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# Corporate Aid of Governmental Authority: History and Analysis of an Obscure Power in Delaware Corporate Law

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ARTICLE

**CORPORATE AID OF GOVERNMENTAL  
AUTHORITY: HISTORY AND ANALYSIS OF  
AN OBSCURE POWER IN DELAWARE  
CORPORATE LAW**

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ABSTRACT

*The Delaware General Corporation Law contains an obscure provision stating that all corporations have the power to “[t]ransact any lawful business which the corporation’s board of directors shall find to be in aid of governmental authority.” DEL. CODE tit. 8, § 122(12). This oddly worded section has never been applied, analyzed, or interpreted by any court. It has received almost no treatment by corporate law scholars. In this Article, I examine the history behind this strange power and analyze its applicability to pressing social policy questions surrounding corporate law.*

*My analysis leads both to narrow and broad policy conclusions. The narrow conclusion is that title 8, section 122 of the Delaware Code is a textual mess that should be amended for coherence and clarity. The analysis herein contributes to the case for reforming corporate law to require directors to actively attend to the interests of multiple stakeholders, not just shareholders.*

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## I. INTRODUCTION

The Delaware General Corporation Law contains a provision stating that “[e]very corporation . . . shall have power to . . . [t]ransact any lawful business which the corporation’s board of directors shall find to be in aid of governmental authority.”<sup>1</sup> This oddly-worded section has been hiding in plain sight from lawyers, jurists, and scholars for more than forty years. No reported cases reference or analyze it. Scholars, who can usually be counted on to make whole museums of academic exhibits from a curious sliver of statutory language, have ignored it almost entirely.<sup>2</sup> This lack of attention is surprising, given that by its own terms the provision seems to implicate fundamental corporate law concerns such as the purpose of corporations, the scope of directors’ fiduciary obligations and discretion, and the relationship between corporate law and corporate social responsibility. In this Article, I examine the history of this strange provision and analyze its relevance to pressing policy questions surrounding corporate law.

My analysis leads both to narrow and broad policy conclusions. The narrow conclusion is that section 122 of the Delaware corporate code is, in general, a textual mess that should be amended for coherence and clarity. The Delaware legislature should, in particular, clarify what it intends to authorize through section 122(12)’s grant of corporate power to aid governmental authority. The broad conclusion is that the account herein contributes to the case for reforming corporate governance law to require directors to actively attend to the interests of multiple stakeholders, not just shareholders.

The Article is structured as follows. Section II develops a historical account of the emergence and amendment of section 122(12) in Delaware’s corporate code. Section III undertakes a doctrinal analysis of section 122(12) in light of both this history and the Delaware Supreme Court’s general corporate law jurisprudence. I examine the key question: does the “aid of governmental authority” provision authorize directors to make cor-

1. DEL. CODE tit. 8, § 122(12) (2000).

2. One interesting recent exception is Robert J. Rhee, *Fiduciary Exemption for Public Necessity: Shareholder Profit, Public Good, and the Hobson’s Choice During a National Crisis*, 17 GEO. MASON L. REV. 661 (2010). I discuss Rhee’s treatment of § 122(12) *infra* Section IV.

porate decisions intended to serve non-shareholder interests? I also analyze whether section 122(12) is mandatory or mutable, and whether there are substantive limits on the section's grant of power to aid governmental authority. Section IV provides a normative analysis of section 122(12), and critiques another scholar's recent policy prescription relating to it. Section V gives a brief conclusion.

## II. HISTORY OF THE STATUTORY PROVISION

In this Section, I present as detailed an account of the development of section 122(12) of the Delaware corporate code as can be gleaned from the scant historical record on the matter.<sup>3</sup> My purpose here is to showcase the drafting process behind section 122(12), as a way of setting the stage for the doctrinal and normative assessments that will follow in Sections III and IV.

### A. *Promulgation of the Original Section 122(12) in 1967*

An effort to interpret powers *granted* in the Delaware corporate code—or any modern corporate code—must begin by appreciating that such provisions were written against a historical backdrop of law that strictly *limited* corporate powers.<sup>4</sup> Until the nineteenth century, people could not carry on business through the corporate form unless a corporate charter was granted to them by specific legislative action.<sup>5</sup> These one-off

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3. Similar versions of the power described in Delaware's section 122(12) can be found today in the corporate statutes of many states. *See, e.g.*, N.Y. BUS. CORP. LAW § 201(c)(McKinney 2010) ("In time of war or other national emergency, a corporation may do any lawful business in aid thereof, notwithstanding the purpose or purposes set forth in its certificate of incorporation, at the request or direction of any competent governmental authority"); *but see* the California Corporations Code (no cognate provision to Delaware's § 122(12)). I have found no cases or other relevant material from those other states that shed light on the historical and interpretive questions that are undertaken in this Article.

Delaware is the focus here because most large corporations buy their charters from Delaware. *See* John Armour et al., *Delaware's Balancing Act*, 87 IND. L.J. 1345, 1348, 1382 (2012) (sixty percent of all publicly traded corporations and sixty-three percent of Fortune 500 companies are Delaware corporations). There is still academic dispute as to why Delaware dominates. The whiggish view is that Delaware law is highly advantageous to shareholders and thus managers, competing with other firms for scarce investment dollars, must incorporate there. The critical view insists that Delaware dominates because it offers lax oversight of managers, and thus managers charter there so they can exploit shareholders with impunity. Most mainstream scholars today subscribe to the view that Delaware prevails because it enhances shareholder value. From the perspective of this Article, the more interesting question is not what impact Delaware dominance has on shareholders, but what impact it has on non-shareholding constituencies of the corporation, including workers, consumers, communities, and the polity generally. *See* KENT GREENFIELD, *THE FAILURE OF CORPORATE LAW* 107–22 (2006) (exploring "Democracy and the Dominance of Delaware").

4. *See generally*, S. Samuel Arsht, *A History of Delaware Corporation Law*, 1 DEL. J. CORP. L. 1 (1976); JOHN MICKLETHWAIT & ADRIAN WOOLDRIDGE, *THE COMPANY: A SHORT HISTORY OF REVOLUTIONARY IDEA* (2003); *see also* ERNEST L. FOLK, III, *THE DELAWARE GENERAL CORPORATION LAW: A COMMENTARY AND ANALYSIS* (1972).

5. *See* Arsht, *supra* note 4, at 2–8. There are many advantages to operating business through a corporate entity. These include limited liability to the corporation's investors for the debts of the corporation, protection of the assets of the corporation against claims by creditors of the firm's

charters would narrowly specify the kinds of activities in which a corporation could engage, for example, building a canal or running a railroad. By the late-nineteenth century, increased demand for access to the corporate form had rendered grants by specific legislative action a cumbersome, corrupt way of running business.<sup>6</sup> States (Delaware in 1899) began to streamline the process of granting corporate charters by routine administrative action, for a fee, essentially to all comers. These newer corporate statutes, however, still required corporations to specify in their articles of incorporation the purpose or purposes for which they were organized (e.g., to run a hair salon, to publish books, etc.), and the state could enjoin or break up a firm if it waded into areas unauthorized in its charter.<sup>7</sup>

In the first several decades of the twentieth century, Delaware emerged as the leading purveyor of corporate charters in the United States. But by the early 1960s, other states were modernizing and liberalizing their statutes in ways that potentially threatened Delaware's dominance.<sup>8</sup> Reluctant to lose its chartering business, the Delaware legislature in 1963 appointed a special Revision Committee to overhaul and update its corporation statute.<sup>9</sup> Among many changes, the 1967 revision gave corporations the option to simply state in their founding documents that "the purpose of the corporation is to engage in any lawful act or activity," instead of having to specify more particularly the purposes it was to formed to undertake.<sup>10</sup> The 1967 revision to Delaware's statute also granted new "specific powers" to *all* corporations. Among these new powers was section 122(12), the subject of our present inquiry.

The original version of section 122(12) was composed of very different, much more limited language than that which is found in the section today. To comprehend the contemporary version of section 122(12), it is crucial to understand how the original 1967 language first made it into the statute. The 1967 version stated:

Every corporation . . . shall have power . . . [*i*]n time of war or other national emergency, to do any lawful business in aid thereof, notwithstanding the business or purposes set forth in its certificate of incorporation, *at the request or direction of any apparently authorized governmental authority*.<sup>11</sup>

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investors (also known as "affirmative asset partitioning"), and perpetual life of the corporate entity. *See generally* Henry Hansmann & Reinier Kraakman, *The Essential Role of Organizational Law*, 110 *YALE L.J.* 387 (2000) (explaining advantages of the corporate form).

6. *See* Arsht, *supra* note 4, at 2–8.

7. *See id.*

8. *See* FOLK, *supra* note 4, at xii–xiii. Reforms in those other states were largely modeled on the Model Business Corporations Act, which had first been published by the American Bar Association in 1950. *See* Ernest L. Folk, III, *Some Reflections of a Corporation Law Draftsman*, 42 *CONN. B.J.* 409, 409–10 (1968).

9. *See* Arsht, *supra* note 4, at 15–17; *see also* FOLK, *supra* note 4, at xii–xiii.

10. *DEL. CODE* tit. 8, § 102(a)(3) (1967).

11. *DEL. CODE* tit. 8, § 122(12) (1967) (emphasis added).

The Revision Committee that developed this language for the Delaware legislature took its cues from Professor Ernest Folk, III, a corporate law scholar from the University of North Carolina School of Law,<sup>12</sup> whom the Committee hired to serve as its Reporter.<sup>13</sup> Folk undertook a comprehensive study of Delaware's existing corporation statute and produced a report specifying his proposed changes. The Revision Committee took the "Folk Report," as it came to be known, as the point of departure for its own work. In his Report, Folk wrote:

A number of other corporate powers, not now specifically recognized by Delaware statutes, should be enumerated in Section 122. Although some of these may have been recognized in judicial rulings, and many of them are inserted in charters, it is desirable to eliminate any doubt as to a Delaware corporation's plenitude of power, especially since the Model Act and all recent corporation law revisions explicitly [sic] provide these powers.<sup>14</sup>

The first new explicit power contemplated by the Folk Report was the one that would become section 122(12) in the 1967 revision. Under the heading "(a) Wartime or Emergency Business," Folk wrote:

Many statutes, *e.g.*, Model Act §4(n); N.Y. Bus.Corp.Law § 201(b), specifically authorize a corporation, irrespective of the purposes stated in the certificate of incorporation, to do any lawful business in time of war or other national emergency. Its effect is to eliminate the necessity for a formal amendment of the certificate, by shareholder action; and in war or emergency times, especially in a nuclear age, this may be important. Accordingly, Delaware should, of all states, make this power clear and unmistakable, and protect its corporations in the exercise thereof. . . . Accordingly, language such as the following would seem indispensable:

In time of war or other national emergency, a corporation may do any lawful business in aid thereof, notwithstanding the purpose or purposes set forth in its certificate of incorporation, at the request or direction of any competent governmental authority.

This provision is taken from N.Y. Bus. Corp. Law § 201(b), and is superior to the more amorphous language of Model Act Section 4(n) and states following that Act.<sup>15</sup>

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12. Folk later enjoyed a long career on the faculty of the University of Virginia Law School.

13. Arsht, *supra* note 4, at 15–17. Folk is deceased (he passed away in 1989), as are most of the lawyers involved in the promulgation and amendment of § 122(12).

14. ERNEST L. FOLK, III, REVIEW OF THE DELAWARE CORPORATION LAW 40 (1967) [hereinafter, FOLK REPORT], available at <http://law.widener.edu/LawLibrary/Research/OnlineResources/DelawareResources/DelawareCorporationLawRevisionCommittee.aspx> (last visited Jan. 1, 2014).

15. *Id.* (emphasis in original).

There were not then, and are not now, any cases citing or analyzing the New York version of the “wartime or emergency” power that Folk references. Of greater relevance is the extent to which Folk was influenced here, and throughout his work on the Delaware revision, by the Model Act.<sup>16</sup>

The Model Business Corporations Act (“Model Act,” or “MBCA”) started out in 1940 as a project by a group of lawyers from the American Bar Association (“ABA”) who undertook to draft a Federal Corporation Act that could be used if the federal government moved to offer or require federal chartering.<sup>17</sup> That reform did not materialize (yet), but the ABA’s project continued in the direction of a Model Act that was made available to states looking to modernize their own corporate law statutes. The committee that drafted the original Model Act, which was first published in 1950, had fourteen members: three from Illinois, three from New York, two from Ohio, but *none* from Delaware.<sup>18</sup>

The 1950 Model Act, conceived with memories of the Second World War still vivid and the reality of the Cold War becoming clear, stipulated that: “[e]ach corporation shall have power: . . . (n) in time of war to transact any lawful business in aid of the United States in the prosecution of the war.”<sup>19</sup> The first published version of the Model Act contained no comment at all on this power. But the official annotation to the Model Act, published by the ABA in 1960, contained this important Comment: “The section explicitly recognizes that in time of war a corporation *may validly assume responsibilities* that it would not normally undertake in peacetime.”<sup>20</sup> This annotation listed fourteen states as having statutory versions of this provi-

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16. Members of the Delaware Revision Committee on occasion expressed a prideful resistance to the Model Act. For example, the minutes of one meeting note that committee member Mr. David H. Jackman, “emphasized that Delaware should not adopt the Model Act because we do not want to be a ‘me too’ State in view of the fact that in the past most of the other States had copied our laws and that we should be a leader not a follower.” Minutes of Fourth Meeting of Delaware Corporation Law Study Committee, July 14, 1964 at 2–3 available at <http://law.widener.edu/LawLibrary/Research/OnlineResources/DelawareResources/DelawareCorporationLawRevisionCommittee.aspx>, (last visited Jan. 1, 2014) [hereinafter *Minutes of Fourth Meeting*]. Perhaps in part to patronize this anxiety, the Folk Report worked within the idiosyncratic, at times byzantine structure and numbering system of the existing Delaware code, instead of introducing the more streamlined Model Act approach. In the end, the Revision Committee accepted most of the substantive changes that Folk borrowed from the Model Act.

17. Ray Garrett, *History, Purpose and Summary of the Model Business Corporation Act*, 6 BUS. LAW. 1, 1 (1950) (“The preparation of the Model Business Corporation Act began some ten years ago when the Committee [on Business Corporations of the Section of Corporation, Banking and Mercantile Law of the American Bar Association] was requested to prepare an appropriate form of Federal Corporation Act for use in case there should ever be a serious demand for such a statute.”). Garrett’s passive formulation leaves unanswered the tantalizing question: was requested *by whom?*

18. MODEL BUS. CORP. ACT xi (Revised 1950) (listing committee members).

19. MODEL BUS. CORP. ACT ANN. § 4(n) (West 1960).

20. *Id.* at ¶ 4 (emphasis added).

sion (notably absent were Delaware and New York) but indicated that there were no cases “of general interest” interpreting the power.<sup>21</sup>

Folk acknowledged that he was influenced by the Model Act when he suggested a “wartime or emergency” power in his report to Delaware’s Revision Committee. What is less clear is whether he shared the Model Act’s view that this power authorized an expansion of ordinary corporate “responsibilities.” Neither the Folk Report, nor the Revision Committee’s minutes, nor other extant discourse from the Delaware 1967 revision process, explicitly adopts or repudiates the view taken in the Comment to the Model Act.<sup>22</sup>

After Folk submitted his Report, each member of the Revision Committee was assigned a section of it to review and report on to the full group.<sup>23</sup> The section on “Powers” was assigned to Mr. Samuel Arsht, who was a partner at the (then and now) powerful Delaware corporate law firm of Morris, Nichols, Arsht, and Tunnell.<sup>24</sup> In a memorandum addressed to Revision Committee members on April 19, 1965, Arsht wrote:

The seven additional specific powers suggested by Folk . . . are as follows: (a) Wartime or Emergency Business (b) Contracts, Guaranties, Borrowing, etc. (c) Investing Funds (d) Power to be Incorporator or Promoter (e) Power to be Partner (f) Compensation (g) Power to Insure Directors, Officers, Employees and Stockholders. While no one would seriously doubt the existing power of a Delaware corporation to do the things authorized by these seven provisions, they appear in the Model Act and in other corporation statutes, and their inclusion in the Delaware statute may give it an appearance of modernity, liberality, or permissiveness that may add to its appeal. I see no objection to the suggested powers, but I cannot say they are necessary additions.<sup>25</sup>

Curiously, further minutes of the Committee indicate that (at least) initially the Committee rejected Folk’s (and Arsht’s) suggestion to adopt the wartime and emergency powers that would eventually become section 122(12). Minutes from the May 18, 1965 meeting of the Committee state,

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21. *Id.* at ¶ 3. The annotation also conveys that “Ohio requires that such activities be ‘at the request or direction of the United States Government or any agency thereof,’” a requirement not found in the Model Act, but which would be reflected in Delaware’s original section 122(12). *See id.* at ¶ 2.

22. *See supra* text accompanying note 20 (quoting MODEL BUS. CORP. ACT ANN. § 4(n), ¶ 4).

23. *Minutes of Fourth Meeting, supra* note 16, at 4.

24. *Id.*

25. Memorandum from S. Samuel Arsht to the members of the Corporate Law Revision Committee 3–4 (Apr. 19, 1965) (on file with the University of Virginia School of Law Library, Special Collections, MSS 90-2, Box 4, n. 8).



“WARTIME OR EMERGENCY BUSINESS as set forth on pages 40 and 41 of the Folk Report, paragraphs (a), (b) and (c) were *disapproved*.”<sup>26</sup>

After the Revision Committee as a whole had made its substantive decisions (largely in the form of accepting or rejecting recommendations from the Folk Report), it fell to a sub-committee consisting of Arsht and two other lawyers on the Committee (and associates from the Committee members’ law firms) to actually draft the statute.<sup>27</sup> Arsht later acknowledged that the legislation-drafting sub-committee did not always follow the substantive decisions that the Revision Committee had made.<sup>28</sup> From his memo, and, as will be seen, his subsequent involvement with the ABA’s Model Act,<sup>29</sup> we know that Arsht supported section 122(12). So it is not inconceivable that under his guidance the drafting sub-committee put the “wartime and emergency” power back in after the Revision Committee had initially rejected it. In any event, the Revision Committee approved the draft legislation, without amendment, and without any further comment on the power that was put into section 122(12).<sup>30</sup> The statute, as Folk had suggested, facially expanded the power as described in the Model Act by authorizing aid to government not only in time of “war” but also during “other national emergency.” Delaware’s formulation, however, was also more limited than the Model Act since it required that the aid be in response to a request by government (or, in the Revision Committee’s oddly placed paean to agency law, any “apparently authorized” governmental authority).<sup>31</sup>

Having completed its work, the Revision Committee forwarded its draft statute to the Delaware legislature. No public hearings were held on the legislation.<sup>32</sup> The Delaware legislature adopted the entire new statute in July 1967, without amendment, without debate, and without leaving any legislative history.<sup>33</sup>

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26. *Minutes of Seventeenth Meeting of Delaware Corporation Law Study Committee*, May 18, 1965, at 2, available at <http://law.widener.edu/LawLibrary/Research/OnlineResources/DelawareResources/DelawareCorporationLawRevisionCommittee.aspx> (last visited Jan. 1, 2014) (emphasis added).

27. Arsht, *supra* note 4, at 15–16.

28. *Id.* at 16 (“[A] satisfactory bill could not be drafted without making numerous substantive decisions that the full Committee had not made and reversing some that it had made.”).

29. *See infra* text accompanying notes 43–46.

30. In fact, it seems just as likely that the word “disapproved” was a typographic error in the minutes for the May 18, 1965 meeting, and that paragraphs (a) (and (b) and (c) were in fact “approved” at that meeting, given that the substance of all three paragraphs were ultimately included in the statute.

31. *See* DEL. CODE tit. 8, § 122(12) (1967).

32. *See* Comment, *Law for Sale: A Study of the Delaware Corporation Law of 1967*, 117 U. PA. L. REV. 861, 869–70 (1969).

33. *Id.*

In 1967, Arsht published a long review of the newly reformed Delaware statute which he co-authored with his law-firm partner, Walter Stapleton.<sup>34</sup> In their review, Arsht and Stapleton wrote:

Some powers, not previously specified, have been added to the list of specific powers, *the most notable of which* are the powers to enter into contracts of guaranty or suretyship, to be a partner or joint venturer, to establish pension, profit sharing, stock option and other compensation plans, and to insure the lives of directors, officers, employees and stockholders [§ 122 (11), (13), (15), (16)]. The exercise of each of these powers *for the benefit of the corporation and in pursuit of its authorized objectives* was generally accepted as proper under prior law, however, and these additions have been made solely for the purpose of clarification.<sup>35</sup>

Notably, Arsht and Stapleton did not consider section 122(12) to be among the “most notable” powers specifically listed in the new statute: they omitted any reference to it. They do make clear that the newly specified powers in section 122 were acceptably exercised for the “benefit of the corporation and in pursuit of its authorized objectives.”<sup>36</sup> The absence of section 122(12) in their discussion leaves open the question: did they understand the use of section 122(12) *also* to be acceptable only when exercised for the benefit of the corporation and its authorized objectives, or does the omission of section 122(12) from this discussion suggest that section 122(12) may be acceptably exercised for some other benefit, or some other objective? Of course, the paragraph is only an unofficial synopsis of the new law, drafted by one member of the Revision Committee and his colleague.

Also in 1967, Professor Folk authored a pamphlet titled, *The New Delaware Corporation Law*, that was a kind of long-form advertisement sponsored by the Corporations Service Company, a Delaware firm that processed incorporation documents.<sup>37</sup> In this pamphlet, Folk addressed the new section 122(12):

A significant new provision authorizes a corporation to do any lawful business, notwithstanding limitations in its certificate of incorporation as to its business purposes, if in time of war or other national emergency, it is requested or directed to do so by any “apparently authorized” governmental authority. Thus, war work

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34. Stapleton would go on to a distinguished judicial career; he is today a Senior Federal Appeals Court Judge for the Third Circuit Court of Appeals.

35. S. SAMUEL ARSHT & WALTER K. STAPLETON, *Analysis of the 1967 Delaware Corporation Law*, 2 Corp. Guide (P-H) 321, 325 (1967) (emphases added) (brackets in original).

36. *Id.*

37. ERNEST L. FOLK, III, *THE NEW DELAWARE CORPORATION LAW* (1967). *See also* ERNEST L. FOLK, III, *THE RED BOOK DIGEST OF THE NEW DELAWARE CORPORATION LAW* (1968) [hereinafter *THE RED BOOK DIGEST*].

may be done without the need to obtain a prior charter amendment.<sup>38</sup>

So Folk did consider section 122(12) to be “significant,” but his summary in the pamphlet emphasizes only the expansion of a permissible area of business—“war work”—without any reference to expanded corporate responsibility associated with the provision. This is perhaps an unsurprising gloss on the power, given the intended audience of the pamphlet. It cannot be considered decisive.

#### B. *The Amendment of Section 122(12) in 1969*

In 1969, section 122(12) of the Delaware General Corporation Law was significantly altered to read:

Every corporation . . . shall have power to . . . [t]ransact any lawful business which the corporation’s board of directors shall find to be in aid of governmental authority.<sup>39</sup>

Two important changes to the 1967 provision were wrought by this amendment. The original section 122(12) power was only operable during time of “war or other national emergency,” whereas under the revised version it is *always* available.<sup>40</sup> That is a *huge* difference. The other change is just as striking. The original version’s sweeping authority was only actualized after a government agent “request[ed]” or “direct[ed] it.”<sup>41</sup> Thus, in the original version, the discretion to use the power described in the section had to come in the first instance from *outside* of the corporation, specifically, from government. After the change, the authority was fully vested in every corporation’s board of directors.

There is no formal legislative history for this amendment to the Delaware corporate code. The Revision Committee had completed its work and disbanded in 1967. It seems that the 1969 amendment came out of Delaware’s regular legislative process. Ordinary amendments to the state’s corporate law, then and now, pass through the Delaware Bar Association’s Section of Corporation Law, but there are no extant records from the Section bearing on the amendment to section 122(12) in 1969.<sup>42</sup>

Nevertheless, a connection can be drawn between changes to the Model Act in the mid-1960s and Delaware’s 1969 amendment to section 122(12). In 1966, the ABA’s Committee on Corporate Laws set itself the

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38. FOLK III, THE NEW DELAWARE CORPORATION LAW, *supra* note 37, at 8. *See also* FOLK III, THE RED BOOK DIGEST, *supra* note 37, at 10.

39. DEL. CODE tit. 8, § 122(12) (1969).

40. *Id.*

41. DEL. CODE tit. 8, § 122(12) (1967).

42. *See* Delaware Bar Association Website, <http://www.dsba.org/sections-committees/sections-of-the-bar/corporation-law/> (describing role of Section on Corporation Law in developing Delaware’s business law).

task of creating a new set of annotations for the Model Act.<sup>43</sup> While working on the new annotations the Committee decided to make substantive changes to the Model Act itself. Those reforms included a dramatic expansion of the original Model Act's "wartime power." Importantly, for our inquiry, it appears that the first time anyone from Delaware served on an ABA Committee charged with tending to the Model Act was in connection with these mid-1960s revisions, which were formally published as a revised version of the Model Act in 1969.<sup>44</sup> The Committee that developed those changes to the Model Act had nineteen members, including our old friend Samuel Arsht of Wilmington, Delaware.<sup>45</sup> Arsht, recall, was an influential corporate lawyer and had played an instrumental role on the Delaware Revision Commission which overhauled Delaware's statute in 1967.<sup>46</sup> While I have found no "smoking gun," the most likely scenario is that Arsht brought the changes his ABA committee was making to the "wartime" powers in the Model Act home to Delaware in 1969.

The 1969 change to the Model Act had dropped the reference to "war" and now generally authorized, "any corporate business which the board of directors shall find to be in aid of governmental authority."<sup>47</sup> The formal annotations to the 1969 revisions<sup>48</sup> provided this explanation for the change:

Most of the powers expressed in section 4 are of great antiquity, being in fact more or less inherent in the nature of a corporation. The "war power" as formerly expressed in section 4(n), on the other hand, is an outgrowth of modern warfare. One of its earliest appearances was in Illinois in 1919.<sup>[49]</sup>

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43. See Willard P. Scott, *Changes in the Model Business Corporation Act*, 24 BUS. LAW 291, 292-93 (1968) (noting that the committee initially was charged with writing a new set of annotations for the Model Act but ended up developing substantive changes to it).

44. MODEL BUS. CORP. ACT IV (1969) (listing committee members).

45. *Id.*

46. See *supra* text accompanying notes 24-36.

47. MODEL BUS. CORP. ACT ANN. 2d. § 4(n) (1969).

48. The annotations were not published until 1971.

49. The annotation's reference to Illinois may be related to the fact that Illinois was so well represented on the committee that drafted the original Model Act and its revisions. Section 5 of the Illinois Business Corporation Act Annotated (1934) stated: "In order to carry out the purposes for which it is organized, each corporation shall have power . . . (m) In time of war to transact any lawful business in aid of the United States in the prosecution of war, to make donations to associations and organizations aiding in war activities, and to lend money to the State or Federal government for war purposes." *Id.* at 15-16 (emphasis added). The Illinois provision thus appears to have permitted director's discretion to exercise the wartime power only to the extent that doing so advanced the purposes for which the firm was organized. This is a more limited authorization than the original Model Act, which contains no such "in order to carry out the purposes for which it is organized" language, and which contained an official Comment specifying that the provision was meant to recognize that in wartime corporations may take on "responsibilities" other than those which they ordinarily have. See *supra* text accompanying note 20. The formal annotations to the 1934 Illinois statute simply state that "[t]his is a reenactment, without material change, of section 6(12) of the 1919 act." *Id.* I have found no cases interpreting, nor other material explaining the genesis of, this provision in the 1919 Illinois code.

About half of the states now have a provision authorizing transaction of business in prosecution of wars. Until 1969 the power granted under this subdivision was in similar terms and was effective “in time of war.” However, changing conditions rendered this grant defective in two respects. The first was the waging of undeclared wars and engagement in varying forms of hostilities, leaving uncertain the legal basis for exercise of the power. The second was the emergence of other equally important areas of government support in the elimination of poverty, disease and civil strife. Hence, the adoption in 1969 of the existing provision, which is intended to enlarge the corporate powers in support of governmental policy.

This power enlarges the specific purposes that may be set out in the articles. As a general power available to all corporations it avoids an amendment of the articles in order to establish clearly the corporation’s power to engage in business in aid of governmental policy, regardless of the purposes set out in the articles.<sup>50</sup>

This comment recognizes (or posits) that the grant of wartime powers in the original 1950 Model Act was itself a departure from “antiquity.” It then proceeds to dramatically expand this innovative power. It beggars credulity to claim that the “elimination” of “poverty, disease and civil strife” had emerged as a government concern only between 1950 and 1967. What *had* emerged in that time, apparently, was a change in the ABA Committee on Corporate Law’s view of the propriety of business corporations aiding government in these longstanding policy areas.<sup>51</sup>

The substantive revision and explanatory comments to the 1969 Model Act revision reflect the social milieu in which they were conceived. Major work on the revision was undertaken in 1968, a time, a year, wild with war abroad and civil strife at home.<sup>52</sup> The Vietnam War was raging, getting worse each day. The great civil rights leader, Dr. Martin Luther King, Jr., was assassinated in Memphis, Tennessee. Senator Robert F. Kennedy was

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50. MODEL BUS. CORP. ACT ANN. 2d § 4(n), ¶ 2.

51. The first sentence of the final paragraph of the annotation excerpt, *supra* text accompanying note 50, makes no sense. The revised section did nothing to enlarge the powers that “may be set out in the articles” of an MBCA corporation. Corporate aid to government activity was not *forbidden* prior to this amendment for firms that had a purpose “set out” in their articles to undertake “any lawful act,” or firms formed specifically for the purpose of working with the government. Instead, as the rest of the comment more accurately specifies, the provision imported a new default provision into *all* corporate charters. The annotation to the 1969 Model Act (published in 1971) also stated that “Delaware has a provision identical to the Model Act,” but that was not accurate, since the Delaware statute used the phrase “governmental authority” rather than “governmental policy.” DEL. CODE tit. 8 § 122(12) (1969). The 1973 Supplement to the Model Act purported to correct this error, stating, “Delaware and Kansas have provisions identical in substance, to the Model Act except that each provision has as its last word ‘authority.’” MODEL BUS. CORP. ACT ANN. 2d § 4(n), ¶ 3.01 (Supp. 1973). As my discussion in this section makes clear, I do not think the substance of the Model Act and the Delaware versions of the provision can necessarily be construed as identical.

52. *See generally* MARK KURLANSKY, 1968: THE YEAR THAT ROCKED THE WORLD (2004).

assassinated in Los Angeles, California, after launching his campaign for the Democratic Party's presidential nomination. The Civil Rights Act of 1968 was passed. Soviet troops invaded Czechoslovakia in violent reply to Prague's invigorated resistance to Russian domination. A committee of lawyers, engaged in a quintessential act of civil society, drafted a model for legislation in a crucial area of public policy, and sought to respond to the charged social atmosphere in which they were working.

Writing in the *Boston University Law Review* in 1970, Professor Philip Blumberg reviewed the 1969 changes to the Model Act, and appraised the change to the "war powers" in particular. Blumberg thought the changes were too limited because he interpreted them as tethering socially oriented corporate activity too strictly to government policy:

Section 4(n) raises a serious question about those social expenditures not "in aid of governmental policy." Instead of a pluralistic society in which differing approaches are made by different groups, the reference to "governmental policy" may have the unfortunate consequence of restricting constructive corporate efforts to programs headed by governmental effort.

. . . .

It is therefore disappointing and troubling to note . . . section 4(n)[']s] omission of reference to purely private efforts in the very attack on "poverty, disease and civil strife" which the Committee wished to assist.<sup>53</sup>

This seems to be a sound reading of the 1969 Model Act language, whatever one might think of its merits. But it was rejected as too literal and narrow by George Gibson, a prominent member of the Committee that worked on the revision.<sup>54</sup> In a presentation Gibson made in St. Louis in the summer of 1970, he responded to Blumberg's article:

I feel sure . . . that the Committee on Corporate Laws had no idea whatever of restricting this concept of corporate participation by any of the technical limitations that Professor Blumberg observes in the language of [the Model Act] . . . Subsection (n) originally read that every corporation should, in addition to its declared purposes, have authority "to conduct any business that might be helpful to government in time of war." [sic]

It now reads to transact any other business that may be "in aid of governmental policy." Now that certainly was not designed to force corporations to wait for government to tap them on the shoulder; still less, to make them abdicate their initiative and responsibility. We thought that when governmental policy had been articulated to include health, education, and welfare, that busi-

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53. Phillip J. Blumberg, *Corporate Responsibility and the Social Crisis*, 50 B.U. L. REV. 157, 197-98 (1970).

54. See 1 MODEL BUS. CORP. ACT ANN. 2d at XI.

ness, in aid of governmental policy, had crossed the great divide and *it was the intention of the committee, I believe, to embrace the widest possible public good.*<sup>55</sup>

The social, cultural, and political foment in which the 1969 “government aid” revisions to the Model Act were made is palpable in the language lawyers present at its creation used to explain what they were doing. It is also clear that these lawyers saw their efforts as essentially conservative in nature. They were trying to find a way to sustain the fundamental design of the corporate form in the midst of a torrent of social change. Concluding his presentation in 1970, Gibson said, “if these great powers [of the corporation, to influence its employees and society generally] are ignored or abused, society will interpose its veto and may change the whole system of corporate organization, which will extend even to the foundations of private property.”<sup>56</sup>

Unfortunately, there is no record of this kind of interpretive back and forth regarding the expansion of Delaware’s section 122(12) power in 1969. Professor Folk made no mention of the dramatic change to it in a long article he published in the *Virginia Law Review* titled, *Corporation Law Developments—1969*.<sup>57</sup> Arsht and Stapleton co-authored a piece titled, *Analysis of the 1969 Amendments to the Delaware Corporation Law* that touched briefly on the change to section 122(12), but without much illumination.<sup>58</sup>

Section 122 of the General Corporation Law sets forth powers which each Delaware corporation shall have in addition to those granted by its certificate of incorporation and elsewhere in the statute. Paragraph (12) thereof, as amended, provides that every Delaware corporation shall have the power to transact any lawful business which the corporation’s board of directors shall find to be in aid of governmental authority. The prior statute contained a provision of like import except that it was limited by the phrase “in time of war or other national emergency.”<sup>59</sup>

Arsht and Stapleton failed to note that the amendment also put the authority to exercise the power directly in the hands of corporate directors, rather than the government.

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55. George Gibson, *New Trends in the Development of Corporate Law*, 26 *BUS. LAW.* 527, 529 (1970) (emphasis added).

56. *Id.* at 531.

57. Ernest L. Folk, III, *Corporation Law Developments—1969*, 56 *V.A. L. REV.* 755 (1970).

58. S. SAMUEL ARSHT & WALTER K. STAPLETON, *Analysis of the 1969 Amendments to the Delaware Corporation Law*, 2 *P-H CORPORATION LAW SERVICES* 347 (Delaware division). This was conceived as a follow-up to their full-length article analyzing the 1967 statutory revision, ARSHT & STAPLETON, *Analysis of the 1967 Delaware Corporation Law*, *supra* note 35.

59. ARSHT & STAPLETON, *Analysis of the 1969 Amendments to the Delaware Corporation Law*, *supra* note 58, at 348.

In 1972, Folk published a comprehensive treatise on the revised Delaware General Corporation Law that he had been so deeply involved in shaping.<sup>60</sup> The book is generally outstanding and remains a vital resource for corporate lawyers and scholars, but its treatment of section 122(12) is unsatisfying. Folk wrote:

Section 122(12), as amended in 1969, broadly authorizes any corporation to transact any lawful business which the board of directors finds to be in aid of governmental authority. Such statutory power would override provisions in the certificate of incorporation specifying the permissible purposes of the corporation, although it is likely that corporations will increasingly take advantage of the “all purpose” clause authorized in 1967 by § 102(a)(3), so that the chance of conflict between declared charter purposes and the new statutory provision is markedly diminished.

The 1967 revision introduced this concept into the statute for the first time by authorizing a corporation, “in time of war or other national emergency,” to do any lawful business “at the request or direction of any apparently authorized governmental authority.” The 1969 amendment deletes the national emergency or war limitation and focuses upon the board’s finding, presumably sustained under the business judgment rule, that the corporate action would be “in aid of governmental authority,” notwithstanding purpose limitations in the charter.<sup>61</sup>

Folk’s treatise might be read to say that section 122(12) does nothing to extend the powers or responsibilities of a corporation otherwise organized to undertake “any lawful act.” The sole effect of the provision, under this interpretation, is to expand the powers of firms organized for a limited purpose (e.g., to run a railroad) into two “extra” areas under the 1967 version—war or emergency work—and into a very wide “extra” area in the 1969 reforms—any work aiding governmental authority.

But is this really a satisfying explanation, given the legacy of the provision in the Model Act that we have reviewed? Why, after all, single out government work if the only intention was to add to the areas in which directors were free to pursue shareholder interests? Why not also provide extraordinary authorization to engage in, say, mining operations, or technological innovation if the board found it useful? A straightforward reading of “wartime or emergency” circumstances, and authorization to give “aid of governmental authority,” suggests an expansion of corporate *responsibilities*—not merely an expansion of authorized areas of business practice. Any other interpretation would require a suspension of our ordinary understand-

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60. FOLK, *THE DELAWARE GENERAL CORPORATION LAW*, *supra* note 4, at xii.

61. *Id.* at 37–38. Folk then drops a footnote: “*Cf.* §110, authorizing emergency by-laws operative during periods of nuclear or atomic disasters or like emergencies.” *Id.* at 38 n.12.



ing of language. Nevertheless, the historical record provides limited guidance on the issue, and Folk's treatise leaves open more questions than it answers.

It is plain that neither Delaware's adoption of the "wartime or national emergency" version of section 122(12) in 1967, nor its 1969 expansion to include all "aid of governmental authority," elicited sustained deliberation on the part of those who drafted and adopted it.<sup>62</sup> Reviewing the thin historical record, one has the sense that both times the provisions were put into the statute as a kind of half-thought-out expressive contrition to public spiritedness, a sort of Freudian (Rawlsian?) slip on the part of the drafters who wanted to maintain self and group conceptions of being engaged in public-oriented policymaking, even as their more direct observations revealed that what they were doing was drafting a statute that had the attributes corporate managers, lawyers, and professors wanted to see. Reflecting on his work as Reporter for Delaware's Revision Committee, Folk reflected on the "fiction" under which those engaged in the process operated.<sup>63</sup> He wrote:

Committees undertaking to rewrite corporation statutes usually believe, with varying degrees of devoutness, that they are pursuing an ideal of fairly and equitably balancing the varied and sometimes conflicting interests of the constituents of any corporation.

. . . .

This is a fiction. . . . Clearly, the Delaware statute does not represent a balancing of interests. The excellent and able committee consisted chiefly of pro-management corporation attorneys, with a divided minority representing the specialized interests of the Secretary of State's office and of the derivative suit plaintiff. The majority was strengthened by two representatives of the service companies.

. . . .

Naturally, the product reflects this fact.<sup>64</sup>

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62. Indeed, if a board of directors adopted a major corporate policy with so little deliberation it might very well fall short of the process obligations Delaware courts have said are owed by directors to their shareholders. See JAMES D. COX & THOMAS L. HAZEN, *BUSINESS ORGANIZATIONS LAW* 197–226 (2011) (discussing the business judgment rule).

63. Folk, *Some Reflections*, *supra* note 8.

64. *Id.* at 412. Compare Folk's overview to the less mercenary description by Ray Garrett, chairman of the original Model Business Corporation Act's drafting committee, in his Preface to the first publication of the Model Act:

The Committee presents the Model Act as a modern statute that preserves in proper balance the interests of the state and the rights and interests of corporations, shareholders and management. It may not appeal to a state that is soliciting corporate business, but it will be attractive to any state that seeks to provide a sound and modern law under which its business corporations in general can be organized and continue to exist.

RAY GARRETT, PREFACE, MODEL BUSINESS CORPORATION ACT X (Revised 1950).

These men (and one woman) perhaps wanted to see themselves in some kind of Philadelphia summer, drafting in the public service a structure for the operation of business in the modern age. Perhaps the dissonance between this desire and the simpler reality of their project was resolved by putting in section 122(12), and leaving to future scholars, lawyers, courts, and policymakers the task of figuring out just exactly what it meant.<sup>65</sup>

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65. A footnote in an anonymous student Note in the Yale Law Journal in 1971 speculates on the proximate motivation for Delaware's 1969 change to section 122(12). See Note, *Liberalizing SEC Rule 14a-8 Through the Use of Advisory Proposals*, 80 YALE L.J. 845 (1971). The Note critically assessed the shareholder proposal mechanism developed by the Securities and Exchange Commission ("SEC"). The "shareholder proposal" mechanism gives shareholders the right to have (some kinds of) proposals relating to corporate operations included in corporate proxy-voting materials that firms send to shareholders for routine corporate votes. The note urged shareholder activists to make "advisory" proposals that, if passed by shareholders, would "suggest" a policy change to a firm's board of directors, but would not purport to require adoption of the policy. This was offered as a way to work around the SEC's insistence that corporate boards could exclude a shareholder proposal if it was in conflict with state incorporation law. *Id.* Since most state law (including Delaware) empowers directors, and not shareholders, to set corporate policy, shareholder proposals that purported to change corporate policy were conceivably in conflict with state law and, by that logic, excludable. The "advisory" proposal was seen as a way of evading formal conflict with state corporate law, thereby making such proposals non-excludable. Justifying its approach, the Note argued that "to tie shareholder functions guaranteed under the 1934 Act to the vagaries of state law might lead to the emasculation of those functions should a state explicitly disavow them." *Id.* at 854. The author dropped a footnote in that sentence that referenced Delaware's 1969 amendment to section 122(12), claiming the change had something to do with a recent controversy surrounding a shareholder proposal championed by the Medical Committee for Human Rights, a shareholder activist group, which tried to force the Dow Chemical Company to cease the manufacture of napalm for use in the Vietnam War. See *Medical Committee for Human Rights v. SEC*, 432 F.2d 659 (D.C. Cir. 1970). The footnote speculated:

An amendment to the Delaware Corporation Statute in July, 1969 indicates the danger of preemption which is inherent in a state law standard. Although the change was not accompanied by any legislative history, it was enacted shortly after the *Medical Committee* controversy began. Sec. 122(12) formerly providing that "In time of war or other national emergency, [corporations are permitted] to do any lawful business in aid thereof, notwithstanding the business or purposes set forth in its certificate of incorporation at the request of direction of any apparently authorized governmental authority" was amended to permit corporations to "transact any lawful business which the corporation's board of directors shall find to be in aid of governmental authority." The amendment appears to be an attempt by the Delaware legislature to avoid a recurrence of a challenge like that of the Medical Committee.

See Note, *supra* at 854 n.43 (emphasis in original).

The Note's author apparently thought the 1969 amended version of section 122(12) would make corporate decisions about munitions manufacture (or the like) explicitly a board prerogative and thus insulate Delaware boards from shareholder proposals of the Medical Committee sort. I have found no evidence, and no innuendo of any kind other than this Note, linking Delaware's 1969 version of section 122(12) with the *Medical Committee* controversy or the shareholder proposal mechanism. Without such evidence, it seems to me highly speculative and unlikely that there was any causal link between the two.

My efforts to identify the author of this note, so that I might discuss it with him or her, have proved fruitless. This highlights the foolishness of the legal academy's past practice of publishing student notes without attribution. Happily, this tradition is no longer patronized in our law reviews.

### III. DOCTRINAL INTERPRETATION

In this section I take up three difficult interpretive issues regarding section 122(12). First, I pursue more deeply the fundamental question at which this inquiry is directed: For whose benefit may the power described in section 122(12) of the Delaware corporate code be deployed? Second, and related to this, I examine whether the power described in section 122(12) is mandatory or merely a default rule. Finally, I consider what limits Delaware courts might impose on a corporate board's exercise of the section 122(12) power.

#### A. *The Corporate Maximand Revisited: For Whose Benefit May the Section 122(12) Power be Exercised?*

Corporate law discourse suffers confusion stemming from a failure to clearly distinguish between three distinct issues: corporate purposes, corporate powers, and corporate beneficiaries. Let us identify these distinctions. Traditionally, a corporation's "purpose" referred to the business it was authorized to undertake. As noted above,<sup>66</sup> until the mid-nineteenth century, corporations had to specify what business they wished to enter, and would (or might) be granted a charter to operate as a corporate entity for that limited purpose. Modern corporation statutes still require corporations to specify their "purpose," but Delaware after its 1967 reforms allows firms to generally state that their "purpose" is to engage in "any lawful act."<sup>67</sup> Most corporations today use this catch-all purpose. But to clearly distinguish between purposes, powers, and beneficiaries, let us for the moment presume that a corporation has been granted a charter for the "purpose" of running a railroad.<sup>68</sup> The corporate "powers" used to accomplish this purpose might include "making contracts," say, between the corporation and suppliers of steel, or it might include "making charitable contributions" to humanitarian groups (to improve the company's reputation in the community, making it easier for the railroad to deal with workers, consumers, or the government). Delaware's statute provides all corporations both of these powers.<sup>69</sup>

Neither the "purpose" nor the "powers" of the corporation, however, clarify who or what is the intended *beneficiary* of the railroad corporation's operations. The beneficiary might be designated as the capital investors in the railroad, or it might be designated as the firm's workers or consumers, or all three, or some other constituency. No one could doubt that a Delaware corporation whose "purpose" is to run a railroad, or whose purpose is to engage in "any lawful act," and happens now to be engaged in the opera-

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66. *See supra* text accompanying notes 4–10.

67. DEL. CODE tit. 8, § 101(b) (1967).

68. Or we can just imagine a corporation chartered for the purpose of engaging in "any lawful act" that happens to be running a railroad.

69. DEL. CODE tit. 8, § 122(9), (13) (1969).

tion of a railroad, has the “power,” per section 122(12), to spend money that advances the government’s policy of, say, reducing carbon emissions or curbing childhood obesity. The difficult question is this: Can directors take this action under section 122(12) only when they sincerely believe it will advance the interests of their shareholders, or does section 122(12) authorize them to do it *irrespective* of the shareholders’ interests?

One possible interpretation is that the power to aid governmental authority is circumscribed always by the obligation to only use the power in a fashion consistent with the background fiduciary obligations that bind directors in Delaware.<sup>70</sup> Under this interpretation, directors can cause the corporation to aid governmental authority, but only when doing so is in the best interests of the shareholders. Another interpretation is that section 122(12) is an *exception* to the usual rule that requires directors to run their firms in the interests of shareholders. A third view, held by some scholars and activists, might claim that Delaware corporate law does not, as a general matter, require directors to manage firms only in the interests of shareholders, but instead always permits directors some discretion to attend to non-shareholder interests.<sup>71</sup> This third interpretation must conclude that there is really nothing very special about section 122(12), it merely reiterates or states more specifically a general principle of Delaware law.

My doctrinal assessment, with section 122(12) bracketed-out or ignored (as corporate law study has done for forty years), is that Delaware’s corporate law charges directors with running their corporations in the best interests of shareholders, and that directors are forbidden from pursuing other concerns that conflict with shareholder interests.<sup>72</sup> While Delaware’s statute is (remarkably) silent on the beneficiary issue, the Delaware courts have construed the statute as imposing on directors an obligation to exercise corporate powers on behalf of shareholders, and no other corporate constituency. Normatively, I am critical of this shareholder primacy rule,<sup>73</sup> but I believe it is clear that shareholder primacy is in fact the law as expressed by Delaware jurists. Whatever we make of its text and history, section 122(12) must be interpreted against this doctrinal background. Before proceeding, I must summarize my positive position on the background rule of shareholder primacy, as it is controversial.<sup>74</sup>

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70. See David G. Yosifon, *The Law of Corporate Purpose*, 10 BERKELEY BUS. L.J. 181 (2014).

71. See *id.* at 121–58 (critiquing scholarship making this claim).

72. *Id.*

73. I summarize this view *infra* Section IV. See also generally, David G. Yosifon, *The Consumer Interest in Corporate Law*, 43 U.C. DAVIS L. REV. 253 (2009); David G. Yosifon, *The Public Choice Problem in Corporate Law: Corporate Social Responsibility After Citizens United*, 89 N.C. L. REV. 1197 (2011); David G. Yosifon, *Consumer Lock-In and the Theory of the Firm*, 35 SEATTLE U. L. REV. 1429 (2012).

74. This section summarizes my view that the positive law of Delaware is shareholder primacy. Skeptics or agnostics on this point may find useful a painfully (in a good way) detailed

The clearest way to see that shareholder primacy is the law in Delaware is to examine the arguments of those who claim it is not. Some corporate law scholars point to *Unocal v. Mesa*<sup>75</sup> in support of the view that Delaware directors are *not* required to always attend exclusively to the shareholder interest.<sup>76</sup> In *Unocal*, the Delaware Supreme Court reviewed corporate boards' authority to respond defensively to hostile takeover attempts by outsiders. The Court held that Delaware boards have broad authority in such circumstances.<sup>77</sup> Fleshing out its conclusion, the Court remarked that a proper decision about whether to accept or contest an unwelcome offer:

entails an analysis by the directors of the nature of the takeover bid and its effect on the corporate enterprise. Examples of such concerns may include: inadequacy of the price offered, nature and timing of the offer, questions of illegality, *the impact on "constituencies" other than shareholders (i.e., creditors, customers, employees, and perhaps even the community generally)*, the risk of nonconsummation, and the quality of securities being offered in the exchange.<sup>78</sup>

But the Delaware Supreme Court quickly reversed, or clarified, this language in *Revlon, Inc. v. MacAndrews & Forbes Holdings, Inc.*, decided just one year later.<sup>79</sup> In the course of reluctantly selling its company, Revlon's board favored a bidder who promised to support the value of debt notes that the firm had recently exchanged for some of its outstanding shares. Although an active second bidder may have been prepared to offer more for the firm, the board resolved to sell to the first bidder instead. Helpfully (for present purposes), the Revlon board acknowledged that it favored the first bid because it was better for the noteholders.<sup>80</sup> The Delaware Supreme Court held that such a motive was forbidden. It took the occasion to say what it had meant to say in *Unocal*:

The Revlon board argued that it acted in good faith in protecting the noteholders because *Unocal* permits consideration of other

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version of this argument, which addresses other scholars' differing analyses, in Yosifon, *The Law of Corporate Purpose*, *supra* note 70.

75. *Unocal Corp. v. Mesa Petroleum Co.*, 493 A.2d 946 (Del. 1985).

76. See, e.g., LYNN STOUT, *THE SHAREHOLDER VALUE MYTH: HOW PUTTING SHAREHOLDERS FIRST HARMS INVESTORS, CORPORATIONS, AND THE PUBLIC* 18–31 (2012); see also Yosifon, *The Law of Corporate Purpose*, *supra* note 70, at 121–58 (critiquing Stout and others making similar claims).

77. *Unocal*, 493 A.2d at 954–55. Because of the “specter that a board may be acting primarily in its own interests” when rebuffing a bid by an outsider to gain control of the company, “there is an enhanced duty which calls for judicial examination at the threshold before the protections of the business judgment rule may be conferred.” *Id.* However, directors can satisfy this enhanced judicial scrutiny “by showing good faith and reasonable investigation.” *Id.* at 955 (internal citations omitted).

78. *Id.* at 955 (emphasis added).

79. *Revlon, Inc. v. MacAndrews & Forbes Holdings, Inc.*, 506 A.2d 173, 182 (Del. 1986).

80. *Id.*

corporate constituencies. Although such considerations may be permissible, there are fundamental limitations upon that prerogative. A board may have regard for various constituencies in discharging its responsibilities, *provided there are rationally related benefits accruing to the stockholders*. However, such concern for non-stockholder interests is inappropriate when an auction among active bidders is in progress, and the object no longer is to protect or maintain the corporate enterprise but to sell it to the highest bidder.<sup>81</sup>

If the non-shareholder interest is unrelated (i.e., not “rationally related”) or adverse to the shareholder interest, then such interest is not a proper consideration under Delaware law.

Some scholars claim that *Revlon* only requires directors to maximize shareholder interests during the sale of a firm, which was the circumstance of that case.<sup>82</sup> These scholars deduce from this that directors are therefore free to pursue other interests at other times in the life of a firm. But that is a non sequitur.<sup>83</sup> And it is not a plausible reading of *Revlon*. Look closely at the pull-quote above. When the Court writes, “[a] board may have regard for various constituencies . . . provided there are rationally related benefits accruing to the stockholders,” the Court is clarifying the “permit” it granted in *Unocal*. In *Unocal* the board was *not* selling the firm, but was instead determined to continue as a going concern. The “rationally related benefits” qualification therefore is explaining the board’s obligations *in the going concern condition*. It is only after the Court explained this that it moves on to conclude that in the context of a sale of the firm, this principle requires the board to sell to the highest bidder (since what other constituencies think of the firm is no longer relevant to the firm’s value to shareholders).<sup>84</sup>

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81. *Id.* (emphasis added) (citation omitted).

82. *See, e.g.*, STOUT, *supra* note 76, at 31.

83. For the proposition if A (sale of firm) then B (maximize profits), one cannot conclude that if not A (no sale of firm) then not B (no maximize profits). Among Lyman Johnson’s many insightful comments on an earlier draft of this paper was the remark that with respect to this formulation, “not A” (no sale of firm) also does not as a matter of logic imply “B” (maximize profits). While this is true, my point is to emphasize the logical fallacy indulged by those who would use *Revlon*’s auction rule to conclude that shareholder primacy is not the rule in the going concern context, and to insist that *Revlon*, *Macmillan*, *infra* note 84, and *eBay*, *see infra* text accompanying notes 87–90, must be read to state clearly that directors must always manage firms in the interest of shareholders, and not for any other competing stakeholder. The life of the shareholder primacy norm in Delaware has not been logic, it has been case law.

84. In another takeover case from the 1980s, *Mills Acquisition Co. v. Macmillan, Inc.*, the Court also made clear that there is nothing fundamentally different in terms of the object—the beneficiary—of corporate governance during the going concern condition, on the one hand, or the sale-of-firm context, on the other: “*like any other business decision*, the board has a duty in the design and conduct of an auction to act in ‘the best interests of the corporation and its shareholders.’” 559 A.2d 1261, 1287 (1989) (emphasis added) (citation omitted). I address the relevance of the “corporation and its shareholders” formulation to the corporate beneficiary debate, *infra* text accompanying notes 92–95.

Like all clever people, the Delaware Supreme Court is aware that serving the corporation and its shareholders will often involve caring for the firms' other constituencies, since being good to workers, consumers, communities, and the environment has reputational effects that can grease the engines of profitability. But like all serious people, the Delaware Supreme Court recognizes that this felicitous harmony is not always present. Where choices have to be made that can only leave one group better off and will leave other groups worse off, Delaware case law requires that corporate directors manage in favor of shareholders and no other constituency. While a firm is a going concern, Delaware defers to directorial discretion about whether profits will best be maximized by harvesting them all today, taking some today and leaving some for tomorrow, or leaving all for tomorrow. But there is nothing in *Revlon's* injunction to maximize present profits in the last period which authorizes directors to pursue non-shareholder interests at the expense of shareholders in the going concern condition.<sup>85</sup>

That the Delaware Supreme Court believes shareholder primacy is its law has been clear since *Revlon*.<sup>86</sup> But the Court of Chancery has more recently expressed Delaware's shareholder primacy rule as explicitly as possible in *eBay, Inc. v. Newmark*.<sup>87</sup> In that case the founders of Craigslist, Inc., undertook a series of governance machinations that were designed to keep control of the company with its founders and their heirs, and out of the hands of eBay, Inc., which had become a minority shareholder in the firm.<sup>88</sup> As in *Revlon*, the directors were refreshingly candid about the reasons for their moves. Their goal, they said, was to allow Craigslist, Inc. to maintain its public service orientation and not have it come under the sway of eBay, which wanted to monetize the thing.<sup>89</sup> Chancellor Chandler rejected this motive as inconsistent with Delaware law:

The corporate form in which craigslist operates, however, is not an appropriate vehicle for purely philanthropic ends, at least not when there are other stockholders interested in realizing a return on their investment. Jim and Craig opted to form craigslist, Inc. as a *for-profit Delaware corporation* and voluntarily accepted millions of dollars from eBay as part of a transaction whereby eBay became a stockholder. Having chosen a for-profit corporate form, the craigslist directors are bound by the fiduciary duties and standards that accompany that form. Those standards include acting

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85. The command to maximize profits when a firm is being sold and shareholders cashed-out is a judicial recognition that in that final period there is no longer *any* reason to defer to the directors' discretion about what is the best *time horizon* in which to pursue shareholder interests. A *Revlon* analysis suspends the deference Delaware typically shows in evaluating directorial fidelity to their fiduciary obligations, but it does not alter those obligations. It suspends the business judgment rule, but it does not change the fiduciary rules.

86. *Revlon*, 506 A.2d at 182.

87. *eBay Domestic Holdings, Inc. v. Newmark*, 16 A.3d 1 (Del. Ch. 2010).

88. *Id.* at 34–35.

89. *Id.* at 34.

to promote the value of the corporation for the benefit of its stockholders. The “Inc.” after the company name has to mean at least that. Thus, I cannot accept as valid for the purposes of implementing the Rights Plan [the entrenchment plan] a corporate policy that specifically, clearly, and admittedly seeks *not* to maximize the economic value of a for-profit Delaware corporation for the benefit of its stockholders—no matter whether those stockholders are individuals of modest means or a corporate titan of online commerce.<sup>90</sup>

Chandler cited no statutory authority or case law for his proposition. He was making, excuse me, *finding* this command of corporate beneficiary in (what is now no longer merely) the brooding omnipresence of the common law.<sup>91</sup>

Some Delaware cases include verbiage stating that directors owe fiduciary obligations to “the corporation and its shareholders.”<sup>92</sup> Corporate law scholars sometimes interpret this “and” as demonstrating that directors may or must manage their firms for stakeholders other than shareholders.<sup>93</sup> I think the “corporation and its shareholders” formulation cannot bear that interpretation. The verbiage is better read to distinguish between the synthetic legal entity (the corporation) and the artificial or natural persons who are to benefit from the corporation’s operations (the shareholders). Usually this linguistic distinction (“the corporation” and “its shareholders”), even when it is written in a judicial opinion, plays no role whatsoever in the action of the case. In the few cases where the distinction is meaningful, it showcases the question of *who* has authority to control the corporation, directors or shareholders, rather than *what* is being decided or in whose interests things are being decided. This uncertainty comes up most acutely when directors try to obstruct shareholders from freely participating in a non-coercive tender offer for their shares.<sup>94</sup> It can also arise in the context of

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90. *Id.* (emphasis in original) (citation omitted).

91. *Cf.* *Southern Pac. Co. v. Jensen*, 244 U.S. 205, 222 (1917) (Holmes, J. dissenting) (“The common law is not a brooding omnipresence in the sky, but the articulate voice of some sovereign or quasi sovereign that can be identified.”).

92. *See Mills Acquisition Co.*, 559 A.2d at 1287; *Smith v. Van Gorkom*, 488 A.2d 858, 872 (Del. 1985) (“In carrying out their managerial roles, directors are charged with an unyielding fiduciary duty to the corporation and its shareholders”).

93. *See* Yosifon, *The Law of Corporate Purpose*, *supra* note 70, at 135–42 (discussing scholarship).

94. *See, e.g., Grand Metro. Pub. Ltd. v. Pillsbury Co.*, 558 A.2d 1049 (Del. Ch. 1988) (determining that Pillsbury’s directors could not raise structural defenses that would preclude Pillsbury shareholders from electing to participate in Grand Metropolitan’s non-coercive tender offer). Even this “who decides” distinction between “the corporation” and “its shareholders” has become largely irrelevant as Delaware jurisprudence has developed in a direction that almost always concludes that it is directors, not shareholders, who get to decide. *See, e.g., Paramount Commc’n, Inc. v. Time, Inc.*, 571 A.2d 1140 (1989) (permitting structural defenses that preclude even a non-coercive tender offer); *Air Prods. & Chems., Inc. v. Airgas, Inc.*, 16 A.3d 48 (Del. Ch. 2011) (same).



shareholder proposals for reform of corporate operations.<sup>95</sup> But there are *no* cases that use the “corporation and its shareholders” formulation to express the view that directors may pursue their obligations to the “corporation” in a manner that privileges the interests of non-shareholders at the expense of shareholders.

Given that Delaware has made clear that any consideration of non-shareholder interests must be “rationally related” to shareholder interests,<sup>96</sup> it is similarly implausible to claim that directors may pursue non-shareholder interests so long as there is “some” gain to shareholders. Surely directors may choose a course of action that will deliver the firm’s product to consumers, say, twenty percent more cheaply than the firm has previously offered it, so long as the directors sincerely believe the decision will be profitable for shareholders (for example, by increasing consumption of the product now or in the future). If that is all there is to the decision, then there is no problem with the choice to “benefit” consumers. But directors may not choose to give their product to consumers twenty percent more cheaply, or with twenty percent less damage to the environment, if the directors believe that doing so will reduce profits (over all time horizons) compared to some other policy. A decision to choose a less profitable over a more profitable course because the less profitable is better for non-shareholders is not a decision that is rationally related to advancing shareholder interests.<sup>97</sup>

Finally, let us bring corporate charitable giving into this analysis. Section 122(9) of the Delaware corporate code gives all corporations the power to make charitable contributions.<sup>98</sup> One might be tempted to argue that even if I am right in my interpretation of Delaware’s shareholder primacy orientation *generally*, section 122(12) should be interpreted as a kindred spirit to the corporate charitable giving provision, which, this temptation suggests, is an exception to Delaware’s general shareholder primacy command. But I do not think that is right. Unlike section 122(12), the charitable giving power under section 122(9) has been interpreted by Delaware case law. That case law imposes a “reasonableness” limitation on corporate charitable giving.<sup>99</sup> This “reasonableness” requirement has *two* components: first, charitable gifts must be of a reasonable magnitude, and second, charitable gifts must bear a reasonable relation to the overarching obligation of directors to man-

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95. See *supra* note 65.

96. *Revlon*, 506 A.2d at 176.

97. See also *City Capital Assocs. L.P. v. Interco, Inc.*, 551 A.2d 787, 802 (1988) (“[*Revlon*’s] holding that the board could not prefer one bidder to another but was required to permit the auction to proceed to its highest price unimpeded, can be seen as *an application of traditional Delaware law*: a fiduciary cannot sell for less when more is available on similar terms.”) (emphasis added).

98. “Every corporation . . . shall have power to . . . [m]ake donations for the public welfare or for charitable, scientific or educational purposes, and in time of war or other national emergency in aid thereof . . . .” DEL. CODE tit. 8, § 122(12) (2000).

99. See *Kahn v. Sullivan*, 594 A.2d 48, 61 (Del. 1991); *Theodora Holding Corp. v. Henderson*, 257 A.2d 398, 404 (Del. Ch. 1969).

age Delaware corporations in the best interests of shareholders.<sup>100</sup> I draw this conclusion after reviewing the leading cases, both of which (there are only two of them) sanction corporate charitable gifts only after concluding that the gifts were modest in relation to the wealth of the firm, *and* that the gifts were plausibly related to advancing the reputation of the firm among firm stakeholders or improving the socio-political atmosphere in which the firm was operating its business, and thus were rationally related to shareholder interests.<sup>101</sup>

This interpretation of the reasonableness requirement imposed on the corporate charitable giving power by Delaware courts is buttressed, I believe, by reflection on the following hypothetical. Suppose a corporate board decided to make a modest (relative to the firm's earnings) charitable gift after engaging in a deliberative process which reached the sincere, good faith determination that the gift would harm the reputation of the company and would adversely affect the short, medium, and long-term interests of the shareholders. Faced with such a situation, guided by its own statute and precedent, I think Delaware would enjoin the gift, and perhaps hold the directors liable for a violation of their duty of good faith governance on behalf of shareholders.

A similar hypothetical must test the meaning of section 122(12). Suppose a board deliberated and determined to aid governmental authority in a fashion that the board in good faith believed would be adverse to the interests of its shareholders over all time periods. Would this be permissible? If Delaware were to interpret section 122(12) consistently with the rest of its jurisprudence, including section 122(9), I think the answer must be no. Certainly Delaware courts will defer to a corporate board's discretion about what course is in the best interests of its shareholders. Often directors taking the long-view will conclude in good faith that it is desirable for the corporation to behave in a socially responsible manner lest it alienate constituencies—like workers, consumers, and the government—that are crucial to sustaining the operation's profitability. But directors are required to take whatever view they sincerely believe is in the best interests of the shareholders. This may be a view that involves less regard for non-shareholders.

In sum, Delaware's statute is silent as to whether directors may run their firms in the interests of shareholders alone or whether they have broader discretion, but Delaware case law clearly holds that the law requires directors to run their firms in the interests of shareholders. Directors may consider the interests of non-shareholders only to the extent that doing so is rationally related to advancing shareholder interests. My analysis of Delaware's prevailing jurisprudence fits uncomfortably with my discussion in the previous section concerning the development of section 122(12). The

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100. See Yosifon, *The Law of Corporate Purpose*, *supra* note 70, at 142–49.

101. See *Kahn*, 594 A.2d at 62; *Theodora Holding Corp.*, 257 A.2d at 404.

section's drafting legacy, such as can be reconstructed, and its express terms, at least suggest that it was meant to authorize corporate decision-making motivated to serve a broader constituency than just shareholders.

*B. Is Section 122(12) Mandatory or Permissive?*

Given real uncertainty about the meaning of section 122(12), some corporations might prefer to organize themselves without it. Some holders of capital might prefer to invest in corporations organized without it. Is it permissible for corporate founders, or subsequent boards or shareholders, to opt-out of "specific powers" supplied by Delaware's code, including section 122(12)?

A straightforward grammatical reading of the statute leads to the conclusion that the power described in section 122(12) cannot be renounced in a firm's articles of incorporation. Section 122 begins with the words "[e]very corporation created under this chapter shall have power to."<sup>102</sup> Section 122(1), the first power listed, then states: "[h]ave perpetual succession by its corporate name, *unless a limited period of duration is stated in its certificate of incorporation.*"<sup>103</sup> This "unless" language in section 122(1), explicitly giving permission to limit the power that is described, must by ordinary principles of construction lead us to conclude that powers described in the rest of the section are mandatory (corporations "shall" have them), since the language "unless . . . stated in its certificate of incorporation" is not appended to any of them, including section 122(12).<sup>104</sup>

This interpretation would especially make sense if section 122(12) is viewed as a corporate power that benefits, or might benefit, non-shareholders. Shareholders should not be able to excise a protection or prerogative of non-shareholders. This explanation is buttressed by looking at other "powers" described in section 122 that are indubitably designed to protect non-shareholders. For example, section 122(2) provides that all corporations "shall have the power to . . . be sued."<sup>105</sup> Would anyone really think (or would anyone really expect a Delaware court to hold) that a corporation

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102. DEL. CODE tit. 8, § 122(12) (2000) (emphasis added).

103. *Id.* § 122(1) (2000).

104. Recall that the original 1967 version of section 122(12) stated "Every corporation . . . shall have power . . . [i]n time of war or other national emergency, to do any lawful business in aid thereof, *notwithstanding the business or purposes set forth in its certificate of incorporation.*" DEL. CODE tit. 8 § 122(12) (1967) (emphasis added). The 1969 revision removed this "notwithstanding the business or purposes set forth in its certificate of incorporation" language when section 122(12) was changed to read "[e]very corporation . . . shall have power to . . . [t]ransact any lawful business which the corporation's board of directors shall find to be in aid of governmental authority." DEL. CODE tit. 8 § 122(12) (1969). But this cannot easily be read as a change that made an immutable rule mutable, since the 1969 version of the power is still qualified by "every corporation," and is not qualified by "unless otherwise provided in the articles." The "notwithstanding" language could very well have been removed in the 1969 amendment because it was seen as duplicative of the "every corporation" language that already qualified the scope of the power.

105. DEL. CODE tit. 8, § 122(2).

may in its articles of incorporation deny itself this power? Surely not, since the “power” of a corporation to be sued is one that “every corporation” has, not only for the corporation’s benefit, but for the benefit of third parties (especially, for example, tort victims) dealing with (or dealt with by) the corporation. The same may be said of the power to aid governmental authority, if it is taken as a power which exists to benefit the public, irrespective of the shareholder interest.

However, if one views the section 122(12) power as being constrained by directors’ fiduciary obligations to shareholders, then it might be plausible to conclude that it is mutable, despite the grammar of the statute. To support such an interpretation, consider section 122(16), which provides that “all corporations shall have” the power to “[p]rovide insurance for its benefit on the life of any of its directors, officers or employees . . . .”<sup>106</sup> It seems far-fetched to think that Delaware courts would hold that articles of incorporation that forbid a particular corporation from insuring the lives of its directors, officers, or employees would be void as inconsistent with the statute. Or if a firm purported in its articles of incorporation to limit its corporate operations to the territorial boundaries of Delaware, it is probably implausible to conclude that Delaware courts would refuse to enforce the limitation because it ran afoul of section 122(8), which gives “all corporations” the power to “[c]onduct its business, carry on its operations and have offices and exercise its powers within or without this State.”<sup>107</sup>

Yet such a “mutable” interpretation of the aid to governmental authority power of section 122(12) is wholly at odds with a broader interpretation of the provision which claims that it merely adds an “extra” business area available to a corporation when the firm’s articles of incorporation state a purpose narrower than to engage in “any lawful act.” That interpretation must conclude that you cannot exclude the government aid power by stating a narrow purpose, that is, a purpose that does not include it, in the articles of incorporation. Unless we are to say that in order to be rid of the power it must be specifically “renounced” in the articles of incorporation, rather than simply stating a limited corporate purpose that does not include it.

In contradistinction to the apparently mandatory nature of section 122(12) in the Delaware code, note a subtle but decisive drafting difference that appears to make the Model Act’s version of the power mutable. The most recent version of the Model Act’s “General Powers” section begins:

Unless its articles of incorporation provide otherwise, every corporation has perpetual duration and succession in its corporate name and has the same powers as an individual to do all things necessary or convenient to carry out its business and affairs, including without limitation power.<sup>108</sup>

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106. *Id.* § 122(16).

107. *Id.* § 122(8).

108. MODEL BUS. CORP. ACT § 3.02 (2011).

The Model Act then lists several powers, including, “(14) to transact any lawful business that will aid governmental policy.”<sup>109</sup> The grammatical structure of the Model Act’s formulation clearly makes the reservation “unless its articles of incorporation provide otherwise,” apply to *everything* that follows. A Model Act corporation could therefore, apparently, elect *not* to give its corporation the power to aid governmental policy. But this is not a very satisfactory interpretation, given the much clearer legacy in the Model Act linking the government aid power to an expansion of corporate responsibilities, rather than merely an expansion of the domain in which a corporation might pursue its ordinary responsibilities to shareholders.<sup>110</sup> Moreover, this interpretation would also lead to the anomalous conclusion that a Model Act corporation could also include in its articles of incorporation a statement renouncing the power to be sued, which does not really make sense.

This textual analysis leads perhaps most clearly to the conclusion that the “powers” sections of both the Model Act and the Delaware statute are poorly written and in need of revision.

### C. *Limitation on the Power Described in Section 122(12)*

Setting aside the issue of who is the rightful beneficiary of the corporate power to aid governmental authority, and whether or not the section is mutable, how broadly does section 122(12) expand a board’s authority for the (rare) firm with a specified purpose that is narrower than the catch-all purpose of “any lawful act”?

Facially, the section must be read to empower something more than the narrow purpose specified in a firm’s articles of incorporation, but something less than “any lawful act,” otherwise the aid to governmental authority power would collapse entirely into the broad “any lawful act” purpose that the firm could have chosen.

One limitation appears to be that narrow-purpose firms are not empowered by section 122(12) to transact lawful business that the firm’s board of directors finds to be in aid of, say, religious authority, intellectual authority, or the authority of the arts. It is only aid of “governmental authority” that is empowered. But what is “governmental authority”? Does “governmental authority” refer only to specific legislative or administrative projects? Does it include particular executive orders? Perhaps even specific judicial holdings? A public policy half-articulated at the penumbra of the common law? May governmental authority refer to either federal, state, or local governments? May it refer to an international governmental authority, such as the International Criminal Court? May it refer only to governmental authority in a jurisdiction in which the corporation is operating? Or is the

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109. *Id.* § 3.02(14).

110. *See supra* text accompanying notes 19–21, 43–56.

power rightly triggered in aid of any governmental authority anywhere?<sup>111</sup> Worth repeating in this connection is the Revised Model Act drafting committee's explicit consideration of government's engaging in "the performance of covert hostile acts of general acceptance" and the committee's apparent view of the legitimacy of corporations giving aid to such endeavors.<sup>112</sup>

In addition to the statutory phrase "governmental authority" imposing some limit on the section 122(12) power, so too might the phrase "transact any lawful business" be read to impose some kind of limit on what the provision authorizes. It should at least be understood as specifying something distinct from giving gifts or charity, which is the domain of section 122(9).<sup>113</sup> Note also the apparent significance of the wording change between section 102(a)(3), which allows firms to specify a purpose of undertaking "any lawful *act*," and section 122(12), which empowers corporations aiding governmental authority the right to "transact any lawful *business*." The two different words ("act" and "business") in the two sections should be construed as referring to different things, with "business" presumably comprising a subset of "act[s]." But "transact . . . business" is not really a term of art. For example, it does not specify that the business must be profitable. It is hard to find a meaning for "business" in this provision that would exclude something that would be allowed by "act."

In his 1972 treatise on Delaware law, Folk briefly addressed the standard of review that would attend decisions pursuant to section 122(12). The provision, he wrote, "focuses upon the board's finding, presumably sustained under the business judgment rule, that the corporate action would be 'in aid of governmental authority.'"<sup>114</sup> If Folk was right, courts would decline to review the substance of board determinations regarding "aid to governmental authority" so long as the decisions were informed, deliberate, disinterested, and lawful.<sup>115</sup> And it is true that most corporate decisions, big, small, successful or disastrous, get business judgment rule protection. But not all types of decisions get it, and there may be reason to doubt Folk's "presum[ption]" about the standard of review for section 122(12) decisions. Charitable contributions made pursuant to section 122(9), for example, are not given business judgment rule deference. They are instead subject to a substantive "reasonableness" standard, under which courts evaluate the ap-

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111. It should be noted here that the 1969 version of the Model Act dropped the modifier "United States" from government, and thus suggests that the corporation has the power to aid *any* government policy (or in the case of Delaware, any government "authority") including, for example, an authoritarian or repressive government in some foreign land in which the corporation is doing business.

112. See Scott, *supra* note 43, at 292-93.

113. Section 122(9) specifically authorizes charitable contributions "in time of war or other national emergency in aid thereof." DEL. CODE tit. 8, § 122(9) (1969).

114. See FOLK, *supra* note 4, at 38.

115. See COX & HAZEN, *supra* note 62, at 197-226.

propriateness of the gift's magnitude (relative to corporate earnings) and the plausibility of the gift's relationship to advancing shareholder interests.<sup>116</sup> It is quite possible that guided by its section 122(9) jurisprudence, Delaware would impose a "reasonableness" limitation on the section 122(12) power.<sup>117</sup>

#### IV. NORMATIVE ANALYSIS

My analysis of section 122(12) in the previous section suggested that while the authors of the Model Act, on which the Delaware power was based, clearly had the idea that the provision expanded the permissible beneficiaries of corporate action, such an interpretation is in tension with extant Delaware jurisprudence on the fiduciary obligations of Delaware corporate directors, and Delaware courts would be unlikely to interpret section 122(12) in a manner that deviates from the shareholder primacy norm.

But section 122(12) *is* in the statute, and remembering its history at least gives us a point of departure to critically assess what we want our corporate law to do in our own era. A recent engaging article by Professor Robert J. Rhee did just this, breaking the law reviews' forty year silence with a thoughtful, if in my view flawed, normative analysis that makes use of section 122(12).<sup>118</sup> I review Rhee's argument here for the dual purpose of showcasing it on its own terms, and to situate the very different normative lesson I draw from the legacy of section 122(12).

Taking the 2008 financial crisis as his narrative context, Rhee draws on, among other things, section 122(2) to argue that it is both legally permissible and normatively desirable for corporate boards to depart from the shareholder primacy norm, but only in times of national emergency (as will

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116. In fact, the *Kahn* case appears to hold that the "reasonableness" inquiry in the corporate charitable giving context puts the burden on directors to establish in the first instance that their decision was reasonable. If that burden is carried, the decision becomes cloaked by business judgment rule protection, which defendants might nevertheless still attempt to overcome, however unlikely that effort would be. *See Kahn*, 594 A.2d at 52–54.

117. In their treatise on Delaware law, Franklin Balotti and Jesse Finkelstein opine that the 1969 "revision of Section 122(12) grants the board of directors full discretion to authorize any lawful business in aid of governmental authority." 2 R. FRANKLIN BALOTTI & JESSE A. FINKELSTEIN, *DELAWARE LAW OF CORPORATIONS & BUSINESS ORGANIZATIONS* § 122 (3d ed. 1969 & Supp. 2001). This is a plain reading of the section 122(12) language, but as I suggest in the text, "full discretion" is probably an overstatement. *Cf. Topkis v. Del. Hardware Co.*, 23 Del. Ch. 125, 135 (1938) ("power conferred by the statute upon a majority of the stockholders or upon the directors, though conferred in terms that are absolute, is nevertheless subject to restraint by a court of equity if it be inequitably exercised.").

118. *See Rhee*, *supra* note 2. Beyond the few mentions in hornbooks, casebooks, and Model Act annotations that I have reviewed here, I have found only two other very brief references to § 122(12) in the law journals prior to Rhee's 2011 article. Both came in the 1970s. *See Note: Herald v. Seawell: A New Corporate Social Responsibility*, 121 U. PA. L. REV. 1157 (1973); David L. Engel, *An Approach to Corporate Social Responsibility*, 32 STAN. L. REV. 1, 14, n.45 (1979) (noting the similarity between Delaware's §122(12) and (then) §4(n) of the Model Act).

be seen, my normative assessment differs from Rhee's, but we at least share the baseline view that the law in Delaware is shareholder primacy).<sup>119</sup>

Rhee reviews in detail Bank of America's shotgun acquisition, over the course of a few weeks in November and December 2008, of the then-collapsing investment firm Merrill Lynch. After the merger agreement had been signed by both firms, but before it closed, Merrill Lynch's financial position further deteriorated to the point where Bank of America considered walking away from the deal by invoking the "material adverse condition" clause in the merger agreement.<sup>120</sup> Many observers, including high-ranking officials in the federal government, believed that a collapse of the Bank of America and Merrill Lynch merger would throw already weakened financial markets into a tailspin, significantly worsening the national (and global) credit crisis. Federal officials threatened to exercise an obscure banking regulation that authorized the federal government to remove the entire Bank of America Board if it canceled the merger.<sup>121</sup> Thereafter, Bank of America directors thought further about it and ultimately concluded that the deal was, ahem, in the best of interests of its shareholders after all. The merger went through. But Rhee uses this scenario to set the stage for this hypothetical: Suppose the Bank of America Board had reached the conclusion that its shareholders would have been better off if the deal was canceled, but that doing so would cause or exacerbate a national financial emergency.<sup>122</sup> Could the board have legitimately gone through with the deal anyway, in order to serve the public interest?

Rhee reads section 122(12) as authorizing such a profit-sacrificing decision. He acknowledges that there has been little scholarship and no judicial interpretation of the statute, and he does not himself undertake the history or doctrinal analysis developed in the previous sections of this Article.<sup>123</sup> But he urges a construction of section 122(12) that would recognize "a rule of fiduciary exemption," holding that "upon a public necessity, a board of a firm that is uniquely situated to avert or mitigate a public crisis is exempt from its ordinary fiduciary duty to the corporation insofar as it distributes corporate assets with the intent to aid the government or the public."<sup>124</sup> Rhee would apparently cap profit-sacrifice in the "safe harbor" not by a reasonableness standard, but by a survival requirement: "Corporate . . .

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119. *See supra* Part IIIA.

120. *See Rhee, supra* note 2, at 669–72. A "material adverse change" clause in a merger agreement provides that the agreement may be voided if the financial condition of one party changes in drastic, unforeseeable ways before the merger is completed.

121. *See id.* at 673.

122. *Id.* at 696–97.

123. *Id.* at 704–05. This was not the purpose of Rhee's insightful and thought-provoking piece; my comment here is simply clarifying, it is not a criticism.

124. *Id.* at 710. Rhee also believes that self-preservation would provide a strong practical limitation on profit-sacrificing conduct in his contemplated safe-harbor: "The instinct for market self-preservation and personal self-interest are powerful constraints on a desire to provide overly generous provision of aid to the impairment of the corporate enterprise." *Id.* at 709.



suicide is not an aspirational end of corporate law. . . . [A] reasonable limiting principle may be that the board would be irrational when it takes action knowing *ex ante* that its action would impair the corporation . . . as a going concern.”<sup>125</sup>

Rhee compares his approach to the “necessity” rule in tort law, which excuses a violation of ordinary property rights when doing so allows the (heroic) tortfeasor to prevent extreme personal or public harm at the expense of the property interest.<sup>126</sup> It is a bit of a strained analogy, Rhee admits, since directors are not strangers to the tort victims (the shareholders), as is the traditional necessity tortfeasor.<sup>127</sup> Indeed, directors are fiduciaries of the shareholders. This is presumably why Rhee seeks a statutory imprimatur to his shareholder primacy “safe harbor” program, rather than relying entirely on tort law. To buttress his appeal to section 122(12), Rhee offers an interesting (but ultimately unavailing) textual analysis of the statutory phrase “aid of governmental authority”:

The plain meaning of “aid” is “help given[;] tangible means of assistance (as money or supplies).”<sup>[128]</sup> The historical definition is a “subsidy or tax granted to the king for an *extraordinary* purpose” as well as a “benevolence or tribute (i.e., a sum of money) granted by the tenant to his lord in times of *difficulty and distress*.”<sup>129</sup>

He continues, “[t]his etymology is meaningful in the context of the DGCL. Under section 122(12), a corporation would have the specific and broad power to make a corporate acquisition for the purpose of aiding governmental authority during a global financial meltdown.”<sup>130</sup> Rhee relies on his historical definition of “aid” as support for a necessity *limitation* on the section 122(12) power. For Rhee, this limitation is paramount because he wants to ensure the usual dominance of the shareholder primacy norm in corporate operations, which he advocates. But given the historical evolution of section 122(12) itself, in which the 1969 amendment *removed* the “in time of war or other emergency” qualification from the power to aid gov-

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125. Rhee, *supra* note 2, at 708.

126. *Id.* at 707–16.

127. *See id.* at 714.

128. *Id.* at 705 (citing WEBSTER’S NINTH NEW COLLEGIATE DICTIONARY 66 (9th ed. 1985)).

129. *Id.* (citing BLACK’S LAW DICTIONARY 80–81 (9th ed. 2009) (emphasis added)). The Black’s Law Dictionary historical definition from which Rhee quotes goes on to explain that, “[o]ver time, these grants evolved from being discretionary to *mandatory*. The three principal aids were: (1) to ransom the lord’s person if he was taken prisoner; (2) to contribute toward the ceremony of knighting the lord’s eldest son; and (3) to provide a suitable dowry for the lord’s eldest daughter.” *Id.* (emphasis added). Since § 122(12) clearly does not involve “mandatory” contributions to governmental authority, it would appear that this “historical definition” is of limited utility in construing the meaning of § 122(12).

130. Rhee, *supra* note 2, at 705 & nn. 269–70.

ernmental authority, this effort to restrict 122(12)'s authority to times of "difficulty and distress," is implausible.<sup>131</sup>

So there is not much textual or historical support for Rhee's construction of section 122(12). But his treatment nevertheless provides an occasion to reflect on what *might* be normatively desirable in something like a section 122(12) in corporate law. After all, if Rhee's argument is sound, Delaware could amend its statute to provide for it.

Rhee wants the profit-sacrificing aid to government power to be used only in those situations where the cost-benefit analysis in a specific situation "overwhelmingly weighs in favor of such action."<sup>132</sup> This is because Rhee accepts that, in the ordinary course, social utility is advanced by adherence to the shareholder primacy norm in corporate governance.<sup>133</sup>

Taking the historical perspective on the development of corporate law that I have pursued in this Article helps highlight the post-hoc nature of justifications for the shareholder primacy. Let us briefly review those justifications as articulated by legal theorists, though not by those who crafted our corporate law.<sup>134</sup> The best defense of shareholder primacy in corporate governance is that it is the rule that gives capital the confidence it needs to invest in corporate enterprises that create wealth, jobs, and affordable consumer goods. Once having contributed their capital, shareholders cannot demand the firm buy back their shares, nor will the shareholders have any significant control over how their capital is deployed by firm managers. Nevertheless, legally enforceable (and ethically compelling) bonds of fiduciary obligation can help ensure directors "work hard and honestly" on behalf of shareholders.<sup>135</sup> Workers and consumers, on the other hand, do not need fiduciary-type attention in firm governance because they can attend to their own stakes in corporate operations through labor contracts and take-it-or-leave-it decisions at the cash register. Where firms are able to exploit employees or workers, or non-contracting parties in local or distant communities, shareholder primacists insist that it is better to have external govern-

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131. *See supra* Part II(B).

132. *See Rhee, supra* note 2, at 663. It is not clear whether Rhee intends board or bench to have the bigger say in the calculation of this cost-benefit analysis. Is the decision to deviate from shareholder primacy in a particular instance given business judgment rule protection, substantive reasonableness reviews, or is it subject to some other standard? Ordinary tort law does not defer to the informed, deliberate, disinterested judgment of the tortfeasor, but instead imposes an objective reasonable person standard (sometimes construed as an objective cost-benefit standard).

133. *Id.* at 663–64.

134. There are several good summary justifications for the shareholder primacy norm available from its stalwarts. Among the most accessible is STEPHEN M. BAINBRIDGE, *THE NEW CORPORATE GOVERNANCE IN THEORY AND PRACTICE* (2008). *See also* Henry Hansmann & Reinier Kraakman, *The End of History for Corporate Law*, 89 *Geo. L.J.* 439 (2001).

135. This memorable summary of the bounds of fiduciary obligation in the corporate context comes from the seminal FRANK H. EASTERBROOK & DANIEL R. FISCHEL, *THE ECONOMIC STRUCTURE OF CORPORATE LAW* 91 (1991).

ment regulations curb corporate overreach, rather than detract from the utility of single-minded, shareholder-oriented governance in the boardroom.

Historically, policymakers and ordinary people evinced skepticism about the ability of government to bridle large aggregations of capital focused singularly on the pursuit of profit.<sup>136</sup> And this skepticism was well-grounded, because the shareholder primacy story does not add up. Once directors are charged with focusing only on shareholders, they will predictably pursue profits at the expense of workers, consumers, and the communities in which they operate, when they can get away with it. They will try to do this in ways they have been seen to do it—by skimping on worker safety, manipulating consumer risk perceptions, and polluting the environment. The social utility of shareholder primacy is brought into doubt by this logic (and experience), and it can find no viable escape hatch through its defenders' promise of external government regulation to curb such exploitative corporate activities. Reliance on such regulation is implausible because of the skillful presence of profit-maximizing firms within the very legislative arena that shareholder primacy theorists *count on* to restrain exploitative corporate conduct. The Supreme Court's opinion in *Citizens United v. Federal Election Commission* gives corporations a constitutional right to operate in that legislative domain. So long as *Citizens United* is good constitutional law, shareholder primacy will be bad corporate theory.<sup>137</sup>

As a supporter of the baseline shareholder primacy norm in corporate governance, Rhee wants policymakers to adopt only a very narrow exception in times of emergency, when the social-utility cost-benefit analysis clearly points in favor of attending to non-shareholder interests.<sup>138</sup> Thus, Rhee would allow Bank of America to deviate from the shareholder primacy norm to complete a merger that would help keep a credit crisis from becoming a credit catastrophe. But before and after the crisis, the Bank of America Board would again be strapped firmly in the shareholders' yolk. The irony is that the acute social crisis to which Rhee would permit (not

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136. See generally MICKLETHWAIT & WOOLDRIDGE, *supra* note 4.

137. *Citizens United v. Federal Election Commission*, 558 U.S. 310 (2010).

138. Rhee's "necessity" exception is not itself clearly defined, and may give shareholder primacists pause for its nebulosity. Rhee writes that "[t]he financial crisis of 2008 was unquestionably a 'national emergency' of the highest order, and closing the Merrill acquisition was in the public interest." Rhee, *supra* note 2, at 702. But I have no way of knowing whether that is true. To be sure, a lot of people were saying that there was a "national emergency," but there were also reasonable people claiming that there was no real emergency, or that the best thing to do in the face of the emergency, or to avert a greater emergency, was to allow failing financial institutions to fail. He claims that, "[t]he nature of crises, being what they are, is fairly indisputable." *Id.* at 709. But that is not true. Is the obesity epidemic a crisis? Was the war in Iraq? Is the war on terror? I spent the evenings while drafting this paper reading John Steinbeck's *THE GRAPES OF WRATH* (1939), and am left with the certain impression that one person, or class, or region, or industry's crisis, is another's business as usual. In tort law, someone, a judge or jury, has to *decide* that the "necessity" defense is valid.

require)<sup>139</sup> Bank of America to respond was itself undoubtedly, at least in part, a *product* of the unchecked operation of the shareholder primacy norm in the ordinary course of American business.<sup>140</sup> The more coherent and challenging conclusion from this and similar episodes would seem to be that the shareholder primacy norm itself is a threat to social utility when allowed to operate in the ordinary course. Socially conscious corporate governance should be the norm, not the exception that cleans up the mess that shareholder exclusivity in firm governance predictably makes.

Recounting the history of section 122(12) can serve to rekindle an attitude towards corporate social responsibility that the forgers of our corporate law considered a legitimate, even fundamental, aspect of what corporate law and corporate lawmakers should be doing. This pedigree should embolden corporate law reformers, who should see themselves as endeavoring to fulfill a historical legacy, even as they work for corporate law's future.

In light of this history, and the faulty logic and experience of shareholder primacy, I advocate a reform of corporate governance standards that would require directors to attend to the interests of multiple stakeholders, not just shareholders. To operationalize multi-stakeholder governance, corporate directors could be compelled to apply the same elixir that mainstream corporate theory already relies on to promote sound corporate operations: open, honest deliberation about the stakes of corporate decision-making, but now as they relate to all stakeholders impacted by the firm, not shareholders alone. Without micro-managing the substance of directorial decision-making, corporate law may nevertheless require that directors become informed about, think about, and earnestly talk about the consequences of corporate conduct for multiple stakeholders. This kind of fulsome conversation within our corporations might help theorists and

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139. Rhee, *supra* note 2, at 734 (“I do not advocate an affirmative duty to rescue. A shift from an informed, voluntary action of a board to a legal mandate for a rescue would swing the pendulum too far in favor of sacrificing private property for the public welfare.”).

140. Proving some causal relationship between shareholder primacy and the subprime mortgage crisis is beyond the scope of this Article. For present purposes my point is made if the reader considers it plausible that the crisis is an example of the kind of policy failure that my analysis of shareholder primacy predicts will be commonplace under that corporate governance paradigm. For critical evaluation of the role that corporate governance law played in the subprime mortgage fiasco, see Claire A. Hill & Brett H. McDonnell, *Reconsidering Board Oversight Duties After the Financial Crisis*, 2013 U. ILL. L. REV. 859, 860 (2013) (“Corporate behavior in the crisis yielded enormous negative externalities for the greater society.”); Christopher M. Bruner, *Corporate Governance Reform in a Time of Crisis*, 36 J. CORP. L. 309, 313 (2011) (“While a full explanation of the crisis lies well beyond the scope of this Article—and likely far in the future—it is patently clear that excessive risk-taking to boost financial firm stock prices must figure prominently in any account of the financial and economic crisis emerging in 2007.”); Nicholas Calcina Howson, *When “Good” Corporate Governance Makes “Bad” (Financial) Firms: The Global Crisis and the Limits of Private Law*, 108 MICH. L. REV. FIRST IMPRESSIONS 44, 44 (2009) (“In this case, however, more effective corporate governance may not be a serious part of the solution; instead, ‘good’ (or effectively functioning) corporate governance may have been one of the major factors that contributed to the global financial meltdown.”).

policymakers better assess what regulatory structure, internal or external to our corporations, will be required to improve the social utility of corporate law.

The current, facial ambiguity of section 122(12) impedes this kind of broad, reformative agenda. Its ambiguity hampers the development of a clearly thought-out and articulated call for corporate governance changes that would require corporations to behave in a more socially responsible fashion. The human propensity to engage in motivated reasoning is exacerbated by ambiguous data, which the mind exploits by bending to fit a thinker's preferred conclusion.<sup>141</sup> The broad history of section 122(12) reveals an intention to give corporate directors the power to pursue socially desirable ends irrespective of the impact on shareholders. Under prevailing Delaware jurisprudence, the provision is unlikely to be given such a construction. But its continued presence in the statute provides rhetorical conciliation to those who are motivated to find social responsibility already provided for in prevailing corporate law. Section 122(12) is a mirage of corporate social responsibility, with no substantive importance.<sup>142</sup> But it is a mirage that threatens to distract from the corporate social responsibility movement's progress towards a genuine system of multi-stakeholder governance.

Even if a non-shareholderist understanding of section 122(12) was adopted by the Delaware courts, the power described in it would be inadequate to the task of enabling socially responsible corporate governance. The power as written is a strictly permissive one, exercised only if directors choose. Highly competitive markets for capital and management, the exclusivity of the shareholders' power to elect directors, and contemporary corporate cultural expectations, are likely to keep merely permissive directorial discretion focused on shareholder interests. To overcome these structural dynamics, corporate governance reforms must pursue mandatory attention to the interests of multiple stakeholders at the level of firm governance. Programmatically, this kind of reform would likely require a federalization of corporate chartering, as a pro-social reform in one state would quickly be supplanted by a race back towards the present regime by other states looking to cash-in by selling shareholder primacy charters. This too would resuscitate a legacy of section 122(12), the earliest version of which was borrowed from a Model Act that started off as a project to draft a federal chartering statute.<sup>143</sup>

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141. See Jon Hanson & David G. Yosifon, *The Situational Character: A Critical Realist Perspective on the Human Animal*, 93 GEO. L.J. 1, 90–120 (2004) (examining the social scientific research on “motivated reasoning”).

142. See Ronald Chen & Jon Hanson, *The Illusion of Law: The Legitimizing Schemas of Modern Policy and Corporate Law*, 103 MICH. L. REV. 1 (2004).

143. See *supra* text accompanying note 17.

## V. CONCLUSION

The foregoing analysis leads me to conclude that Delaware should clarify what it intends to authorize through section 122(12). Delaware case law clearly specifies that all corporate decisions must be taken with the good faith motive to advance shareholder interests. This jurisprudence looms large because the statute itself is generally silent on the question of corporate beneficiary. Section 122(12), by its language and history, is at least in tension with, and might fairly be understood as directly contradicting, this judicial construction. Delaware legislators may be content to wait for their judiciary to interpret section 122(12) within the shareholder primacy paradigm. Or (much less likely), the legislature may wait until a court, forced by litigants to rule on the section, concludes that Delaware's shareholder primacy case-law has been wrong all along, at which point the legislature would probably overturn the decision, but not without providing an occasion for considerable uproar from those concerned about the social responsibility of corporations. It is only fortune, or perhaps its opposite, that has kept the provision from being litigated to date. As the leading corporate law jurisdiction in the known universe, Delaware takes particular pride in providing certainty and predictability. It should thus clarify what section 122(12) does or does not do.

Normatively, such clarification would also be desirable for those who are broadly concerned with the legal foundations of corporate social responsibility. To the extent that there is ambiguity in the statute, there is a real risk that the ambiguity will manifest in such a way as to give the superficial appearance that corporations are formally authorized to act in a socially responsible way, even as risk-averse lawyers, managers, and directors interpret the law as providing no such leeway when social concerns conflict with shareholder interests. While it would be helpful for directors to know they have the latitude to consider non-shareholder interests if they so desire, my view is that this power, even if it were recognized, would be inadequate to encourage socially responsible corporate behavior. Directors of publicly traded corporations should be obliged to actively consider the interests of multiple stakeholders, not just allowed to do it if they so desire. This obligation should extend to consideration of the impact of corporate activity on the firm's constituencies in ways that are not directly related to furthering government authority, or, indeed, which may conflict with government authority.