2-1-2010

To Be or Not to Be? Citizens United and the Corporate Form

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DRAFT 2/1/10

TO BE OR NOT TO BE? *CITIZENS UNITED* AND THE CORPORATE FORM

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In *Citizens United vs. FEC*, the Supreme Court struck down a Federal ban on direct corporate expenditures on political campaigns.[2] The decision has been widely criticized and praised as a matter of First Amendment law.[3] But it is also interesting as another step in the evolution of our legal views of the corporation.[4] The thesis of this Article is that by viewing *Citizens United* through the prism of theories about the corporate form, it is possible to understand why both the majority and the dissent departed from previous Supreme Court cases on the First Amendment rights of corporations, and to predict what arguments can be expected next.

Historically, the corporation evolved from its origins in Roman law in a series of four major transformations. First, the concept of the corporation as a separate legal person from its owners or members had to be developed, and this development was only completed with the work of the civil law Commentators in the fourteenth century. By the end of the Middle Ages, the membership corporation, i.e., a corporation with several members who chose others to succeed them, had legal personality (the capacity to own property, sue and be sued, and even bear criminal responsibility) and unlimited life, was well established in both civil and common law jurisdictions. The next important step was the shift from non-profit membership corporations to for-profit business corporations, which took place in England and the U.S. in the end of the eighteenth and beginning of the nineteenth century. The third transformation was the shift from closely-held corporations to corporations whose shares are widely held and publicly traded, and with it the rise of limited liability and freedom to incorporate, which took place by the end of the nineteenth century and the beginning of the twentieth. Finally, the last major transformation was from corporations doing business in one country to multinational enterprises whose operations span the globe, which began after World War II and is still going on today.

Each of these four transformations was accompanied by changes in the legal conception of the corporation. What is remarkable, however, is that throughout all these changes spanning two millennia, the same three theories of the corporation can be discerned. Those theories are the aggregate theory, which views the corporation as an aggregate of its members or shareholders; the artificial entity theory, which views the corporation as a

[1] Irwin I. Cohn Professor of Law, the University of Michigan.
[2] Citizens United v. FEC, 2010 US Lexis 766 (2010), striking down 2 USC 441b (ban on corporate-funded independent expenditures).
[3] [cites]
[4] For an extensive discussion see Reuven S. Avi-Yonah, The Cyclical Transformations of the Corporate Form: A Historical Perspective on Corporate Social Responsibility, 30 Del. J. Cop. L. 767 (2005).

creature of the State; and the real entity theory, which views the corporation as neither the sum of its owners nor an extension of the state, but as a separate entity controlled by its managers.[5]

In this Article, I will first discuss how the three theories of the corporation are reflected in our historical jurisprudence, and then attempt to show how *Citizens United* fits within this tradition. Part I discusses the cyclical evolution of the three corporate theories from the 18th century onward and shows that each transformation brought forth all three theories, but that the real entity view always won and was the established view during periods of stability. Part II applies this analysis to *Citizens United* and its antecedents *Bellotti* and *Austin* and shows that all three theories arise in *Bellotti* and *Austin*, but that both the majority and the dissent in *Citizens United* adopt the real entity view. Part III concludes by predicting that the next confrontation will be about distinguishing between domestic and foreign corporations for First Amendment purposes, that all three theories will be advanced, and that ultimately the real entity view will prevail in this context as well.

I. The Cyclical Evolution of Corporate Theories[6]

a. From Nonprofit to For-Profit Corporations.

By the time the American colonies declared themselves to be "free and independent states," the corporation was well established in English law as a membership corporation, i.e., a corporation made up of members who selected their own successors, like the President and Fellows of Harvard College still do today. As such, a corporation had legal personality, i.e., the rights to own property, sue and be sued, act under a common seal, and other such "chestnuts."[7] Private corporations were used primarily for non-profit purposes (e.g., hospitals and universities), but by the 18th century there were also some commercial ones (e.g., the East India Company).[8]

There were two important limitations on corporations in this period. The first was royal control over corporations; in England and other European countries corporations could only be established by royal charter. Blackstone notes that although in Roman law corporations could be established without "the prince's consent", "with us in England, the king's consent is absolutely necessary."[9] Second, some degree of outside control over management was established through the institution of the committee of visitors, which represented the interests of the founder and of the wider community.[10]

[5] These three theories are the standard ones in the literature. See, e.g., David Millon, Theories of the Corporation, 1990 Duke L.J. 201.
[6] This part is based on Avi-Yonah, Cyclical Transformations, supra.
[7] Robert C. Clark, Corporate Law (1989). For a discussion how these basic features of corporate legal personality were established see Cyclical Transformations, supra.
[8] See the classification and description of various corporations in William Blackstone, 1 Commentaries, chap. XVIII (1765).
[9] Blackstone, 460; Tipling v. Pexall, 3 Bulstrode 233 (1614) ("the King creates them"). For an example of a charter enumerating corporate legal rights, see, e.g., Sutton's Hospital Case, 10 Co. Rep. 1 (1612).
[10] Blackstone, 467-469.

But other than in extraordinary cases, the real entity view of the corporation prevailed throughout this period and management (the members) were firmly in control. "A corporation aggregate of many is invisible, immortal, and rests only in intendment and consideration of the law."[11] As such, it was a self-perpetuating body subject to relatively little outside regulation. Corporations, Blackstone notes, are "artificial persons, who may maintain a perpetual succession, and enjoy a kind of legal immortality."[12] When the members "are consolidated and united into a corporation, they and their successors are then considered as one person in law: as one person, they have one will, which is collected from the sense of the majority of the individuals… for all the individual members that have existed from the foundation to the present time, or that shall ever hereafter exist, are but one person in law, a person that never dies."[13] This one person then acquires all the rights of corporations, including perpetual succession, the right to sue and be sued, the right to own property, to have a common seal, to make by-laws, and to be subject to certain criminal liabilities.[14] The king constituted corporations, and the king or other visitors exercised some degree of supervision over them, but once established, the corporation (i.e., its members) remained subject to relatively little outside regulation.

This situation meant that corporate status was very desirable, especially since the members also enjoyed limited liability for corporate debts.[15] But the English Kings were very cautious with granting corporate charters, especially in the case of for-profit enterprises; only corporations that were clearly vested with a public purpose and benefited the public fisc, like the East India and Hudson Bay Companies, received royal approval, and accumulated vast power. As more capital was required for commercial enterprises this resulted in promoters organizing corporations with transferable shares and claiming that under authority of a lost or obsolete charter the shareholders enjoyed limited liability. After the South Sea Bubble burst in 1720, this problem (and the desire of the East India Company to retain its monopoly) led to the Bubble Act, under which it became a crime to organize such corporations without explicit royal consent.[16] Although prosecutions under the Bubble Act were rare, it meant that the entire Industrial Revolution in England (1760-1820) took place outside the corporate form and without limited liability.[17] The Bubble Act was ultimately repealed in 1825, after the Industrial Revolution was over, but with the provision of unlimited liability for shareholders, which continued to be the rule in England until 1855.[18]

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[11] Sutton's Hospital Case, 10 Co. Rep. 1, 973 (1612).
[12] Blackstone, 455.
[13] Blackstone, 456.
[14] Blackstone, 463.
[15] Although this was not clear in the Roman sources, it was well established by Blackstone's time for royally chartered corporations. "The debts of a corporation, either to or from it, are totally extinguished by its dissolution, so that the members cannot recover, or be charged with them, in their natural capacities." Blackstone, 472 (citing Ulpian).
[16] The Bubble Act, 6 Geo. I c. 18 (1720). See Ron Harris, Industrializing English Law: Enterpreneurship and Business Organization, 1720-1844 (2000).
[17] For attempts to avoid the Bubble Act which led to prosecutions see King v. Dodd, 9 East 516 (1808) and King v. Webb, 14 East 406 (1811). See Harris, supra.
[18] Bubble Act Repeal, 6 Geo. IV c. 91 (1825); Limited Liability Act, 18 & 19 Vict. C. 133 (1855).

This situation, which can be seen as a way of maintaining state control over corporations through restrictions on charters, meant that the next great shift in the use of corporate form took place in the fledgling United States. There, once the revolution was over, every state could issue corporate charters. The result was an explosion of charters for commercial enterprises. One of the first treatises written on corporate law was Joseph Angell and Samuel Ames' Treatise on the Law of Private Corporations Aggregate, published in Boston in 1832.[19] Angell and Ames begin their book by stating that-

> The reader does not require to be told, that we have in our country an infinite number of corporations aggregate, which have no concern whatever with affairs of a municipal nature. These associations we not only find scattered throughout every cultivated part of the United States, but so engaged are they in all the varieties of useful pursuit, that we see them directing the concentration of mind and capital to…the encouragement and extension of the great interests of commerce, agriculture, and manufacturing. There is a great difference in this respect between our own country, and the country from which we have derived a great portion of our laws. What is done in England by combination, unless it be the management of municipal concerns, is most generally done by a combination of individuals, established by mere articles of agreement. On the other hand, what is done here by the co-operation of several persons is, in the greater number of instances, the result of a consolidation effected by an express act or charter of incorporation.[20]

The main reason for this proliferation of corporations in the United States was the second great transformation in the role of the corporation in society: from primarily a non-for-profit to primarily a for-profit enterprise. As Judge Kent stated, "the multiplication of corporations in the United States, and the avidity with which they are sought, have arisen in consequence of the power which a large and consolidated capital gives them over business of every kind; and the facility which the incorporation gives to the management of capital, and the security which it affords to the persons of its members, and to their property not vested in the corporate stock."[21]

This was a profound shift, and not surprisingly it led to a revival of the centuries- old debate about the nature of the corporate form and its relationship to the shareholders and to the state. This debate can be seen if we examine the opinions on the subject issued by the first great American jurist, John Marshall. Three of Marshall's opinions, written decades apart, are particularly relevant here: *Bank of the United States v. Deveaux* (1809),

[19] Angell and Ames were preceded by the English work of John Kyd, published in London in 1793, but that treatise was devoted primarily to municipal corporations. See Angell & Ames, vi. The Angell & Ames treatise was very successful, with 11 editions published until 1875.
[20] Angell & Ames, v; see also ibid, 35: "In no country have corporations been multiplied to so great an extent, as in our own…There is scarcely an individual of respectable character in our community, who is not a member of, at least, one private company or society which is incorporated…Acts of incorporation are moreover continually solicited at every session of the legislature."
[21] Angell & Ames, 36, citing 2 Kent's Com. 219. The last sentence refers to limited liability, which will be discussed below.

Dartmouth College v. Woodward (1819), and *Bank of the United States v. Dandridge* (1827).[22] These opinions represent the evolution of his thinking on corporations, which moved from the aggregate view (Deveaux) to the artificial entity view (Dartmouth College) to the real entity view (Dandridge).

Deveaux involved an attempt by the state of Georgia to tax the Savannah branch of the Bank of the United States, a corporation established by Congress in 1791, as part of the early struggles around federalism. The Bank was a membership corporation ("The President, Directors and Company of the Bank of the United States") and all the members were citizens of Pennsylvania. The Bank refused to pay the tax and the State sent its collectors to enforce payment, whereupon the Bank sued the collectors in federal court, claiming diversity jurisdiction. The issue facing the court was whether a corporation made up of members from one state could sue citizens of another state in federal court on diversity grounds. This in turn required deciding between the view that "the individual character of the members is so wholly lost in that of the corporation, that the court cannot take notice of it", and the contrary view that "a corporation is composed of natural persons", i.e., between the entity (artificial or real) and aggregate views.[23]

Marshall decided in favor of the aggregate view. He stated that the corporation itself, "that mere legal entity", cannot be a citizen or sue in federal court, unless it can be regarded as "a company of individuals".[24] However, since the reasons that led Congress to enact diversity jurisdiction applied to corporations as well, Marshall was inclined to see the controversy as being between the members "suing in their corporate character" and their opponents.[25] "The controversy is substantially between aliens, suing by a corporate name, and a citizen…in this case the corporate name represents persons who are members of the corporation."[26] The Court therefore held that federal jurisdiction existed.

Ten years later Marshall was faced with another difficult issue involving corporations. In the famous *Dartmouth College* case, the state of New Hampshire attempted to alter the charter of Dartmouth College (incorporated as a membership corporation by George III in 1769, under the name of The Trustees of Dartmouth College), by transferring the appointment of trustees to the state, thereby effectively taking it over. The trustees objected, arguing that the charter constituted a contract and altering it violated the contracts clause of the Constitution.[27]

Marshall held that as the College was a private corporation, its charter was a contract and was protected by the contracts clause. He began by noting that the funds for the College came from private sources and its educational character did not make it public either. He

[22] 9 U.S. (5 Cranch) 61 (1809); 17 U.S. (4 Wheat.) 518 (1819); 25 U.S. (12 Wheat.) 64 (1827).
[23] Deveaux, 9 U.S. 63-64.
[24] 9 U.S. 86-87.
[25] Ibid., 87-88.
[26] Ibid., 91.
[27] The Trustees of Dartmouth College v. Woodward, 17 U.S. (4 Wheat.) 518 (1819).

then got to the heart of the question- whether the act of incorporation by the state makes it possible for the state to take it over. In frequently quoted language, Marshall held that-

> A corporation is an artificial being, invisible, intangible, and existing only in contemplation of law. Being the mere creature of law, it possesses only those properties which the charter of its creation confers upon it, either expressly, or as incidental to its very existence.[28]

This language reflects the artificial entity view of the corporation. But Marshall then went on to note that, having created the corporation, the state may not treat it as a mere extension of itself: "this being does not share in the civil government of the country, unless that be the purpose for which it was created."[29] Even though its object is to promote governmentally approved aims, this does not make corporations into mere instruments of government. Instead, the corporation exists to represent the interest of the founder and his descendants in the aims for which it was founded. This interest is in the United States protected by the contracts clause, although in England, Marshall recognized, Parliament had the power to annul the charter.[30] In this country "the body corporate, as possessing the whole legal and equitable interest, and completely representing the donors, for the purpose of executing the trust, has rights which are protected by the constitution."[31]

It should be noted that while Marshall held that the state may not take over a private corporation, even one founded for public ends, the emphasis on the artificial nature of the corporation left ample room for state regulation via the original charter. Since states were busy granting charters by the hundreds, the Dartmouth opinion thus enabled the states to regulate corporations, should they wish to do so.

Finally, six years later, Marshall was once more called to opine on the nature of corporations in another case involving the Bank of the United States.[32] The case involved a suit by the Bank on a bond executed by Dandridge, one of its cashiers, in which the defendant argued that the bond had never been approved by the Board of Directors, as required by the charter of incorporation. The key issue was whether the level of evidence required of corporations was higher than that required of individuals, since corporations are incapable of acting not in writing. Justice Story for the Court held that no distinction should be made: "The same presumptions are…applicable to corporations."[33] Marshall, however, dissented. He argued that—

> The corporation being one entire impersonal entity, distinct from the individuals who compose it, must be endowed with a mode of action peculiar to itself, which will always distinguish its transactions from those of its members. This faculty

[28] 17 U.S. 636.
[29] Ibid.
[30] 17 U.S. 642-643.
[31] 17 U.S. 654.
[32] Bank of the United States v. Dandridge, 25 U.S. (12 Wheat.) 64 (1825).
[33] 25 U.S. 70.

> must be exercised according to its own nature…This can be done only in writing.[34]

The Court's view was the more pragmatic one, but Marshall's view was more consistent with the real entity view of the corporation as distinct from its members, individually or collectively. It certainly forms an interesting contrast with the views he expressed in the *Deveaux* case sixteen years earlier.

How can one explain the shift in Marshall's view of the corporation from aggregate (*Deveaux*) to artificial (*Dartmouth College*) to real (*Dandridge*)? In part, this stems from the circumstances of these particular cases. In *Deveaux*, Marshall wanted to confer diversity jurisdiction to protect a federal institution (he was after all a Federalist), and the only way to do so was to look through the corporation to its members. In *Dartmouth College*, the issue involved the relationship of private corporations (albeit "imbued with a public purpose"; the full fledged private/public distinction had not yet evolved) to the state, and thus Marshall emphasized the role of the state in creating the corporation, while placing clear limits on its ability to regulate corporations thereafter. These limits were required as the result of the proliferation of corporations, especially for- profit business corporations, since otherwise the state would be able to take over purely private businesses. The result in *Dartmouth College* favored in practice the real entity view, since once a private corporation was created, it could no longer be taken over or perhaps even be overly regulated by the state. Thus, it may not be surprising that by the time he came to write his *Dandridge* dissent Marshall took the real entity view, even though it contradicted his opinion in *Deveaux* (which is not mentioned).

Two important legal developments during the same period strengthened the real entity view and weakened the aggregate and artificial entity views of the corporation: the rise of limited liability and the spread of general incorporation laws. Limited liability weakened the aggregate view, and general incorporation weakened the artificial entity view.

First, limited liability: As we have seen, in England limited liability did not exist for corporations until 1855. In the United States, however, most states adopted limited liability in the 1830s.[35] In their second edition, Angell & Ames explain that this was the primary distinction between a partnership and a corporation:

> In every private unincorporated company, the members are liable for the debts without limitation, whereas in incorporated societies, they are only liable to the extent of their shares…It is frequently the principal object, in this and in other countries, in procuring an act of incorporation, to limit the risk of the partners to their shares in the stock of the association; and prudent men are always backward

[34] 25 U.S. 91-92.
[35] Phillip I. Bloomberg, The Multinational Challenge to Corporation Law (1993).

> in taking stock when they become mere copartners as regards their personal liability for the company debts.[36]

When Angell & Ames wrote this limited liability was by no means a universally established rule for corporations[37]; they were thus trying to establish the law as much as describing the law that existed. Their main argument, familiar from current debates on limited liability[38], was that "[t]he public, therefore, gain by acts incorporating trading associations, as by such means persons are induced to hazard a certain amount of property for the purposes of trade and public improvement, who would abstain from doing so, were not their liability limited."[39]

Eventually this argument won the day, and by 1840 most of the states established limited liability.[40] Limited liability, in turn, led to a decline in the emphasis on the aggregate theory, because the aggregate view of corporations tends to reduce the distinction between the corporation and its members or shareholders that is at the heart of limited liability.[41]

The decline of the aggregate view can clearly be seen in two cases from the period 1839-1844, in which the Supreme Court repudiated Marshall's opinion in *Deveaux*. In *Bank of Augusta v. Earle* the Court held that a corporation incorporated by Georgia may execute a valid contract in Alabama on comity grounds, but it rejected the argument that Alabama was required to accept the contract on the basis of the privileges and immunities clause applied directly to the corporation's members (as required by the aggregate view), stating that *Deveaux* has never been extended that far. Chief Justice Taney emphasized that he

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[36] Angell & Ames, 23; see also id., at 349: "No rule of law we believe is better settled, than that, in general, the individual members of a private corporate body are not liable for the debts." See also the cite from Judge Kent, supra, emphasizing limited liability as a reason to incorporate.
[37] Bloomberg, supra.
[38] See, e.g., Henry Hansmann and Reinier Kraakman, Toward Unlimited Shareholder Liability for Corporate Torts, 100 Yale L J. 1879 (1991); Joseph A. Grundfest, The Limited Future of Unlimited Liability: A Capital Markets Perspective, 102 Yale J. on Reg. 387 (1992); Henry Hansmann and Reinier Kraakman, Do the Capital Markets Compel Limited Liability? A Response to Professor Grundfest, 102 Yale J. on Reg. 427 (1992); Nina A. Mendelson, A Control-Based Approach to Shareholder Liability for Corporate Torts, 102 Colum. L. Rev. 1203 (2002).
[39] Angell & Ames, 24. They go on to argue that states who pursue the contrary policy, like Massachusetts, "drive millions of capital into the neighboring states for investment"- an early instance of a "race" (to the top or bottom). Ibid., 362.
[40] This was subject to one limitation, the "trust fund" doctrine, which held that the capital stock of corporation was to be held in trust for paying corporate debts and thus could not be distributed to shareholders while debts were outstanding. See Wood v. Dummer, 30 Fed. Cas. 435 (Cir. Ct. D. Maine, 1824).
[41] See generally Henry Hansmann & Reinier Kraakman, The Essential Role of Organizational Law, 110 Yale L.J. 387, 393 (2000) (describing the "core defining characteristic of a legal entity" as the "partitioning off of a separate set of assets in which the creditors of the firm have a prior security interest"); Margaret M. Blair, Locking in Capital: What Corporate Law Achieved for Business Organizers in the Nineteenth Century, 51 UCLA L. Rev. 387 (2003) (arguing that the main purpose of incorporation in the 19th century was to "lock in" capital in the firm because shareholders cannot force distributions, in exchange for limited liability).

rejected the aggregate view because of its implications for limited liability, as well as its implications for state regulation of the corporations operating in it:

> The result of this [aggregate view] would be to make the corporation a mere partnership in business, in which each stockholder would be liable to the whole extent of his property for the debts of the corporation…Besides, it would deprive every state of all control over the extent of corporate franchises proper to be granted in the state.[42]

In *Louisville, Cincinnati, and Charleston Railroad Co. v. Letson*, decided in 1844, the Court explicitly limited *Deveaux* to its facts, holding that diversity jurisdiction may arise even when some of the members of a defendant corporation are citizens of the same state as the plaintiff.[43] The Court stated that the *Deveaux* results "have never been satisfactory to the bar" and that a corporation "seems to us to be a person, although an artificial one, inhabiting and belonging to that state [of incorporation], and therefore entitled, for purposes of suing and being sued, to be deemed a citizen of that state."[44]

This result was required by the proliferation of business corporations having many shareholders in many states, as opposed to the membership corporations of Marshall's early days. As Angell & Ames stated, by 1832 "Joint stock companies are composed of persons who seldom know any thing of the business of the company, but who leave the management of it entirely to the board of directors, and are contented with receiving such periodical dividends as the directors think proper to make."[45] The separation of management from ownership, and the rise of limited liability, rendered the aggregate view implausible.[46]

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[42] Bank of Augusta v. Earle, 38 U.S. 519, 586-587 (1839).
[43] 43 U.S. 497 (1844).
[44] 43 U.S. 376. See also Marshall v. Baltimore & Ohio Railroad Co., 57 US 314 (1853), in which the Court held that for diversity purposes a corporation should be deemed a resident of its place of incorporation. This led to the current rule, adopted in 1958, under which a corporation is for diversity purposes a citizen of both the state it is incorporated in and the state in which it has its principal place of business. 28 USC 1332 ©.
[45] Angell & Ames, 32.
[46] See also Chief Justice Shaw's statement in Burrill v. Nahant Bank, 43 Mass. 163 (1840), that "A board of directors of the banks of Massachusetts is a body recognized by law. By the by-laws of these corporations, and by a usage, so general and uniform as to be regarded as part of the law of the land, they have the general superintendence and active management of all the concerns of the bank, *and constitute, for purposes of dealing with others, the corporation*" (emphasis added). It is hard to imagine a clearer rejection of the aggregate view. Similarly, in Hoyt v. Thompson's Executor, decided by the New York Court of Appeals in 1859, the court held that "[i]n corporate bodies the powers of the board of directors are, in a very important sense, original and undelegated. The stockholders do not confer, nor can they revoke those powers. They are derivative only in the sense of being received from the State in the act of incorporation. The directors convened as a board are the primary possessors of all the powers which the charter confers, and like private principals they may delegate to agents of their own appointment the performance of any acts which they themselves can perform. The recognition of this principle is absolutely necessary in the affairs of every corporation whose powers are vested in a board of directors. Without it the most ordinary business could not be carried on, and the corporate powers could not be executed." 19 N.Y. 207, 216 (1859). This constitutes a recognition that the aggregate view deriving from the membership corporation could not be

Second, general incorporation: The granting of corporate charters by state legislatures became in the 1820s and 1830s a process fraught with corruption.[47] Some Jacksonians reacted by advocating elimination of the rights of states to grant corporate charters. But the corporate form was so widely used that this was impracticable; instead, laws were passed in all the states permitting anyone to form a corporation on payment of a fee, without permission by the state legislature.[48] This democratizing move meant that the artificial entity theory, under which the corporation derives its powers from the state, lost most of its appeal, since the state was only vestigially involved in creating corporations. Instead, corporations were viewed as separate from both their shareholders and the state, and the real entity view reigned supreme.[49]

b. From Closely-Held to Widely-Held Corporations.

The situation between the 1820s and the end of the Civil War was thus the proliferation of for profit corporations, incorporated under general incorporation laws with minimal interference by the state, and whose shareholders enjoyed limited liability. Those shareholders were, however, relatively limited in number; despite the Angell & Ames quotation above, few corporations before 1865 required massive amounts of capital, and most were small, closely held enterprises. This enabled the Civil War income tax on corporate income to be imposed directly on the shareholders of corporations.[50]

This state of affairs began to change with the advent of the railroads, followed by the steel and oil companies. With the rise of large corporate enterprises, massive amounts of capital were required, and between 1865 and the 1890s the widely held, publicly traded, non-owner managed enterprise gradually became the norm for U.S. business activities. This was followed from 1890 to 1906 by a wave of consolidation that left several important business areas dominated by monopolies run by the "robber barons."

The shift from small, closely held enterprises to massive, publicly held ones once again necessitated a re-examination of the corporate form, and again all three theories of the corporation appear. A classic example of the aggregate view is the *Santa Clara* case, ultimately decided by the Supreme Court in 1886. This case is famous for Chief Justice Waite's statement that "The court does not wish to hear argument on the question whether the [equal protection clause] applies to these corporations. We are all of the

maintained as a practical matter in corporations with hundreds or thousands of shareholders, as already existed in the 1850s.

[47] See Angell & Ames, 35-36.

[48] See, e.g., the act adopted in 1837 by Connecticut permitting incorporation of "any lawful business", ch. 63, 1837 Conn. Pub. Acts 49, and various cases upholding such laws, e.g., Nesmith v. Sheldon, 48 US 812 (1849). See also President Jackson's veto message of the second bank of the United States, cited in Davis, 611: "If [the government] would confine itself to equal protection, and, as Heaven does its rains, shower its favors alike on the high and the low, the rich and the poor, it would be an unqualified blessing."

[49] The same result was obtained in England by the adoption of the Regulation and Incorporation Act, 19 & 20 Vict. C. 47 (1856).

[50] Reuven S. Avi-Yonah, Corporations, Society and the State: A Defense of the Corporate Tax, 90 Va. L. Rev. 1193 (2004).

opinion that it does."[51] Some scholars identified this as an application of the real entity view to corporations, but Prof. Horwitz has shown by examining Justice Field's opinion in the court below that it actually represented an application of the aggregate view. Specifically, Field held that the equal protection clause must apply to corporations for the following reasons:

> Private corporations consist of an association of individuals united for some lawful purpose, and permitted to use a common name in their business and have succession of membership without dissolution…But these members do not, because of such association, lose their right to protection, and equality of protection…Whatever affects the property of the corporation- that is, of all the members united by the common name- necessarily affects their interests…So, therefore, whenever a provision of the constitution or of a law guarantees to persons protection in their property… the benefits of the provision are extended to corporations; not to the name under which different persons are united, but to the individuals composing the union. The courts will always look through the name to see and protect those whom the name represents [citing *Deveaux.]*[52]

A clearer statement of the aggregate view can hardly be imagined; most remarkable is Field's reliance on *Deveaux* despite the fact that the Supreme Court overturned its results forty years earlier. Similarly, in *Pembina Consolidated Co. v. Pennsylvania*, decided two years later, Justice Field for the Court stated that "Under the designation of person there is no doubt that a private corporation is included. Such corporations are merely associations of individuals united for a special purpose."[53]

However, the artificial entity view was also raised in these cases. In *Santa Clara*, the railroad corporations made the argument that because they were operating under special congressional legislation they should be regarded as an extension of the federal government and therefore California could not tax them.[54] Field rejected this view (citing *Dartmouth College*), but noted that "when the instrumentality is the creation of the state- a corporation formed under its laws-and is employed or adopted by the general government for its convenience…it remains subject to the taxing power of the state."[55] And notably, in *Pembina* Field followed Taney in rejecting the argument that the privileges and immunities clause applied to corporations because they were not "citizens", even though the aggregate view he adopted in *Santa Clara* might have led to the contrary position. Instead, Field emphasized the relationship between the corporation and the incorporating state under the artificial entity view:

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[51] Santa Clara County v. Southern Pacific R.R. Co., 118 U.S. 394 (1886). See Morton J. Horwitz, Santa Clara Revisited: The Development of Corporate Theory, 88 W. Va. L. Rev. 173 (1985).
[52] 18 F. 385 (C.D.D. Cal. 1883), 409-410.
[53] 125 U.S. 181, 189 (1888). See also Mason v. Pewabic Mining Co., 133 U.S. 50 (1890), in which the Court stated that "we do not see that the right of the parties in regard to the assets of this corporation differ from those of a partnership on its dissolution."
[54] 18 F. Rep. 387.
[55] 18 F. Rep. 389.

> The term citizens, as used in this clause, applies only to natural persons, members of the body politic owing allegiance to the State, not to artificial persons created by the legislature, and possessing only such attributes as the legislature has prescribed…a grant of corporate existence was a grant of special privileges to the corporators, enabling them to act for certain specified purposes as a single individual, and exempting them, unless otherwise provided, from individual liability.[56]

Moreover, all three views of the corporation appear in *Hale v. Henkel*, decided by the Supreme Court in 1906. The issues were whether an agent of a corporation could invoke the Fifth Amendment privilege against self-incrimination or the Fourth Amendment protection against unreasonable search and seizure in the name of the corporation. On the Fifth Amendment issue, the Court held that the right against self-incrimination does not apply to corporations:

> The right of a person under the Fifth Amendment to refuse to incriminate himself is purely a personal privilege of the witness…The question whether a corporation is a "person" within the meaning of this Amendment really does not arise…since it can only be heard by oral evidence in the person of some one of its agents or employees.[57]

This is closest to the real entity view, since it rejects (like Marshall in *Dandridge*) the aggregate position of looking through a corporation to its shareholders, and takes into account the special characteristics of the corporation itself.

On the other hand, on the Fourth Amendment issue, the Court at first emphasized the artificial entity view, using it to justify regulation by the state:

> Conceding that the witness was an officer of the corporation under investigation, and that he was entitled to assert the rights of the corporation with respect to the production of its books and papers, we are of the opinion that there is a clear distinction in this particular between an individual and a corporation, and that the latter has no right to refuse to submit its books and papers for an examination at the suit of the State. The individual may stand upon his constitutional rights as a citizen…Upon the other hand, the corporation is a creature of the State. It is presumed to be incorporated for the benefit of the public. It receives certain special privileges and franchises, and holds them subject to the laws of the State and the limitations of its charter. Its powers are limited by law. It can make no contract not authorized by its charter. Its rights to act as a corporation are only preserved to it so long as it obeys the laws of its creation. There is a reserved right in the legislature to investigate its contracts and find out whether it has exceeded its powers. It would be a strange anomaly to hold that a State, having

[56] 125 US 187-88.
[57] Hale v. Henkel, 201 U.S. 43, 69-70 (1906).

> chartered a corporation to make use of certain franchises, could not in the exercise of its sovereignty inquire how these franchises had been employed, and whether they had been abused, and demand the production of the corporate books and papers for that purpose…While an individual may lawfully refuse to answer incriminating questions unless protected by an immunity statute, it does not follow that a corporation, vested with special privileges and franchises, may refuse to show its hand when charged with an abuse of such privileges.[58]

However, having clearly stated its reasons for limiting the application of the constitutional right, the Court suddenly reverts to the aggregate view when facing the question whether corporations have any Fourth Amendment rights at all:

> [W]e do not wish to be understood as holding that a corporation is not entitled to immunity, under the Fourth Amendment, against unreasonable searches and seizures. A corporation is, after all, but an association of individuals under an assumed name and with a distinct legal entity. In organizing itself as a collective body it waives no constitutional immunities appropriate to such body. Its property cannot be taken without compensation. It can only be proceeded against by due process of law, and is protected, under the Fourteenth Amendment, against unlawful discrimination. Corporations are a necessary feature of modern business activity, and their aggregated capital has become the source of nearly all great enterprises.[59]

What can explain this remarkable oscillation between the three views? The key is the last sentence quoted. As noted above, the period between 1890 and 1906 marked the height of the debate on the rise of the great corporations. The Court is trying to strike a balance between the rights of the corporations, which can best be protected under either the aggregate or the real entity views, and the regulatory power of the state, which is best reflected in the artificial entity view. On the one hand, as the Court states, "[c]orporations are a necessary feature of modern business activity" and must be protected. On the other hand, the right of the state to regulate must also be preserved, especially since the context of *Hale v. Henkel* was

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[58] 201 US 74-75. Remarkably, the court applies this analysis to give powers to the federal government over state corporations: "It is true that the corporation in this case was chartered under the laws of New Jersey, and that it receives its franchise from the legislature of that State; but such franchises, so far as they involve questions of interstate commerce, must also be exercised in subordination to the power of Congress to regulate such commerce, and in respect to this the General Government may also assert a sovereign authority to ascertain whether such franchises have been exercised in a lawful manner, with a due regard to its own laws. Being subject to this dual sovereignty, the General Government possesses the same right to see that its own laws are respected as the State would have with respect to the special franchises vested in it by the laws of the State. The powers of the General Government in this particular in the vindication of its own laws, are the same as if the corporation had been created by an act of Congress. It is not intended to intimate, however, that it has a general visitatorial power over state corporations." Ibid, 75. This issue came up in the corporate tax debate as well. Avi-Yonah, corporate tax, supra.

[59] Ibid., 76 (cites omitted).

an antitrust investigation into two major corporations, the American Tobacco Company and McAndrews & Forbes Inc.

Ultimately, however, the real entity view prevailed.[60] This involved first the rejection of the aggregate view. For example, in *Western Turf Association v. Greenberg*, decided just one year after *Hale v. Henkel*, Justice Harlan emphasized that a corporation is a separate entity from its shareholders, and therefore is not a "citizen" for purposes of the privileges and immunities clause or entitled to the protection of the due process clause: "the liberty guaranteed by the Fourteenth Amendment against deprivation without due process of law is the liberty of natural, not artificial, persons."[61] But by itself this position would have led to too much state regulation for the Lochner court. Thus, in *Southern Railway Co. v. Greene*, decided in 1909, the Court came out clearly for the position that the corporation *as such* was entitled to constitutional protection under the equal protection clause, without any reference to its shareholders: "the corporation…is within the meaning of the Fourteenth Amendment, a person within the jurisdiction of the state of Alabama, and entitled to be protected against any statute of the State which deprives it of the equal protection of the laws."[62]

Once again, the triumph of the real entity view can be explained by several factors. The aggregate view was raised by Field and others to protect the rights of corporations, but it was even more incongruous in the context of the mega-corporations of the 1890s, with thousands of shareholders, than in the pre-civil days. It also gave the corporation too many rights vis-a-vis the state, as seen in *Hale v. Henkel* and in *Greenberg*. The artificial entity view gave the state too much power to regulate corporations, as the *Hale v. Henkel* court came to realize when it laid out its implications. The real entity view was the most congruent with business realities as well as the one most suited to some balance between corporations and the state. By 1909, it was well established as the dominant view of the corporation, as reflected in contemporary debates surrounding the enactment of the corporate tax.[63]

[60] This view was also reflected in contemporary books and law review articles. See, e.g., Freund, The Legal Nature of Corporations (1897); Deiser, The Juristic Person, 57 U. Pa. L. Rev. 131 (1908); Machen, Corporate Personality, 24 Harv. L. Rev. 253 (1911); Laski, The Personality of Associations, 29 Harv. L. Rev. 404 (1916) ; I. Maurice Wormser, Piercing the Veil of Corporate Entity, 12 Columbia L. Rev. 496 (1912) (all rejecting the aggregate view). Compare for a statement of the aggregate view Morawetz, A Treatise on the Law of Private Corporations (1882), at iii ("the existence of the corporation as an entity independent of its members is a fiction.")

[61] 204 U.S. 359, 363.

[62] 216 U.S. 400, 417. Remarkably this case involves a discriminatory state tax similar to the one struck down by Field on aggregate grounds in Santa Clara. See also similar statements in Ludwig v. Western Union Tel. Co., 216 US 146, 157 (1910); Pullman Co. v. Kansas, 216 US 56, 64 (1910); Western Union Tel. Co. v. Kansas, 216 US 1, 36 (1910), which finally eliminated the restrictions imposed by Bank of Augusta v. Earl. See Horwitz, supra.

[63] See Avi-Yonah, corporate tax, supra.

The rise of the real entity view is also reflected in two other contemporary developments: the rise of the business judgment rule, and the decline of the *ultra vires* doctrine.[64] The business judgment rule rejected the aggregate view in holding that the board of directors held powers that were not delegated from the shareholders and that shareholders could not normally call into question the exercise of those powers. The *ultra vires* doctrine represented the ability of the state to require corporations to adhere to their charter, and was thus based on the artificial entity view; its decline thus reinforced the rejection of that view.

The first full statement of the business judgment rule was made in *Leslie v. Lorillard*, decided by the New York Court of appeals in 1888. The court held that-

> In actions by stockholders, which assail the acts of their directors or trustees, courts will not interfere unless the powers have been illegally or unconscientiously executed…Mere errors of judgment are not sufficient as grounds for equity interference; for the powers entrusted with corporate management are largely discretionary.[65]

A year later the same court expanded this statement, holding that-

> All powers directly conferred by statute, or impliedly granted, of necessity, must be exercised by the directors who are constituted by the law as the agency for the doing of corporate acts. The expression of the corporate will and the performance of corporate functions in the management of a corporation, may originate with its directors…Within the chartered authority they have the fullest power to regulate the concerns of a corporation, according to their best judgment…In the management of the affairs of the corporation, they are dependent solely upon their own knowledge of its business and their own judgment as to what its interests require.[66]

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[64] Another related development was the strengthening of limited liability resulting from the demise of the “trust fund” doctrine, which held that the capital stock of a corporation must be held in trust for the benefit of its creditors. This doctrine, which originated from Justice Story’s opinion in Wood v. Dummer, 30 Fed. Cas. 435 (1824), was upheld by the Supreme Court in Sawyer v. Hoag, 84 U.S. 610 (1873) on the basis on the aggregate view (“after all this artificial body is but the representative of its stockholders, and exists mainly for their benefit, and is governed and controlled by them through the officers whom they elect”, 84 U.S. 623). See also W. W. Cook, Stock & Stockholders (1887), 322. However, in 1892 the Supreme Court of Minnesota held in Hospes v. Northwestern Mfg. & Car Co., 48 Minn. 174, that “this trust fund doctrine…is not sufficiently precise or accurate to constitute a safe foundation upon which to build a system of legal rules…corporate property is not held in trust…Absolute control and power of disposition are inconsistent with the idea of trust. The capital of a corporation is its property…a corporation is in law as distinct a person as an individual is, and is entitled to hold property (if not contrary to its charter) as absolutely as an individual can hold it.” The doctrine then fell into desuetude, reinforced by the invention of no par stock in the early 20th century. See Horwitz, supra.

[65] 110 N.Y. 519, 532 (1888).

[66] Beveridge v. New York Elevated Railroad Co., 111 N.Y. 1 (1889).

This rule became well established, so that by 1905 a court could write that "it is [the board's] judgment, and not that of its stockholders outside of the board of directors, that is to shape [a corporation's] policies or decide upon its corporate acts. This principle is not disputed, and the citation of authorities in its support is unnecessary."[67] The rule reflected the real entity view, which equates the corporation with its management, and rejected the aggregate view of the corporation as an aggregate of its shareholders.[68]

The one potential limitation on the power of the board was the *ultra vires* doctrine, which held that a board could not act contrary to the powers conferred on it by the state. The *ultra vires* doctrine thus represented the artificial entity view. The doctrine originated in the pre- civil war era,[69] but became prominent in the arguments on the relationship of the state and the corporation in the 1880s and 1890s.[70] The artificial entity argument for upholding the limitation was stated clearly by the New York Court of Appeals in 1888-

> In the granting of charters the legislature is presumed to have had in view the public interest; and public policy is (as the interests of stockholders ought to be) concerned in the restriction of corporations within chartered limits, and a departure therefrom is only deemed excusable when it cannot result in prejudice to the public or to the shareholders. As artificial creations, they have no powers or faculties, except those with which they were endowed when created…Corporations are great engines for the promotion of the public convenience, and for the development of public wealth, and, so long as they are conducted for the purposes for which organized, they are a public benefit; but if allowed to engage, without supervision, in subjects of enterprise foreign to their charters, or if permitted unrestrainedly to control and monopolize the avenues to that industry in which they are engaged, they become a public menace, against which public policy and statutes design protection.[71]

The doctrine was upheld by the Supreme Court in the following year. Referring to the artificial entity doctrine, the Court stated that --

> It may be considered as the established doctrine of this court in regard to the powers of corporations, that they are such and such only as are conferred upon them by the acts of the legislatures of the several States under which

[67] Siegman v. Electric Vehicle Co., 140 F. 117, 118 (D.D.C.N.J. 1905). See also Manson v. Curtis, 223 N.Y. 313, 323 (1918), in which the court held that "[d]irectors are the exclusive, executive representatives of the corporation and are charged with the administration of its internal affairs and the management and use of its assets. Clearly the law does not permit the stockholders to create a sterilized board of directors."

[68] It also represented a transition from an agency to a trustee model of the relationship between shareholders and management. See Millon, supra.

[69] See, e.g., Abbott v. American Hard Rubber Co., 33 Barb. 578 (NY Sup. Ct. 1861).

[70] See, e.g., the extensive discussion in W.W. Cook's treatise, ch. 19 and 38 (1887).

[71] Leslie v. Lorillard, 110 N.Y. 519, 531-533 (1888).

> they are organized. A corporation in this country, whatever it may have been in England at a time when the crown exercised the right of creating such bodies, can only have an existence under the express law of the State or sovereignty by which it is created. And these powers, where they do not relate to municipal corporations exercising authority conferred solely for the benefit of the public, and in some sense parts of the body politic of the State, have in this country until within recent years always been conferred by special acts of the legislative body under which they claim to exist. But the rapid growth of corporations, which have come to take a part in all or nearly all of the business operations of the country, and especially in enterprises requiring large aggregations of capital and individual energy, as well as their success in meeting the needs of a vast number of most important commercial relations, have demanded the serious attention and consideration of law makers. And while valuable services have been rendered to the public by this class of organizations, which have stimulated their formation by numerous special acts, it came at last to be perceived that they were attended by many evils in their operation as well as much good, and that the hasty manner in which they were created by the legislatures, sometimes with exclusive privileges, often without due consideration and under the influence of improper motives, frequently led to bad results.[72]

The reference to corporate abuses relates to the rise of trusts, and indeed the *ultra vires* doctrine was used to dissolve sugar and oil trusts under New York and Ohio law.[73] However, in 1895 the Supreme Court rejected an antitrust challenge to the sugar trust on the grounds that the Sherman Act applied only to corporations engaged directly in interstate commerce.[74] And in 1896 the Court rejected an *ultra vires* challenge to the ability of the Union Pacific Railway to lease its tracks for 999 years to another railroad, when the charter would not permit an outright sale.[75] This literal decision significantly reduced the power of the *ultra vires* doctrine.[76]

The ultimate demise of the doctrine resulted not from a court decision but from the competition among states to attract corporate charters, which was begun by New Jersey in 1890 and continued by Delaware in the 1900s.[77] This competition meant

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[72] Oregon Railway & Navigation Co. v. The Oregonian Railway Co. Ltd., 130 U.S. 1 (1889).
[73] See People v. North River Sugar Refining Co., 121 N.Y. 282 (1890); State v. Standard Oil Co., 49 Ohio St. 137 (1892). See also Theodore Dwight, The Legality of Trusts, 3 Poli. Sci. Q. 592 (1888); William Cook, The Corporation Problem (1891).
[74] United States v. E.C. Knight Co., 156 U.S. 1 (1895).
[75] Union Pacific Railway Co. v. Chicago, Rock Island and Pacific R.R. Co., 163 U.S. 564 (1896).
[76] See W. Cook, Treatise on Stock and Stockholders, 971-73 (3rd ed. 1894): "The courts are becoming more liberal, and many acts which fifty years ago would have been held to be ultra vires would now be held to be intra vires." By 1898 Cook wrote that "the doctrine of ultra vires is disappearing." Cook, Treatise on the Law of Corporations vii (4th ed. 1898). On this entire development see Horwitz.
[77] See Edward Q. Keasbey, New Jersey and the Great Corporations, 13 Harv. L. Rev. 198 (1899); Lincoln Steffens, New Jersey: A Traitor State, 25 McLure's Magazine 41 (1905); Russel Larcom, The Delaware Corporation (1937), ch. 1. On the "race to the bottom/race to the top" debate see generally William Cary,

that New Jersey and Delaware had every incentive to relax any limiting elements in their charters that restricted the power of corporate management.[78] Thus, for example, the long-lasting prohibition against corporations owning stock in other corporations, which led to the necessity of "trusts", was eliminated by New Jersey in its 1890 law.[79] As a result, although the Supreme Court still held in 1899 that such a combination was *ultra vires* under New York law, this holding became rather meaningless since most large, publicly traded corporations were incorporated in New Jersey.[80] As the New Jersey statute explains:

> It was formerly the rule in this State that acts of a corporation in excess of its express powers, or those necessarily implied, were void, and contracts which were *ultra vires* the corporation were incapable of enforcement or ratification…This rule no longer obtains.[81]

The decline of the *ultra vires* doctrine was sealed by the spread of corporate laws permitting incorporation "for any lawful purpose". With the doctrine gone, the artificial entity view of the corporation became less plausible, and the real entity view reigned supreme again.[82]

c. The Hostile Takeover Crisis.

In 1926 John Dewey published an article in the Yale Law Journal in which he dismissed as irrelevant the debate among the aggregate, artificial entity, and real entity views of the corporation. These views, he explained, could be deployed to suit any purpose; and he used examples relying on the cyclical nature if these theories. His conclusion was that theory should be abandoned for an examination of reality.[83]

Dewey was influential in that the theoretical debate on corporate personality largely disappeared until the 1970s. As a practical matter, however, the real entity view predominated for large, publicly traded corporations. The board ran the corporation as it saw fit, protected from the shareholders by the separation of ownership from management noted by Berle & Means in the 1930s, and by the business judgment rule,

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Federalism and Corporate Law: Reflections on Delaware, 83 Yale L.J. 663 (1974); Ralph K. Winter, State Law, Shareholder Protection and the Theory of the Corporation, 6 J. Legal S. 251 (1977); Lucian Benchuk, Federalism and the Corporation: The Desirable Limits on State Competition in Corporate Law, 105 Harv. L. Rev. 1435 (1992); Robert Daines, Does Delaware Law Improve Firm Value, 62 J. Fin. Econ. 525 (2001).

[78] See James Dill, Trusts-Their Uses and Abuses (1901); "New Jersey Legislating for the United States", Indianapolis Journal (Nov. 11, 1901);

[79] General Corporation Act of New Jersey (1890 rev.), sec. 51. See also sec. 104 (authorizing mergers); W.W. Cook, A Treatise on the Law of Corporations (4th ed., 1898), vi.

[80] De La Vergne Refrigerating Machine Co. v. German Savings Institution, 175 U.S. 40 (1899).

[81] General Corporation Law of New Jersey, 10 (1896).

[82] See Machen, supra. Another significant development in this period was states passing statutes that allowed a majority of shareholders to sell corporate assets (before the 1890s, shareholder unanimity was required). This greatly facilitated mergers and also represented the decline of the aggregate view. See Horwitz, supra.

[83] John Dewey, The Historical Background of Corporate Legal Personality, 35 Yale L.J. 655 (1926).

and protected from the state by the relaxation of corporate law limits begun by New Jersey and continued by Delaware.[84]

The next significant practical change in this state of affairs only arose in the 1980s. As a result of the invention of the junk bond market, it suddenly became possible for hostile raiders to threaten takeovers of even the largest corporations. After RJR Nabisco was taken private for $25 billion in 1988, it was clear that no board was safe. As a result, debates on the nature of the corporation and its relationship to the shareholders and the state, which began in the academic literature in the 1970s, once again became a matter of practical concern. And once again all three theories of the corporation reappeared, as can be seen if one examines three seminal cases decided between 1982 and 1989 by the Supreme Courts of the United States and of Delaware.

Edgar v. MITE Corp., decided by the Supreme Court in 1982, involved the constitutionality of an anti-takeover act enacted by the state of Illinois.[85] Under the Illinois Business Take-Over Act, a hostile tender offer for the shares of a company covered by the act had to be registered by the Secretary of State and the offeror had to give both the target and the state a 20 day notice during which only the target could communicate with its shareholders regarding the offer. The act applied both to corporations 10% of whose shareholders were resident of Illinois and to corporations that were either incorporated in the state or had their principal office in it. The MITE corporation made a hostile offer for an Illinois corporation and refused to comply with the act, arguing that it violated the commerce clause.

The Supreme Court agreed with MITE. Writing for a 5-4 majority, Justice White held that the Illinois act was unconstitutional because it could apply to tender offers that did not affect a single Illinois *shareholder;* “the state has no legitimate interest in protecting nonresident shareholders.”[86] Moreover, the fact that the target corporation was an Illinois corporation was irrelevant since state regulation only applied to the corporation’s “internal affairs”: “Tender offers contemplate transfers of stock by stockholders to a third party and do not themselves implicate the internal affairs of the target company.”[87] Instead, the focus should be entirely on the impact of blocking the tender offer on the company’s shareholders and their relationship with management:

> The effects of allowing the Illinois Secretary of State to block a nationwide tender offer are substantial. Shareholders are deprived of the opportunity to sell their shares at a premium. The reallocation of economic resources to

[84] This state of affairs prompted Adolph Berle, the prime intellect behind the shareholder primacy doctrine in the 1930s, to concede defeat in 1956. See Adolph A. Berle, Jr., Rosenthal Lectures at Northwestern University, in Richard Ellis, Corporation Giving in a Free Society 29 (1956): “Twenty years ago, the writer had a controversy with the late Professor E. Merrick Dodd, of Harvard Law School, the writer holding that corporate powers were powers in trust for shareholders while Professor Dodd argued that these powers were held in trust for the entire community. The argument has been settled, at least for the time being, squarely in favor of Professor Dodd’s contention.”
[85] 457 U.S. 624 (1982).
[86] 457 U.S. 644.
[87] 457 U.S. 645.

> their highest valued use, a process which can improve efficiency and competition, is hindered. The incentive the tender offer mechanism provides incumbent management to perform well so that stock prices remain high is reduced. See Easterbrook & Fischel, The Proper Role of a Target's Management in Responding to a Tender Offer, 94 Harv. L. Rev. 1161, 1173-1174 (1981); Fischel, Efficient Capital Market Theory, the Market for Corporate Control, and the Regulation of Cash Tender Offers, 57 Texas L. Rev. 1, 5, 27-28, 45 (1978); H. R. Rep. No. 94-1373, p. 12 (1976).

This part of the opinion clearly reflects the aggregate view: The focus is entirely on the impact on the corporation's shareholders, and the corporation itself (including its management) barely exist, as indicated by the statement that a change in corporate control has no relevance to the internal affairs of the corporation. The market for corporate control is praised because of its ability to overcome the agency cost problem and the incentive it provides for management to maximize stock prices. Moreover, White quotes the work of Easterbrook and Fischel, who are among the principal proponents of the "nexus of contracts" theory of the corporation, according to which the corporation is merely a convenient legal term for a series of contracts, the most important of which is the contract between shareholders and management.[88]

This part of the opinion, which rejects both the artificial entity and the real entity theories, evoked some misgivings on the part of Justice Powell, even though he joined it to provide the crucial fifth vote. Powell noted that in some cases the state may have a legitimate interest because the corporation has a real presence that goes beyond a contract between management and the shareholders, reflecting both the artificial and real entity views:

> I join Part V-B because its Commerce Clause reasoning leaves some room for state regulation of tender offers. This period in our history is marked by conglomerate corporate formations essentially unrestricted by the antitrust laws. Often the offeror possesses resources, in terms of professional personnel experienced in takeovers as well as of capital, that vastly exceed those of the takeover target. This disparity in resources may seriously disadvantage a relatively small or regional target corporation. Inevitably there are certain adverse consequences in terms of general public interest when corporate headquarters are moved away from a city and State.*
>
> * The corporate headquarters of the great national and multinational corporations tend to be located in the large cities of a few States. When

[88] See Easterbrook & Fischel, supra. Fischel stated that "[a] corporation…is nothing more than a legal fiction that serves as a nexus for a mass of contracts which various individuals have voluntarily entered into for their mutual benefit." The point that the nexus of contracts theory is a reinvention of the aggregate view has been made repeatedly. See, e.g., William W. Bratton Jr., The New Economic Theory of the Firm: Critical Perspectives from History, 41 Stan. L. Rev. 1471 (1989); Millon, supra.

> corporate headquarters are transferred out of a city and State into one of these metropolitan centers, the State and locality from which the transfer is made inevitably suffer significantly. Management personnel -- many of whom have provided community leadership -- may move to the new corporate headquarters. Contributions to cultural, charitable, and educational life -- both in terms of leadership and financial support -- also tend to diminish when there is a move of corporate headquarters.

Five years later Powell had the opportunity to translate these misgivings into an opinion for the Court that emphasized instead the artificial entity view of the corporation. *CTS Corp. v. Dynamics Co.* involved a so-called "second generation" anti-takeover statute, i.e., one that was drafted to get around the problems with the Illinois statute struck down in MITE.[89] The Indiana statute applied only to corporations incorporated in Indiana, which have specified level of shareholders within the state, and which opt for its protection. Under the statute, an acquirer who acquired "control shares" in such an Indiana target could vote them only with the approval of a majority of the pre-existing disinterested shareholders, to be obtained in a meeting within 50 days after the acquisition.

The Court of Appeals followed MITE and declared the statute unconstitutional under the commerce clause, because it interfered with the market for corporate control: "Even if a corporation's tangible assets are immovable, the efficiency with which they are employed and the proportions in which the earnings they generate are divided between management and shareholders depends on the market for corporate control- an interstate, indeed international, market that the State of Indiana is not authorized to opt out of."[90]

The Supreme Court reversed. Justice Powell, writing for a 5-4 majority, stated that-

> No principle of corporation law and practice is more firmly established than a State's authority to regulate domestic corporations, including the authority to define the voting rights of shareholders…We think the Court of Appeals failed to appreciate the significance for Commerce Clause analysis of the fact that state regulation of corporate governance is regulation of entities whose very existence and attributes are a product of state law. As Chief Justice Marshall explained: "A corporation is an artificial being, invisible, intangible, and existing only in contemplation of law. Being the mere creature of law, it possesses only those properties which the charter of its creation confers upon it, either expressly, or as incidental to its very existence. These are such as are supposed best calculated to effect the object for which it was created." Trustees of Dartmouth College v. Woodward, 4 Wheat. 518, 636 (1819).[91]

[89] 481 U.S. 69 (1987).
[90] 481 U.S. 77 (quoting from 794 F.2d 264).
[91] 481 U.S. 89.

Powell thus rejected the view that states do not have the right to regulate transactions affecting shareholders, including shareholders in other states. He argued that the "free market system depends at its core upon the fact that a corporation…is organized under, and governed by, the law of a single jurisdiction…A State has an interest in promoting stable relationships among parties involved in the corporations it charters."[92] And he explicitly rejected the market for corporate control and its underlying aggregate theory: "The Constitution does not require the States to subscribe to any particular economic theory…there is no reason to assume that the type of conglomerate corporation that may result from repetitive takeovers will result in more effective management or otherwise be beneficial to shareholders…the very commodity that is traded in the "market for corporate control"- the corporation- is one that owes its existence and attributes to state law."[93]

This entire opinion, with its quotation from Dartmouth College, is clearly based on the artificial entity view that the corporation owes its existence to the incorporating state and that state may therefore regulate it, including in ways that affect shareholders' ability to sell their shares. Not surprisingly, Justice White dissented, arguing that while the statute may help Indiana corporations "particularly in helping those corporations maintain the status quo", it is inimical to the interests of the shareholders and constitutes "economic protectionism."[94]

After CTS, the battle for corporate control moved to state law, and the most important state in this regard was Delaware, in which most major US corporations are incorporated. Delaware law was favorable to hostile takeovers until 1989, when the Supreme Court of Delaware issued an opinion in *Paramount v. Time* that in practice ended the hostile takeover boom.[95] Paramount had made a $175 (later raised to $200) per share offer for Time at the time when Time was about to enter into a $70 per share merger with Warner. Paramount argued that under the previous decisions of the Delaware Supreme Court in *Unocal* (1985) and *Revlon* (1986), Time was "up for sale" and therefore the business judgment rule was suspended and Time's board was required to maximize shareholder value by accepting the much higher Paramount bid.

The Delaware Supreme Court held in favor of Time. It stated that-

> Two key predicates underpin our analysis. First, Delaware law imposes on a board of directors the duty to manage the business and affairs of the corporation. This broad mandate includes a conferred authority to set a corporate course of action, including time frame, designed to enhance corporate profitability. Thus, the question of "long-term" versus "short-term" values is largely irrelevant because directors, generally, are obliged to charter a course for a corporation which is in its best interest without regard to a fixed investment horizon. Second, absent a limited set of circumstances as defined under *Revlon*, a board of

[92] 481 U.S. 90-91.
[93] 481 U.S. 92-94.
[94] 481 U.S. 100.
[95] 571 A.2d 1140 (1989).

> directors, while always required to act in an informed manner, is not under any per se duty to maximize shareholder value in the short term, even in the context of a takeover.[96]

The court thus rejected the view that maximizing short-term shareholder value was always required; instead, the board was permitted to pursue its view of the best long-term corporate strategy:

> Delaware law confers the management of the corporate enterprise to the stockholders' duly elected board representatives. The fiduciary duty to manage a corporate enterprise includes the selection of a time frame for achievement of corporate goals. That duty may not be delegated to the stockholders. Directors are not obliged to abandon a deliberately conceived corporate plan for a short-term shareholder profit unless there is clearly no basis to sustain the corporate strategy.

Thus, the board was permitted to prefer preservation of the "Time culture" (its stated goal over maximizing the cash return to shareholders). This effectively killed the takeover threat, because any board could find good long-term share value maximization reasons to reject a superior cash bid. The Delaware court, in thus enhancing managerial power, in effect endorsed the real entity view: A corporation was an entity with its own corporate culture, which should not be subordinated to the shareholders or to the state. This view was ratified when the ALI corporate governance project adopted a rule that corporate boards may take into account the interests of other "stakeholders," not just the shareholders.[97]

Why did the real entity view prevail? The obvious answer was that corporate management determines the state of incorporation, and therefore the Delaware Supreme Court felt that it had to side with management once the U.S. Supreme Court had approved the anti-takeover laws of other states, lest corporations choose to relocate there. However, it seems unlikely that this was the only reason; Delaware is very well established as the preferred state of incorporation, and stock values would likely decrease if shareholders perceive that management were leaving Delaware just to protect themselves. Instead, it seems likely that the Delaware Supreme Court genuinely believed that a corporation like Time had a corporate existence and culture with implications for other stakeholders, and therefore rejected the aggregate view equating the corporation with its shareholders. In that way, its concerns were similar to those raised by Justice Powell in his concurrence in MITE: A corporation is more than a "nexus of contracts", and courts and legislatures are allowed to take the interests of other stakeholders into account.

d. From National Corporations to Multinational Enterprises.

[96] 571 A.2d 31.
[97] ALI, supra.

The last transformation in the nature of the corporation began in the 1950s and is still going on, so that its ultimate outcome is hard to judge. This is the transformation from corporations based mostly in one country to multinational enterprises based in many countries.

Multinationals, in the sense of corporations owning assets overseas, have existed since the 17th century. However, as recently as the 1950s, the shareholders and other sources of capital, the management, most of the production facilities, and most of the markets of even large multinationals tended to be in one country, so that "what was good for G.M. was good for America." By the 1990s, however, this has changed profoundly. As more countries opened up to foreign direct investment, communications improved, and many products became lighter and easier to ship, more and more corporations became "globalized." In a globalized multinational, the sources of capital are in many countries: The shares of large multinationals trade on as many as twenty exchanges, and borrowing facilities are similarly diversified. Research and development and production facilities are likewise spread throughout the globe, as are markets. The only thing that usually ties a modern multinational to its home country is the location of management.

In this context, the debate over the nature of the corporation has re-opened. There is abundant academic writing on the relationship between multinationals and the state, and most writers from both left and right concede that this relationship has changed profoundly so that the home state (the state of incorporation) has become powerless to control "its" multinationals; it is hard even to identify to which country multinationals "belong".[98] On a practical level this situation has led to attempts by home states to control the behavior of multinationals abroad in areas as diverse as trading with the enemy, antitrust, corruption and others, with varying success.[99] The most recent development in this regard has been "inversion" transactions, in which the management changes the country of incorporation of a multinational's parent corporation. These transactions are undertaken primarily for tax reasons, but they have corporate governance implications as well.[100] Specifically, the artificial entity theory becomes hard to maintain when management can pick weak countries like Bermuda as the country of incorporation for the parent of a multinational.

The relationship with shareholders has also undergone changes as shareholders now tend to come from many countries. One implication of this has been that the securities laws of the weakest country tend to dominate because of cross-country price arbitrage.[101] Another

[98] Robert Reich, Who is Us?, 32 Harv. Bus. Rev. 53 (1990); Edward M. Graham and Paul Krugman, Foreign Direct Investment in the United States 86-93 (1995); but see Laura d'Andrea Tyson, They Are Not Us: Why American Ownership Still Matters, Am. Prospect (Winter 1991).

[99] Raymond Vernon, In the Hurricane's Eye (1998); Blumberg, supra; P. Muchlinski, Multinational Enterprises and the Law (1996); Reuven S. Avi-Yonah, National Regulation of Multinational Enterprises: An Essay on Comity, Extraterritoriality, and Harmonization, 42 Columbia J. Transnat'l L. 5 (2003).

[100] Reuven S. Avi-Yonah, For Haven's Sake: Reflections on Inversion Transactions, 95 Tax Notes 1793 (June 17, 2002). For the Congressional response see IRC 7874 (2004).

[101] Amir N. Licht, Regulatory Arbitrage for Real: International Securities Regulation in a World of Interacting Securities Markets, 38 Va. J. Int'l L. 563 (1998).

is academic proposals to let management choose the country of securities law as well as the country of incorporation.[102] On a practical level globalization has led the SEC to relax requirements for some foreign issuers.[103] This trend has tended to weaken the applicability of the aggregate view as well. It is hard to predict where these trends will lead, but at the moment they appear once more to favor the real entity view.

e. Conclusion

To summarize: Throughout all the transformations we have studied, the same pattern recurs. As the relationship of the corporation to the state, to society and to its members or shareholders changes, all three views of the corporation emerge, submerge and then re-emerge in a slightly different but fundamentally similar form. In the end, however, the real entity view prevails.

Why does the real entity view prevail? In part, this is no doubt due to the fact that it represents the most congenial view to corporate management, because it shields them from undue interference from both shareholders and the state. Corporate management wields political power and it influences the outcome of the debate; judges again and again refer to the importance of corporations, by which they mean corporate management. But the very fact that corporate management wields this power shows that there is another reason why the real entity view prevails: It fits reality much more than the other two. In some periods (e.g., the Roman Empire or 18th century Europe) the power of the state is overwhelming and the artificial entity view seems plausible, and in other periods (the medieval membership corporation, the 19th century close corporation) the aggregate view seems plausible, but in most periods equating the corporation either with the state or with shareholders must have seemed to most non-academics highly implausible.[104] The real

[102] Roberta Romano, Empowering Investors: A Market Approach to Securities Regulation, 107 Yale L.J. 2359 (1998); Andrew Guzman, Portable Reciprocity: Rethinking the International Reach of Securities Regulation, 71 S. Cal. L. Rev. 903 (1998); Merritt B. Fox, Retaining Mandatory Securities Disclosure: Why Issuer's Choice is Not Investor Empowerment, 85 Va. L. Rev. 1335 (1999).

[103] Merritt B. Fox, The Political Economy of Statutory Reach: US Disclosure Rules in a Globalizing Market for Securities, 97 Mich. L. Rev. 696 (1998).

[104] The real entity view is clearly the dominant one in sociology and some branches of economics. As one sociologist has stated, "[t]he recurrent problem in sociology is to conceive of corporate organization, and to study it, in ways that do not anthropomorphize it and do not reduce it to the behavior of individuals or of human aggregates." Guy E. Swanson, The Tasks of Sociology, 192 Science 665 (1976). A whole branch of economic sociology centers on the study of organizations, and there are numerous books devoted to the topic. Most of these books revolve around the study of large corporations, since these are the dominant forms of organization in this society. See, e.g., James D. Thompson, Organizations in Action: Social Science Bases of Administrative Theory (1967, reissued 2003); W. Richard Scott, Organizations: Rational, Natural, and Open Systems (5th ed. 2003); Jeffrey Pfeffer and Gerald R. Salancik, The external control of organizations: A resource dependence perspective (1978, reissued 2003); Walter W. Powell and Paul j. DiMaggio (eds.), The New Institutionalism in Organizational Analysis (1991); Neil J. Smelser and Richard Swedberg (eds.), The Handbook of Economic Sociology (1994), especially Part II, Section C, The Sociology of Firms, Organizations, and Industry. Moreover, they are informed by the economic perspective inaugurated by Ronald Coase in his classic "Nature of the Firm" article from 1937, and developed by Oliver Williamson and others into transaction cost economics. Ronald Coase, The Nature of the Firm, 4 Economica 386 (1937); Oliver E. Williamson, Transaction cost economics and organization theory, in Smelser and Swedberg, supra; for a critique see Mark Granovetter, Economic action and social structure:

entity view prevailed because it was more *real* than the others. And this observation enables us to move from the historical to the contemporary and ask how *Citizens United* and its antecedents fit the historical pattern.

II. *Citizens United*: A Real Entity Case

The Supreme Court first addressed the question whether corporations had a right to engage in political speech under the First Amendment in *First National Bank of Boston v. Bellotti*, decided in 1978.[105] *Bellotti* involved a Massachusetts statute that prohibited banks and business corporations from expending funds on advertising to influence the result of political referenda. In the context of a referendum to introduce progressive taxation on individuals, the Massachusetts Supreme Judicial Court held that the law was constitutional because the First Amendment rights of corporations are limited to issues that "materially affect its business, property, or assets."[106]

The Supreme Court reversed. The three opinions in the case reflect the three theories of the corporation. Justice Powell for a five Justice majority adopted the real view, stating that –

> If the speakers here were not corporations, no one would suggest that the State could silence their proposed speech. It is the type of speech indispensable to decisionmaking in a democracy, and this is no less true because the speech comes from a corporation rather than an individual. The inherent worth of the speech in terms of its capacity for informing the public does not depend upon the identity of its source, whether corporation, association, union, or individual.[107]

The majority thus treated corporations as equivalent to individuals, citing *Santa Clara* for the proposition that corporations are persons for Fourteenth Amendment purposes and therefore protected by the First Amendment (as applied under the Fourteenth Amendment to the states).[108] It explicitly rejected the artificial entity theory advanced by Massachusetts ("corporations, as creatures of the State, have only those rights granted them by the State") because the national banks that brought the case are "creatures of federal law…and their existence is in no way dependent on state law."[109] And the majority also explicitly rejected the aggregate view that the intent of the statute was to

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The problem of embeddedness, 91 Am J Sociology 481 (1985) This branch of economics, which now forms part of the "new institutional economics", begins by recognizing that the firm is fundamentally different from the market because of its hierarchical structure, and proceeds to investigate when operating as a firm as opposed to buying in the market makes sense (the "make or buy" issue). Transaction cost economics has become the leading explanation for the most recent transformation of the corporation- the rise of multinational enterprises. Pitelis and Sugden, The Nature of the Transnational Firm (1991).

[105] First National Bank of Boston v. Bellotti, 435 US 765 (1978).

[106] Bellotti, 767.

[107] Bellotti, 777.

[108] Bellotti, 780 n. 15.

[109] Bellotti, 719 n. 14.

protect shareholders from management expressing different views than their own, stating that the normal "procedures of corporate democracy" are sufficient to protect them.[110]

The heart of Justice Powell's opinion lies in his concern that striking down the Massachusetts statute would infringe on corporate activities that he views as beneficial, but unrelated to corporate business operations: "Thus corporate activities that are widely viewed as educational and socially constructive would be prohibited. Corporations no longer would be able safely to support—by contributions or public service advertising—educational, charitable, cultural, or even human rights causes."[111] And Justice Powell rejected as unsupported by the record the view that "corporations are wealthy and powerful and their views may drown out other points of view."[112] This also reflects the real view because corporations are judged as standing on their own, not as reflecting the views of shareholders or as creatures of the state. The aggregate view, as reflected in Milton Friedman's writings from the same period, would object to the same kind of "corporate social responsibility" considerations as not being in the shareholders' interest.

Justice White's dissent, on the other hand, advances the aggregate view. He argues that –

> There is now little doubt that corporate communications come within the scope of the *First Amendment*. This, however, is merely the starting point of analysis, because an examination of the *First Amendment* values that corporate expression furthers and the threat to the functioning of a free society it is capable of posing reveals that it is not fungible with communications emanating from individuals and is subject to restrictions which individual expression is not…. Shareholders in [for profit corporate] entities do not share a common set of political or social views, and they certainly have not invested their money for the purpose of advancing political or social causes or in an enterprise engaged in the business of disseminating news and opinion. … Of course, it may be assumed that corporate investors are united by a desire to make money, for the value of their investment to increase. Since even communications which have no purpose other than that of enriching the communicator have some *First Amendment* protection, activities such as advertising and other communications integrally related to the operation of the corporation's business may be viewed as a means of furthering the desires of individual shareholders. This unanimity of purpose breaks down, however, when corporations make expenditures or undertake activities designed to influence the opinion or votes of the general public on political and social issues that have no material connection with or effect upon their business, property, or assets. Although it is arguable that corporations make such expenditures because their managers believe that it is in the corporations' economic interest to do so, there is no basis whatsoever for concluding that these views are expressive of the heterogeneous beliefs of their shareholders whose convictions on many political issues are undoubtedly shaped by considerations other than a desire to endorse any electoral or ideological cause which would tend to increase the value of a

[110] Bellotti, 794.
[111] Bellotti, 782 n. 18.
[112] Bellotti, 789.

> particular corporate investment. This is particularly true where, as in this case, whatever the belief of the corporate managers may be, they have not been able to demonstrate that the issue involved has any material connection with the corporate business. Thus when a profitmaking corporation contributes to a political candidate this does not further the self-expression or self-fulfillment of its shareholders in the way that expenditures from them as individuals would.[113]

This is clearly an aggregate view, and it is congruent with the position taken by Justice White in *MITE* four years later.[114] The emphasis is entirely on the shareholders, not on the corporation itself.

Justice Rehnquist, on the other hand, dissented from the majority from an artificial entity perspective. He stated that although the Fourteenth Amendment does protect corporations, there are limits to such protection because the corporation is a creature of the state, citing *Dartmouth College*:

> The appellants herein either were created by the Commonwealth or were admitted into the Commonwealth only for the limited purposes described in their charters and regulated by state law. Since it cannot be disputed that the mere creation of a corporation does not invest it with all the liberties enjoyed by natural persons, … our inquiry must seek to determine which constitutional protections are "incidental to its very existence." *Dartmouth College, supra*, at 636.
>
> There can be little doubt that when a State creates a corporation with the power to acquire and utilize property, it necessarily and implicitly guarantees that the corporation will not be deprived of that property absent due process of law. Likewise, when a State charters a corporation for the purpose of publishing a newspaper, it necessarily assumes that the corporation is entitled to the liberty of the press essential to the conduct of its business. … Although the Court has never explicitly recognized a corporation's right of commercial speech, such a right might be considered necessarily incidental to the business of a commercial corporation.
>
> It cannot be so readily concluded that the right of political expression is equally necessary to carry out the functions of a corporation organized for commercial purposes. A State grants to a business corporation the blessings of potentially perpetual life and limited liability to enhance its efficiency as an economic entity. It might reasonably be concluded that those properties, so beneficial in the economic sphere, pose special dangers in the political sphere. Furthermore, it might be argued that liberties of political expression are not at all necessary to effectuate the purposes for which States permit commercial corporations to exist. So long as the Judicial Branches of the State and Federal Governments remain

[113] Bellotti, 804-5.
[114] Edgar v. MITE, discussed supra.

> open to protect the corporation's interest in its property, it has no need, though it may have the desire, to petition the political branches for similar protection. Indeed, the States might reasonably fear that the corporation would use its economic power to obtain further benefits beyond those already bestowed. [6] I would think that any particular form of organization upon which the State confers special privileges or immunities different from those of natural persons would be subject to like regulation, whether the organization is a labor union, a partnership, a trade association, or a corporation. …
>
> I can see no basis for concluding that the liberty of a corporation to engage in political activity with regard to matters having no material effect on its business is necessarily incidental to the purposes for which the Commonwealth permitted these corporations to be organized or admitted within its boundaries. Nor can I disagree with the Supreme Judicial Court's factual finding that no such effect has been shown by these appellants. Because the statute as construed provides at least as much protection as the *Fourteenth Amendment* requires, I believe it is constitutionally valid.[115]

It is hard to imagine a clearer statement of the artificial and aggregate views than the positions taken by Justices Rehnquist and White respectively. But the majority taking the real entity view prevailed, presumably because in1978 it was hard to view corporations as a mere aggregation of their shareholders or as mere creatures of the state. Surprisingly, the majority opinion was written by Justice Powell, who as we have seen took an artificial entity view in *MITE* and *CTS.* The explanation is that the hostile takeover movement threatened the same educational and charitable activities of corporations that Powell sought to defend in *Bellotti,* so in that context he needed to empower the state to save "its" corporations.

The emphasis on the artificial entity view in *CTS* may also have influenced the result in the Court's next First Amendment case related to corporations, *Austin v. Michigan State Chamber of Commerce,* decided three years after *CTS*.[116] The issue in *Austin* was whether a state could ban corporate direct expenditures in support of or in opposition to candidates for state office, as opposed to expenditures through "Political Action Committees" (PACs) organized for this purpose. Justice Marshall for a six Justice majority that included Rehnquist and White held that the ban was constitutional. The majority opinion reflects the artificial entity view held by Rehnquist:

> State law grants corporations special advantages -- such as limited liability, perpetual life, and favorable treatment of the accumulation and distribution of assets -- that enhance their ability to attract capital and to deploy their resources in ways that maximize the return on their shareholders' investments. These state-created advantages not only allow corporations to play a dominant role in the Nation's economy, but also permit them to use "resources amassed in the

[115] Bellotti, 823-828. Rehnquist rejects the argument that some of the corporations were not chartered by Massachusetts by pointing out that they were all permitted to do business there, Bellotti, 824 n. 2.
[116] Austin v. Michigan State Chamber of Commerce, 494 US 652 (1990).

> economic marketplace" to obtain "an unfair advantage in the political marketplace." … the political advantage of corporations is unfair because
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> "[t]he resources in the treasury of a business corporation . . . are not an indication of popular support for the corporation's political ideas. They reflect instead the economically motivated decisions of investors and customers. The availability of these resources may make a corporation a formidable political presence, even though the power of the corporation may be no reflection of the power of its ideas."
>
> We therefore have recognized that "the compelling governmental interest in preventing corruption support[s] the restriction of the influence of political war chests funneled through the corporate form." …
>
> The Chamber argues that this concern about corporate domination of the political process is insufficient to justify a restriction on independent expenditures. Although this Court has distinguished these expenditures from direct contributions in the context of federal laws regulating individual donors, *Buckley, 424 U.S., at 47*, it has also recognized that a legislature might demonstrate a danger of real or apparent corruption posed by such expenditures when made by corporations to influence candidate elections, *Bellotti, supra, at 788, n. 26*. … Michigan's regulation aims at a different type of corruption in the political arena: the corrosive and distorting effects of immense aggregations of wealth that are accumulated with the help of the corporate form and that have little or no correlation to the public's support for the corporation's political ideas. … We emphasize that the mere fact that corporations may accumulate large amounts of wealth is not the justification for ß 54; rather, the unique state-conferred corporate structure that facilitates the amassing of large treasuries warrants the limit on independent expenditures. Corporate wealth can unfairly influence elections when it is deployed in the form of independent expenditures, just as it can when it assumes the guise of political contributions. We therefore hold that the State has articulated a sufficiently compelling rationale to support its restriction on independent expenditures by corporations.[117]

Why did the majority emphasize the artificial entity view? It may have been influenced by the adoption of that view in *CTS.* But it is more likely that what really bothered Justice Marshall was the "corrosive and distorting effect of immense aggregations of wealth" per se, but he could not take that position because it was rejected as to rich individuals by *Buckley v. Valeo* (1976).[118] Justice Scalia in dissent points out the weakness of the majority's position, stating that while the state charters corporations, "[i]t is rudimentary that the State cannot exact as the price of those special advantages the forfeiture of First Amendment rights," and that the aggregation of wealth argument is inconsistent with Buckley.[119] Justice Brennan also felt that the majority was on weak ground, and in his concurrence took the aggregate view that the purpose of the statute is to protect

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[117] Austin, 658-661.
[118] This was explicitly recognized by Justice Stevens in Davis v. FEC, 128 S Ct 2759 (2008).
[119] Austin, 680.

shareholders.[120] Justice Kennedy in his dissent rejects both the aggregate and the artificial entity views, relying on *Bellotti* to argue (in accordance with the real entity view) that corporations are equal to individuals and therefore their speech must be protected.[121]

We thus arrive at the most recent addition to the Supreme Court's jurisprudence on the corporate form, *Citizens United*. The question presented in that case was whether Congress could impose the same kind of limits on corporations that Michigan state law applied in *Austin*. The Court could have ruled narrowly that the limits were unconstitutional as applied to a nonprofit corporation formed for advocacy purposes by individuals, but decided instead to use the case for a much broader ruling that all corporate direct expenditures are permitted under the First Amendment, overruling *Austin*.

What is remarkable about *Citizens United*, although maybe not surprising to the reader at this point, is that both the majority and the dissent adopt the real view of the corporation, so that their only disagreement is in divergent assessments of the implications for the First Amendment. The majority opinion by Justice Kennedy emphasizes, for example, that the ban on corporate speech is not alleviated by the fact that a PAC organized and controlled by the same corporation can speak freely because "[a] PAC is a separate association from a corporation."[122] This assertion can only be made under the real entity view because under the aggregate view both the corporation and the PAC are owned by the same ultimate shareholders, and under the artificial entity view both the PAC and the corporation are created by the same state.

The majority relies on *Bellotti* for the proposition that "the First Amendment does not allow political speech restrictions based on a speakers corporate identity."[123] It rejects the "antidistortion" rationale of *Austin* as overbroad and inconsistent with *Buckley* and as permitting the government to ban speech by media corporations. The aggregate view advanced by the Solicitor General and by Justice Brennan in his concurrence in *Austin* is likewise rejected in reliance on the "procedures of corporate democracy" of *Bellotti*.[124] Interestingly, the majority does not even mention the artificial entity view, even though it (and not the antidistortion rationale per se) was key to the holding in *Austin*. While the statute at issue is a federal one and corporations are chartered by states, it could be argued that the federal government also confers benefits on business corporations by protecting the market that enables them to engage in business.[125]

Justice Scalia, in concurrence, does admit that the First Amendment was originally intended to apply to individuals, "[b]ut the individual person's right to speak includes the right to speak in association with other individual persons."[126] But this does not mean that he adopts the aggregate view, since that view as applied to the shareholders underlay the principal argument of the Government and was soundly rejected by the majority. Instead,

[120] Austin, 674-678.
[121] Austin, 699.
[122] Citizens United, 47.
[123] Citizens United 63.
[124] Citizens United 87.
[125] This argument was made to justify a federal tax on state chartered corporations as early as 1909. See Avi-Yonah, Corporations, Society and the State (2004).
[126] Citizens United, 138.

what he means is presumably corporate management working together as an association of persons: "to exclude or impede corporate speech is to muzzle the principal agents of the modern free economy. We should celebrate rather than condemn the addition of this speech to the public debate."[127]

Nor does the dissent in *Citizens United* attempt to advance any view other than the real entity view. Instead, it emphasizes that corporations are different than natural persons and therefore may be more heavily regulated:

> In the context of election to public office, the distinction between corporate and human speakers is significant. Although they make enormous contributions to our society, corporations are not actually members of it. They cannot vote or run for office. Because they may be managed and controlled by nonresidents, their interests may conflict in fundamental respects with the interests of eligible voters. The financial resources, legal structure, and instrumental orientation of corporations raise legitimate concerns about their role in the electoral process. Our lawmakers have a compelling constitutional basis, if not also a democratic duty, to take measures designed to guard against the potentially deleterious effects of corporate spending in local and national races.[128]

This is all about the corporation itself, not about the shareholders or the state. Similarly:

> The same logic applies to this case with additional force because it is the identity of corporations, rather than individuals, that the Legislature has taken into account. As we have unanimously observed, legislatures are entitled to decide "that the special characteristics of the corporate structure require particularly careful regulation" in an electoral context. Not only has the distinctive potential of corporations to corrupt the electoral process long been recognized, but within the area of campaign finance, corporate spending is also "furthest from the core of political expression, since corporations' *First Amendment* speech and association interests are derived largely from those of their members and of the public in receiving information," … Campaign finance distinctions based on corporate identity tend to be less worrisome, in other words, because the "speakers" are not natural persons, much less members of our political community, and the governmental interests are of the highest order. Furthermore, when corporations, as a class, are distinguished from noncorporations, as a class, there is a lesser risk that regulatory distinctions will reflect invidious discrimination or political favoritism. [129]

Not a word here on the corporation's relationship to the state or to the shareholders. The artificial entity theory does get discussed later in the dissent, but purely in a historical context: When explaining the Framers' view of corporations, Justice Stevens emphasizes their relationship to the state ("Corporations were created, supervised, and conceptualized

[127] Citizens United, 141.
[128] Citizens United, 143.
[129] Citizens United, 197-98 (citiations omitted).

as quasi-public entities").[130] But he emphasizes that this was a historical artifact that disappeared with general incorporation statutes, and that "many scholars have long since rejected the concession theory of the corporation."[131] He does mention briefly the artificial entity rationale for *Austin*, but does not emphasize it in comparison with corporate power.[132]

The dissent also addresses the aggregate theory at the very end when discussing the dissenting shareholder rationale of Brennan's concurrence in *Austin*, but only as a limited and secondary argument "beyond the distinctive legal attributes of the corporate form."[133] The main emphasis in this section of the dissent is on the weakness of the "procedures of corporate democracy" (voting and shareholder derivative suits are "so limited as to be almost nonexistent" and selling the stock faces many practical difficulties.)[134] This is very far from viewing the corporation as a mere "nexus of contracts" with the primary contract being that with the shareholders.

The entire *Citizens United* opinion, both the majority and the dissent, are thus reflective of the real entity view. Corporations stand on their own, independent of both the state that created them and the shareholders than own them. The debate between the majority and the dissent is about what follows from this perspective on corporations: In the majority's opinion, this means that corporations are speakers just like individuals and entitled to the same First Amendment protection, while the dissent takes the view that because of the special characteristics of corporations, they have more limited First Amendment rights:

> The fact that corporations are different from human beings might seem to need no elaboration, except that the majority opinion almost completely elides it. *Austin* set forth some of the basic differences. Unlike natural persons, corporations have "limited liability" for their owners and managers, "perpetual life," separation of ownership and control, "and favorable treatment of the accumulation and distribution of assets . . . that enhance their ability to attract capital and to deploy their resources in ways that maximize the return on their shareholders' investments." Unlike voters in U.S. elections, corporations may be foreign controlled. [70] Unlike other interest groups, business corporations have been "effectively delegated responsibility for ensuring society's economic welfare"; [71] they inescapably structure the life of every citizen. "'[T]he resources in the treasury of a business corporation,'" furthermore, "'are not an indication of popular support for the corporation's political ideas.'" "'They reflect instead the economically motivated decisions of investors and customers. The availability of these resources may make a corporation a formidable political presence, even though the power of the corporation may be no reflection of the power of its ideas.'"

[130] Citizens United, 202.
[131] Citizens United, 204-5, 214.
[132] Citizens United 224.
[133] Citizens United, 295.
[134] Citizens United, 292

> It might also be added that corporations have no consciences, no beliefs, no feelings, no thoughts, no desires. Corporations help structure and facilitate the activities of human beings, to be sure, and their "personhood" often serves as a useful legal fiction. But they are not themselves members of "We the People" by whom and for whom our Constitution was established. …
>
> It is an interesting question "who" is even speaking when a business corporation places an advertisement that endorses or attacks a particular candidate. Presumably it is not the customers or employees, who typically have no say in such matters. It cannot realistically be said to be the shareholders, who tend to be far removed from the day-to-day decisions of the firm and whose political preferences may be opaque to management. Perhaps the officers or directors of the corporation have the best claim to be the ones speaking, except their fiduciary duties generally prohibit them from using corporate funds for personal ends. Some individuals associated with the corporation must make the decision to place the ad, but the idea that these individuals are thereby fostering their self-expression or cultivating their critical faculties is fanciful. It is entirely possible that the corporation's electoral message will *conflict* with their personal convictions. Take away the ability to use general treasury funds for some of those ads, and no one's autonomy, dignity, or political equality has been impinged upon in the least.[135]

It is hard to imagine a more forceful statement of the real entity view: the actual human beings almost disappear completely. In a footnote, Justice Stevens does acknowledge the existence of other theories of the corporation, but it is clear which theory he favors.[136] The artificial entity theory advanced by then Justice Rehnquist in *Bellotti* and relied upon by the majority in *Austin* and the aggregate theory advanced by Justice White in *Bellotti* and Justice Brennan in *Austin* have almost disappeared, and both the majority and the dissent take the real entity view. Once again, like so many times in the past, the real entity view reigns supreme.

III. Conclusion: What's Next?

As the reader can expect by now, it is hardly likely that this state of affairs will remain stable forever. When the next transformation in the status of corporations is addressed by

[135] Citizens United, 272-75.

[136] "Nothing in this analysis turns on whether the corporation is conceptualized as a grantee of a state concession, see, *e.g., Trustees of Dartmouth College v. Woodward, 17 U.S. 518, 4 Wheat. 518, 636, 4 L. Ed. 629 (1819)* (Marshall, C. J.), a nexus of explicit and implicit contracts, see, *e.g.,* F. Easterbrook & D. Fischel, The Economic Structure of Corporate Law 12 (1991), a mediated [*273] hierarchy of stakeholders, see, *e.g.,* Blair & Stout, A Team Production Theory of Corporate Law, *85 Va. L. Rev. 247 (1999)* (hereinafter Blair & Stout), or any other recognized model. *Austin* referred to the structure and the advantages of corporations as "state-conferred" in several places, *494 U.S., at 660, 665, 667, 110 S. Ct. 1391, 108 L. Ed. 2d 652*, but its antidistortion argument relied only on the basic descriptive features of corporations, as sketched above. It is not necessary to agree on a precise theory of the corporation to agree that corporations differ from natural persons in fundamental ways, and that a legislature might therefore need to regulate them differently if it is human welfare that is the object of its concern. Cf. Hansmann & Kraakman 441, n. 5." Citizens United, 273 n. 72.

the Court, it is inevitable that the artificial entity and aggregate theories of the corporation will re-emerge to once again contend with the real entity view. In fact. Once can see this process germinating even now within *Citizens United*.

An important rhetorical move made by Justice Stevens in his dissent and echoed by other critics of the decision (like President Obama in the State of the Union address) is its impact on the rules restricting foreigners from participating in US elections. Justice Stevens states that the majority's approach "would appear to afford the same protection to multinational corporations controlled by foreigners as to individual Americans."[137] This drew a strong disclaimer from the majority, arguing that even if the Government has a compelling interest in limiting foreign influence over our political process, the corporate expenditure ban is overbroad because it "is not limited to corporations or associations that were created in foreign countries or funded predominantly by foreign shareholders."[138]

Predictably, Congress will react by reaffirming the application of the ban on contributions and expenditures made by foreign nationals to foreign corporations.[139] But how define what is a foreign corporation?

The majority in *Citizens United* envisages two possibilities. One is to define foreign corporation as a corporation created by a foreign state. This approach is the one taken by our tax laws and it follows the artificial entity view.[140] The problem, of course, would be that if this were the only definition, it would be too easy for foreigners to become Americans merely by incorporating a shell in one of the states.

The other approach mentioned by the majority is to take the aggregate view and look at the identity of the shareholders, so that a corporation the majority of whose shareholders are US citizens will count as American and others as foreign. This may work for closely held corporations, and this approach is taken for example in determining foreignness for purposes of the rules restricting foreign ownership of media and transportation corporations. But for publicly traded multinational enterprises the aggregate view is very difficult to maintain because the shares trade on multiple exchanges, the ownership is constantly shifting, and most of the owners trade under "street names" than make it very hard even for the IRS to know their true identity. Thus, I predict that the same reasons that forced the Court to abandon the aggregate view for diversity jurisdiction will apply in this context as well.

The third possibility would be to take the real view and confront directly the question of whether in a globalized world corporations have a meaningful nationality. As discussed above this issue is extensively debated and reasonable minds can differ.[141] It lies at the

[137] Citizens United, 198.
[138] Citizens United, 88.
[139] 2 USC 441(e).
[140] IRC 7701(a)(30). But see IRC 7874 (defining some foreign corporations as domestic based on the identity of their shareholders).
[141] See Reich and Tyson, supra.

heart of the current transformation of the corporate form from mainly national to multinational enterprises that do not owe any particular allegiance to any state. Whatever the ultimate outcome of this debate, it is already possible to predict than once again the real entity definition of the nationality of corporations, which focuses on where they are "managed and controlled", will triumph over a narrow focus on the creating state (too remote and manipulable) and the shareholders (too remote and diffused).[142] To be continued…

[142] "Managed and controlled" is a familiar definition of corporate residency from the tax laws of many countries, relying on a UK House of Lords decision from the 19th century. See Avi-Yonah, For Haven's Sake, supra.