ESSAY

ON THE PROMISE OF STAKEHOLDER GOVERNANCE: A RESPONSE TO BEBCHUK AND TALLARITA

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INTRODUCTION

For a generation, or two, and for better or (as we think) worse, the guiding principle of corporate governance in the United States has been that directors should manage companies to maximize returns for stockholders. Leave to the side just for now the debatable questions whether Milton Friedman's 1970 ukase actually contemplated a stockholder primacy model, or whether corporate law before then required directors to prioritize stockholder interest over all others, or whether *Revlon* or any other precedential authority tells corporate fiduciaries that their obligation runs to stockholders alone. Leave them to the side precisely because they are debatable, whereas this is not: for better or (as we think) worse, the stockholder-first model has dominated the governance conversation for decades. So cowed are directors by this orthodoxy that many believe they cannot look out for other constituencies without risking being named in a lawsuit. *Revlon*, the slogan—maximize stockholder value, only and always!—has enjoyed a decades-long run that has far outpaced the jurisprudential confines of *Revlon*, the decision.

If Milton Friedman is celebrated as the founding prophet of this orthodoxy, Professor Bebchuk ranks among its most fervent acolytes. For the better part of twenty years, working with

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an all-star team of academic collaborators, Professor Bebchuk has published a steady and influential stream of scholarship in support of the view that immediate financial returns to equity should trump other corporate governance concerns. Among many other policies, Team Bebchuk defends event-driven investors who seek quick profits from quick turnarounds, casts a skeptical eye on index funds that hold for the long term and reflect the broader economy,[1] seeks to empower temporary majorities of stockholders to fundamentally revise corporate policy,[2] and encourages high-octane executive compensation schemes that incentivize managers to drive up short-term stock prices.[3] The common thread of the scholarship is that directors are held accountable only through the constant discipline of the current share price, and that without that discipline, directors should be expected to stray from their duties and extract private benefits at the expense of stockholders.

No surprise, then, that Professor Bebchuk and his coauthor Roberto Tallarita have launched a broadside against recent efforts of business leaders, scholars, and lawyers to promote a corporate governance model that permits directors to take into account interests other than stockholders—a governance regime that authorizes directors to manage their corporations having in mind the interests not of stockholders alone, but also of employees and customers and society at large.[4] Calling the prospect of stakeholder governance an "illusory promise," Bebchuk and Tallarita trundle out a familiar litany of reasons why change won't work and that the only

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1 *See* Lucian Bebchuk & Scott Hirst, *Index Funds and the Future of Corporate Governance: Theory, Evidence, and Policy*, 119 COLUM. L. REV. 2029, 2139–40 (2019) (arguing that index funds lack incentives to engage in appropriate stewardship); Lucian A. Bebchuk, Alon Brav, & Wei Jiang, *The Long-Term Effects of Hedge Fund Activism*, 115 COLUM. L. REV. 1085, 1154–55 (2015) (arguing that there is no evidence that hedge fund activism results in only short-term gains).

2 *See* Leo E. Strine, Jr., *Can We Do Better by Ordinary Investors? A Pragmatic Reaction to the Dueling Ideological Mythologists of Corporate Law*, 114 COLUM. L. REV. 449, 460 n.33 (2014) (noting that "Bebchuk has made clear that he believes stockholder majorities should be able to displace board policy upon short notice," identifying numerous examples, and collecting sources).

3 *See* LUCIAN BEBCHUK & JESSE FRIED, PAY WITHOUT PERFORMANCE: THE UNFULFILLED PROMISE OF EXECUTIVE COMPENSATION x, 8–9, 140 (2004) (suggesting that executive pay packages should be more sensitive to "performance," defined as executives' impact on stock price and financial metrics, and proposing reforms intended to increase shareholder power).

4 *See, e.g.*, RICHARD A. POSNER, A FAILURE OF CAPITALISM: THE CRISIS OF '08 AND THE DESCENT INTO DEPRESSION xii, 260 (2009) (revisiting position on deregulation in the wake of the financial crisis).

productive path forward is the same path that has guided corporate governance over the past decades.[5]

For reasons summarized below and to be elaborated in ongoing research, we suggest that Professors Bebchuk and Tallarita should reconsider their all-chips-in approach to the share price maximization model. We see in our daily work that business leaders have been forced to focus too heavily on share prices and quarterly earnings to the exclusion of the health of their businesses and of the broader society. We see a system that no one thinks is functioning as it should. We recognize that a more inclusive corporate governance model will not solve all these problems. But stakeholder- and society-facing corporate governance remains an urgent imperative nonetheless—if for no other reason than to reinforce the institutional legitimacy of the form of business organization that has been an engine of growth for generations and whose contribution is needed now more than ever. At all events, doing nothing, staying the familiar course—which is the Bebchuk prescription—should not be an option.

I
THE FAILED PROMISE OF STOCKHOLDER PRIMACY

This should be the golden age of shareholder primacy. Fifty years ago the principle was announced from the pages of the New York Times Magazine as the intellectual gold standard.[6] Thirty-five years ago, it was approved in the courts as a polestar of director decision making in the context of corporate control transactions.[7] In the years since, every element of the corporate governance landscape has been oriented to the shareholder primacy model. And every element of the model has been endorsed, directly or indirectly, by Professor Bebchuk and his various collaborators. Proxy advisory firms safeguard stockholder interest with the ferocity of Cerberus at the gates of the Underworld. At the urging of the governance experts, executive pay is now generally linked to near-term price targets, the better to ensure management alignment with share price. "Activist" investors, now capable of accumulating vast stakes of

5 *See* Lucian A. Bebchuk & Roberto Tallarita, *The Illusory Promise of Stakeholder Governance*, 106 CORNELL L. REV. 91, 176–77 (2020).

6 *See* Milton Friedman, *A Friedman Doctrine—The Social Responsibility of Business Is to Increase Its Profits*, N.Y. TIMES (Sept. 13, 1970), https://www.nytimes.com/1970/09/13/archives/a-friedman-doctrine-the-social-responsibility-of-business-is-to.html [https://perma.cc/5VZT-YF8H].

7 *See* Revlon, Inc. v. MacAndrews & Forbes Holdings, Inc., 506 A.2d 173, 185 (Del. 1986).

even our largest public companies, exercise massive influence over corporate policy, demanding rapid-fire returns on investment and often receiving significant board representation. Meanwhile, well-capitalized stockholder-plaintiffs' law firms stand ready to ferret out any and all deviation from fiduciary orthodoxy, real or merely perceived, aided by permissive procedural rules and incentivized by the potential for lucrative paydays for even questionable cases.

What could possibly go wrong?

An awful lot, as it turns out. Notwithstanding remarkable advances in productivity and technology, the corporate economy isn't working. By generating profits for investors but reducing security for employees, corporations are seen as prime culprits in a burgeoning crisis of economic inequality.[8] By pursuing short-term profits at the cost of long-term sustainability, corporations are seen as prime culprits in the now-upon-us climate crisis. By focusing on share price rather than purpose, corporations are seen as betraying the public trust and exacerbating economic crises.[9] Public confidence in corporations is at all-time lows.[10] Here's how the Financial Times expressed the situation:

> [Milton] Friedman's argument [caught on], setting out a doctrine of shareholder primacy that has defined Anglo-Saxon capitalism for almost 50 years and shaped a world that is increasingly driven by corporations.
>
> The pursuit of returns to companies' owners at the expense of other stakeholders has undoubtedly led to greater profits, generating enormous wealth for investors and the executives whose rewards have been increasingly tied to shareholder returns. But it has come at a cost to employees, customers

[8] *See, e.g.*, Leo E. Strine, Jr., Aneil Kovvali & Oluwatomi O. Williams, *Lifting Labor's Voice: A Principled Path Toward Greater Worker Voice and Power Within American Corporate Governance*, 106 MINN. L. REV. — (forthcoming 2022) (acknowledging concerns that workers lack power within corporations and proposing policy solutions); Anna Stansbury & Lawrence H. Summers, *The Declining Worker Power Hypothesis: An Explanation for the Recent Evolution of the American Economy*, Brookings Papers on Econ. Activity 63 (Spring 2020) (concluding that reduced worker power within corporations explains sluggish wage growth and a declining labor share of income).

[9] *Cf.* Aneil Kovvali, *Countercyclical Corporate Governance* (manuscript) (on file with author) (urging that shareholder value maximization norm is inappropriate in periods of macroeconomic crisis).

[10] *See* EDELMAN, EDELMAN TRUST BAROMETER 2020, https://cdn2.hubspot.net/hubfs/440941/Trust%20Barometer%202020/2020%20Edelman%20Trust%20Barometer%20Global%20Report.pdf?utm_campaign=Global:%20Trust%20Barometer%202020&utm_source=website [https://perma.cc/5AY8-5TG3] (last visited July 1, 2021).

> and the environment; incentivized boards to pay less tax; diverted cash to earnings-flattering share buybacks rather than investment; and—among those outside the privileged club of equity owners—eroded the trust on which companies ultimately depend.[11]

No wonder that Elizabeth Warren and many like-minded political leaders want to tear down the whole contemporary edifice of corporate governance. More moderately, business leaders across the economy and around the world have recognized the need to modulate from a shareholder-facing model to one that encourages companies to take account of a broader range of social concerns. Important institutional investors like BlackRock, State Street, and Vanguard have embraced an understanding that corporations must be run with a view to the interests of all their stakeholders. *Nobody* thinks the shareholder-maximization governance model is working.

Not even Professors Bebchuk and Tallarita. Tucked away at the seventy-eighth page of their essay is this indictment of the shareholder primacy model, remarkable as much for its breadth as its clinical understatement:

> There is currently a widespread and growing recognition that, although corporations have been a major engine for growth, their profit-seeking operations contribute to a wide array of society's problems and impose serious negative externalities on employees, communities, consumers, and the environment.[12]

Appended to this concession is a footnote directing readers to a curated selection of "recent discussions of such societal problems and negative externalities."[13] Bebchuk and Tallarita then go on to acknowledge that corporate policy has been blamed for "stagnant growth in wages" and "the loss of jobs" and as well as "a substantial fraction of greenhouse gas emissions, thereby playing a major role in climate change."[14] The professors do not deny that these problems exist or contest that corporations operating within the shareholder-primacy model they have championed have played a role in creating them. Nor do they address the perfectly logical inference that limited-liability corporations, operating in a governance regime demanding near-term shareholder returns, would predictably

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11 Andrew Edgecliffe-Johnson, *Beyond the Bottom Line: Should Business Put Purpose Before Profit?*, FIN. TIMES (Jan. 4, 2019), https://www.ft.com/content/a84647f8-0d0b-11e9-a3aa-118c761d2745 [https://perma.cc/D5D2-W5BA].

12 Bebchuk & Tallarita, *supra* note 5, at 168.

13 *Id.* at 168 n.233.

14 *Id.* at 169–70.

seek to systematically shift risks to the community at large and from the present to the future.

Instead, the professors say that the solution to this failure of shareholder primacy lies outside and beyond the realm of corporate governance: "laws, regulations, and policies offer the only real prospect for [stakeholder] protections."[15] This same "prospect" for stakeholder protection has of course been available since the beginning of the shareholder primacy era and—as experience now confirms—has done little to ward off a crisis in confidence regarding the corporate form. Nor do Bebchuk and Tallarita offer any account as to how or why the present political environment should provide greater confidence that government is positioned better now than in years past to address "societal problems" and "negative externalities." We doubt such an account could be seriously articulated.

Even in the professors' telling, then, shareholder primacy is a broken model. Their policy response—steady as she goes—is an analytical non sequitur. There must be a better way.

II
THE PROMISE OF STAKEHOLDER GOVERNANCE

Stakeholder governance has emerged as the most appealing alternative to the failed shareholder primacy model. The stakeholder-facing approach has been articulated in various ways by various commentators, but they all come down to a simple idea: in setting corporate policy, directors should not seek only to maximize share price, but should also consider the interests of diverse stakeholders—employees, customers, suppliers, the community at large—and to have the discretion to manage with these other environmental and social interests in mind.

The logic in support of stakeholder governance is uncomplicated. States universally authorize the creation of corporations to benefit the common good, not just the investment class. Also universally, state corporation law places management of corporations in the hands of directors who are elected periodically, now usually annually, by stockholders. During their term in office, directors enjoy broad latitude to govern, subject to the duty of care (which requires them to act on an informed basis) and the duty of loyalty (which requires them to refrain from extracting any personal or parochial benefit in the exercise of corporate power).

15 *Id.* at 175.

Under a stakeholder governance paradigm, the directors would use that discretion to manage corporate policy in the service of multiple constituencies, and with respect for corporate social responsibility, rather than exclusively to drive share price. The directors may (but need not) tether these policy choices to a statement or understanding of corporate purpose. In so doing, directors would also be giving effect to leading investor voices:

> [A] company cannot achieve long-term profits without embracing purpose and considering the needs of a broad range of stakeholders. A pharmaceutical company that hikes prices ruthlessly, a mining company that shortchanges safety, a bank that fails to respect its clients—these companies may maximize returns in the short term. *But, as we have seen again and again, these actions that damage society will catch up with a company and destroy shareholder value.* By contrast, a strong sense of purpose and a commitment to stakeholders helps a company connect more deeply to its customers and adjust to the changing demands of society. *Ultimately, purpose is the engine of long-term profitability.*[16]

Because stockholders can vote out directors, there is no risk that directors seeking to implement stakeholder governance will abandon stockholder interests. For this reason, astute commentators recognize that stakeholder governance can only succeed if it constitutes a partnership—a pursuit of shared interests—among stockholders, stakeholders, directors, and corporate officials.[17] There is increasing reason to believe that such a partnership is attainable. Considered statements of the Business Roundtable and large institutional investors suggest a convergence of interests among investors and business leaders, and they suggest an emerging consensus. This is no surprise. For diversified investors to succeed—for the actual people who ultimately invest to succeed—a pop in the share price of one company won't do. To the contrary, those investors share society's broader interest in ensuring that the environment is sustained, that the workforce be fairly

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16 Larry Fink, *A Fundamental Reshaping of Finance*, HARV. L. SCH. F. ON CORP. GOVERNANCE (Jan. 16, 2020), https://corpgov.law.harvard.edu/2020/01/16/a-fundamental-reshaping-of-finance/ [https://perma.cc/2KFF-FLF2] (emphasis added) (boldface emphasis omitted).

17 For example, and most notably, Martin Lipton's "New Paradigm" calls for a "voluntary collaboration among corporations, shareholders and other stakeholders to achieve sustainable long-term value and resist short-termism." *See* Martin Lipton, *It's Time to Adopt the New Paradigm*, HARVARD L. SCH. F. ON CORP. GOVERNANCE (Feb. 11, 2019), https://corpgov.law.harvard.edu/2019/02/11/its-time-to-adopt-the-new-paradigm/ [https://perma.cc/RD4A-WB9U].

treated, and that corporations be permitted to take account of social responsibility. That is the promise of stakeholder governance.

To which Bebchuk and Tallarita say: it can't happen, it won't happen, and it shouldn't happen. The reason it can't happen, they say, is that Delaware requires shareholder primacy and thus precludes stakeholder governance.[18] To address this objection we will avoid the temptation to argue about the meaning of *Revlon*; goodness knows there's been ample opportunity to do that already and another occasion will soon arise. We think for now it suffices to insist that Delaware law surely permits directors to advance stockholders' interests as the stockholders themselves understand their interests. Investors today—or a critical mass of them at any rate—recognize that their interests require a broader focus, including stakeholders, and a clearer sense of corporate purpose. We pass over as unrealistic the suggestion that informed and unconflicted directors, directing corporate policy with the benefit of knowledgeable advisors, implementing a stakeholder-facing agenda with the support of the stockholder body, in a manner intended to render the corporation stronger over the long term, could or would be constrained from doing so under any viable conception of fiduciary duty.

This is not to deny that there remains robust disagreement regarding whether corporate law is ultimately designed to promote stockholders' interests. Nor do we disagree with the professors' assessment that in certain stylized situations, stockholder and stakeholder interests could come into irreducible conflict, or that proponents of stakeholder governance may sometimes wish away the potential for conflict, or even that in the context of an individual decision, a board might be advised that its duties to stockholders require a stockholder-centric choice. All that may well be true. None of it, however, supports the conclusion that a board, elected on a platform of stakeholder governance, implementing a stockholder-supported pro-

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18 Bebchuk & Tallarita, *supra* note 5, at 137-38 & n.152 (citing Leo E. Strine, Jr. *The Dangers of Denial: The Need for a Clear-Eyed Understanding of the Power and Accountability Structure Established by the Delaware General Corporation Law*, 50 WAKE FOREST L. REV. 761, 768 (2015) [hereinafter Strine, *Dangers of Denial*]). Bebchuk and Tallarita's discussion does not capture important aspects of Chief Justice Strine's complex views. For example, his recent writing situates corporate attention to employee, environmental, social, and governance issues squarely within the normal duties and requirements imposed by Delaware law. *See* Leo E. Strine, Jr., Kirby M. Smith & Reilly S. Steel, Caremark *and ESG, Perfect Together: A Practical Approach to Implementing an Integrated, Efficient, and Effective* Caremark *and EESG Strategy*, 106 IOWA L. REV. 1885, 1887 (2021).

gram of stakeholder governance, balancing the interests of important stakeholder constituencies in a manner rationally designed to ensure the long-term health and welfare of the company and its stakeholder constituencies, would find a disabling obstacle in the law of Delaware or any other jurisdiction. That would make no sense. The law will not stand in the way of responsible stakeholder governance.[19]

But the professors also claim that even if directors can manage for stakeholder benefit, they will choose not to. "[C]orporate leaders," they say, "have incentives not to provide stakeholders with any benefits that would come at the expense of shareholders," and so "corporate leaders should [thus] be expected . . . not to use their discretion to provide stakeholders with any such benefits."[20] They offer two closely-related points in support of this claim: they observe that the power structure of the corporate form, in which directors are elected by stockholders alone, means that directors will always prioritize immediate stockholder interests, and that directors of companies incorporated in states with constituency statutes—who are legally free to manage in stakeholders' interests—have not deployed that greater discretion to advance those interests.[21]

The evidence supporting these points is thin. The professors emphasize that most corporations, including those signatory to the Business Roundtable statement on stakeholder governance, pay top executives in performance-based equity, "directly linked to shareholder value."[22] So, the professors reason, executives will manage for immediate share price, without regard to any stated commitment to stakeholder value.

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19 Indeed, the broader tendency of Delaware law has been to authorize corporate directors to structure stockholder decisions in a way that engages their practical and moral faculties. As Professors Hart and Zingales have shown, shareholders are more likely to act on their broader interests when they vote than when they decide whether to tender into an offer. *See* Oliver Hart & Luigi Zingales, *Companies Should Maximize Shareholder Welfare Not Market Value*, 2 J.L. FIN. & ACCT. 247, 255–56 (2017). Delaware law has largely empowered boards to channel stockholder decisions about acquisitions into voting, instead of through uncoordinated transactions with the acquirer. *See, e.g.*, Air Prods. & Chems., Inc. v. Airgas, Inc., 16 A.3d 48, 129 (Del. Ch. 2011) (approving board's use of a poison pill defense preventing uncoordinated transactions and channeling decision to stockholder vote at next annual meeting).

20 Bebchuk & Tallarita, *supra* note 5, at 157–58.

21 These points are so closely related they may not even be analytically distinct. The professors' point seems to be that directors who have the discretion to attend to stakeholder interests do not do so, because they ultimately answer to stockholders at the polls. Accordingly, the legal rules governing corporate purpose are irrelevant, they suggest, so long as stockholders cast all the votes in director elections.

22 Bebchuk & Tallarita, *supra* note 5, at 148.

There's more than a little irony here, insofar as Professor Bebchuk's advocacy is one the reasons that CEO pay is so slavishly tethered to stock price. The professors thus point to a problem they have worked mightily to embed in corporate governance as a reason to resist reform. But the problem is not remotely insoluble. A growing number of companies have sought to tie executive compensation to metrics focused on environmental, social, and governance issues.[23] Some prominent companies following this trend include Royal Dutch Shell, which is seeking to tie executive compensation to carbon emissions targets; Chevron, which is also seeking to tie compensation to carbon emissions targets; Clorox, which is seeking to tie compensation to metrics on environmentally friendly packaging; Alcoa, which ties compensation to safety, environmental, and diversity objectives; and Airbnb, which is tying compensation to goals on guest safety and sustainability.[24] The compensation reflexes of the shareholder primacy model can be—and already are being—updated to account for stakeholder governance.[25]

The professors also serve up a quasi-empirical study of public-to-private buyout transactions of companies incorporated in states with constituency statutes. Their point seems to be that, in the recent past, directors with the freedom to engineer transactions in the interests of all stakeholders have generally failed to do so. Rather, say Bebchuk and Tallarita, the directors who negotiated this subset of deals seem to prioritize stockholder value, negotiating only unenforceable protection for employees and "soft" promises to protect the community. Citing nothing, with no knowledge of the situation, and apparently imagining that sellers can impose whatever terms they like, the professors tell us that corporate leaders had the "negotiating power to secure . . . constraints on

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23 Sullivan & Cromwell LLP, *Sustainability Matters: The Rise of ESG Metrics in Executive Compensation* (Mar. 10, 2020), https://www.sullcrom.com/files/upload/SC-Publication-Sustainability-Matters-The-Rise-of-ESG-Metrics-in-Executive-Compensation.pdf [https://perma.cc/Y84Q-EQSU].

24 *Id.*; John D. Stoll, *Airbnb's New Compensation Plan Asks Shareholders to Share with Other Stakeholders*, WALL ST. J. (Jan. 18, 2020), https://www.wsj.com/articles/airbnbs-new-compensation-plan-asks-shareholders-to-share-with-other-stakeholders-11579358335 [https://perma.cc/6EZM-534U].

25 The labor market for executives is also setting new incentives that may promote responsible behavior. *See* Xin Dai, Feng Gao, Ling Lei Lisic & Ivy Zhang, *Can Socially Responsible CEOs Find Better Jobs?*, THE CLS BLUE SKY BLOG (Mar. 10, 2020), https://clsbluesky.law.columbia.edu/2020/03/10/can-socially-responsible-ceos-find-better-jobs/ [https://perma.cc/Y87B-JY4K] (reporting results that "suggest that the managerial labor market rewards CEOs for their social performance").

the power of the private equity buyer to make choices that would adversely impact stakeholders," but that they failed to do so.[26]

There's no telling whether this is true, but let's say it is. All it would establish is that directors overseeing a change-in-control transaction prioritize stockholder value over all other variables. This is no argument against stakeholder governance, at least not in the professors' world. To the contrary, it tends to confirm that stockholder interests will be fairly protected even if directors are given broad and express discretion to look after stakeholders too. Nor is there any surprise that directors focus on stockholder value in control transactions without regard to jurisdiction. Directors understand that litigation challenging such transactions is nearly inevitable and that stockholder plaintiffs will complain about any failure, real or imagined, to maximize stockholder value. Directors are advised by their lawyers and bankers, moreover, that the price maximization principle enshrined by *Revlon* has purchase in courts beyond Delaware, even in jurisdictions with constituency statutes. Director deliberation in the sale context is powerfully influenced by the stockholder-maximization norm, no matter the governing law. If that norm is revised, director action may follow—though there exists no reason to think that directors would fail to attend vigorously to stockholder interests in corporate sales, even under a stakeholder-governance framework.

More credible, in our view, is the professors' claim that directors should be expected to attend to stockholder interest no matter the legal regime because it is stockholders who elect and reelect them. There is some force to this claim. Even when stakeholder governance is firmly established as a best practice, we would expect that directors would consider stockholder interest as a key factor in decision making. Stockholders are of course among a corporation's stakeholders, and their interests deserve a board's constant focus. Stockholders should be free to elect directors with a broad mandate to consider stakeholder interests as well, but we do not expect—and do not advocate—a system in which directors are free from regular accountability to stockholders. That may well mean, as the professors suggest, that directors will always aggressively advance stockholder interests. But what the professors do not show—cannot show—is that directors expressly authorized to address

26 Bebchuk & Tallarita, *supra* note 5, at 156.

broader social and community interests would not take situationally-appropriate advantage of that discretion.

Finally, Bebchuk and Tallarita argue that stakeholder governance should be rejected, even if achievable. They offer two grounds in support of this conclusion: First, they say, stakeholder governance will leave directors free from accountability to stockholders, with various imagined disastrous effects. Second, according to the professors, stakeholder governance, if implemented, will crowd out effective external regulation.

This is the most important part of the essay, and it is the weakest. The claim that stakeholder-facing directors will be accountable to no one is facially false, as directors are nearly everywhere subject to annual reelection and will be removed by stockholders whenever stockholders are displeased with their performance. The claim is supported by no empirical evidence. To the contrary, the claim is in tension with the professors' argument that directors in constituency-statute states disproportionately conduct corporate auctions to benefit stockholders. It is likewise in tension with their claim that incumbent executive compensation arrangements incentivize directors to attend to stockholder interests.

Still worse, the professors' account rests on a caricature of director conduct. They seem to imagine that directors, freed from the shackles of share-price maximization, will descend into a frenzy of rent seeking and wish fulfillment, ordering corporate affairs to their own taste, without regard to corporate purpose or corporate value. No one who has actually advised a board would recognize any aspect of this account.[27] Directors are imperfect of course, but they are—or perhaps more accurately, the overwhelming majority of them are—decent, careful women and men making important and difficult decisions with imperfect information, with limited time, and under persistent public scrutiny. Norms matter to them. Reputation matters. Doing the right thing matters. Changing the governance dial to encourage directors to consider a broader range of interests would allow them to more freely pursue corporate purpose and responsibility while still driving value. If they fail, they'll be voted out. If they are disloyal, they'll be sued. All stakeholder

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27 Academics are also increasingly attentive to this fact of corporate life. *See, e.g.*, John Armour, Jeffrey Gordon & Geeyoung Min, *Taking Compliance Seriously*, 37 YALE J. ON REGUL. 1, 36–37 (2020) (noting that corporate directors are driven by "intrinsic" motivation to do a good job, as they understand it); Lynn A. Stout, *On the Proper Motives of Corporate Directors (or, Why You Don't Want to Invite* Homo Economicus *to Join Your Board)*, 28 DEL. J. CORP. L. 1, 24 (2003) (describing phenomenon of director "altruism").

governance does is encourage a broader field for the exercise of director discretion. Powerful accountability mechanisms remain in place.

As to Bebchuk and Tallarita's claim that stakeholder governance will crowd out effective regulation:[28] let's begin with the consensus that two and a half generations of shareholder primacy have produced a complete failure of adequate external regulation. The professors have produced no evidence to indicate that the incumbent governance model is more inviting, or has been more successful in facilitating, effective regulation than any alternative, including a stakeholder-facing model.

Nor have they provided any basis to think that government officials will abandon the regulatory effort if companies embrace stakeholder governance. To the contrary, the Business Roundtable's announcement was greeted with immense skepticism by political leaders anxious to radically increase corporate regulation.[29] Nor have the professors explained why heavy-handed regulation is a superior means to improve corporate governance than reforms reflecting the cooperative commitment of stockholders, directors, and their communities. One of us has written elsewhere that the historical experience of mandatory corporate governance regulation shows that it frequently undermines business flexibility, constrains innovation, and exacerbates negative externalities.[30]

The simplest answer to the professors' claim is that they have supplied zero evidence to establish that stakeholder governance will nudge aside effective regulation. To the contrary, the growing demands for stakeholder governance stem in part

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28 For further discussion of this claim and related claims in the corporate governance and law and economics literature, see Aneil Kovvali, *Stark Choices for Corporate Reform* (manuscript) (on file with author).

29 *See, e.g.*, Letters from Sen. Elizabeth Warren to Chief Exec. Officers of Amazon et al. (Oct. 3, 2019), https://www.warren.senate.gov/imo/media/doc/2019-10-03%20Letters%20to%20CEOs.pdf [https://perma.cc/TKM3-M48S] ("If you, and the other 181 corporate executives who signed the BRT's new *Statement on the Purpose of a Corporation*, plan to live up to the promises you made, I expect that you will endorse and wholeheartedly support the reforms laid out in the *Accountable Capitalism Act* to meet the principles you endorse."); Sanders Campaign, *Corporate Accountability and Democracy*, BERNIE https://berniesanders.com/issues/corporate-accountability-and-democracy/ [https://perma.cc/DA3Y-5V94] (last visited Apr. 4, 2020) ("This year, the Business [R]oundtable released empty words recognizing the error in admitting corporations put profits and shareholder returns above everything else. Empty words are not enough.").

30 *See* Martin Lipton & William Savitt, *Stakeholder Governance—Issues and Answers*, HARV. L. SCH. F. ON CORP. GOVERNANCE (Oct. 25, 2019), https://corpgov.law.harvard.edu/2019/10/25/stakeholder-governance-issues-and-answers/ [https://perma.cc/ZX4P-73J2].

from the government's refusal to address urgent public problems.[31] The public is increasingly exasperated by public officials who seem unable or unwilling to step in, and so is demanding better performance from the corporations they interact with. Pointing to regulation, or the lack of it, as a reason to avoid governance reform lacks support in logic or historical experience.

CONCLUSION

The promise of stakeholder governance is not "illusory." Far more accurate to say that the approach is as yet untried. But its promise is substantial. Directors have for too long been in thrall to a perceived mandate to manage up the near-term share price, with consequences that no one—not even Bebchuk and Tallarita—can defend. Stakeholder governance insists on broadening the boardroom conversation as to corporate purpose and corporate objectives. It reminds everyone involved in the corporate project that society created the corporate form, and the remarkable gift of limited liability, not primarily to create wealth for the investing class but to promote the economy and opportunity for society at large.

The promise of the approach is ultimately a question for investors and managers and directors to work out together. Increasingly, stockholders are urging the companies in which they invest to adopt long-term policies for achieving sustainable growth that account for the environmental and social effects of corporate conduct. Increasingly, directors recognize that they must act accordingly—protect the corporate reputation; combat environmental externalities; recruit and incentivize and fairly treat a skilled and motivated workforce.

Whether the promise of socially responsive corporate governance proves to be illusory will turn on whether stockholders are prepared to partner with companies to take a longer and broader view of corporate policy. We think they will. We think the conversation is changing in that direction already. Key institutional shareholders—notably including BlackRock, State Street, and Vanguard—have recognized that companies must serve broader social purposes. Survey after survey of major investors confirms that they expect companies to articulate a socially and economically valuable purpose and to for-

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31 *See* Tim Wu, *The Goals of the Corporation and the Limits of the Law*, THE CLS BLUE SKY BLOG (Sept. 3, 2019), https://clsbluesky.law.columbia.edu/2019/09/03/the-goals-of-the-corporation-and-the-limits-of-the-law/ [https://perma.cc/YPV9-HW9W].

mulate long-term policy with the rising risks of income inequality and environmental deterioration in steady view.

Maybe it's all just eyewash, as the professors suggest—we doubt that, but even indulging the claim, the more the commitment to stakeholder responsibility is repeated the more it becomes real. Progress will be slow and spotty even in the best-case scenario—but no one wants to live in a world that is more polluted or more riven. Let boards listen to stockholders who promote our better angels. Make them partner with stakeholders—employees, communities—to broaden the distribution of benefits. Nudge the conversation toward social engagement. All this is readily achievable. It's not a revolution and it's not an illusion. It is progress. It is the promise of stakeholder governance.