast, the other articles provided the building blocks for a positive theory of the firm. They did not focus on anything as dramatic as the hostile takeover. Testable hypotheses may not have been as obvious. In some cases, perhaps they were too obvious and everyone already knew the results. For example, there was no debate that shareholders did not regularly undertake proxy fights to throw out underperforming management. In that sense *Some Theoretical Aspects of Share Voting* simply provided an analytical and academic explanation for a widely observed phenomenon. Work on institutional responses to the problem of agency costs has proceeded slowly, and in some cases, uncertainly. Why compensation of top management is not more directly related to performance remains a mystery.¹⁵⁴ There has been relatively little inquiry into the existence and operation of the market for managers.¹⁵⁵ On the other hand, work on the role of competition in corporate law has proceeded steadily, with little acknowledgment of Manne's initial contributions to this area. I am personally guilty in this area.

For the moment, I can conclude only that brilliant insights alone are not enough to rise to the top of the all-time law review hit parade; being in the right place at the right time when others suddenly become intensely interested in a subject must matter. And it appears that others rarely become intensely interested in theory unless it is related to today's headlines. *Mergers and the Market for Corporate Control* combined both brilliant insights and material that became the subject of headlines in the business sections of newspapers throughout the country.

¹⁵³ 111 CONG. REC. 28, 257-58 (1965) (statement of Sen. Williams on S. 2731, the predecessor bill to the Williams Act).

¹⁵⁴ See George P. Baker et al., *Compensation and Incentives: Practice vs. Theory*, 43 J. FIN. 593 (1988).

¹⁵⁵ But see Eugene Fama, *Agency Problems and the Theory of the Firm*, 88 J. POL. ECON. 288 (1980).

B. Manne and the Courts

It should surprise no one that academic articles are not cited frequently in judicial opinions. It should surprise no one that articles using economic analysis, rather than traditional legal doctrine, would be cited even less by the courts. A LEXIS search of all state and federal court opinions produced one citation for each of the articles studied here. The phrase "market for corporate control" appeared 38 times.

Fred McChesney has previously made the point that we have no theory about how intellectuals influence the "real world" of practical affairs.¹⁵⁶ This section, if anything, provides evidence in support of that statement, and is consistent with his earlier findings that academics have little interest in changing law and regulation. McChesney found that legal academics largely ignored the regulatory and social changes of the 1930s. In the period after Manne wrote *Mergers and the Market for Corporate Control*, it could hardly be said that academics ignored the rapid changes in this market and in corporate governance—McChesney being one of those who wrote about these changes.¹⁵⁷ The relatively frequent references to the market for corporate control are some evidence of academic influence on the courts, albeit without the citations that we, the producers of academic literature, would prefer. Much of our influence on the courts must come through the classroom, where Henry's analysis is now widely known and accepted, and perhaps through judicial clerks—at least for a generation.

C. Manne and the Economists

Manne's works other than *Mergers and the Market for Corporate Control* fared relatively better with economists. In one sense all of these articles were notably ignored. A 1981 article by Oliver Williamson is notable for its failure to cite any of Manne's works.¹⁵⁸ Williamson repeated his error in 1988, in a discussion of takeovers in transaction cost economics.¹⁵⁹ While it is understandable that an economist might neglect the law review literature, it's surprising that he ignored *Mergers and the Market for Corporate Control*, which was published in an economics journal. The omission is even more surprising when one examines the tangential contributions of some articles cited by Williamson to the theory of the firm. In fairness,

¹⁵⁶ Fred S. McChesney, *Intellectual Attitudes and Regulatory Change: An Empirical Investigation of Legal Scholarship in the Depression*, 38 J. LEGAL EDUC. 211, 216 (1988).

¹⁵⁷ David D. Haddock et al., *Property Rights in Assets and Resistance to Tender Offers*, 73 VA. L. REV. 701 (1987); Jonathan R. Macey & Fred S. McChesney, *A Theoretical Analysis of Corporate Greenmail*, 95 YALE L.J. 13 (1985).

¹⁵⁸ Williamson, *The Modern Corporation*, *supra* note 14.

¹⁵⁹ Williamson, *supra* note 12, at 83-87.

Williamson seems to take a narrow view of what constitutes transaction cost literature that excludes much literature about firms.¹⁶⁰ And his narrowness may be representative of the profession. Winter and Demsetz claim that transaction cost economics is about pre- and post-contractual behavior in market exchanges, rather than about the costs that occur within firms.¹⁶¹ Much research about the nature of the firm has focused on contractual arrangements to reduce agency costs, while Manne's work focuses on forces that are one step removed from internal firm arrangements.

Finally, I commissioned a study of two social science databases that collectively cover the period 1969-1999, although their coverage of journals may not be identical.¹⁶² Because they cover some law journals, they duplicate to some extent the previous LEXIS search. Table 2 below sets out the results of this search.

Table 2
Frequency of Citation in Social Sciences Indexes

	Law	Econ.
	<u>Journals</u>	<u>Journals</u>
Phrase, "Market for Corporate Control" ¹⁶³	7	23
<i>The 'Higher Criticism' of the Modern Corporation</i>	35	6
<i>Some Theoretical Aspects of Share Voting</i>	65	13
<i>Mergers and the Market for Corporate Control</i>	161	108
<i>Our Two Corporation Systems: Law and Economics</i>	101	9
<i>Cash Tender Offers for Shares – A Reply to Chairman Cohen</i>	41	1

One surprising result is the frequency of citation by economists of articles other than *Mergers and the Market for Corporate Control*. All of the other articles were published in law journals, where they were less accessible to economists. The other surprise is that this survey showed a higher number of citations in law journals for all articles other than *Mergers and the Market for Corporate Control* than my LEXIS search, suggesting an earlier recognition of the importance of these articles by law professors than the LEXIS database was able to capture.

¹⁶⁰ Demsetz, *supra* note 21, at 151 (noting that the problems of agency costs—moral hazard analysis, shirking, and opportunism—are arguably outside the definition of transaction cost economics.)

¹⁶¹ See *id.* at 144-45; Winter, *supra* note 6, at 172-73.

¹⁶² The SOCIAL SCIENCES CITATION INDEX was employed for the period 1969-1986, and the WEB OF SCIENCE database was employed for the period 1987-1999.

¹⁶³ This was not checked for the period 1969-1986 in the SOCIAL SCIENCES CITATION INDEX.

Because it was impracticable to search for the phrase "market for corporate control" in the SOCIAL SCIENCES CITATION INDEX, I conducted a more limited search of economics journals in the JSTOR database.¹⁶⁴ Manne's name appears more than 200 times in these articles, the maximum number displayed by the search engine. The phrase "market for corporate control" also appears more than 200 times. Oddly, most of these appearances are not connected: the combination of "Manne" and "market for corporate control" appears only 35 times. Again, this demonstrates how the phrase has entered our language, generally without credit to its creator.

IV. CONCLUSION

While Berle and Means set the intellectual tone for the higher criticism of the corporation for thirty years, their work was derivative from the earlier work of Ripley, a fact they acknowledged.¹⁶⁵ Henry Manne's contribution to the theory of the firm and to a broader understanding of corporate law is both totally original and unmatched. He introduced both economists and lawyers to the role markets play in shaping firms. He first articulated the important features of the behavior of shareholders and the role markets play in protecting them. He explained the major features of the market for corporate control. Finally, he described the role of corporate law, and the forces that shape it. In all of this he was a pioneer. These achievements alone should give him a prominent place in the intellectual history of law, economics, and law and economics. As the other contributors to this Symposium demonstrate, that was only one of his many facets as a scholar and educator.

¹⁶⁴ This database, sponsored by the Mellon Foundation, contains the following journals: *American Economic Review*; *Econometrica*; *Economic Journal*; *Journal of Applied Econometrics*; *Journal of Economic History*; *Journal of Economics*; *Journal of Economic Perspectives*; *Journal of Finance*; *Journal of Financial and Quantitative Analysis*; *Journal of Industrial Economics*; *Journal of Industrial Economics*; *Journal of Money, Credit and Banking*; *Journal of Political Economy*; *Quarterly Journal of Economics*; *Review of Economic Studies*; *Review of Economics and Statistics*; and *Review of Financial Studies*. Most of these databases do not contain journals later than 1993.

¹⁶⁵ See BERLE & MEANS, *supra* note 2, at ix (acknowledging Ripley's contribution). See generally WILLIAM Z. RIPLEY, *MAIN STREET AND WALL STREET* (1927). For a summary of Ripley's book, see McChesney, *supra* note 156, at 235-36.