

SHAREHOLDER WEALTH MAXIMIZATION: VARIATIONS ON A THEME

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INTRODUCTION

In the corporate law imagination, no case symbolizes the end of managerialism and the triumph of the shareholder wealth maximization norm better than *Revlon, Inc. v. MacAndrews & Forbes Holding, Inc.*¹ Decided in the midst of the hostile takeover decade of the 1980s, the case has given rise to Revlon duties, namely the idea that when a “company was for sale . . . directors . . . [were] charged with getting the best price for the

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1. *Revlon, Inc. v. MacAndrews & Forbes Holding, Inc.*, 506 A.2d 173 (1986).

stockholders. . . .² By 1994, “a sale” was interpreted to include a change in control,³ and by 2009, with the development of the standard of good faith, the directors’ charge became not to “utterly fail[] to attempt to obtain the best price.”⁴ Still, *Revlon* remains fundamental. As Leo E. Strine Jr., former Chief Justice of the Delaware Supreme Court, writes, “in the discussion of what directors must focus on as their central goal, within the limits of their legal discretion, *Revlon* is central, and clearly states a board can only consider the interests of other constituencies if ‘rationally related benefits accru[e] to the stockholders.’”⁵

Justice G.T. Moore who wrote the decision in *Revlon* did not reference a precedent to support the idea that shareholder wealth maximization should guide directors seeking to sell their company.⁶ More broadly, the origins of the shareholder wealth maximization ideal remain unexplored. As Karen Ho writes in her ethnography of Wall Street, “despite its ubiquity and dominance in American capitalism, ‘shareholder value’ continues to be a black box, an uninterrogated concept that desperately needs to be contextualized within particular power relationships, institutional configurations, and a specific interpretation of financial history.”⁷

This Article begins to unpack the history of corporate law’s presumed commitment to shareholder value, offering a new framework by which to assess corporate law’s devotion to shareholder wealth maximization. Using three cases, each marking a different stage in the history of corporate law and theory—the early-twentieth-century *Dodge v. Ford Motor Co.* (out of Michigan), the midcentury *Bayer v. Beran* (out of New York), and the late-century *Revlon* (out of Delaware)—this Article examines how the shareholder wealth maximization idea emerged and developed and its bearing on the law of corporate purpose. Specifically, this Article explores how, in each period, distinct concerns for minority shareholders led courts to use the language of profit maximization not to impose affirmative duties

2. *Id.* at 182.

3. *Paramount Commc’ns, Inc. v. QVC Network, Inc.*, 637 A.2d 34 (Del. 1994).

4. *Lyondell Chem. Co. v. Ryan*, 970 A.2d 235, 244 (Del. 2009).

5. Leo E. Strine, Jr., *The Dangers of Denial: The Need for a Cleareyed Understanding of the Power and Accountability Structure Established by the Delaware General Corporation Law*, 50 WAKE FOREST L. REV. 761, 767 fn. 20 (2015).

6. See also *Dodge v. Ford Motor Co.*, 204 Mich. 459, 507 (1919) (holding, without precedent, that “[a] business corporation is organized and carried on primarily for the profit of the stockholders”); *eBay Domestic Holdings, Inc. v. Newmark*, 16 A.3d 1, 34–35 (Del. Ch. 2010) (failing to include precedent for the conclusion that “directors of a for-profit Delaware corporation cannot deploy a [policy] to defend a business strategy that openly eschews stockholder wealth maximization.”).

7. KAREN HO, *LIQUIDATED: AN ETHNOGRAPHY OF WALL STREET* 123 (2009).

on directors and executives nor to define a single corporate purpose, but simply to assure minority shareholders that corporations were run for their benefit so as to promote equity investment and the continued success of the securities markets.

The first part, *1900s-1930s: The Progressive Origins of Shareholder Wealth Maximization*, explores the shareholder primacy idea in the early twentieth century. Placing *Dodge* and the famous debate between Adolf A. Berle and E. Merrick Dodd about directors' duties and corporate social responsibilities in their historical context, I argue that Progressive jurists viewed the requirement that corporations maximize shareholder wealth as a means of sanctioning the power of those in control (typically controlling shareholders who also served as corporate directors and executives) while protecting minority shareholders against potential abuse of power by the control group.

The second part, *1940s-1950s: The Individual Minority Shareholder in Court*, probes *Bayer* to demonstrate how, in the midcentury years, discussions about shareholder wealth maximization were buried within the analysis of directors' duties, especially their duty of loyalty. I argue that in the 1940s, the New York courts, for example, sought to balance boosting entrepreneurial freedom with assurances to individual shareholders, who were typically invested for steady income and who had little control over the affairs of their companies, that their investments would yield profit. As the courts moved away from strict prohibition of conflict-of-interest transactions to the more relaxed standard of fairness, and thus were more likely to affirm managerial power and discretion, judges also attempted to assure plaintiffs that, in fact, their corporations were profitable. By making wealth maximization, if only in *dicta*, an aspect of the discussion of fiduciary obligations, by bringing together profitability and loyalty, these midcentury cases planted the seeds for the late-twentieth-century discourse of shareholder profit maximization.

The third part, *1960s-1980s: Fairness and Profit in the Age of Finance*, focuses on Delaware courts in the second half of the twentieth century. It examines how in the 1960s, as these courts embraced the idea that managers should have broad discretion, shielded from liability by the presumption of the business judgment rule, they gradually made efficiency the only matrix by which directors' actions could be evaluated. By the 1980s, as President Reagan's deregulation policies helped unleash a wave of hostile takeovers, the Supreme Court of Delaware brought this matrix to bear upon its analysis of fiduciary duties when directors engaged in friendly mergers or responded to hostile tender offers. Just as large corporations and well-to-do financiers replaced the minority, individual shareholder as the typical plaintiff in

corporate litigation, the Delaware courts made share price an element of the fairness standard for assessing directors' decisions. Like similar assertions throughout the twentieth century, *Revlon's* charge that directors must get "the best price for the stockholders at a sale of the company" was thus a statement about the standard of review applicable in cases involving allegations of a breach of the duty of loyalty, not about corporate purpose.

In 1992, legal historian Morton Horwitz noted that "an important task of legal theory . . . is to uncover the specific historical possibilities of legal conceptions—to 'decode' their true concrete meanings in real historical situations."⁸ Three decades later, the rules governing the relationship between directors, officers, and shareholders continue to be discussed in abstract. Little, if any, attention is given in corporate law scholarship to the social, cultural, or political circumstances that influenced courts' decisions. By exploring the shareholder wealth maximization idea in the contexts in which it developed throughout the past century, this Article demonstrates that the norm is nothing more than rhetoric, developed not to ensure that shareholders profit, but rather to assuage minority shareholders' concerns while, in fact, sustaining the absolute discretion of corporate managers. In so doing, I hope this Article sheds light not only on our understanding of corporate law's commitment to shareholder value, but also on the significance of context to the study of corporate law.

I. 1900-1930S: THE PROGRESSIVE ORIGINS OF SHAREHOLDER WEALTH MAXIMIZATION

Proponents of the proposition that corporate directors must maximize value for the corporation's shareholders often trace the idea back to two early-twentieth-century sources: the Michigan Supreme Court's 1919 decision in *Dodge v. Ford* and Adolf A. Berle's statements in his early-1930s scholarly debate with E. Merrick Dodd. As I elaborate below, neither *Dodge* nor Berle embraced the idea that shareholder wealth maximization was corporate law's purpose. Rather, both reflected the early-twentieth-century favor for protecting minority shareholders against abuse of power by those in control.⁹

8. MORTON J. HORWITZ, *THE TRANSFORMATION OF AMERICAN LAW 1870-1960: THE CRISIS OF LEGAL ORTHODOXY* 106-07 (1992).

9. On corporate purpose in the early twentieth century, see generally Dalia T. Mitchell, *From Dodge to eBay: The Elusive Corporate Purpose*, 13 VA. L. BUS. REV. 155, 163-180 (2019).

A. “One of the most famous corporate cases of all time”¹⁰

The saga of *Dodge v. Ford* began in 1903, when John and Horace Dodge, then owners of an auto-parts making business, entered an exclusive agreement with Henry Ford to supply parts to the new Ford Motor Company. Ford, who had suffered successive business failures, could not pay for the initial parts, and instead offered the Dodge brothers fifty shares each of the Ford Motor Company’s one thousand authorized and issued common stock in exchange for their notes of \$5,000 each.¹¹ Under Ford’s control, the Ford Motor Company was extremely successful and the Dodge brothers, as shareholders, received large amounts of special dividends.¹² But in 1916, Ford had decided to stop paying special dividends, announcing that he intended to put the profits back into the company, hire more employees, and further reduce the price of Ford cars.¹³ The Dodge brothers, who by 1913 stopped making parts for the Ford Motor Company and began manufacturing their cars, sued, claiming that Ford’s actions turned the company into a semi-eleemosynary institution in violation of its charter.¹⁴ Chief Justice Ostrander held for them, stating:

A business corporation is organized and carried on *primarily* for the profit of the stockholders. The powers of the directors are to be employed for that end. The discretion of directors is to be exercised in the choice of means to attain that end and does not extend to a change in the end itself, to the reduction of profits, or to the non-distribution of profits among stockholders in order to devote them to other purposes.¹⁵

Since then, many have turned to *Dodge v. Ford* to justify the proposition that corporations’ sole responsibility is to maximize profit to their shareholders (often ignoring the qualifier “primarily” in the quote

10. Geoffrey Miller, *Narrative and Truth in Judicial Opinions: Corporate Charitable Giving Cases*, 2009 MICH. ST. L. REV. 831, 833 (2009).

11. M. Todd Henderson, *The Story of Dodge v. Ford Motor Company: Everything Old is New Again*, in CORPORATE LAW STORIES 37, 47–48 (J. Mark Ramseyer ed., 2009).

12. Miller, *supra* note 10, at 833.

13. *Dodge v. Ford Motor Co.*, 204 Mich. 459, 465, 490, 505 (1919) (“‘My ambition,’ said Mr. Ford, ‘is to employ still more men, to spread the benefits of this industrial system to the greatest possible number, to help them build up their lives and their homes. To do this we are putting the greatest share of our profits back in the business.’”).

14. *Id.* at 504; *see also* Miller, *supra* note 10, at 835 (discussing the lawsuit and critiquing the court’s claim that Ford’s actions were charitable).

15. *Dodge*, 204 Mich. at 507 (emphasis added).

above).¹⁶ Others have suggested that the decision did not aim to determine a purpose for corporations but rather to protect minority shareholders from the power of those in control.¹⁷ Notably, a careful reading of the case reveals that the legal doctrine according to which the case was decided is rather vague. Placing *Dodge* in its historical context indeed suggests a more tentative reading of Ostrander's statement. As I elaborate below, *Dodge* was a transitional case, situated between the nineteenth-century approach to protecting minority shareholders in closely held corporations and the early twentieth-century's emerging concerns about the power that corporations, especially the growing publicly held corporations, and their control group held over individual investors and the economy at large.

Minority shareholders have historically been in a precarious situation. As Naomi Lamoreaux and Jean-Laurent Rosenthal documented, those in control “negotiated contracts with other companies in which they had a financial interest, elected themselves to corporate offices at lucrative salaries that they themselves set, arranged mergers that earned themselves impressive capital gains while leaving other shareholders in the lurch, and engaged in a wide variety of other actions” benefiting themselves at the expense of other corporate constituencies.¹⁸ And minority shareholders had few if any effective tools to protect their interests against the control group's abuse of power. Voluntary dissolution was not available and, typically, minority shareholders did not own enough stock to elect a new slate of directors. If the company was publicly traded, shareholders might have been able to sell their shares but generally “at a price discounted to reflect the majority's behavior.”¹⁹ If the company was closely held, as it often had been, “the only buyers for their shares were the same majority shareholders with whom they were in conflict.”²⁰ As Lamoreaux and Rosenthal conclude, controlling

16. See, e.g., Stephen M. Bainbridge, *In Defense of the Shareholder Wealth Maximization Norm: A Reply to Professor Green*, 50 WASH. & LEE L. REV. 1423 (1993) (arguing that *Dodge v. Ford* supports the idea that shareholder profit maximization is corporate law's “fundamental norm.”).

17. See, e.g., Lynn Stout, *Why We Should Stop Teaching Dodge v. Ford*, 3 VA. L. & BUS. REV. 164, 166–168 (2008) and citations there (arguing that the decision in *Dodge v. Ford* intended to protect minority shareholders from oppressive actions by those in control, not to articulate a purpose for corporations).

18. Naomi R. Lamoreaux & Jean-Laurent Rosenthal, *Corporate Convergence and the Plight of Minority Shareholders in the United States before the Great Depression* 3–4 (2004), available at www.nber.org/papers/w10900 [<https://perma.cc/5WFX-JCUC>].

19. *Id.* at 4.

20. *Id.*

shareholders were “effectively dictators.”²¹

In 1832, the New York court held that “stockholders might, after demonstrating that the corporation was controlled by those who were abusing their trust, file a bill in their own names, ‘making the corporation a party defendant.’”²² In so empowering minority shareholders “to sue on behalf of the corporation when the corporation will not or is unable to do so,” the court “recognized that noncontrolling shareholders needed a legal recourse when defrauded or otherwise treated inequitably by those who did control the corporation.”²³ Courts in other states followed suit, and in 1855, so did the U.S. Supreme Court.²⁴ Still, because at the time, most corporations were closely held and controlled, with a few, if any, public shareholders, the derivative action was rarely used.²⁵

Trust law offered “justification[s] for the intervention of equity to prevent fraud,” and courts stressed that where directors or controlling shareholders “acting in bad faith, carry into effect a scheme which, even if lawful upon its face, is intended to circumvent the minority stockholders and defraud them out of their legal rights,” courts would “remedy the wrong.”²⁶ But courts were restrained in determining “what constituted an abuse of trust by those in control.”²⁷ Seeking to encourage the growth of corporations, they

21. *Id.* at 14. Commonly, the power struggle at the time was between minority and controlling shareholders, and “this struggle, furthermore, took place in corporations that had far fewer shareholders than the publicly traded leviathans of the twentieth century.” Harwell Wells, *A Long View of Shareholder Power: From the Antebellum Corporation to the Twenty-First Century*, 67 FLA. L. REV. 1033, 1036 (2015).

22. Lamoreaux & Rosenthal, *supra* note 18, at 22. See also *Robinson v. Smith*, 3 Paige 222 (1832) (holding that the corporation was a necessary party in a lawsuit brought by its stockholders against its directors).

23. Wells, *supra* note 21, at 1048.

24. Jessica Erickson, *The Lost Lessons of Shareholder Derivative Suits*, 77 WASH. & LEE L. REV. 1131, 1141 (2020); *Dodge v. Woolsey*, 59 U.S. 331 (1855). See also John Matheson, *Restoring the Promise of the Shareholder Derivative Suit*, 50 GA. L. REV. 327, 344 (2016) (“This recognition of the derivative suit solidified the concept of holding directors and officers of corporations accountable for their actions”); George D. Hornstein, *Problems of Procedure in Stockholder’s Derivative Suit*, 42 COLUM. L. REV. 574, 574 (1942) (“For more than a hundred years it has been established that . . . [w]here a corporation has been injured and should sue, but refuses or neglects to do so, a stockholder may maintain a suit in equity on its behalf”).

25. JOHN C. COFFEE, *ENTREPRENEURIAL LITIGATION: ITS RISE, FALL AND FUTURE* 33 (2015).

26. Chester Rohrllich, *Suits in Equity by Minority Stockholders as Means of Corporate Control*, 81 U. PA. L. REV. 692, 695 (1933) (quoting the New York Court of Appeals in *Flynn v. Brooklyn City R.R. Co.*, 158 N. Y. 493, 507–8 (1899)).

27. Lamoreaux & Rosenthal, *supra* note 18, at 23. Lamoreaux and Rosenthal note that, at least in part, the courts’ reluctance to intervene was their concern that by protecting minority

were reluctant to intervene in a corporation's affairs (and the affairs of those in control) to protect the interests of minority shareholders unless the latter could demonstrate "gross fraud or abuse of trust" harmful to the corporation or the shareholders.²⁸ As the United States Supreme Court declared in *Hawes v. Oakland*, to sustain litigation "in a court of equity in his own name," a minority shareholder would have to show

a fraudulent transaction completed or contemplated by the acting managers, in connection with some other party, or among themselves, or with other shareholders as will result in serious injury to the corporation, or to the interests of the other shareholders; Or where the board of directors, or a majority of them, are acting for their own interest, in a manner destructive of the corporation itself, or of the rights of the other shareholders; Or where the majority of shareholders themselves are oppressively and illegally pursuing a course in the name of the corporation, which is in violation of the rights of the other shareholders²⁹

Most significantly, "shareholders could not sue officers and directors of corporations simply because they pursued policies that the former thought were wrongheaded or disadvantageous. Such disagreements were matters of business judgment and, as such, beyond the purview of the courts."³⁰

Why, then, didn't the Supreme Court of Michigan view the conflict between the Dodge brothers and Ford merely as a disagreement about business judgment? Fortunately for John and Horace Dodge, in the nineteenth century, "corporations were expected to pay profits out in regular dividends unless prevented by financial difficulty."³¹ And courts were more likely to intervene when the control group stopped payments of dividends while continuing to pay itself salaries, a practice known as freezing-out minority shareholders.³² Ford stopped paying special dividends so that he

shareholders, they might "undermin[e] the legal differences between corporations and partnerships" by "creating a situation in which disagreements among members of the firm could disrupt the functioning of corporations as easily as they did partnerships." *Id.* According to Lamoreaux and Rosenthal, "for this reason, the courts were very conservative in defining what constituted an abuse of trust by those in control." *Id.*

28. Ruth H. Bloch & Naomi R. Lamoreaux, *The Private Rights of Organizations: The Tangled Roots of the Family, the Corporation, and the Right to Privacy* 52 (2007), available at <http://www.econ.ucla.edu/people/papers/Lamoreaux/Lamoreaux468.pdf> [<https://perma.cc/K9XD-TJQ8>].

29. *Hawes v. Oakland*, 104 U.S. 450, 460 (1881). See also Bloch & Lamoreaux, *supra* note 28, at 44–52 (exploring the treatment of minority shareholders in nineteenth century corporate law).

30. Lamoreaux & Rosenthal, *supra* note 18, at 23.

31. Wells, *supra* note 21, at 1046.

32. Rohrlich, *supra* note 26, at 701.

could, presumably, reduce the price of his cars, but his actions resembled a typical freeze-out. Ostrander's opinion could thus be seen as extending to the Dodge brothers the common protection against the control group's abuse of their dividend power.³³

Moreover, as the following section I.B elaborates, by the time *Dodge* was decided, changes to the structure of corporations and investment that took place in the early twentieth century helped change jurists' attitudes toward minority shareholders and likely swayed the Michigan court's opinion, making *Dodge* a precursor for modern corporate law.

B. The Modern Corporation's Minority Shareholders

The reluctance of nineteenth-century courts to protect minority shareholders' interests reflected not only a commitment to the promotion of business and their managers, but also cultural attitudes toward investment in securities. For a large part of American history, ownership of private property has been considered the foundation of the republic.³⁴ Responsible citizenship was associated with ownership of productive property, not idle money. Even after the growth of corporations and the gradual abolition of property requirements for suffrage began to transform the cultural and legal understanding of proprietorship and citizenship, financial speculation remained an anathema to republican values.³⁵

The tide began to shift at the turn of the twentieth century. The financing of the railroads introduced public security financing of industry and helped change public opinion.³⁶ Beginning in the merger wave of the 1880s, rapid industrial and business growth increased the demand for capital.³⁷ Seeking to maximize their own profits, entrepreneurs found ways to convince the American public to invest in their enterprises, first in railroad bonds and industrial preferred stock, and then, by the second decade of

33. *Id.*; see also Note: *Minority Shareholders Suits to Compel Declaration of Dividends*, 64 HARV. L. REV. 299 (1950).

34. L.S. Zacharias, *Repaving the Brandeis Way: The Decline of Developmental Property*, 82 NW. U. L. REV. 596, 618 (1988).

35. JULIA C. OTT, *WHEN WALL STREET MET MAIN STREET: THE QUEST FOR AN INVESTORS' DEMOCRACY* 12–14 (2011).

36. *Hearings before the Committee on Interstate and Foreign Commerce, House of Representatives on H.R. 1493, H.R. 1821, and H.R. 2019 (bills to suspend the authority of the Securities and Exchange Commission under section 14(a) and section 14(b) of the Securities Exchange Act to issue rules relating to the solicitation of proxies, consents, and authorizations during the period of war emergency)*, 78th Cong. (June 9–11, 1943).

37. *Id.* at 3–4.

twentieth century, in common stock.³⁸ After the Liberty Bonds drives of World War I, investment in securities became associated with modern citizenship and the American democratic ideal.³⁹ Low-wage employees, women, and recent immigrants were all welcomed into and included within a new nation of investors.⁴⁰

At the same time, changes to state corporation laws have helped erode investors' ability to affect their corporations' affairs. These changes included the erosion of the *ultra vires* doctrine,⁴¹ the reintroduction of the idea that the board's power was "original and undelegated,"⁴² and the elimination of the shareholders' right to remove directors at will, all of which helped minimize shareholder control.⁴³ So too did changing voting rules. Proxy voting became the norm and states gradually adopted statutes allowing a simple majority of the shareholders to approve the sale of corporate assets, abolishing the nineteenth-century rule of unanimity.⁴⁴ The newly legalized holding company further undermined shareholders' power, allowing one corporation to control the majority of stock of many direct and indirect subsidiaries through pyramiding.⁴⁵ Limitations on the voting rights of certain classes of shareholders, including non-voting stock and conditional voting stock, also became common in the first decades of our century.⁴⁶

Indeed, despite growing number of equity investors, and perhaps due to

38. OTT, *supra* note 35, at 132.

39. *Id.* at 54–56; see also Janette Rutterford & Dimitris P. Sotiropoulos, *The Rise of the Small Investor in the US and the UK, 1895 to 1970*, 18 ENTERPRISE & SOCIETY 485, 490 (2017) ("In the United States, early common stock investors were primarily bankers and industrialists. It was not until after the merger boom of 1897 to 1904 that common stocks, and in particular preference shares were issued to fund the large corporations being formed and began to be held by a broader spectrum of investors, albeit a relatively small number in total.").

40. HO, *supra* note 7, at 180–81; Rutterford and Sotiropoulos, *supra* note 39, at 92–93. *But see* Sarah C. Haan, *Corporate Governance and the Feminization of Capital*, available at https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3740608 [<https://perma.cc/Q94A-77S5>] (exploring the role of women investors in the early twentieth century and the discriminatory attitudes they faced).

41. HORWITZ, *supra* note 8, at 77–78.

42. *Id.* at 99 (quoting *Manson v. Curtis*, 119 N.E. 559, 562 (N.Y. 1918)).

43. *Id.* at 88–89.

44. *Id.* (discussing the erosion of the unanimity rule in the early twentieth century); see also Adam Winkler, "Other People's Money": *Corporations, Agency Costs, and Campaign Finance Law*, 92 GEO. L. J. 871, 907–09 (2004) (noting how changes to corporate voting rules during the nineteenth century weakened shareholder control).

45. Winkler, *supra* note 44, at 907–08; W.H.S. Stevens, *Shareholders' Voting Rights and the Centralization of Voting Control*, 40 Q.J. ECON. 353, 354–55 (1926).

46. Stevens, *supra* note 45, at 362–67. See also Dalia Tsuk Mitchell, *Shareholders as Proxies: The Contours of Shareholder Democracy*, 63 WASH & LEE L. REV. 1503, 1522–27 (2006) (describing these different changes).

concerns about the influx of new investors,⁴⁷ the control of productive property remained concentrated in the hands of a few wealthy entrepreneurs and their investment bankers,⁴⁸ raising grave concerns among Progressive scholars about the potential for abuse of power by those in control and about the plight of the individual shareholder.⁴⁹ In 1904, Thorstein Veblen noted that “under corporate organization the owners of the industrial material have no voice in its management.”⁵⁰ In 1911, an article titled *Evils of Corporate Control* declared that “[t]he facility with which capital passes under the control of strong groups of individuals creates one of the most serious problems of modern times.”⁵¹ In 1913, the report of the Pujo (Banking and Currency) Committee announced the existence of a money trust, consisting of a small number of financiers sitting on multiple corporate boards. According to the report, these financiers controlled the economy with the assistance of the New York Stock Exchange, which allowed practices such as pooling and other stock price manipulation techniques to the detriment of working- and middle-class individual investors.⁵² And in 1914, shortly before he was appointed to the United States Supreme Court, Louis Brandeis explained that investment bankers became “[t]he dominant element in our financial oligarchy.”⁵³ They became promoters and directors of corporations, and were able, through their economic power, to control even those boards on which they did not sit.⁵⁴ By controlling other people’s money, Brandeis wrote, investment bankers and their associates could “control the people through the people’s own money.”⁵⁵

Calls for state and federal legislation to protect minority investors also mounted, becoming more vocal by the end of the First World War as corporations were trying to lure “citizen-investors holding excess cash from

47. See, e.g., Haan, *supra* note 40, at 14–19 (discussing the expansion of stockholding and the bull market in the 1920s).

48. See, e.g., Miguel Cantillo Simon, *The Rise and Fall of Bank Control in the United States: 1890–1939*, 88 AM. ECON. REV. 1077, 1081 (1998) (“By 1912, 18 financial institutions sat on the boards of 134 corporations with \$25.325 billion in combined assets. Of these 18 institutions, 5 banks . . . sat on the boards of 68 nonfinancial corporations with \$17.273 billion in assets . . . U.S. GNP in 1912 was \$39.4 billion.”).

49. Mitchell, *supra* note 46, at 1528–35.

50. THORSTEIN VEBLÉN, *THE THEORY OF BUSINESS ENTERPRISE* 146 (1904).

51. William E. Harmon, *Evils of Corporate Control*, 2 PROC. ACAD. POL. SCI. N.Y.C. 48 (1911).

52. OTT, *supra* note 35, at 32–33.

53. LOUIS D. BRANDEIS, *OTHER PEOPLE’S MONEY: AND HOW THE BANKERS USE IT* 4 (1914).

54. See *id.* at 1–27 (describing the confluence of factors supporting the concentration of power in investment bankers).

55. *Id.* at 17–18.

Liberty bond, War Savings, or Government Savings redemptions and interest payments.”⁵⁶ And courts supplemented calls for state and federal legislation by beginning to hold those in control of business enterprises to stricter obligations toward minority shareholders.⁵⁷ In 1914, Brandeis, concerned about the small investor, noted that:

The small investors, particularly the women, who are holding an ever-increasing proportion of our corporate securities, commonly buy on the recommendation of their bankers. The small investors do not, and in most cases cannot, ascertain for themselves the facts on which to base a proper judgment as to the soundness of securities offered. And even if these investors were furnished with the facts, they lack the business experience essential to forming a proper judgment.⁵⁸

Not surprisingly, in 1919, Justice Brandeis held that:

The rule of corporation law and of equity invoked is well settled and has been often applied. The majority has the right to control; but when it does so, it occupies a fiduciary relation toward the minority, as much so as the corporation itself or its officers and directors. If through that control a sale of the corporate property is made and the property acquired by the majority, the minority may not be excluded from a fair participation in the fruits of the sale.⁵⁹

Dodge, also decided in 1919, reflected a similar sentiment. “There should be no confusion (of which there is evidence),” Ostrander stressed, “of the duties which Mr. Ford conceives that he and the stockholders owe to the general public and the duties which in law he and his co-directors owe to protesting, minority stockholders.”⁶⁰ The duty to maximize profit to the shareholders applied only in the latter context.⁶¹

Notably, Horace and John Dodge, successful businessmen, were unlike

56. OTT, *supra* note 35, at 127.

57. See Douglas K. Moll, *Of Donahue and Fiduciary Duty: Much Ado About . . . ?*, 33 W. NEW ENG. L. REV. 471, 471–72 (2011) (describing the stricter obligations toward minority shareholders).

58. BRANDEIS, *supra* note 53, at 199–200.

59. *S. Pac. Co. v. Bogert*, 250 U.S. 483, 487–88 (1919).

60. *Dodge*, 204 Mich. at 507.

61. *Id.* Indeed, Ostrander was quick to emphasize, that

there is committed to the discretion of directors, a discretion to be exercised in good faith, the infinite details of business, including the wages which shall be paid to employees, the number of hours they shall work, the conditions under which labor shall be carried on, and the price for which products shall be offered to the public.

Id.

the individual shareholder on which Progressives' attention focused. For the typical minority shareholder, ownership of productive property was often improbable. Instead, employees found an investment in their employer's business a way to capture the profits to which they contributed, while women, who, after the Civil War, were gradually allowed to control their own property but continued to have limited employment opportunities, have found investment in stock a means of receiving regular income and supporting their families.⁶²

Still, at a time when corporations were seeking to convince investors, typically of middle-class background, to invest in their corporate stock while simultaneously lobbying for legal changes that minimized these investors' control, the Michigan court's statement in *Dodge* that "a business corporation is organized and carried on primarily for the profit of the stockholders"⁶³ was significant. Just as Michigan (like other midwestern states) was witnessing the rapid "rise of factory and decline of farm,"⁶⁴ Ostrander opted to encourage investment in factories by assuring minority shareholders that state courts would protect them from abuse of power by the control group. To do so, Ostrander, perhaps inadvertently, also turned the traditional limitation on the accountability of those in control (their fraud or abuse of trust had to have been detrimental to the corporation and its shareholders) into an affirmative duty to maximize profits. As the following section I.C explores, in the decade that followed *Dodge*, Progressive scholars, most notably Adolf A. Berle, Jr., brought a similar outlook to bear upon the fate of the more common, minority shareholder.

C. "[T]he privilege of taking the golden eggs laid by somebody else's goose"⁶⁵

The decade that followed *Dodge* witnessed an "unprecedented influx of new investors into the stock market."⁶⁶ In the early part of the 1920s, corporations marketed their shares directly, especially to their employees and customers, "in the hopes of repelling unionization and federal intrusions into labor relations" as well as deflecting antitrust suits.⁶⁷ By the second part of the 1920s, financial firms began to encourage investment in stock "as a

62. OTT, *supra* note 35, at 185–86.

63. *Dodge*, 204 Mich. at 505.

64. Craig R. Olson, *Michigan in the Twentieth Century*, 84 J. OF AM. HIST. 181, 182 (1997).

65. BRANDEIS, *supra* note 53, at 18.

66. OTT, *supra* note 35, at 169.

67. *Id.* at 152.

mechanism for subjecting corporate capitalism to democratic discipline.”⁶⁸

The growing numbers of individual investors exacerbated the need to protect minority shareholders from the power of control. As one editorial put it, “[m]any managements, swollen with power, came to believe that their enterprises had ceased to be reservoirs of trust funds for stockholders and creditors but had become agencies for their own private immediate gain.”⁶⁹ Huge salaries and bonuses, management’s participation in its own underwriting, using corporate funds to manipulate the market, and other forms of self-dealing became common.⁷⁰ Rather than being an “economic savior,” management turned out to be “often without vision, incapable of self-regulation, unmindful of duties to investors, and almost unaware of its responsibilities to society as a whole.”⁷¹

Adolf Berle, a Columbia Law School professor who would become a member of Franklin Roosevelt’s brain trust, shared the sentiment.⁷² In 1925, he cautioned that “power without responsibility is, philosophically, a perilous matter.”⁷³ As he elaborated, because management stock would likely be controlled by the investment banking house that served as a promoter for the corporation, “it [was] possible, if not probable, that there [would] be attractive opportunities for manipulation of securities, for negotiating favorable contracts with allied interests, or even for giving value to stock which represent[ed] no real investment.”⁷⁴ Given the “web of economic interests” which the investment banking house served and from which it made its profits, it was likely that management stock would be voted for transactions that benefited the investment banking house, or even the controlling groups, but not the controlled corporation.⁷⁵

For Berle, imposing strict fiduciary obligations on the control group was a means of protecting the new, individual minority shareholders. As he wrote, “with neither power nor information, the stockholder becomes merely the beneficiary—*cestui*—of the corporate management . . . Deprive him of any right by way of fiduciary relation, and the business becomes too

68. *Id.* at 169; see also JONATHAN BARRON BASKIN AND PAUL J. MIRANTI, JR., A HISTORY OF CORPORATE FINANCE 189–97 (1997).

69. *Business Versus the Public*, 8 ACCT. REV. 162, 163 (1933).

70. *Id.*

71. *Id.*

72. On Berle’s career, see generally JORDAN A. SCHWARZ, LIBERAL: ADOLF A. BERLE AND THE VISION OF AN AMERICAN ERA (1987).

73. Adolf A. Berle, Jr., *Non-Voting Stock and “Bankers’ Control,”* 39 HARV. L. REV. 673, 674 (1925–26).

74. *Id.* at 676.

75. *Id.*

hazardous to continue.”⁷⁶ Wishing himself to be the “Marx of the shareholder class,”⁷⁷ Berle’s work throughout the 1920s emphasized the need to protect minority investors from fraud and manipulative practices that, at the time, plagued the securities markets; he wanted to rein in the power of the control group. This work culminated in his 1931 article, titled *Corporate Powers as Powers in Trust*.⁷⁸

Published shortly after the 1929 market crash, *Corporate Powers as Powers in Trust* focused on the power to issue stock, the power to declare dividends, the power to amend the charter, and the power to engage in fundamental transactions. Berle declared that these corporate powers were held in trust for the benefit of shareholders.⁷⁹ While the courts had previously considered these and similar managerial powers a matter of contract law (perhaps because corporations were closely held) and thus susceptible to statutory changes and the possibility of opting out, Berle wanted to make these powers (especially in the context of publicly held corporations) a matter of the control group’s trusteeship duties.⁸⁰

Many have since suggested that Berle’s argument offered an early articulation of the shareholder wealth maximization ideal. For the most part, these assessments draw on the only response the article elicited, E. Merrick Dodd’s.⁸¹ Dodd’s vision of corporate management was one of public service. He wanted to validate corporate social policies that benefited different constituencies, including employees, consumers, investors, and the community at large, even when such policies resulted in diminution of profits for the shareholders. Announcing that he was “thoroughly in sympathy with Mr. Berle’s efforts to establish a legal control which [would] more effectually prevent corporate managers from diverting profit into their own pockets from those of stockholders,” Dodd stated that the corporation nonetheless had “social service as well as a profit-making function.”⁸²

Dodd’s characterization failed to recognize, however, that Berle was focused on protecting minority shareholders from the power of control, not on finding a purpose for the corporation. Not surprisingly, Berle, who did

76. Adolf A. Berle, *Publicity of Accounts, Management Purchase of Stock and Control of Security Value*, in *STUDIES IN THE LAW OF CORPORATIONS FINANCE* 180 (1928).

77. SCHWARZ, *supra* note 72, at 62; *see also* *NAVIGATING THE RAPIDS, 1918–1971: FROM THE PAPERS OF ADOLF A. BERLE* 26 (Beatrice Bishop Berle & Travis Beal Jacobs eds., 1973).

78. Adolf A. Berle, Jr., *Corporate Powers as Powers in Trust*, 44 *HARV. L. REV.* 1049 (1931).

79. *Id.*

80. *Id.* at 1050–72.

81. E. Merrick Dodd, Jr., *For Whom Are Corporate Managers Trustees?* 45 *HARV. L. REV.* 1145 (1932).

82. *Id.* at 1147–48.

not anticipate the rebuttal, responded promptly and swiftly. Lawyers, Berle wrote, “know what the social theorist does not,” namely that “when the fiduciary obligation of the corporate management and ‘control’ to stockholders is weakened or eliminated, the management and ‘control’ become for all practical purposes absolute.”⁸³ Accordingly, one could not “abandon emphasis on ‘the view that business corporations exist for the sole purpose of making profits for their stockholders’ until such time as [one is] prepared to offer a clear and reasonably enforceable scheme of responsibilities to someone else.”⁸⁴ Managers could be trusted to run corporations, but clear guidelines had to be set as to how they would perform their duties.

Within a year of its publication, Berle’s *Corporate Powers as Powers in Trust* was reprinted as chapter VII in *The Modern Corporation and Private Property*, a book Berle co-authored with Gardiner C. Means.⁸⁵ Careful to distinguish the duties of the control group from the broader question of corporate social responsibilities, Berle and Means stressed that “it is the purpose of this chapter to state this theory, with full realization of the possibility that private property may one day cease to be the basic concept in terms of which the courts handle problems of large scale enterprise and that the corporate mechanism may prove the very means through which such modification is brought about.”⁸⁶

Offering an example of a potential modification to the system of private property, *The Modern Corporation and Private Property* indeed concluded by proclaiming that shareholders, “by surrendering control and responsibility over the active property, have surrendered the right that the corporation should be operated in their sole interest,—they have released the community from the obligation to protect them to the full extent implied in the doctrine of strict property rights.”⁸⁷ If “the corporate leaders . . . set forth a program comprising fair wages, security to employees, reasonable service to their public, and stabilization of business, all of which would divert a portion of the profits from the owners of passive property,” the interests of the latter “would have to give way.”⁸⁸

For Berle, as it was for Justice Ostrander in *Dodge*, the duties those in

83. Adolf A. Berle, Jr., *For Whom Corporate Managers are Trustees: A Note*, 45 HARV. L. REV. 1365, 1367 (1932).

84. *Id.* (footnote omitted).

85. ADOLF A. BERLE, JR. AND GARDINER C. MEANS, *THE MODERN CORPORATION AND PRIVATE PROPERTY* 247–76 (1932).

86. *Id.* at 247.

87. *Id.* at 355.

88. *Id.* at 356.

control owed minority investors were not inconsistent with the corporation's broader duties toward the community at large.⁸⁹ An admirer of Louis Brandeis's work,⁹⁰ Berle called for federal regulation, supplemented by judicial enforcement of fiduciary obligations as a means of ensuring that individual shareholders could safely invest. While he did not necessarily believe in the ability of shareholders to participate in corporate management, Berle strongly believed in the potential effectiveness of fiduciary duties. Concerned that existing corporate statutes—especially the Delaware statute, “whose drafting and enactment [Berle] attributed to powerful New York business lawyers—gave managers extremely broad power without accompanying statutory limitations,”⁹¹ Berle viewed shareholders' disempowerment as a justification for imposing fiduciary duties on management and the control group for the benefit of the corporation and society. Indeed, by promoting shareholder protection, albeit not empowerment, Berle avoided addressing potential conflicts between the shareholders' perceptions of their interests and broader corporate goals.⁹²

As the following Part II explores, in the midcentury years, minority shareholders, informed by similar ideas yet more vocal about their interests, began challenging directors' and officers' actions as violations of their fiduciary obligations. In analyzing their cases, the courts developed the contours of directors' duties while also offering rhetoric to suggest that the directors' role was to maximize value for the shareholders. Part III will explore how, in the 1980s, the Delaware courts embedded this rhetoric in corporate law.

II. 1940S-1950S: THE INDIVIDUAL MINORITY SHAREHOLDER IN COURT

By the 1940s, concerns about the power of those in control dissipated as the New Deal regulatory state took shape,⁹³ and war-production helped

89. C.A. Harwell Wells, *The Cycles of Corporate Social Responsibility: An Historical Retrospective for the Twenty-First Century*, 51 KAN. L. REV. 77, 87 (2002). See also Rohrlich, *supra* note 26, at 696 (“That the corporation itself is a trustee for the stockholders is well settled. Nor is there any doubt that directors are ‘trustees’ for the corporation.”).

90. Jessica Wang, *Neo-Brandeisianism and the New Deal: Adolf A. Berle, Jr., William O. Douglas and the Problem of Corporate Finance in the 1930s*, 33 SEATTLE U. L. REV. 1221 (2010).

91. Leo Strine, Lawrence A. Hamermesh, R. Franklin Belotti, & Jeffrey M. Gorriss, *Loyalty's Core Demand: The Defining Role of Good Faith in Corporation Law*, 93 GEO. L. J. 629, 642 (2010).

92. For a detailed analysis of Berle's approach, see Mitchell, *supra* note 46, at 1532–35.

93. See, e.g., Herbert Hovenkamp, *The Classical Corporation in American Legal*

turn corporations and their managers from a threat to the American dream into a vehicle for achieving the American democratic ideal.⁹⁴ Corporate litigation changed, too. Rather than a tool in the hands of well-to-do minority shareholders against their corporation's control group, bringing suits became a means for minority shareholders to claim a place for themselves in corporate America. Their arguments pushed the courts to (re)define the duties of directors and officers and, if only in *dicta*, address their responsibility to maximize profits for the shareholders.

Notably, the cases did not directly examine the question of corporate purpose. As I have previously argued, midcentury cases explicitly analyzing corporate purpose, most notably *A.P. Smith Mfg. Co. v. Barlow*,⁹⁵ embraced the corporation as a quintessential American institution with obligations to ensure the survival of American democracy, for example, through charitable contributions.⁹⁶ In turn, the cases addressing claims of breaches of fiduciary obligations merely explained the appropriate role of corporate managers in ways that also focused on their corporations' profits.⁹⁷ As courts relaxed the standards of review by which directors' actions were measured so as to promote entrepreneurial freedom, they also sought to assure minority shareholders that their corporations were run to their benefit. Balancing both goals, the courts brought the question of profit to bear upon the developing business judgment jurisprudence.

Thought, 76 GEO. L. J. 1593, 1688 (1988) (noting that after the New Deal "little was left of the classical corporation" as the federal securities acts regulated its relationship with investors, federal labor laws regulated its dealing with workers, and antitrust laws regulated its relationship to consumers and suppliers).

94. See, e.g., SCOTT R. BOWMAN, *THE MODERN CORPORATION AND AMERICAN POLITICAL THOUGHT: LAW, POWER, AND IDEOLOGY* 185–91 (1996) (detailing the change in opinion towards the corporations and their managers).

95. *A. P. Smith Mfg. Co. v. Barlow*, 13 N.J. 145 (1953).

96. Mitchell, *supra* note 9, at 182–87.

97. For analyses of corporate purpose and the law of fiduciary obligations, see generally Lyman Johnson, *Law and the History of Corporate Responsibility: Corporate Governance*, 10 U. ST. THOMAS. L. J. 974 (2013) (detailing the limited role corporate law has played in impacting corporate responsibility); Lyman Johnson, *Relating Fiduciary Duties to Corporate Personhood and Corporate Purpose*, in *RESEARCH HANDBOOK ON FIDUCIARY LAW* (D. Gordon Smith & Andrew Gold eds., 2016) (examining the connections between corporate personhood, corporate purpose, and fiduciary duties to demonstrate that corporations have a purpose beyond maximizing wealth for their shareholders); Jonathan Povilonis, *The Use and Misuse of Fiduciary Duties: Why Corporate Fiduciary Duties Aren't Worth Fighting For*, available at <https://ssrn.com/abstract=3752756> [<https://perma.cc/M7SM-A5M2>] (arguing that fiduciary duties are limited in their scope and thus a poor means to advance corporate social responsibility).

A. “Nominal shareholders ‘having no real financial interest in the corporation,’”⁹⁸

The debate between Berle and Dodd died as quickly as it began. The market’s collapse in October 1929 brought home the devastating consequences of the “feverish activity of speculation” that characterized the 1920s.⁹⁹ The losses were tremendous. According to one report, “in the ten years before 1933, total investor losses through worthless securities were approximately \$25 billion, or half of all those issued.”¹⁰⁰ According to the same report, even before the Depression, investors’ losses “reached a staggering annual total of \$1.7 billion, of which \$500 million alone was accounted for within the state of New York.”¹⁰¹

After the election of Franklin D. Roosevelt, Congress responded swiftly with a variety of new federal laws, aiming to regulate securities, investment banking and the investment industry. The Glass-Steagall Act, “prohibited bank affiliates from owning and dealing in securities, thereby severing commercial banks from investment banks.”¹⁰² The Securities Act of 1933 required issuance of new securities to be registered and “accompanied by full publicity and information and that no essentially important element attending the issue shall be concealed from the buying public.”¹⁰³ The Securities and Exchange Act of 1934 focused on the registration of the stock exchanges and the requirement that firms traded on these exchanges file annual and quarterly reports with a newly established agency, which the Act created—the Securities and Exchange Commission (SEC). The Act further prohibited certain manipulative devices such as short selling, which corporate insiders and exchange members used to exploit the market, and it regulated insider trading by both management and controlling shareholders.¹⁰⁴ Moreover, it limited the formation of control groups by requiring individuals or groups owning more than five percent of a corporation’s stock to file with the SEC.¹⁰⁵ In order to prevent fraudulent reporting, the Act also required “certified periodical audits for any

98. FRANKLIN WOOD, N.Y. CHAMBER OF COMMERCE, SURVEY AND REPORT REGRADING STOCKHOLDERS’ DERIVATIVE SUITS 112 (1944).

99. RALPH F. DE BEDTS, THE NEW DEAL’S SEC: THE FORMATIVE YEARS 11 (1964).

100. *Id.* at 11.

101. *Id.*

102. Mark Roe, *Political Theory of American Corporate Finance*, 91 COLUM. L. REV. 10, 17 (1991).

103. MICHAEL E. PARRISH, SECURITIES REGULATION AND THE NEW DEAL 47 (1970) (quoting from Roosevelt’s message in support of the first draft).

104. DE BEDTS, *supra* note 99, at 76–77.

105. Roe, *supra* note 102, at 25–27.

corporation listing its securities on a national exchange.”¹⁰⁶ As to the shareholders’ role in the corporation—the 1934 Act put their fate in the hands of the SEC, which was authorized to adopt rules regarding proxy voting when appropriate “in the public interest or for the protection of investors.”¹⁰⁷

The number of individual shareholders continued to rise, although it remained limited through the 1960s. After the crash, some investors, especially those who only recently began investing, left the market; one report noted that women “who once crowded brokerage desks in the 1920s . . . virtual[ly] disappear[ed] from the market” after the crash.¹⁰⁸ Still, by 1934, the House Report on the Securities Exchange bill estimated that more than 10 million individuals owned stocks or bonds, and that “over one fifth of all the corporate stock outstanding in the country [was] held by individuals with net incomes of less than \$5,000 a year.”¹⁰⁹

For the most part, investors sought steady income and were advised to focus on the intrinsic value of the corporation based on its specific characteristics when making their investment decisions.¹¹⁰ Typically long-term investors, they also turned to the courts to ensure that directors fulfilled their fiduciary obligations. As John Coffee explains, when individual shareholders found themselves holding stock in larger and larger corporations while having little if any sway over those in control, “[t]he derivative action [became] the only legal remedy then available to shareholders,” and its use rapidly increased.¹¹¹ Minority shareholders, not infrequently also of minority social and cultural status, or women, who viewed investment in corporate stock as a means of economic as well as social and cultural advancement, brought derivative suits not necessarily to

106. DE BEDTS, *supra* note 99, at 77.

107. JOEL SELIGMAN, *THE TRANSFORMATION OF WALL STREET: A HISTORY OF THE SECURITIES AND EXCHANGE. COMMISSION AND MODERN CORPORATE FINANCE* 99–100 (1982). On the creation of the SEC, see *id.* at 73–100; PARRISH, *supra* note 103, at 108–44.

108. Rutterford & Sotiropoulos, *supra* note 39.

109. H.R. REP. NO. 73–1383, at 3 (1934).

110. Economists Benjamin Graham and David Dodd argued that investors could ensure satisfactory returns by relying on fundamental valuation to assemble a portfolio of carefully selected diversified stock. BENJAMIN GRAHAM & DAVID DODD, *SECURITY ANALYSIS: PRINCIPLES AND TECHNIQUE* (1934); see also HO, *supra* note 7, at 200 (noting that the lack of “volume on the Exchange” “indicates that even those who did own shares did not trade them often; the dominant shareholding strategy was to hold stocks, to wait for shares to appreciate slowly as generators of steady income”).

111. COFFEE, *supra* note 25, at 33; see also Naomi R. Lamoreaux & Laura Phillips Sawyer, *Voting Trusts and Antitrust: Rethinking the Role of Shareholder Litigation in Public Regulation, From the 1880s to the 1930s*, 39 L. & HIST. REV. 569, 577–83 (2021) (discussing the use of derivative suits against anticompetitive mergers).

enrich their pockets but rather to ensure that corporate managers acted in their best interest, to ensure, perhaps, their place in corporate America.¹¹²

Notably, much of the litigation took place in the New York courts,¹¹³ where these shareholders were often represented by lawyers who were descendants of recent immigrants.¹¹⁴ Many were Jewish, and their commitment to the protection of minority shareholders was borne out of their experiences of discrimination and exclusion in American society. Seeking economic success and “excluded from . . . the elite corporate bar,” these lawyers “turned to other forms of legal practice, including challenging . . . corporations through derivative litigation . . . to make a living.”¹¹⁵

The Chamber of Commerce of the State of New York was sufficiently concerned about the threat that these lawyers posed to its elite status that it commissioned a study of a decade of derivative litigation in New York courts.¹¹⁶ Franklin Wood, who conducted the study and wrote a report based upon it, concluded that “derivative actions were filed . . . by nominal shareholders ‘having no real financial interest in the corporation.’”¹¹⁷ Accordingly, “the only one likely to profit substantially in the event of success is the [plaintiff’s] attorney.”¹¹⁸ The Wood Report was particularly critical of “the prominence of women among the plaintiffs and list[ed] those suits which feature[d] women plaintiffs, . . . sarcastically speculat[ing] as to

112. While there is no aggregate data of investors by ethnicity or religion, many cases, especially in NY, involved litigants with common Jewish surnames. For lists of cases in NY, see appendices in WOOD, *supra* note 98. For an early-twentieth-century notion that investors can use money to affect politics, see, for example, *Power of Women Investors to Unite and Prevent War*, WALL ST. J., Mar. 18, 1914, at 2.

113. In the midcentury, New York was the leading jurisdiction developing the duties of directors. See generally Dalia T. Mitchell, *Legitimizing Power: A Brief History of Modern U.S. Corporate Law*, in RESEARCH HANDBOOK ON THE HISTORY OF CORPORATE AND COMPANY LAW 510 (Harwell Wells ed., 2018).

114. At the time, “the plaintiff’s bar . . . consisted of solo practitioners and very small firms.” COFFEE, *supra* note 25, at 38. The exception was Abe Pomeranz. *Id.*; see also Spencer Klaw, *Abe Pomeranz is Watching You*, FORTUNE, Feb. 1968, at 144.

115. Lawrence E. Mitchell, *Gentleman’s Agreement: The Antisemitic Origins of Restrictions on Stockholder Litigation*, available at http://ssrn.com/abstract_id=321680 [<https://perma.cc/NH4Q-RWXS>], at 17–18 (George Washington Univ. L. Sch., Public Law and Legal Theory Research Paper Series No. 44, 2022), <https://dx.doi.org/10.2139/ssrn.321680> [<https://perma.cc/47T8-AAUT>].

116. Robert B. Thompson, *The New Look of Shareholder Litigation: Acquisition-Oriented Class Actions*, 57 VAND. L. REV. 133, 149 (2004). The report covered the years 1932 to 1942. *Id.*

117. WOOD, *supra* note 98, at 112.

118. COFFEE, *supra* note 25, at 38–39.

their financial sophistication and research behavior.”¹¹⁹ A majority of the plaintiffs listed in the report also had Jewish surnames.¹²⁰

Wood was not concerned about shareholder suits in closely held corporations. Like *Dodge v. Ford*, suits involving the latter were “usually brought by minority shareholders with a significant stake who alleged misbehavior by the majority.”¹²¹ Instead, he focused on individual shareholders in publicly held corporations. His goal was to demonstrate that many derivative suits were “brought primarily for their nuisance value.”¹²² The Report recommended limiting standing in derivative litigation “to shareholders who owned stock at the time of the alleged wrongdoing, and to require the shareholder plaintiff to post security for costs in the event the litigation were found to have been meritless.”¹²³ Convinced by the Report, the New York legislature passed section 61-b,¹²⁴ “the nation’s first security for expenses statute.”¹²⁵

Criticism of the Report was mounted as soon as it was published,¹²⁶ but the impact of the legislation was limited.¹²⁷ At the time, judges “were probably more prepared to question managerial decisions than at any time before or since.”¹²⁸ As the following Section II.B. explores, while individual shareholders rarely won a case, the questions their derivative litigation raised provided fertile ground for judges to develop the law of fiduciary duties. As judges embraced enabling rules, offering managers freedom to act, they also

119. Mitchell, *supra* note 115, at 35.

120. *Id.* at 35–36.

121. David A. Skeel, Jr., *The Accidental Elegance of Aronson v. Lewis* 9 (U. Pa. L. Sch. Inst. for L. & Econ., Research Paper No. 07-28, 2007), <https://dx.doi.org/10.2139/ssrn.1027010> [<https://perma.cc/GM7L-5EUH>].

122. Erickson, *supra* note 24, at 1141.

123. Skeel, *supra* note 121, at 9.

124. Act of April 9, 1944, ch. 668, § 61-b, 1944 N.Y. Laws 1455.

125. *Id.* Several states enacted similar restrictions, and by 1949, the U.S. Supreme Court held that “these state procedural statutes applied in federal court as well to corporations incorporated in these states.” COFFEE, *supra* note 25, at 4041; *see also* Cohen v. Beneficial Indus. Loan Corp., 337 U.S. 541, 555–57 (1949) (holding that a New Jersey statute requiring shareholder plaintiffs to post security for litigation costs applied in federal courts).

126. *See, e.g.*, George D. Hornstein, *The Death Knell of Stockholders’ Derivative Suits in New York*, 32 CAL. L. REV. 123 *passim* (1944) (criticizing the validity and accuracy of the Wood Report).

127. Skeel, *supra* note 121, at 10 (“Although derivative litigation may indeed have been chilled for a time, the prophesies of its demise were greatly exaggerated.”).

128. COFFEE, *supra* note 25, at 36. Notably, many of these New York judges were Jewish (including Bernard Shientag, Albert Cohn, and Irving Lehman, whose opinions are discussed in Section II.B below). For an attempt to “discern common themes in the judicial careers” of Jewish judges who served on state courts, *see* Jeffrey B. Morris, *The American Jewish Judge: An Appraisal on the Occasion of the Bicentennial*, 38 JEWISH SOC. STUD. 195 (1976).

offered their observations about the corporations' duty to maximize shareholder value.

B. Managerial Freedom and Shareholder Protection

As we saw in Part I of this Article, Progressive legal scholars advocated viewing those in control of business enterprises as trustees and imposing strict fiduciary duties upon them. In 1928, Chief Judge Cardozo's opinion in *Meinhard v. Salmon* gave voice to such ideas, holding that "[a] trustee is held to something stricter than the morals of the market place. Not honesty alone, but the punctilio of an honor the most sensitive, is then the standard of behavior."¹²⁹

By the 1940s, however, courts were moving away from a strict rule of prohibition toward one of balance. For one thing, a contract between a corporation and its director could be valid if a disinterested majority of the directors approved it, and it was not "unfair or fraudulent."¹³⁰ As the Supreme Court of Delaware explained in *Guth v. Loft*, "[c]orporate officers and directors are not permitted to use their position of trust and confidence to further their private interests."¹³¹ Yet, while "[t]he rule that requires an undivided and unselfish loyalty to the corporation demands that there shall be no conflict between duty and self-interest," "[t]he occasions for the determination of honesty, good faith and loyal conduct are many and varied, and no hard and fast rule can be formulated. The standard of loyalty is measured by no fixed scale."¹³²

In a few decades, tolerance gave way to acceptance if not sanction, as courts held that transactions between a corporation and any or all its directors were not "automatically voidable" whether or not a disinterested majority of the board authorized them.¹³³ Instead, courts subjected such transactions to scrutiny under a test of fairness, a standard that one commentator described

129. *Meinhard v. Salmon*, 164 N.E. 545, 546 (N.Y. 1928).

130. Harold Marsh, Jr., *Are Directors Trustees? Conflict of Interest and Corporate Morality*, 22 BUS. LAW. 35, 39–40 (1966); see also Note, *The Fairness Test of Corporate Contracts with Interested Directors*, 61 HARV. L. REV. 335, 336 (1948) (noting that "the courts seized upon the board of directors' ability to act through a majority" to approve an otherwise voidable self-dealing transactions).

131. *Guth v. Loft, Inc.*, 5 A.2d 503, 510 (1939).

132. *Id.* The case involved a lawsuit by Loft Inc. against Charles Guth, its president, charging that Guth had taken to himself a corporate opportunity (a controlling investment in Pepsi-Cola Enterprises). *Id.* at 508–09. The Delaware Supreme Court upheld the lower court's ruling in favor of Guth. *Id.* at 515.

133. See, e.g., Marsh, *supra* note 130.

as “measured by the ‘Chancellor’s foot.’”¹³⁴

The reasons for the development were manifold. In part, the courts simply legitimated changes that corporations had begun to put in place through charter provisions permitting self-dealing transactions, subject to the requirements of independent authorization or absence of fraud. In part, the rise of the large publicly held corporation, the passing of control from directors to managers, as well as the rapid pace and “brutal” temper of business ventures made a concept of trust appear “threadbare.”¹³⁵ In part, courts were simply recognizing the needs of business and their managers;¹³⁶ seeking to allow managers and the control group to balance the corporation’s interests with their own, courts moved away from trust toward fairness as the appropriate standard for evaluating conflict-of-interest transactions.

Placing this transformation in a broader historical context, legal historian William Nelson has argued that courts were addressing cultural and social ends beyond the realm of corporate law. In his thorough examination of politics and ideology in New York courts, Nelson argued that the law of fiduciary obligations was historically a tool “to protect property rights and the existing distributions of wealth, on the one hand, and to uphold moral values, on the other.”¹³⁷ According to Nelson, in the midcentury years, judges relaxed the strict requirements applied to fiduciaries so as to enable new entrepreneurs, who were often descendants of turn-of-the-century Catholic and Jewish immigrants from Southern and Eastern Europe, to enter the mainstream of American life.¹³⁸

As Nelson explores, judges “fostered . . . upward mobility” when holding

[T]hat a corporate officer or director, if acting in good faith, may

134. Note, *supra* note 130, at 337. The difference between trust and fairness was significant. A trust standard of review required voiding transactions between the corporation and a director or an officer simply because they involved the self-interest of the latter. In turn, the fairness standard of review allowed courts to validate such transactions, even though they involved the self-interest of the fiduciary, if the result of such transactions was fair to the corporation.

135. Gerald T. Dunne, *Justice Story and the Modern Corporation—A Closing Circle?*, 17 AM. J. LEGAL HIST. 262, 265 (1973).

136. See, e.g., *S. Side Trust Co. v. Wash. Tin Plate Co.*, 97 A 450, 451 (Pa. 1916) (“The interests of corporations are sometimes so interwoven that it is desirable to have joint representatives in their respective managements, and at any rate it is a not uncommon and not unlawful practice.”).

137. WILLIAM E. NELSON, *THE LEGALIST REFORMATION: LAW, POLITICS, AND IDEOLOGY IN NEW YORK 1920–1980*, at 60 (2001).

138. *Id.* at 178; see also William E. Nelson, *The Law of Fiduciary Duty in New York, 1920–1980*, 53 SMU L. REV. 285, 285–86 (2000) (describing the increased freedom given by judges to money managers to facilitate the mobility of new entrepreneurs).

profit from dealings with the corporation if the corporation also profits; . . . that honest reliance on advice of counsel protected directors from personal liability; that “policies of expansion” justified nonpayment of dividends; . . . and that, in the absence of loss of corporate funds or of personal profit to itself, management could authorize a corporation to purchase its own stock in the open market in order to perpetuate management’s control.¹³⁹

As already noted, often, not only the defendants but also the plaintiffs, the shareholders who sought stricter application of fiduciary obligations, were first- and second-generation Americans (and some were also women). Judges were thus pressed to develop pragmatic solutions that would address the needs of both fiduciaries and beneficiaries. To that end, as courts moved away from strict enforcement of trust toward the more relaxed standard of fairness, judges also opined about the directors’ duty to ensure that corporations remained profitable for the benefit of their shareholders. As I argue below, these statements about profits planted the seeds that in the 1980s sprouted to become the shareholder wealth maximization norm.¹⁴⁰

Bayer v. Beran is the most emblematic of these cases. A derivative litigation against the Celanese Corporation of America (“Company”), it was instigated by two of the Company’s public shareholders,¹⁴¹ Seymour Bayer and Benjamin F. Steinberg, who challenged actions by the Company’s board and sought to recover \$1,350,000 for the Company.¹⁴²

The Company was founded by Dr. Camille Dreyfus, a chemist and an immigrant from Switzerland, who developed a variety of cellulose-based products and, with his brother, Henri, set up “three great enterprises,” namely British Celanese Ltd., Canadian Celanese Ltd., and, in 1918, the company that would become Celanese Corporation of America. Camille was “president of the American concern[,] . . . managing director of the British

139. Nelson, *supra* note 138, at 297–98.

140. See also NELSON, *supra* note 137, at 178 (“In particular, the courts grew more tolerant of higher-risk investment practices of entrepreneurial fiduciaries who were seeking to increase income and grow principal and less concerned with ensuring the security of investments.”).

141. At the time of the trial, there were 1,376,500 shares outstanding; the Dreyfus brothers and their families owned about 135,000 shares of common stock, the other directors about 10,000 shares, and the rest of the shares were publicly held. *Bayer v. Beran*, 49 N.Y.S.2d 2, 9 (Sup. Ct. 1944).

142. *Singer’s Career Issue in Suit for \$1,350,000*, N.Y. TIMES, March 11, 1943, at 22. Steinberg was represented by Abraham M. Glickman and Beyer by A. Lincoln Lavine, a Professor of Law and Chairman of the Law Department of St. John’s University School of Commerce.

company and president of the Canadian.”¹⁴³

Bayer’s and Steinberg’s complaint focused on an approval of a radio advertising campaign in which Jean Tennyson, a professional opera singer and Camille’s wife, was sometimes featured.¹⁴⁴ The campaign was initiated after the Federal Trade Commission issued a new rule, requiring Celanese to be labeled rayon; the campaign’s implicit goal was to convince consumers that Celanese was indeed better than rayon. The shareholders argued, first, that the directors were negligent in approving the campaign and, second, that they approved the campaign to further the career of the president’s wife.¹⁴⁵ (The shareholders’ other complaint focused on “certain payments of \$30,000 a year made to Henri Dreyfus, one of its vice-presidents and a director, pursuant to a contract of employment entered into with him by the corporation.”¹⁴⁶)

Justice Bernard Lloyd Shientag of the Supreme Court of New York, known for his “broad humanitarian sympathies,”¹⁴⁷ wrote the court’s opinion. Aware of the growing concerns about the derivative suit, and seeking perhaps to encourage minority shareholders to bring them, Justice Shientag began his decision by noting:

Despite abuses that have developed in connection with the derivative stockholders’ suit, abuses which should be dealt with promptly and effectively, it must be remembered that such an action is, at present, the only civil remedy that stockholders have for breach of fiduciary duty on the part of those entrusted with the management and direction of their corporations. We cannot therefore allow the prevailing mood of justifiable dissatisfaction with some of the temporary incidents of such suits to cause us to lose sight of certain deep-rooted, traditional concepts of the obligations of directors to their corporation and its stockholders.¹⁴⁸

Then, after a careful analysis of the facts, Shientag, eager to encourage managerial freedom, dismissed the complaint on the merits, holding that “the directors acted in the free exercise of their honest business judgment and their conduct in the transactions challenged did not constitute negligence,

143. *Camille Dreyfus of Celanese Dies*, N.Y. TIMES, Sept. 28, 1956, at 27. In 1930, common and preferred stock of the Celanese Corporation of America began trading on the New York Stock Exchange. <https://www.celanese.com/en/About-Us/History/1921-1950> [https://perma.cc/C2YS-KYSV].

144. *Bayer*, 49 N.Y.S.2d at 7.

145. *Id.*

146. *Id.* at 4.

147. James McGurrin, *Tribute to Justice Shientag, Letters to the Editor*, N.Y. TIMES, May 29, 1952, at 26.

148. *Bayer*, 49 N.Y.S.2d at 4–5.

waste or improvidence.”¹⁴⁹

Nonetheless, and perhaps because he dismissed the minority shareholders’ complaint, Shientag’s opinion emphasized two factors related to the responsibility of directors and officers to maximize shareholders’ value. First, Shientag elaborated on the standard of fairness by which transactions involving directors’ or officers’ conflict of interest should be evaluated. Ms. Tennyson advised Dreyfus and helped create the advertising campaign, which consisted of a radio program offering classical music. She was also one of the singers on the program. Yet, while the advertising campaign was tainted with a conflict of interest, Shientag found it to be fair to the corporation. As he pointedly noted, “It would be far-fetched to suggest that the directors caused the company to incur large expenditures for radio advertising to enable the president’s wife to make \$24,000 in 1942 and \$20,500 in 1943.”¹⁵⁰

As to the claim that the directors did not meet to approve the campaign and thus failed to fulfil their duty of care, Shientag pointed out that the directors, all of whom were also executives, were sufficiently informed. Supporting his conclusion, Shientag wrote:

While a greater degree of formality should undoubtedly be exercised in the future, it is only just and proper to point out that these directors, with all their loose procedure, have done very well for the corporation. Under their administration the company has thrived and prospered. Its assets increased from \$44,500,000 in 1935 to upwards of \$103,000,000 in 1942. Its net profits, after taxes, doubled during that period, rising from \$4,000,000 in 1935 to \$8,000,000 in 1942; its net sales rose from \$27,000,000 to upwards of \$86,000,000; and its dividend disbursements to stockholders exceeded \$29,500,000.¹⁵¹

While irrelevant to the legal analysis of directors’ duties, profit mattered. Other cases, addressing a variety of duty-of-loyalty and duty of care claims similarly balanced the interests of managers and shareholders, shielding the former from liability while assuring the latter that their corporations were profitable.

Litwin v. Allen, which preceded *Bayer*, was a derivative suit brought by Eva Litwin, a minority shareholder, represented by Abraham N. Geller, a practitioner based in New York.¹⁵² Writing for the court, Justice Shientag stressed that “a director owes loyalty and allegiance to the company—a

149. *Id.* at 15.

150. *Id.* at 9.

151. *Id.* at 11.

152. On Geller, see *Judge Who Jailed Quill*, N.Y. TIMES, Jan. 5, 1966.

loyalty that is undivided and an allegiance that is influenced in action by no consideration other than the welfare of the corporation.”¹⁵³ Moreover, “[i]n the discharge of his duties a director must, of course, act honestly and in good faith, but that is not enough. He must also exercise some degree of skill and prudence and diligence.”¹⁵⁴ Yet, a careful and detailed consideration of the facts led Shientag to reject three of the plaintiff’s four claims. “The law recognizes that the most conservative director is not infallible,” Shientag wrote, “and that he will make mistakes.”¹⁵⁵ So long as a director used “that degree of care ordinarily exercised by prudent [directors of similar corporations, here bankers] he will be absolved from liability although his opinion may turn out to have been mistaken and his judgment faulty.”¹⁵⁶

Significantly, while the question of profit was not dispositive of any of the issues raised in the case, it was important for Shientag, at the beginning of the discussion to note:

[P]laintiffs have conceded that in all but the four questioned transactions the defendants exercised an unusual degree of care in the management of the Trust Company. This is reflected in the financial condition of the Trust Company. For example, beginning with 1930 (the year after the merger of Guaranty Trust Company and National Bank of Commerce), its deposits increased from \$1,341,639,876 to \$2,088,427,346 in 1939. In the same interval its total assets more than doubled. Despite the depression the Trust Company’s figures of capital, surplus and undivided profits remained substantially the same between 1930 and 1939, being \$297,442,797 in the former year and \$274,701,954 in the latter year.¹⁵⁷

Similarly, in *Turner v. American Metal Co.*, a derivative suit brought by shareholders holding “165 out of a total over 1,200,000 shares of common stock” of their corporation,¹⁵⁸ who argued that the directors usurped corporate opportunity, Judge Albert Cohn for the New York Appellate Court stressed that “[t]he law is well settled that minority stockholders may not interfere with the management of a corporation so long as the trustees are acting honestly and within their discretionary powers.”¹⁵⁹ Moreover, “the mere existence of . . . a divided loyalty did not, of itself, warrant the

153. *Litwin v. Allen*, 25 N.Y.S.2d 667, 677 (1940).

154. *Id.* at 677–78.

155. *Id.* at 678.

156. *Id.*

157. *Id.* at 676–77.

158. *Turner v. American Metal Co.*, 268 A.D. 239, 243 (N.Y. App. Div. 1944).

159. *Id.* at 271.

imposition of liability against directors.”¹⁶⁰ Accordingly, “lean[ing] in the direction of enhancing the entrepreneurial freedom of business managers,”¹⁶¹ Cohn did not find the directors to have breached the trust.¹⁶² Recognizing perhaps that its decision left the minority shareholders without remedy, Cohn added, in *dicta*, that the parent company made profit as a result of the challenged transaction. “The financing of Climax, from American Metal’s point of view, was distinctly profitable,” he concluded.¹⁶³

The balance seemed attainable: directors were free to act, protected by the presumption of the business judgment rule, so long as, in the balance of equities, their companies were profitable. Corporate managers were offered a protective fairness standard while minority shareholders were given a protective rhetoric. As the following Part III explores, by the 1960s, as concerns about upward mobility and the economic assimilation of second-generation Americans subsided, the business judgment presumption came to dominate corporate litigation and the discussion of profits receded. It resurfaced in the Delaware courts amid the hostile takeovers of the 1980s as shareholder wealth maximization became a tool in the hands of Wall Street lawyers and investment bankers seeking to enrich their clients.

III. 1960S-1980S: FAIRNESS AND PROFIT IN THE AGE OF FINANCE

By the 1950s, corporate managements became the “strategic center” of the large publicly held corporation.¹⁶⁴ Management dominated the corporate bureaucracy, organized production, and exercised power over individual lives within the corporation and market transactions outside it.¹⁶⁵ Modern finance theory and neoclassical economics, both developed in the 1960s, helped legitimate the role of corporate directors and executives by suggesting that the stock market would tame potential abuses of managerial power.¹⁶⁶ During the 1980s, as hostile takeovers attempted to make the ideal of the

160. *Id.* at 272; *see also*, *Everett v. Phillips*, 288 N.Y. 227, 43 N.E.2d 18, 22 (1942), in which Chief Judge Irving Lehman, for the court, concluded that the dual position of the directors, while “making the unprejudiced exercise of judgment by them more difficult,” did not in itself “suffice to render the transactions void.”

161. NELSON, *supra* note 137, at 180.

162. Turner, 268 A.D. 239.

163. *Id.* at 264; *see also id.* at 272 (“The decision of the directors of American Metal to render . . . assistance to Climax . . . , was fully justified. Climax made no profits ‘at the expense’ of American Metal and the success of [Climax] . . . resulted in a net profit to American Metal of more than \$16,000,000.”).

164. William W. Bratton, Jr., *The New Economic Theory of the Firm: Critical Perspectives from History*, 41 STAN. L. REV. 1471, 1476 (1989).

165. *Id.*

166. *See* discussion *infra* notes 176-178.

market as regulator a reality, the Delaware courts responded by making shareholder wealth maximization, in fact share price maximization, an aspect of the fairness standard of review as well as the enhanced scrutiny to which directors' responses to hostile bids were subjected. *Revlon* was the result.¹⁶⁷

A. *Changing Tides*

Through the postwar years, stock ownership was not widespread—less than five percent of the population owned stock—and corporations relied upon earnings and, to a more limited extent, external financing from banks to fund their operations.¹⁶⁸ Trading volume was also low, indicating that midcentury shareholders preferred long-term investment.¹⁶⁹ In May 1947, the New York Stock Exchange, seeking to encourage Americans to invest in common stock, placed ads portraying American shareholders as “com[ing] from everywhere . . . from every income group, from every community. They are women as well as men, employees as well as executives, farmers as well as businessmen. They are typical stockholders, the owners of business.”¹⁷⁰ The campaign expanded in the following years, as the Exchange sought to market stock as a means, among others to fight communism, socialism, and fascism.¹⁷¹ The bullish market growth in the succeeding decade confirmed the success of the campaign.¹⁷² In 1952, 6.5 million people owned stock, “by 1956, the total was 8.6 million; by 1959, 12.5 million, [b]y 1962 . . . the number . . . reached an impressive 17 million.”¹⁷³ As the *New York Times* reported:

167. On the role of the Delaware courts in the 1980s, see, e.g., James D. Cox & Randall S. Thomas, *Delaware's Retreat: Exploring Developing Fissures and Tectonic Shifts in Delaware Corporate Law*, 42 DEL. J. CORP. L. 323, 324 (2018) (noting that “[t]he 1980s is . . . considered the Golden Age of Delaware corporate law. During that era, the Delaware courts won international attention . . . by interjecting a fresh perspective on the rights of owners and the prerogatives of managers.”).

168. Lawrence E. Mitchell, *Who Needs the Stock Market? Part I: The Empirical Evidence* 12–15 (2008), https://papers.ssrn.com/sol3/papers.cfm?abstract_id=1292403 [<https://perma.cc/c3WL4-86S5>]. As Mitchell notes, “external financing in general only began to grow from the turn of the twentieth century on, but almost all of that growth was in various forms of debt.” *Id.* at 7 (footnote omitted).

169. Ho, *supra* note 7, at 200–01.

170. J. A. LIVINGSTON, *THE AMERICAN STOCKHOLDER: A COMPREHENSIVE REPORT ON THE WORKINGS OF TODAY'S STOCK-MARKET* 21 (rev. ed. 1963) (1957).

171. Janice Traflet, “Own Your Share of American Business”: *Public Relations at the NYSE During the Cold War*, 1 BUS. & ECON. HIST. 1, 3–4 (2003), http://www.thebhc.org/site/default/files/Trafflet_0.pdf [<https://perma.cc/VX8A-FN7D>].

172. LIVINGSTON, *supra* note 170, at 21–23.

173. *Id.* at 23.

Part of this increase is attributable to employee-participation plans, part to the increased popularity of investment companies, which permit a purchaser to spread his risks while buying only one issue. Nearly a quarter of a million holders have been attracted by the widely publicized Monthly Investment Plan—the application of installment buying to stock ownership. But most of the increase must be credited to greater affluence (more families with savings to invest) and, apparently, to a belief that the market can only go up.¹⁷⁴

The development of modern finance theory coincided with the efforts of the Exchange. As mentioned in Part II above, in the first part of the twentieth century, as corporations sought to create a market for their stock, investors were advised to focus on the intrinsic value of corporations.¹⁷⁵ Beginning in the 1950s, however, modern portfolio theory, developed by Harry Markowitz, suggested that investors could create “an efficient portfolio,” that is, a portfolio that would achieve maximum return by diversifying non-systematic risk, and that the portfolio, rather than individual corporations, should be the focus of investment analysis.¹⁷⁶ The Capital Asset Pricing Model, which William Sharpe and John Lintner developed in the 1960s, offered a regression analysis of a stock’s historical movement in relation to the market to help investors diversify the systematic risk inherent in the market. Rather than study the fundamentals of companies in which they were interested, investors were advised to study the historical performance of their companies’ stock price.¹⁷⁷ As Ronald Gilson and Jeffrey Gordon have demonstrated, the need to ensure ample diversification of both systematic and non-systematic risks led investors to choose mutual funds over direct investment in corporate stock; within a few decades, the percentage of households that owned equities through mutual funds dramatically increased.¹⁷⁸

174. Michael Reagan, *What 17 Million Shareholders Share*, N.Y. TIMES, Feb. 23, 1964, at 11.

175. See discussion *supra* note 110.

176. James R. Hackney, Jr., *The Enlightenment and the Financial Crisis of 2008: An Intellectual History of Corporate Finance Theory*, 54 ST. LOUIS U. L. J. 1257, 1260–62 (2010).

177. Kent L. Womack & Ying Zhang, *Understanding Risk and Return, the CAPM, and Fama-French Three-Factor Model*, available at https://papers.ssrn.com/sol3/papers.cfm?abstract_id=481881 [<https://perma.cc/M9JH-SXC5>]; see also Roberta Romano, *After the Revolution in Corporate Law*, 55 J. LEGAL EDUC. 342, 345 (2005).

178. Ronald J. Gilson & Jeffrey N. Gordon, *The Agency Costs of Agency Capitalism: Activist Investors and the Reevaluation of Governance Rights*, 113 COLUM. L. REV. 863, 884 (2013). Gilson and Gordon also note that, while the percentage of

Informed by modern finance theory, academic attention shifted from concerns about corporate power and the power of the control group to the market as the sole means of regulating the economy. The University of Chicago, in particular, “had become the intellectual home of the idea that markets, not the state, were the proper and most benign central institution of postwar society. . . .”¹⁷⁹ Drawing on microeconomics, a new theory of the firm painted a picture of the corporation as a nexus of private, contractual relationships. The corporation was a collection of “disaggregated but interrelated transactions” among individuals or the convenient fiction of corporate entity in free and efficient markets.¹⁸⁰

The new theory of the firm supported a shift of focus in jurisprudence—from questions of power and control to issues of agency-costs reduction.¹⁸¹ Its proponents reframed the problem of the modern corporation as the problem of the separation of ownership from control and sought to demonstrate how capital markets could eliminate concerns about efficiency associated with this separation.¹⁸² Fiduciary obligations were seen as overly restrictive, corporate litigation was deemed wasteful, and dissatisfied shareholders seeking to ensure that corporate managers act in their best interests were told to exercise their voting power or to sell their shares.¹⁸³

In this context, judges’ focus shifted from balancing managerial freedom with assurances to minority shareholders about profits toward upholding directors’ actions unless the plaintiff shareholder carried the burden of rebutting the presumption of the business judgment rule. The “reification of the business judgment rule,” William Nelson writes,

households that directly own equities has remained about 20% since the late 1970s, mutual funds investment (including but not limited to retirement investment) “has increased the percentage of households that own equities directly or through mutual funds by 30% to a total of 50%” by the middle of the first decade of the twenty-first century. *Id.* Moreover, while in the 1950s, “[e]quities were still held predominantly by households” with institutional investors holding “only approximately 6.1% of U.S. equities,” by the 1980s, “institutional investors held 28.4% of U.S. equities.” *Id.* at 874. By the end of the first decade of the twenty-first century, “institutional investors held 50.6% of all U.S. public equities, and 73% of the equity of the thousand largest U.S. corporations.” *Id.*

179. NICHOLAS LEMANN, *TRANSACTION MAN: THE RISE OF THE DEAL AND THE DECLINE OF THE AMERICAN DREAM* 102 (2019).

180. William W. Bratton, Jr., *The “Nexus of Contracts” Corporation: A Critical Appraisal*, 74 CORNELL L. REV. 407, 416–20 (1989).

181. Bratton, *supra* note 164, at 1498.

182. Dalia Tsuk, *From Pluralism to Individualism: Berle and Means and 20th-Century American Legal Thought*, 30 LAW & SOC. INQUIRY 179, 212–15 (2005).

183. See, e.g., Henry G. Manne, *Some Theoretical Aspects of Share Voting: An Essay in Honor of Adolf A. Berle*, 64 COLUM. L. REV. 1427 (1964) (discussing the impact of share voting on corporate decisions and the fact that votes are bought and sold in the corporate system).

“probably gave judges a better basis than they previously possessed for declining to enforce the duty of loyalty, with its focus ultimately on issues of equity between shareholders, and instead, deciding cases ‘on the practical basis’ that entrepreneurs should be left free to manage corporations efficiently. . . .”¹⁸⁴

Take for example *Shlensky v. Wrigley*.¹⁸⁵ William Shlensky, “a 27-year-old Chicago lawyer, who has owned two shares [of the Chicago Cubs stock] since he was 14,” brought derivative suit against the directors of the Cubs, a Delaware corporation.¹⁸⁶ According to Shlensky, the Cubs suffered operating losses because of inadequate attendance at their home games. He attributed the inadequate attendance to the directors’ refusal to install lights at Wrigley Field and schedule night baseball games. Philip Wrigley, the Cubs’ president and controlling shareholder (he owned approximately 80% of the Cubs’ stock) had “steadfastly . . . kept Wrigley Field the only major league park without lights because he insist[ed] that baseball [was] a day game and night ball would be a nuisance to Wrigley Field neighbors.”¹⁸⁷ Shlensky argued that the directors “have acquiesced in the policy laid down by Wrigley,” allowing him “to dominate the board of directors in matters involving the installation of lights and scheduling of night games, even though they knew he was not motivated by a good faith concern as to the best interests of the . . . corporation.”¹⁸⁸

The Illinois Appellate Court, applying Delaware law, quickly dismissed Shlensky’s claim, holding that “there must be fraud or a breach of that good faith which directors are bound to exercise toward the stockholders in order to justify the courts entering into the internal affairs of corporations.”¹⁸⁹ Then, in *dicta*, and without needing to address the question, the court added:

We feel that plaintiff’s amended complaint was also defective in failing to allege damage to the corporation. . . There is no allegation that the night games played by the other nineteen teams enhanced their financial position or that the profits, if any, of those teams were directly related to the number of night games scheduled. There is an allegation that the installation of lights and scheduling of night games in Wrigley Field would have resulted in large amounts of additional revenues and incomes from increased attendance and related sources of income. Further, the

184. Nelson, *supra* note 138, at 297.

185. *Shlensky v. Wrigley*, 95 Ill. App. 2d 173 (1968).

186. *Stockholder of Cubs Hopes to See the Light*, N.Y. TIMES, Mar. 18, 1966, at 46.

187. *Id.*

188. *Shlensky*, 95 Ill. App.2d at 176.

189. *Id.* at 180.

cost of installation of lights, funds for which are allegedly readily available by financing, would be more than offset and recaptured by increased revenues. However, no allegation is made that there will be a net benefit to the corporation from such action, considering all increased costs.¹⁹⁰

Digging even deeper into the affairs of the Cubs, despite the court's admission that the directors were entitled to the protective presumption of the business judgment rule, Justice Sullivan explained that while Shlensky claimed that "the losses of defendant corporation are due to poor attendance at home games," it seemed that other factors contributed to the team losses. "For example, in 1962, attendance at home and road games decreased appreciably as compared with 1961, and yet the loss from direct baseball operation and of the whole corporation was considerably less."¹⁹¹ As Sullivan concluded, Shlensky "did not feel he could allege that the increased revenues would be sufficient to cure the corporate deficit," and the court would not "speculate as to what other factors might influence the increase or decrease of profits if the Cubs were to play night home games."¹⁹²

Managerial freedom trumped shareholder interests. "Directors are elected for their business capabilities and judgment," Sullivan wrote in *Shlensky*.¹⁹³ Moreover, as Judge Jack Weinstein of the United States District Court for the Southern District of New York elaborated in *Doglow v. Anderson*, shareholder litigation risked putting "many managers of large enterprises. . . some of them . . . men of relatively limited financial resources who have risen quickly and recently through the technical ranks because of their skill and optimism" in "an intolerable position."¹⁹⁴ While, like Shientag in the 1940s, Weinstein stressed that there was no need to "be unduly concerned that small shareholders will misuse the class action device by bringing strike suits,"¹⁹⁵ he ultimately concluded that "[a] rule of law too restrictive and inflexible may over inhibit and dampen [the] drive" of the

190. *Id.* at 181–82.

191. *Id.* at 182.

192. *Id.*

193. *Id.* at 183.

194. *Doglow v. Anderson*, 53 F.R.D. 664, 686 (E.D.N.Y. 1971).

195. *Doglow v. Anderson*, 43 F.R.D. 472, 495 (E.D.N.Y. 1968) (noting that "most shareholders" of publicly held corporations "own comparatively few shares of stock," and that "the few persons who do own a substantial bloc of stock in a corporation are usually either officers, directors, or other 'insiders'— . . . the very people whose conduct the securities laws are designed to regulate. . . . [T]o restrict the use of the class action to those persons would virtually preclude its application in the area of securities regulation.").

new entrepreneurs, “without providing gain to the investor. . . .”¹⁹⁶

No longer looking to assure minority shareholders that their corporations were maximizing profit, courts required shareholders not only to prove that directors’ actions amounted to the dereliction of their duty of loyalty but also that they caused damage to the corporation, a formidable task. Discussions of shareholder profit maximization seemed to be put to rest. Yet, as the following sections III.B and III.C explore, they were resurrected in the 1980s, with a twist.

B. Fairness as Fair Price

By the 1980s, the business judgment rule seemed synonymous with corporate law. As Judge Winter writing for the Second Circuit explained, shareholders voluntarily assumed the risks of business failures (and the potential for success). Because rational shareholders would offset their exposure to business misfortunes by diversifying their portfolios (as modern finance theory dictated), corporate law did not need to protect them from such letdowns.¹⁹⁷ Allowing finance and markets to trump law, the Delaware courts further justified shielding directors from liability by expressing concerns about the potential devastating effects of heightened liability on the willingness of competent directors to serve on boards.¹⁹⁸

The election of Ronald Reagan cemented free economic and political markets as the cornerstones of American democracy. As Kent Greenfield writes, “Reagan embodied a new *Zeitgeist*. He railed against government regulation, took pride in breaking up the power of public-sector unions, and ushered in an era in which people were encouraged to feel good about making money.”¹⁹⁹ While Franklin Roosevelt’s New Deal focused on providing for the vulnerable in our society, a focus that carried through the postwar years, “Reagan ushered in the 1980s proclaiming, ‘What I want to see above all is that this country remains a country where someone can

196. Doglow, 53 F.R.D. at 686; *see also* Nelson, *supra* note 138, at 297 (discussing Judge Weinstein’s opinion in *Doglow v. Anderson*).

197. *See* Joy v. North, 692 F.2d 880 (2nd Cir. 1982) (“Shareholders can reduce the volatility of risk by diversifying their holdings. . . . [C]ourts need not bend over backwards to give special protection to shareholders who refuse to reduce the volatility of risk by not diversifying.”).

198. *See, e.g.*, *Gagliardi v. TriFoods Int’l, Inc.*, 683 A.2d 1049, 1052 (Del. Ch. 1996) (noting that it was “in the shareholders’ economic interest to offer sufficient protection to directors from liability for negligence, etc., to allow directors to conclude that, as a practical matter, there is no risk that, if they act in good faith and meet minimal proceduralist standards of attention, they can face liability as a result of a business loss”).

199. KENT GREENFIELD, CORPORATIONS ARE PEOPLE TOO 44–45 (2018).

always get rich.”²⁰⁰

The stock market became a tool for fulfilling Reagan’s promise. After the bull market of the 1960s helped keep the growing numbers of investors satisfied, in the 1970s, “the stock market slumped.”²⁰¹ Because “stocks fell to five or six times earnings and often traded for less than a company’s book value,” hostile takeovers became feasible, as raiders could offer premium above market price, and “[t]he outlay could be recouped in a half-dozen years—or even sooner, by selling off some of the acquired assets.”²⁰² Seizing the opportunity, investment bankers were quick to justify hostile takeovers by spinning “a compelling narrative of how in the postwar era an elite, complacent, and self-serving managerial class squandered corporate resources extravagantly on themselves or on ill-advised expansions.”²⁰³ Accordingly, a primary goal of the takeover movement was “‘unlocking’ the value of ‘underperforming’ stock prices” to the benefit of the victims in this narrative—the shareholders.²⁰⁴

The takeover boom that followed revolutionized investment banking, as “mergers-and-acquisitions departments [moved] from back room operations . . . into operations that came to rival corporate-finance departments in size—and profits.”²⁰⁵ “Investment bankers, perfecting their sophisticated skills,” Paul Hoffmann writes, “superseded the legal mercenaries as the strategists of tender-offer raids and the tacticians of takeover defense.”²⁰⁶ These investment bankers, focused on increasing the value of their portfolios, and institutional investors, keen on achieving the same, were able to use hostile takeovers to force corporations “to choose between shareholder value and other alternatives of corporate governance.”²⁰⁷ As Karen Ho explains, by creating an “unprecedented environment where all the largest corporations were up for grabs to the highest stock-price bidder,” promoters of shareholder wealth maximization forced these corporations “to be immediately responsive to the exigencies of the stock market.”²⁰⁸

According to one report, “two thousand corporate takeovers a year

200. *Id.* at 45.

201. PAUL HOFFMAN, *THE DEALMAKERS: INSIDE THE WORLD OF INVESTMENT BANKING* 143 (1984).

202. *Id.*

203. HO, *supra* note 7, at 130.

204. *Id.* at 130.

205. HOFFMAN, *supra* note 201, at 142.

206. *Id.* at 141.

207. HO, *supra* note 7, at 129.

208. *Id.* at 129.

valued at more than \$1 million” took place between 1981 and 1983.²⁰⁹ Stock price became the medium for evaluating corporate performance and the ultimate corporate goal. Corporations began using their retained earnings and debt to return value to shareholders, defend against hostile tender offers, and finance successful takeovers.²¹⁰ Before long, the Delaware courts embraced stock price as indicative of managerial efficiency and embedded it in the standard of review applicable to directors’ actions, namely fairness. A trilogy of cases authored by Justice Andrew G.T. Moore—*Weinberger v. UOP, Inc.*,²¹¹ *Unocal v. Mesa Petroleum Co.*²¹² and *Revlon*²¹³—led the way.

Weinberger was first in the trilogy, and the first case to make explicit the connection between directors’ duties and stock price; it remains the definitive case with respect to the fairness standard of review.²¹⁴ A class action,²¹⁵ *Weinberger* addressed “the elimination of UOP’s minority shareholders by a cash-out merger between UOP and its majority owner, The Signal Companies, Inc.”²¹⁶ In determining the price per share it was willing to offer the public shareholders of UOP, Signal used a feasibility study conducted by two of Signal’s members on the UOP board. The study revealed that the merger would be beneficial to Signal at any price up to \$24 per share.²¹⁷ The study was never disclosed to the other members of the UOP board or to UOP’s shareholders before they approved the merger at \$21 per

209. LEMANN, *supra* note 179, at 116. According to Lemann, “[d]uring the 1980s as a whole, more than a quarter of the companies on the Fortune 500 list of the country’s largest corporations were subject to takeover attempts . . . There were thirty-five thousand of these transactions, worth \$2.6 trillion, between 1976 and 1990.” *Id.*

210. *See* Mitchell, *supra* note 168 (providing and examining the empirical evidence supporting this argument).

211. *Weinberger v. UOP, Inc.*, 457 A.2d 701 (Del. 1983).

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

213. *Revlon, Inc. v. MacAndrews & Forbes Holding, Inc.*, 506 A.2d 173 (Del. 1986).

214. On the fairness remedy in parent-subsidary mergers prior to *Weinberger*, *see* Victor Brudney & Marvin A. Chirelstein, *Fair Shares in Corporate Mergers and Takeovers*, 88 HARV. L. REV. 297 (1974) (stating that a “parent stands in a fiduciary relationship to the subsidiary’s public stockholders” but, as of 1974, courts have rarely extended “fiduciary safeguards beyond the point of simple fraud”). For developments after *Weinberger*, *see, e.g.*, *Kahn v. M&F Worldwide Corp.*, 88 A.3d 635 (Del. 2014), designating the business judgment rule as the standard of review when a majority owner conditions a cash-out merger upon the approval of “both an independent, adequately-empowered Special Committee [of the subsidiary’s board] that fulfills its duty of care, and the uncoerced, informed vote of a majority of the minority stockholders [of the subsidiary].”

215. On the shift from derivative litigation to class actions in the postwar years, *see generally* COFFEE, *supra* note 25, at 52–94 (discussing the emergence of class actions).

216. *Weinberger v. UOP, Inc.*, 457 A.2d 701 (Del. 1983).

217. *Id.* at 705.

share.²¹⁸ The shareholders alleged that Signal and its representatives on UOP board breached their duty of loyalty to UOP and its public shareholders.²¹⁹

At the time, there were few Delaware cases addressing fundamental transactions. As Marty Lipton notes, “the law was essentially around control shareholders and what was expected of control shareholders and corporate opportunity.”²²⁰ Attempting, perhaps, to fit *Weinberger* in this framework, the Supreme Court of Delaware explained that the actions of Signal and its appointed directors on the UOP board were sufficient to require that the controlling shareholder and the board prove the entire fairness of the transaction.²²¹ “When directors of a Delaware corporation are on both sides of a transaction,” Justice Moore, a Wilmington attorney for 18 years before his appointment to the Supreme Court in 1982,²²² wrote, “they are required to demonstrate their utmost good faith and the most scrupulous inherent fairness of the bargain.”²²³

The meaning of fairness was a variation on the midcentury’s ideal. Seeking to offer a clearer definition of the concept of fairness in the new age of finance, Justice Moore made stock price one of the elements for evaluating fairness. As he held:

The concept of fairness has two basic aspects: fair dealing and fair price. The former embraces questions of when the transaction was timed, how it was initiated, structured, negotiated, disclosed to the directors, and how the approvals of the directors and the stockholders were obtained. The latter aspect of fairness relates to the economic and financial considerations of the proposed merger, including all relevant factors: assets, market value, earnings, future prospects, and any other elements that affect the intrinsic or inherent value of a company’s stock.²²⁴

Two years later, in *Unocal v. Mesa Petroleum Corp.*, the new fairness

218. *Id.*

219. *Id.*

220. Peter Atkins et al., Univ. of Pa. Law Sch., Insights from Practice: Did Delaware Get It Right or Mess Up in Addressing the Takeover Boom of the 1980s? (Sept 25, 2018).

221. *Weinberger*, 457 A.2d at 703. Because in cash-out mergers, statutory appraisal was already available to dissenting shareholders, the court limited their ability to demand that the directors prove the fairness of the transaction. The court held that before requiring the directors or controlling shareholders to demonstrate the entire fairness of the cash-out merger, the plaintiff shareholder “must allege specific acts of fraud, misrepresentation, or other items of misconduct to demonstrate the unfairness of the merger terms to the minority.” *Id.*

222. *Former Delaware Supreme Court Justice Dies at 83*, WBOC, <https://www.wboc.com/story/39638199/former-delaware-supreme-court-justice-dies-at-83> [<https://perma.cc/Y9QL-8MS5>].

223. *Weinberger*, 457 A.2d at 710.

224. *Id.* at 711.

standard was brought to bear upon the Delaware courts' analyses of hostile tender offers.²²⁵ *Unocal* was the first case to address the board's duties when faced with a hostile takeover. Mesa, "the owner of approximately 13% of Unocal's stock," initiated "a two-tier 'front loaded' cash tender offer for 64 million shares, or approximately 37% of Unocal's outstanding stock at a price of \$54 per share. The 'back-end' was designed to eliminate the remaining publicly held shares by an exchange of [highly subordinated] securities purportedly worth \$54 per share."²²⁶ The Unocal board determined that the price Mesa offered was inadequate, and "that Unocal should pursue a self-tender to provide the stockholders with a fairly priced alternative to the Mesa proposal."²²⁷ Mesa was not permitted to tender its stock into Unocal's self-tender.²²⁸

Given that Unocal's directors would most likely be replaced should Mesa succeed in its hostile tender offer to Unocal's shareholders, the decision of Unocal's board to adopt a defensive tactic, on its face, was tainted with a conflict of interest. Inside directors, in particular, were likely to be concerned about losing their livelihood. (While outsiders might experience reputational loss, their well-paid positions were with their own corporations, corporations where they were insiders.) Given the potential conflict of interest, a decision by a board to engage in a defensive tactic should have been analyzed under the fairness test like any other form of self-dealing. In this vein, the Court of Chancery "temporarily restrain[ed] Unocal from proceeding with the exchange offer unless it included Mesa."²²⁹

On appeal, the Supreme Court of Delaware reversed. Rather than imposing on Unocal's directors the burden to prove the entire fairness of the transaction, Justice Moore, writing for the court, adopted a more lenient test—a two prong test assessing, first, whether the directors "had reasonable grounds for believing that a danger to corporate policy and effectiveness existed" and, second, whether the defensive tactic the board adopted was "reasonable in relation to the threat posed."²³⁰

Then, holding that "the selective exchange offer [was] reasonably related to the threats posed," Justice Moore added:

It is consistent with the principle that "the minority stockholder

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

226. *Id.* at 949.

227. *Id.* at 950.

228. *Id.* at 950–51.

229. *Id.* at 952.

230. *Id.* at 946, 955. As the court further emphasized, if a majority of the independent directors endorsed the defensive tactic, then the board's action would likely meet the burden of the test. *Id.* at 955.

shall receive the substantial equivalent in value of what he had before” . . . *This concept of fairness, while stated in the merger context, is also relevant in the area of tender offer law.* Thus, the board’s decision to offer what it determined to be the fair value of the corporation to the 49% of its shareholders, who would otherwise be forced to accept highly subordinated “junk bonds,” is reasonable and consistent with the directors’ duty to ensure that the minority stockholders receive equal value for their shares.²³¹

Fairness, a standard of review intended to ensure protection to the corporation and its minority shareholders when those in control engaged in self-dealing transactions, was linked to the maximization of stock price and made a tool in the hands of the board seeking to defend against a hostile takeover. As the following section III.C elaborates, by the mid-1980s, gone were also the individual minority shareholder litigants, and in their place, large corporations, often at the behest of their controlling shareholders, became the direct beneficiaries of fairness and the shareholder wealth maximization rhetoric, more broadly. In the hostile-takeovers context, a discourse that originated in the New York courts’ equitable considerations became a means of protecting the powerful. *Revlon*, the last case in the trilogy, made it so.

C. Fairness and Upward Mobility, Revisited

Ronald Perelman’s battle to acquire Revlon Industries had all the makings of a good story.²³² Michel Christian Bergerac, Revlon’s CEO, was “a French-born deal maker.”²³³ He “studied political science and law in Paris. He was awarded a Fulbright Scholarship to study business at the University of California, Los Angeles, where he earned an M.B.A. He became an American citizen in the early 1960s.”²³⁴ Described as “a great raconteur, who knew so much about so many things like wine and art,” Bergerac managed Revlon since 1974, and expanded it “beyond its core cosmetics business, transforming it into a major player in the health care industry.”²³⁵

Perelman, Bergerac’s nemesis, was a third-generation Jewish American; born in North Carolina, not “with a silver spoon in his mouth.

231. *Id.* at 956–57 (emphasis added).

232. The New York Times described it as “[o]ne of the pivotal corporate battles of modern times.” Robert J. Cole, *High-Stakes Drama at Revlon*, N.Y. TIMES, Nov. 11, 1985.

233. *Michel C. Bergerac, Who Made Over Revlon, Dies at 84*, N.Y. TIMES, Sept. 18, 2016.

234. *Id.*

235. *Id.*

More like a sterling place setting for eight,” he was raised in Elkins Park, Pennsylvania.²³⁶ Perelman’s father, Raymond Perelman, was a businessman and philanthropist; he raised his son, Ronald, “to understand the intricacies of balance sheets and cash flow,” and expected him to join the family growing business.²³⁷ “By the time he was eleven, [Ronald] was sitting in on board meetings at his father’s company,”²³⁸ and while in college (undergraduate at Wharton), he helped his father secure a few profitable acquisitions. The deals “provided [Ronald] with his first taste of that unique adrenaline rush on which entrepreneurs thrive . . . the victory was sweet—and highly addicting. Ronald Perelman was hooked.”²³⁹ And he was impatient. Having realized that his father “had no foreseeable desire to retire,” Ronald Perelman decided to “jump[] ship”; he left the family business in Pennsylvania and “without preparation and with characteristic impatience and haste,” moved to New York, “arriv[ing] in Manhattan without important connections or a game plan.”²⁴⁰

Perelman’s first acquisition, in May 1978, was the Cohen-Hatfield jewelry chain, the majority of its business he promptly sold to Sam Walton, chairman of Wal-Mart Stores, leaving the Cohen-Hatfield Industries with their “most profitable operation, the wholesale jewelry.”²⁴¹ His next move was MacAndrews & Forbes, “a supplier of licorice extract and bulk chocolate which had been started a century before.”²⁴² He financed the purchase with low grade, high yield bonds, “precursor of the legendary junk bond” that will come to characterize his operations, consolidated under the “banner of MacAndrews & Forbes Group.”²⁴³

In 1983, Perelman’s acquired Technicolor, “a prominent component of the movie industry,”²⁴⁴ a transaction that would keep him in litigation for a

236. RICHARD HACK, WHEN MONEY IS KING: HOW REVLON’S RON PERELMAN MASTERED THE WORLD OF FINANCE TO CREATE ONE OF AMERICA’S GREATEST BUSINESS EMPIRES, AND FOUND GLAMOUR, BEAUTY AND THE HIGH LIFE IN THE BARGAIN 2 (1996); Jacob Bernstein, *The Debt King*, N.Y. TIMES, Jan. 7, 2022.

237. HACK, *supra* note 236, at 2.

238. *Id.* at 3.

239. *Id.* at 4–5.

240. *Id.* at 9.

241. *Id.* at 10–12.

242. *Id.* at 13.

243. *Id.* at 13–17.

244. *Id.* at 20.

decade longer,²⁴⁵ and in 1984, he took MacAndrews & Forbes private.²⁴⁶ A few months later, MacAndrews & Forbes acquired Pantry Pride, “a supermarket chain discharged from Chapter 11 bankruptcy reorganization in 1981.”²⁴⁷ Shortly thereafter, Eric Gleacher called Perelman.²⁴⁸ An investment banker with Morgan Stanley, Gleacher suggested that Perelman acquire Revlon, “the cosmetic colossus.”²⁴⁹ As Gleacher explained to Perelman, Revlon “was a slumbering Titan”: “profits had fallen . . . the stock had slid”,²⁵⁰ “turning the company around would be a challenge” for which Perelman was well suited.²⁵¹

Perelman was intrigued, and the Revlon saga began. On June 14, 1985, Perelman visited Bergerac’s “lavish penthouse apartment.”²⁵² At the time, Revlon “had over \$2.3 billion in assets and net worth in excess of \$1 billion.”²⁵³ Perelman’s recently acquired Pantry Pride “had assets of \$407 million . . . a net worth of about \$145 million . . . and a huge tax-loss carryforward of over \$300 million,” and Perelman wanted to use it to purchase Revlon.²⁵⁴ Bergerac, the “courtly, somewhat imperious, urbane, witty Frenchman,” was unimpressed with “the crude, brusque, [and] humorless” Perelman.²⁵⁵ “Can you imagine this guy, saying he’s going to make me a rich man?” Bergerac angrily commented after the meeting.²⁵⁶

Indeed, despite Perelman’s successful background, the “Old Boys Club of Wall Street” viewed him as an “upstart”: “a man whose pushy demeanor and cigar smoke gave them more reason for irritation than for confidence.”²⁵⁷ That his banker was Michael Milken of Drexel Burnham with his junk bonds operation did not help matters.²⁵⁸ As Perelman’s lawyer, Donald Drapkin, commented, “They didn’t hit it off . . . Bergerac with his Chateau Lafite, and

245. See, e.g., *Cede & Co. v. Technicolor*, 634 A.2d 345 (Del. 1993). See also *Cede & Co. v. Technicolor*, 2001 WL 515106 (Del. Ch. May 7, 2001) (noting that “the long history of the dispute between these parties is well known not only to the parties, but also to all those who are familiar with Delaware corporate law.”).

246. HACK, *supra* note 236, at 26.

247. CONNIE BRUCK, *THE PREDATORS’ BALL: THE INSIDE OF DREXEL BURNHAM AND THE RISE OF THE JUNK BOND RAIDERS* 193 (1988).

248. HACK, *supra* note 236, at 45.

249. *Id.*

250. *Id.*

251. *Id.*; see also *Revlon Is Called Overpriced by Some Analysts Despite Wide Speculation About a Takeover*, WALL ST. J., May 22, 1984.

252. BRUCK, *supra* note 247, at 193.

253. *Id.*

254. *Id.*

255. *Id.* at 194.

256. *Id.*

257. HACK, *supra* note 236, at 10.

258. BRUCK, *supra* note 247, at 197.

Ronnie with his diet Coke.”²⁵⁹

The aftermath of the June 14th meeting is well documented in corporate law casebooks. Perelman, frustrated that his attempts at a friendly transaction were not reciprocated, made a hostile tender offer to Revlon’s shareholders. Revlon responded by implementing a poison pill and a defensive stock repurchase plan, involving an exchange of notes for shares of Revlon’s stock. The notes included serious limitations on Revlon’s ability to incur additional debt (these restrictions could be waived by a majority of the independent directors on the Revlon board). When Perelman did not back down and continued to bid on Revlon’s stock, the Revlon board responded by negotiating a merger agreement with their chosen knight (Forstmann Little & Co.); it included Revlon’s promise to remove the notes’ covenants. When angered noteholders threatened suit, Revlon solicited Forstmann’s support for the notes’ par value and, in exchange, granted Forstmann an option to purchase certain Revlon assets at “some \$100-\$175 million” below their value if “another acquirer got 40% of Revlon’s shares” and a twenty five million dollar cancellation fee “if another acquirer got more than 19.9% of Revlon’s stock.”²⁶⁰ Perelman “challeng[ed] the lock-up, the cancellation fee . . . and the Notes covenants.”²⁶¹

The financial and legal battle was, as Connie Bruck writes, “a class war, between the corporate America and Wall Street elite, and the Drexel arrivistes.”²⁶² It reflected “the age-old hatred for the outsider, always exacerbated when that undesirable other dares to venture beyond his confines and encroach upon the elite’s preserve.”²⁶³ Unlike the second-generation Americans we saw in Part II of this Article, who, seemingly united against anti-Semitism, aimed to find their place in corporate America by entrepreneurship or investment, Milken and Perelman were fighting against lawyers who, by the 1980s, “were part of the Jewish establishment in New York.”²⁶⁴ As Bruck writes, those within the establishment “feared that the common strain among these nouveau entrepreneurs and their nouveau bankers at Drexel—an overwhelming majority were Jews—would unleash a backlash of virulent anti-Semitism.”²⁶⁵

Joseph Flom of Skadden Arps, Perelman’s lawyers, was accustomed to

259. *Id.* at 194.

260. *Revlon, Inc. v. MacAndrews & Forbes Holding, Inc.*, 506 A.2d 173, 178–79 (Del. 1986).

261. *Id.* at 179; *see also* Cole, *supra* note 232.

262. BRUCK, *supra* note 247, at 197.

263. *Id.*

264. *Id.* at 205.

265. *Id.*

being scorned. Described as “indifferent to social niceties,” he was also well respected; “in the judgment of colleagues and of some adversaries, his will to win was unsurpassed and he was often masterful.”²⁶⁶ As noted in Part II of this Article, in the 1940s, when white-shoe firms looked with disdain on derivative litigation, Jewish lawyers took on the representation of minority shareholders. In the 1950s and 1960s, when “old-line Wall Street law firms” considered it “scandalous for one company to buy another company without the target agreeing to be bought,”²⁶⁷ Flom built his practice and reputation representing those engaged in proxy fights.²⁶⁸ When, in the 1980s, hostile takeovers became, almost overnight, acceptable and what “every law firm wanted to do,” Flom was ready.²⁶⁹ It was Flom, the legal mastermind, who ultimately ensured Perelman’s victory.

The Chancery Court of Delaware, apparently unfazed by the social and cultural wars the case engendered, found for the plaintiffs and issued a preliminary injunction. Citing *Unocal*, Justice Walsh (he was nominated to the Supreme Court three weeks before the decision was announced), wrote the Chancery Court decision, stating:

The board’s primary responsibility after the exchange offer was to bargain for the rights of the remaining equity holders. By agreeing to a lock-up and no shop clause in exchange for protecting the rights of the Noteholders, the Revlon Board failed in its fiduciary duty to the shareholders. The board may have been informed, but its performance did not conform to the other component of the business judgment rule—the duty of loyalty. The board’s self-interest in resolving the Noteholders’ problems led to concessions which effectively excluded Pantry Pride to the detriment of Revlon’s shareholders. Thus, the element of loyalty may turn, as it does here, in the selection of a takeover defense or a bargaining device that is not proportionate to the objective needs of the shareholders but merely serves the convenience of the directors.²⁷⁰

266. MALCOLM GLADWELL, *OUTLIERS: THE STORY OF SUCCESS* 126–27 (2008).

267. *Id.* at 124–25. As Gladwell notes,

up until the 1980s old-line Wall Street law firms had a very specific idea about what it was that they did. They were corporate lawyers. They represented the country’s largest and most prestigious companies, and ‘represented’ meant they handled the taxes and legal work behind the issuing of stocks and bonds and made sure their clients did not run afoul of federal regulators.

Id. at 124.

268. *Id.* at 125–26.

269. *Id.* at 127–28.

270. *MacAndrews & Forbes Holding, Inc. v. Revlon, Inc.*, 501 A.2d 1239, 1250 (Del. Ch. 1985).

While Walsh cited *Unocal* for his statement, his analysis focused on the traditional directors' duty of loyalty, and Flom was the first to notice. As he told Stuart Shapiro, who would argue the case before the Supreme Court of Delaware, "You can't argue that they have an absolute right or absolute obligation to take a certain action. You have to argue that what they did was conflicted and wrong. Not because they chose one course over the other, but because they did it on the wrong basis."²⁷¹

As Flom understood, if Shapiro could demonstrate that the directors, when choosing Forstmann, did so to ensure that Revlon's noteholders were protected, he would demonstrate that the directors breached their duty of loyalty to their shareholders and Perelman would win the case. And Flom was right. Justice Moore for the Delaware Supreme Court began by noting:

The Revlon board's authorization permitting management to negotiate a merger or buyout with a third party was a recognition that the company was for sale. The duty of the board had thus changed from the preservation of Revlon as a corporate entity to the maximization of the company's value at a sale for the stockholders' benefit. . . . The directors' role changed from defenders of the corporate bastion to auctioneers charged with getting the best price for the stockholders at a sale of the company.²⁷²

Because this passage has since been quoted to champion corporate law's commitment to shareholder value, it is worth emphasizing that Moore's was not a statement about corporate purpose. Rather, Moore, who defined fairness in *Weinberger* and applied it in *Unocal*, applied it again in *Revlon*. Revlon's directors, according to *Unocal*, were required to assess the threat of Perelman's bid and respond, bearing in mind the two prongs of the fairness standard: fair dealing and fair price. When the directors allowed their concerns about the noteholders to cloud their judgment, they failed to meet this standard, and thus breached their duty of loyalty. As Moore explained:

The impending waiver of the Notes covenants had caused the value of the Notes to fall, and the board was aware of the noteholders' ire as well as their subsequent threats of suit. The directors thus made support of the Notes an integral part of the company's dealings with Forstmann, even though their primary responsibility at this stage was to the equity owners. . . . The principal benefit went to the directors, who avoided personal

271. JOHN WEIR CLOSE, A GIANT COW-TIPPING BY SAVAGES: THE BOOM, BUST, AND BOOM CULTURE OF M&A 109 (2013).

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

liability to a class of creditors to whom the board owed no further duty under the circumstances. Thus, when a board ends an intense bidding contest on an insubstantial basis, and where a significant by-product of that action is to protect the directors against a perceived threat of personal liability for consequences stemming from the adoption of previous defensive measures, the action cannot withstand the enhanced scrutiny which Unocal requires of director conduct.²⁷³

What has since become known as the Revlon duty, that is, the duty of directors to maximize profit to their shareholders, was nothing more than an application of the 1980s fairness standard of review.²⁷⁴

Notably, the beneficiaries of the decision in *Revlon* were those who traded their shares as the struggle was brewing. “In the last five trading days before the Pantry Pride offer, an average of 1,258,800 shares of Revlon common stock per day traded hands, as compared to 283,760 per day in the preceding five trading days.”²⁷⁵ An entire “shareholder base” had changed before the transaction even happened.²⁷⁶ “Here we built a great American corporation,” Mr. Bergerac noted.²⁷⁷ “Then through this process the stock ended up in the hands of the arbitrageurs, who forced the sale of the company.”²⁷⁸ “In a larger sense,” Karen Ho writes, “the takeover movement of the 1980s helped to radically re-shift the interests of senior executives from the workings and constituents of the corporation . . . to those of Wall Street and large shareholders.”²⁷⁹

In short, a profit-maximization ideal that originated in the Progressives’ concerns about minority shareholders and was shaped in the reform-oriented New York courts in the midcentury, became in Delaware’s capable hands a means of promoting the dominance of financiers and their lawyers.

273. *Id.* at 182, 184.

274. See similarly Lawrence A. Cunningham & Charles M. Yablon, *Delaware Fiduciary Duty Law After QVC and Technicolor: A Unified Standard (and the End of Revlon Duties?)*, 49 BUS. L. 1593–94 (1994) (arguing that, in the 1980s, the Delaware courts have turned “Delaware fiduciary law toward a single, more unified standard, and away from doctrinal fragmentation”). As Cunningham and Yablon note, Justice Moore had grimaced when an attorney used the term “*Revlon-land*” during oral argument in *Paramount Communications, Inc. v. QVC Network, Inc.*, 637 A.2d 34 (Del. 1994). *Id.* at 1593.

275. BRUCK, *supra* note 247, at 215–16.

276. *Id.*

277. Michel C. Bergerac, *Who Made Over Revlon, Dies at 84*, N.Y. TIMES, Sept. 18, 2016.

278. *Id.*

279. HO, *supra* note 7, at 141.

EPILOGUE

“The conquest of Revlon,” Bruck writes, “signaled the end of an era.”²⁸⁰ Revlon and its advisers believed they were defending “a way of corporate life—plush, congenial and secure.”²⁸¹ And they lost to the “junk-bond marauders.”²⁸² A company, connections, relationships were broken.²⁸³ Financially, however, everyone fared well. The lawyers and investment bankers netted high fees;²⁸⁴ Revlon’s senior executives lost their jobs but cashed on their golden parachutes (golden parachutes totaling \$27.2 million were paid out to twelve executives);²⁸⁵ Bergerac’s severance package amounted to \$35 million;²⁸⁶ while Perelman got Revlon, and the social status that was presumably associated with it. The shareholders received \$58 per share and even those who exchanged shares for bonds made profit.²⁸⁷

And here perhaps is the peculiarity of the shareholder wealth maximization idea that many have since associated with *Revlon*. While the litigation was brought against the directors of Revlon, at stake was not the welfare of the corporation (in fact, during the hostile takeover decade, the welfare of the corporation was often at odds with the well-being, or profits, of its constituencies). The question of fiduciary obligations and the associated fairness standard and fair price, more broadly, became focused not on the relationship between directors and shareholders, but rather on the allocation of benefits, or balance of interests, between shareholders and other corporate constituencies, in the case of Revlon, the noteholders.

Paramount Communications, Inc. v. Time, a case addressing defensive tactics that blocked Time’s shareholders from accepting Paramount’s tender offer at almost twice the market price of Time’s stock, illustrates the courts’ shift in focus.²⁸⁸ Describing *Time* as a case involving differences of opinion

280. BRUCK, *supra* note 247, at 227.

281. *Id.* at 277.

282. *Id.*

283. *Id.* at 229.

284. See, e.g., JEFF MADRICK, *AGE OF GREED: THE TRIUMPH OF FINANCE AND THE DECLINE OF AMERICA, 1970 TO THE PRESENT* 216 (2011) (noting that “[t]he Revlon deal produced stunning fees for the bankers and lawyers”); Daniel Hertzberg, *Advice in Revlon Brawl Wasn’t Cheap: Fees in Takeover Fight Will Establish Record*, WALL ST. J., Nov. 8, 1985 at 1 (noting that “[i]nvestment bankers and lawyers were likely to rake in \$100 million or more in fees”).

285. BRUCK, *supra* note 247, at 231–32.

286. *Id.*; CLOSE, *supra* note 271, at 112.

287. BRUCK, *supra* note 247, at 232–33. As Bruck writes, “the only dissonant note in this chorus of happy profiteers came, as is usual in these transactions, from the bondholders of the acquired company who found their paper suddenly downgraded now that the company was so debt-laden.” *Id.* at 233.

288. *Paramount Communications, Inc. v. Time, Inc.*, 571 A.2d 1140 (Del. 1989).

between the directors' vision for the corporation and the shareholders' wish to maximize their profits, the Chancery Court of Delaware saw no need to apply the fairness standard or restrict the directors' actions, irrespective of these actions' impact on the shareholders' wealth (and the Delaware Supreme Court affirmed).²⁸⁹ As Chancellor Allen explained, "[D]irectors, not shareholders, are charged with the duty to manage the firm . . . That many, presumably most, shareholders would prefer the board to do otherwise than it has done does not . . . afford a basis to interfere with the effectuation of the board's business judgment."²⁹⁰

More recent decisions further limited *Revlon's* impact on directors' duties toward their corporations' shareholders, reverting to the courts' embrace of managerial freedom. In *Lyondell Chemical Co. v. Ryan*, a case involving a class action challenge to a merger transaction, the Supreme Court of Delaware concluded that "there are no legally prescribed steps that directors must follow to satisfy their *Revlon* duties. Thus, the directors' failure to take any specific steps during the sale process could not have demonstrated a conscious disregard of their duties."²⁹¹ "[T]here is a vast difference between an inadequate or flawed effort to carry out fiduciary duties and a conscious disregard for those duties," the Court noted.²⁹² And in *Corwin v. KKR Financial Holdings LLC*, the Delaware Supreme Court went further, holding that when a stock-for-stock merger "is approved by a fully informed, uncoerced vote of the disinterested stockholders, the business judgment rule applies."²⁹³

In turn, decisions having to do with the allocation of benefits between different investors, continued to refer to the shareholder wealth maximization. For one thing, the same year *Revlon* was decided, in *Katz v. Oak Industries, Inc.*, Chancellor Allen noted that "[i]t is the obligation of directors to attempt, within the law, to maximize the long-run interests of the corporation's stockholders."²⁹⁴ If they do so "at the expense of others," here the debt holders, it "does not for that reason constitute a breach of duty."²⁹⁵ Two years later, in *Simons v. Cogan*, the Supreme Court of Delaware similarly declined to extend the fiduciary obligations of corporate

289. See *Id.* at 1152 ("We find ample evidence in the record to support the Chancellor's Conclusion that the Time board's decision . . . was entitled to the protection of the business judgment rule.").

290. *Paramount Communications, Inc. v. Time, Inc.*, 1989 Del. Ch. LEXIS 77, at 89–90 (Del. Ch. 1989).

291. *Lyondell Chemical Co. v. Ryan*, 970 A.2d 235, 243 (Del. 2009).

292. *Id.*

293. *Corwin v. KKR Financial Holdings LLC*, 25 A.3d 304, 309 (Del. 2015).

294. *Katz v. Oak Indus., Inc.*, 508 A.2d 873, 879 (Del. 1986).

295. *Id.*

management to holders of convertible debentures. Justice Walsh reasoned: “A debenture is a credit instrument which does not devolve upon its holder an equity interest in the issuing corporation.”²⁹⁶ A convertible debenture was not different, representing “a contractual entitlement to the repayment of a debt and . . . not . . . an equitable interest in the issuing corporation necessary for the imposition of a trust relationship with concomitant fiduciary duties.”²⁹⁷ To trigger a fiduciary duty, Walsh concluded, “an existing property right or equitable interest supporting such a duty must exist.”²⁹⁸ And in *In re Trados Inc. Shareholder Litigation*, which addressed potential conflicting interests between the common and preferred stock during a merger, Vice Chancellor Laster stressed that directors are required to “strive in good faith and on an informed basis to maximize the value of the corporation for the benefit of its residual claimants, the ultimate beneficiaries of the firm’s value, not for the benefit of its contractual claimants.”²⁹⁹

The apparent dissonance between *Revlon*’s impact on directors’ duties to shareholders and Delaware’s statements about shareholder wealth maximization in cases involving other constituencies is resolved when we recognize *Revlon* and its aftermath as the culmination of the history told in this Article. As we saw, the rhetoric of shareholder wealth maximization has consistently been used to assuage shareholders’ concerns while courts empowered directors to act as “Platonic Guardians.”³⁰⁰ Just as courts earlier in the twentieth century pointed to shareholder profit maximization to encourage investment and assure investors that they would continue to receive income from their corporations, the Delaware courts’ refusal to extend fiduciary obligations to holders of debt securities, convertible debt, and preferred stock reassured shareholders that corporations were run for their benefit. At the same time, the cases chipping away at *Revlon*’s reach guaranteed managers their freedom.

Moreover, the rhetoric of shareholder wealth maximization has offered corporate managers a tool with which to thwart challenges to their power (including the threat of hostile takeovers). Like courts throughout the twentieth century, the Delaware courts in the 1980s provided directors language with which they could justify their actions; so long as corporate

296. *Simons v. Cogan*, 549 A.2d 300, 303 (Del. 1988).

297. *Id.*

298. *Id.* at 304.

299. *In re Trados Inc. S’holder Litig.*, 73 A.3d 17, 20, 40–41 (Del. Ch. 2013).

300. For the description of the board of directors as Platonic Guardians, see Robert A. Kessler, *The Statutory Requirement of a Board of Directors: A Corporate Anachronism*, 27 U. CHI. L. REV. 696, 697 (1960); Stephen M. Bainbridge, *Director Primacy: The Means and Ends of Corporate Governance*, 97 NW. U. L. REV. 547, 577 (2002-2003).

directors explained their decisions as maximizing wealth for their shareholders, the Delaware courts were not likely to intervene or evaluate their actions. Shareholder wealth maximization has been and will remain *dicta*, a rhetoric, not an edict.