STARK CHOICES FOR CORPORATE REFORM

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For decades, corporate law scholars insisted on a simple division of responsibilities. Corporations were told to focus exclusively on maximizing financial returns to shareholders while the government tended to all other concerns by adopting new regulations. As reformers challenged this orthodoxy by urging corporations to take action on pressing social problems, defenders of the status quo have responded by suggesting that these efforts could be dangerous. In their view, internal corporate governance reforms could interfere with the adoption of external governmental regulations that would be more effective. The hypothesis that reformers face a stark choice between pursuing internal corporate changes and pursuing new external regulations is playing an increasingly important role in the corporate law literature, but it has not been subjected to meaningful analysis.

This Article seeks to fill that gap. After isolating the "stark choice" hypothesis, the Article unpacks and challenges the assumptions that drive it. There is no clear constraint that forces a choice between internal and external reforms, and there are good reasons to believe that an internal strategy is more likely to generate valuable change. Internal reforms can also lay the groundwork for external reforms as corporations cease to resist or even come to actively support new regulations. Analyzing these dynamics can yield new insights into efforts to improve corporate outcomes on issues like racial justice and climate change.

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INTRODUCTION

Corporate law has been wracked by a decades-long debate. A majority of academics and practitioners support shareholder primacy, the view that corporations exist solely to generate financial returns for shareholders. But an increasingly vocal minority support stakeholder governance, the view that corporate leaders should consider the interests of a broader range of stakeholders, including workers, consumers, and members of surrounding communities. Shareholder primacy theorists have long claimed that stakeholder governance would be costly or ineffective in advancing the interests of stakeholders. But they have recently escalated their attacks by insisting that stakeholder governance rhetoric is potentially dangerous to stakeholders: Eminent commentators have suggested that adopting corporate governance measures to promote stakeholder interests could "derail," "crowd out," "impede," "cannibalize," or otherwise prevent governmental reforms and regulations that would do more to advance stakeholders' interests.[1]

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1. See, e.g., Lucian A. Bebchuk, Kobi Kastiel & Roberto Tallarita, For Whom Corporate Leaders Bargain, 93 S. Cal. L. Rev. 1467, 1471 (2021) ("[A]cceptance of stakeholderism would be counterproductive: rather than protecting stakeholders, stakeholderism would serve the private interests of corporate leaders by increasing their insulation from shareholder oversight and would raise illusory hopes that could deflect pressures to adopt laws and regulations protecting stakeholders."); Lucian A. Bebchuk & Roberto Tallarita, The Illusory Promise of Stakeholder Governance, 106 Cornell L. Rev. 91, 171–78 (2020) [hereinafter Bebchuk & Tallarita, Illusory Promise] ("Stakeholderism Would Impede Reforms . . . ."); Lucian A. Bebchuk & Roberto Tallarita, Will Corporations Deliver Value to All Stakeholders?, 75 Vand. L. Rev. 1031, 1086 (2022) (suggesting that corporate pledges to support stakeholders are "counterproductive" because they "deflect outside pressures to adopt governmental measures that would truly serve stakeholders"); Matteo Gatti & Chrystin Ondersma, Can a Broader Corporate Purpose Redress Inequality? The Stakeholder Approach Chimera, 46 J. Corp. L. 1, 63–70 (2020) [hereinafter Gatti & Ondersma, Stakeholder Approach Chimera] ("A Stakeholder Approach Is Likely Detrimental to Redressing Inequality . . . ."); Matteo Gatti & Chrystin Ondersma, Stakeholder Syndrome: Does Stakeholderism Derail Effective Protections for Weaker Constituencies?, 100 N.C. L. Rev. 167, 170 (2021) (describing "concerns over the fact that stakeholderism could be used as both a shield and a sword: corporations could use it to defend the status quo and interfere with opportunities to achieve reforms that would shift power and resources to weaker constituencies via direct regulation"); Mark J. Roe & Roy Shapira, The Power of the Narrative in Corporate Lawmaking, 11 Harv. Bus. L. Rev. 233, 267 (2021) (suggesting that the "short-termism" narrative could "Crowd Out Good Policymaking"). For a similar set of claims in the popular press, see Kim Phillips-Fein, Opinion, I Wouldn't Bet on the Kind of Democracy Big Business Is Selling Us, N.Y. Times (Feb. 1, 2022), https://www.nytimes.com/2022/02/01/opinion/corporations-democracy.html (on file with the *Columbia Law Review*) ("The ideal of an easy symbiosis between public and private sectors would undermine the kinds of political mobilizations, however difficult to organize and enact, that are needed for reform that benefits most Americans."); Cam Simpson, Akshat Rathi & Saijel Kishan, The ESG Mirage, Bloomberg (Dec. 10, 2021), https://www.bloomberg.com/graphics/2021-what-is-esg-investing-msci-ratings-focus-on-corporate-bottom-line/ [https://perma.cc/W8CU-RJJ6] (reporting sentiment that "the emphasis on" environmental, social, and governance (ESG) concerns at corporations "has delayed and displaced urgent action needed to tackle the climate crisis and other issues"); Tunku Varadarajan, Opinion, Can Vivek Ramaswamy Put Wokeism Out of Business?, Wall St. J. (June 25, 2021), https://www.wsj.com/articles/can-vivek-ramaswamy-put-wokeism-out-of-business-11624649588 (on file with the *Columbia Law Review*) (suggesting that corporations have offered "woke" arguments on issues that are not central to their operations to distract from issues that are central). Similar concerns have also begun to affect the debate over Professor Jack Balkin's "information fiduciaries" proposal, in which companies like Meta would have an obligation to use user data in ways that advance user interests. See Lina M. Khan & David E. Pozen, A Skeptical View of Information Fiduciaries, 133 Harv. L. Rev. 497, 537 (2019) ("[W]e suspect that the fiduciary

The hypothesis that reformers face a stark choice between internal corporate governance reforms and external regulations plays an important role in the case against stakeholder governance.[2] Workers and other stakeholder constituencies have plainly suffered in the past few decades.[3] Stakeholder governance is a movement born of desperation over the plight of these constituencies and pessimism about the likelihood of effective and helpful government intervention. The "stark choice" hypothesis seeks to play one concern against the other.

It is also one of the few arguments for shareholder primacy that would resonate with people focused on stakeholder interests. Critics of stake-holder-governance–based reforms sometimes claim that such initiatives

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approach, if pursued with any real vigor, would tend to cannibalize rather than complement procompetition reforms.").

Somewhat more subtly, former Delaware Chief Justice Leo E. Strine, Jr. has suggested that current corporate law does not allow meaningful consideration of stakeholder interests and that misunderstanding this aspect of current corporate law could impede the adoption of external and internal reforms. Leo E. Strine, Jr., Corporate Power Is Corporate Purpose I: Evidence From My Hometown, 33 Oxford Rev. Econ. Pol'y 176, 177 (2017) [hereinafter Strine, Corporate Power] (arguing that "scholars and commentators obscure the need for legal protections for . . . constituencies" other than shareholders by suggesting that corporate boards are empowered to treat the interests of these other stakeholders as equal to shareholder interests); see also 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, 767 (2015) [hereinafter Strine, Dangers of Denial] ("It is not only hollow but also injurious to social welfare to declare that directors can and should do the right thing by promoting interests other than stockholder interests."). Chief Justice Strine's position suggests that certain pathways to internal reform—such as advocating for corporate consideration of stakeholder interests without pressing for legal changes—could endanger external reforms.

2. This Article generally uses the term "internal" to refer to the bodies and processes that a corporation uses to make decisions and "external" to refer to the rules that shape the context within which decisions are made. To improve outcomes for workers, for example, an internal strategy might involve a company (or government) providing for worker representation on the board of directors, while an external strategy might involve the government raising the minimum wage. However, there is no bright line between these categories, and some policies defy easy categorization. For example, policies that boost unionization are readily categorized as external because unions typically bargain with the corporation at arm's length. But unions also affect internal governance: Workers are arguably just as internal to the corporation as shareholders; unions sometimes make use of internal processes, like leveraging their stock holdings, to achieve their objectives; and union processes for aggregating worker preferences and taking positions are arguably part of a corporation's decisionmaking process. It is also possible for an external process to dictate internal policies, as when legislatures mandate particular corporate governance arrangements.

3. See, e.g., 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, Spring 2020, at 1, 63.

may be destructive because they would create obstacles to corporate acquisitions and other transactions that could generate economic value.[4] But stakeholder governance theorists are likely to accept some loss of economic value to deliver benefits to stakeholders.[5] Only a threat to stakeholder interests is likely to be persuasive. Similarly, critics of stakeholder governance claim that it may not deliver the intended benefits.[6] But that concern alone is not a reason to preclude experimentation with these reforms, especially after decades of shareholders enjoying outsized gains and other corporate constituencies suffering deeply, while external regulators did little to help.[7] To explain why stakeholder governance should not be pursued, shareholder primacy theorists must argue that it would be risky to try. The stark choice hypothesis plays that necessary role in the rhetoric of shareholder primacy theorists.

Despite its enormous importance, the hypothesis that reformers face a stark choice between two exclusive strategies has not been subjected to serious critical analysis. A more careful look reveals that the hypothesis is undertheorized and difficult to square with experience. Like much of the traditional law and economics literature, the hypothesis ignores important realities about the costs of political action.[8] There is no reason to believe that the choices are *mutually exclusive*: No clear constraint forces a choice between the internal and external paths.[9] There is little reason to assume that reformers are *biased or naive* in their expectations: Reformers are often sophisticated to the point of cynicism and are unlikely to overestimate the value of an internal reform or to trade away an achievable external reform

4. See, e.g., Bebchuk & Tallarita, Illusory Promise, supra note 1, at 164–68; Gatti & Ondersma, Stakeholder Approach Chimera, supra note 1, at 63–64 & n.365 (articulating the concern that a stakeholder approach will "take us back to managerialism and empire building," which stands in stark contrast to the shareholder primacy approach that "helped spur growth and efficiency at corporations").

5. Cf. Lee Anne Fennell & Richard H. McAdams, The Distributive Deficit in Law and Economics, 100 Minn. L. Rev. 1051, 1071–72 (2016) [hereinafter Fennell & McAdams, Distributive Deficit] (noting that different social welfare functions may weigh distributive gains and efficiency differently).

6. Bebchuk & Tallarita, Illusory Promise, supra note 1, at 94; Gatti & Ondersma, Stakeholder Approach Chimera, supra note 1, at 9.

7. See Aneil Kovvali & Leo E. Strine, Jr., The Win-Win That Wasn't: Managing to the Stock Market's Negative Effects on American Workers and Other Corporate Stakeholders, 1 U. Chi. Bus. L. Rev. 307, 324–34 (2022) (discussing the failure of corporate law and external regulations to advance the interests of nonshareholder constituencies).

8. See Fennell & McAdams, Distributive Deficit, supra note 5, at 1052–53; Lee Anne Fennell & Richard H. McAdams, Inversion Aversion, 86 U. Chi. L. Rev. 797, 805–07 (2019) (noting that the idea that "welfarists should ignore the distributive consequences of legal rules and conduct all redistribution through tax alone" is a fundamental tenet in law and economics but "depends on a core unrealistic assumption—that political impediments to redistribution are insensitive to the method of redistribution").

9. See infra section II.A.

that would be more effective.[10] And there is no reason to believe that the choices carry *fixed political costs*: Internal reforms could reshape the way that corporations use their formidable political capital with respect to external reforms, making external reforms more likely.[11]

Stakeholder governance theorists have not pressed this case, perhaps because many are not eager to encourage governmental action.[12] But once the stark choice hypothesis is identified and inverted to match reality, it becomes possible to evaluate opportunities to effect real change through internal corporate governance reforms.

In addition to filling a gap in the literature, this Article also illuminates the somewhat confusing corporate law discourse on political process. Supporters of shareholder primacy are sometimes profoundly optimistic about how effective government can be in addressing problems, suggesting that corporate leaders can focus on shareholder profits because government officials will tend to all other issues.[13] On other occasions, they are implicitly pessimistic, suggesting that corporations can actually harm stakeholders for long periods of time without the government interfering in any way that affects corporate profitability.[14] Supporters of stakeholder

10. See infra section II.B.

11. See infra section II.C.

12. See Martin Lipton, Corporate Governance: The New Paradigm, Harv. L. Sch. Forum on Corp. Governance (Jan. 11, 2017), https://corpgov.law.harvard.edu/2017/01/11/corporate-governance-the-new-paradigm/ [https://perma.cc/963E-LGTG] [hereinafter Lipton, New Paradigm] (suggesting that a stakeholder governance paradigm could "forge a meaningful and successful private-sector solution, which may preempt a new wave of legislation and regulation"); Simpson et al., supra note 1 (quoting MSCI chairman and CEO Henry Fernandez as saying that investors should embrace social goals "to protect capitalism . . . [because] [o]therwise, government intervention is going to come, socialist ideas are going to come"); cf. Martin Lipton, Professor Bebchuk's Errant Attack on Stakeholder Governance, Harv. L. Sch. Forum on Corp. Governance (Mar. 4, 2020), https://corpgov.law.harvard.edu/2020/03/04/professor-bebchuks-errant-attack-on-stakeholder-governance/ [https://perma.cc/D5FD-5RRT] (arguing that corporate governance legislation like that proposed by Senator Elizabeth Warren is "unnecessary if companies and investors embrace stakeholder capitalism").

13. See, e.g., Jill E. Fisch, Measuring Efficiency in Corporate Law: The Role of Shareholder Primacy, 31 J. Corp. L. 637, 668 (2006) ("The justification for granting courts a specialized role in protecting shareholder interests vis-à-vis those of other corporate stakeholders, is one of institutional competence. The markets and the political process generally function well with respect to other corporate stakeholders."); Jonathan R. Macey, An Economic Analysis of the Various Rationales for Making Shareholders the Exclusive Beneficiaries of Corporate Fiduciary Duties, 21 Stetson L. Rev. 23, 42–43 (1991) [hereinafter Macey, Economic Analysis] ("If actions of a firm are genuinely detrimental to a local community, the members of that community can appeal to their elected representatives . . . for redress. . . . [L]ocal communities should be able to mobilize into an effective political coalition to press for protection from harmful actions by corporations.").

14. For example, a group of prominent commentators has urged that there is a significant difference between attention to a corporation's long-term interests and attention to externalities and distributional concerns. See Mark Roe, Holger Spamann, Jesse Fried & Charles Wang, The Sustainable Corporate Governance Initiative in Europe, 38 Yale J. on

governance are similarly torn between deep pessimism about the government's ability to address problems[15] and an apparently strong belief in its regulatory capacity.[16] A careful look at the processes for internal and external reform can throw some light on a debate that is normally characterized more by heat.

This Article proceeds as follows. Part I identifies and contextualizes the stark choice hypothesis, situating it in broader concepts from law and economics. Part II presents evidence from current debates and historical reforms suggesting that the stark choice hypothesis is not true. Part III applies the analysis to live areas of debate, including social justice and climate change, and considers potential counterexamples that suggest the scope and limits of the stark choice argument.

I. THE STARK CHOICE HYPOTHESIS IN CONTEXT

This Part identifies and contextualizes the stark choice hypothesis. Section I.A describes the stark choice hypothesis and its role in criticisms of stakeholder governance. It also contextualizes the position by observing that theories about how corporate governance *ought* to work ultimately depend on ideas about how the actual government *does* work.[17] Section I.B shows that the stark choice hypothesis is a cousin of theories in the law and economics literature and discusses emerging criticisms of those theories.

Regul. Bull. 133, 136 (2021), https://www.yalejreg.com/bulletin/the-sustainable-corporate-governance-initiative-in-europe/ [https://perma.cc/4A7W-SRM2] (suggesting that short time horizons and externalities are distinct problems). Presumably, if the government is effective, corporations will be forced to bear the costs of externalities in the long run.

15. See, e.g., Larry Fink, Letter to CEOs: Profit & Purpose, BlackRock (2019), https://www.blackrock.com/corporate/investor-relations/2019-larry-fink-ceo-letter [https://perma.cc/PYS5-GK2V] [hereinafter Fink, 2019 CEO Letter] (suggesting that the move toward stakeholder governance is based in part on "the failure of government to provide lasting solutions" to "fundamental economic changes"); Tim Wu, The Goals of the Corporation and the Limits of the Law, 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/J99A-SNEJ] ("[O]ne reason there is so much mounting pressure for corporations to take action today is that government has failed to act in many areas that people care about, often by overwhelming margins.").

16. For example, Senator Warren's Accountable Capitalism Act would impose a stakeholder approach to corporate governance and provide extremely broad grants of authority to regulators. See Accountable Capitalism Act, S. 3348, 115th Cong. (2018).

17. Cf. William W. Bratton & Michael L. Wachter, Shareholder Primacy's Corporatist Origins: Adolf Berle and *The Modern Corporation*, 34 J. Corp. L. 99, 122–24 (2008) (situating the Berle–Dodd debate over corporate purpose in the New Deal debates about the role of government).

A. *The Stark Choice Hypothesis in the Corporate Governance Literature*

Corporate scholars and practitioners have vigorously debated whether corporations should be managed in a way that benefits shareholders alone or one that considers a broader range of stakeholder interests. In a wave of recent scholarship, shareholder primacy advocates have focused heavily on the claim that reformers must choose between orienting corporations toward stakeholders through internal corporate governance mechanisms and encouraging them to behave better through external regulation.[18]

The conventional view is that the directors and officers of a for-profit corporation have a responsibility to manage the corporation for the benefit of its shareholders, while the government tends to all other social interests by setting taxes and monetary penalties so that profit-seeking corporations undertake the right activities.[19] On this account, internal corporate mechanisms should only serve shareholders, while everyone else in society is protected by external regulations.

But a strong insurgency has argued that directors and officers should have the power and responsibility to manage the corporation for the benefit of everyone affected by its actions.[20] This concept of stakeholder governance has gained increasing traction in the market, even as a vigorous academic debate continues to rage. [21]

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18. See supra note 1 and accompanying text.

19. Standard citations in support of this principle include Revlon, Inc. v. MacAndrews & Forbes Holdings, Inc., 506 A.2d 173, 176 (Del. 1986) (directors and officers can consider stakeholder interests if and only if there is "some rationally related benefit accruing to the stockholders"); Dodge v. Ford Motor Co., 170 N.W. 668, 684 (Mich. 1919) ("A business corporation is organized and carried on primarily for the profit of the stockholders."). There is a vast academic literature discussing this principle. See, e.g., Henry Hansmann & Reinier Kraakman, The End of History for Corporate Law, 89 Geo. L.J. 439, 440–41 (2001) (describing "growing consensus" that "managers of the corporation should be charged with the obligation to manage the corporation in the interests of its shareholders"); Strine, Dangers of Denial, supra note 1, at 768 ("[A] clear-eyed look at the law of corporations in Delaware reveals that, within the limits of their discretion, directors must make stockholder welfare their sole end, and that other interests may be taken into consideration only as a means of promoting stockholder welfare.").

20. Many scholars have written extensively on the stakeholder governance perspective. A lucid, though opinionated, summary of the issues can be found in Lynn A. Stout, The Shareholder Value Myth: How Putting Shareholders First Harms Investors, Corporations, and the Public 7 (2012) ("While the notion that managers should seek to maximize share price remains conventional wisdom in many business circles and in the press, corporate theorists increasingly challenge conventional wisdom.").

21. For examples of statements by prominent businesspeople and organizations in support of stakeholder governance, see, e.g., Business Roundtable Redefines the Purpose of a Corporation to Promote 'An Economy That Serves All Americans', Bus. Roundtable (Aug. 19, 2019), https://www.businessroundtable.org/business-roundtable-redefines-the-purpose-of-a-corporation-to-promote-an-economy-that-serves-all-americans

In an admirably clear statement supporting shareholder primacy and summarizing the choice, Judge Frank Easterbrook and Professor Daniel Fischel acknowledged that firms *could* be made to consider a broad range of social interests. But they suggested that firms *should* be made to focus on shareholder profit maximization while other institutions manipulate their operating environment or redistribute their profits to serve other ends:

> Given wealth as a maximand, society may change corporate conduct by imposing monetary penalties. These reduce the venturers' wealth, so managers will attempt to avoid them. A pollution tax, for example, would induce the firm to emit less. It would behave as if it had the interests of others at heart. Society thus takes advantage of the wealth-maximizing incentives built into the firm in order to alter its behavior at least cost. . . . Society must choose whether to conscript the firm's strength (its tendency to maximize wealth) by changing the prices it confronts or by changing its structure so that it is less apt to maximize wealth. The latter choice will yield less of both good ends than the former.[22]

Statements like this are characterized by inattention to the manner in which society makes its choice between external regulations directed at "prices" and internal reforms directed at "structure." This inattention is arguably a useful defensive measure, as the political process has often failed to deliver changes to the prices confronted by profit-seeking corporations in a way that would protect the interests of societal stakeholders.[23]

This defensive indifference has escalated into offensive assertions about the political process. A wave of recent scholarship has advanced the claim that reformers face a stark choice between the pursuit of internal corporate governance reforms and the pursuit of more effective external regulations. The purpose of this claim is to suggest that advocacy for stakeholder governance is affirmatively dangerous to stakeholder interests.

The mechanisms identified and depth of coverage vary. In their recent critique of stakeholder governance, Professors Lucian Bebchuk and Roberto Tallarita suggest that stakeholder governance reforms have the potential to "impede" reforms that would be more effective.[24] In a brief

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[https://perma.cc/AKX4-EJNZ]; Fink, 2019 CEO Letter, supra note 15; Lipton, New Paradigm, supra note 12.

22. Frank H. Easterbrook & Daniel R. Fischel, The Economic Structure of Corporate Law 37–38 (1991); see also Macey, Economic Analysis, supra note 13, at 26–27 (positing that shareholder primacy facilitates the efficient allocation of benefits between corporate constituencies because shareholders value "the ultimate right to guide the firm" more than any other stakeholders and, consequently, compensate other stakeholders for sole access to that right).

23. See Fink, 2019 CEO Letter, supra note 15 (asserting that governments have failed to effectively address various social and political issues); Wu, supra note 15 (similar).

24. Bebchuk & Tallarita, Illusory Promise, supra note 1, at 171.

discussion, they suggest four mechanisms that might have this effect: (1) Reformers may devote resources to urging internal reforms when those resources would have been better spent on urging external reforms;[25] (2) reformers seeking external changes might be less able to attract support from potential donors, employees, and volunteers who believe that an underlying problem has been solved by internal reforms;[26] (3) policymakers may be less receptive to advocacy for external reforms if they believe less painful internal changes have solved the problem;[27] and (4) stakeholder governance could be used strategically by corporate actors to defeat external regulations.[28]

In an article asserting that stakeholder governance would do little to address wealth inequality, Professors Matteo Gatti and Chrystin Ondersma provide a lengthier argument for the stark choice hypothesis, based on two mechanisms: (1) Corporations may be able to lobby more effectively on behalf of their shareholders or managers if they can claim to be acting on behalf of a broader range of social stakeholders, and (2) the internal stakeholder governance approach could consume political capital and attention that would otherwise be used for external reforms.[29]

In a related article on the rise of narratives about short-termism, Professors Mark Roe and Roy Shapira offer a detailed and insightful account of how powerful forces have sold a story that stock market short-termism was responsible for various social ills.[30] But they offer only two paragraphs of reasoning in support of their claim that "[p]owerful narratives can crowd out good policies."[31] Without citation, they simply assert that strong stories can obtain "a higher priority on lawmakers' crowded policy agenda" and "may well take policymakers, the media, and the public's eyes from more" important problems and better solutions.[32]

Some of these arguments have earlier antecedents in the literature.[33] For example, in a 2008 working paper, Professor Robert Reich outlined a

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25. See id. at 171–72.

26. See id. at 172.

27. See id.

28. See id. at 173.

29. See Gatti & Ondersma, Stakeholder Approach Chimera, supra note 1, at 63–64, 67–68.

30. See Roe & Shapira, supra note 1, at 266–68.

31. See id. at 267–68.

32. Id.

33. Though it is somewhat removed from the debate between stakeholder governance and shareholder primacy, Professor Urska Velikonja has argued that when corporate scandals make a legislative response inevitable, investors have historically channeled the response toward requirements that corporate boards include independent directors, thus defeating regulations that would be more consequential. See Urska Velikonja, The Political Economy of Board Independence, 92 N.C. L. Rev. 855, 860 (2014). Professor Velikonja's analysis is premised on the idea that the independent board members would seek to maximize shareholder value and, therefore, do little to improve social welfare. See id. at

case against corporate social responsibility that focused on the proper allocation of roles across corporations and democratically accountable political institutions.[34] Reich asserted that an emphasis on corporate social responsibility would detract from more meaningful external reforms, which could only come through ordinary politics. The assertion was based on claims that: (1) Pessimism about the likelihood of external reform was not justified and could become "a self-fulfilling prophesy";[35] (2) optimism about the likelihood of internal reform was not justified because consumers and investors would not pay for better corporate behavior;[36] (3) corporate social responsibility debates blur responsibility and prevent the public from holding politicians accountable for the failure of external reform;[37] (4) corporate social responsibility initiatives give employees, customers, investors, and the public a false sense of accomplishment;[38] and (5) corporations can deploy temporary concessions strategically to prevent meaningful and lasting reform.[39]

Though these arguments are somewhat undertheorized, they share a common structure.

First, they share an underlying assumption that reformers and the political process can only produce a limited amount of reform. Some constraint—limited political capital, limited time and attention by key players, or limited capacity to tolerate large amounts of change—is thought to make it necessary for reformers to choose between different options. Without this assumed constraint, there would be no need to choose between internal and external strategies.

Second, they share an assumption that key players will fail to properly evaluate reforms. Reformers will either act based on mistaken beliefs about the relative efficacy of internal and external reforms or settle for weak internal reforms when strong external reforms were obtainable. Reformers, or the public, are similarly assumed to believe that an ineffective or temporary corporate concession is sufficient to make an external reform unnecessary. Without this assumption, there would be little reason to fear

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901. It is also unclear that better external regulations could have been obtained after the corporate scandals she analyzes. Accounting or financial scandals that damage shareholder value may well call for internal as opposed to external reforms. And Congress responded to the bribery scandals of the 1970s with the Foreign Corrupt Practices Act. See Mike Koehler, The Story of the Foreign Corrupt Practices Act, 73 Ohio St. L.J. 929, 932–34 (2012). While the Act contains provisions relating to corporate governance, it also takes an external approach and authorizes monetary fines for violations. Id. at 981.

34. See Robert B. Reich, The Case Against Corporate Social Responsibility 3 (Goldman Sch. of Pub. Pol'y, Working Paper No. GSP08-003, 2008), https://ssrn.com/abstract=1213129 [https://perma.cc/E76C-22PG].

35. Id. at 4.

36. See id. at 14–15.

37. See id. at 5.

38. See id. at 5–6.

39. Id. at 33.

efforts to put potential internal reforms on the table; weak reforms will only be adopted if stronger measures could not be pushed through.

Third, they do not engage with potential differences in political costs or dynamic effects. Beyond simple assumptions that external reforms are possible,[40] there is little discussion of the relative likelihood that either type of reform would be adopted or of the impact that adoption of internal reforms might have on the adoption of external reforms. Instead of wrestling with a dynamic process, in which reforms impact the feasibility of further reforms, they treat the issue as a simple one-time choice with two options available.

These claims sit uncomfortably with the broader theory of shareholder primacy, which assumes that government officers will defend stakeholder interests. If corporate leaders focus exclusively on maximizing shareholder profits, third parties will suffer unless the government imposes taxes and penalties that align shareholder profits with social welfare.[41] As a result, the assumption of an effective government that acts appropriately to prevent socially destructive conduct continues to play an important role in the shareholder primacy perspective. As discussed in Part II below, these claims are also subject to challenge in their own right.[42]

B. *Related Claims in the Law and Economics Literature*

The first fundamental theorem of welfare economics holds that under certain strong assumptions such as the existence of complete markets, trading will naturally drive the economy to an optimal equilibrium in which no one can be made better off without making someone else worse

40. See, e.g., Bebchuk & Tallarita, Illusory Promise, supra note 1, at 174 ("To be sure, our analysis is based on the premise that the possibility of stakeholder-protecting reforms is not completely blocked."); Fisch, supra note 13, at 666 ("Labor, suppliers, customers, and community members all have the ability to participate in the political process. Other corporate stakeholders may have particular advantages in political participation relative to shareholders."); Macey, Economic Analysis, supra note 13, at 42–43 ("Under either a pluralist or a republican understanding of governmental process, local communities should be able to mobilize into an effective political coalition to press for protection from harmful action by corporations.").

41. See, e.g., Easterbrook & Fischel, supra note 22, at 39 ("We do not make the Panglossian claim that profit and social welfare are perfectly aligned. When costs fall on third parties—pollution is the common example—firms do injury because harm does not come back to them as private cost."); Macey, Economic Analysis, supra note 13, at 42–43 (noting that, if the "actions of a firm are genuinely detrimental to a . . . community, the . . . community [ought to] appeal to [its] elected representatives in . . . government for redress" instead of relying on an "amorphous, open-ended fiduciary duty," which only "transforms . . . managers . . . from private businessmen into unelected and unaccountable public servants").

42. See infra Part II.

off.[43] The second fundamental theorem of welfare economics holds that under certain stronger assumptions, any desired optimal equilibrium can be better achieved by first redistributing wealth and then allowing markets to pursue efficiency.[44]

Laundered versions of these theoretical claims are endemic in the law and economics literature. Echoing the second fundamental theorem of welfare economics, Professors Louis Kaplow and Steven Shavell have famously argued that the government should focus exclusively on efficiency when designing legal rules and use tax and transfer schemes to redistribute wealth as needed to achieve the desired outcome.[45]

This tidy separation of issues closely resembles the suggestion that internal corporate governance rules should be designed with an exclusive focus on efficiency, and external regulations and taxes should be used as needed to direct the economy toward a desired outcome.[46] Instead of adopting an inefficient corporate governance rule calling on firms to care for workers, the government could simply transfer wealth to workers until they can demand better conditions, or it could adopt regulations that match what the workers would demand in those circumstances.[47]

Criticism of this line of thinking can come from two directions. First, ideas like the fundamental theorems of welfare economics hold true only in a specific imagined environment that includes features like complete markets. These conditions are not present in the real world. Indeed, the

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43. See Andreu Mas-Colell, Michael D. Whinston & Jerry R. Green, Microeconomic Theory 326 (1995) ("If the price p^* and allocation ($x_1^*, \ldots, x_I^*, q_1^*, \ldots, q_J^*$) constitute a competitive equilibrium, then this allocation is Pareto optimal.").

44. See id. at 327 ("For any Pareto optimal levels of utility ($u_1^*, \ldots, u_I^*$), there are transfers of the numeraire commodity ($T_1, \ldots, T_I$) . . . such that a competitive equilibrium reached from the endowments . . . yields precisely the utilities ($u_1^*, \ldots, u_I^*$).").

45. See Louis Kaplow & Steven Shavell, Why the Legal System Is Less Efficient Than the Income Tax in Redistributing Income, 23 J. Legal Stud. 667, 677 (1994) ("Redistribution is accomplished more efficiently through the income tax system than through the use of legal rules, even when redistributive taxes distort behavior."); see also Fennell & McAdams, Distributive Deficit, supra note 5, at 1065 & n.42; David A. Weisbach, Should Legal Rules Be Used to Redistribute Income?, 70 U. Chi. L. Rev. 439, 447 (2003).

46. Compare Kaplow & Shavell, supra note 45, at 677 (arguing that redistribution through taxes is more efficient than redistribution through legal rules), with Bebchuk & Tallarita, Illusory Promise, supra note 1, at 167 ("[B]y hurting corporate performance and the economic value produced by corporations, these managerial inefficiencies would also reduce the aggregate wealth available to society . . . . If the economic pie produced by the corporate sector becomes smaller, all who benefit from slices of it . . . might end up worse off."). In a thought-provoking essay, Professor Luigi Zingales has similarly compared Milton Friedman's claim that corporations should focus exclusively on shareholder profits to the First Theorem of Welfare Economics, drawing out Friedman's implicit premises and questioning whether they apply to very large corporations. Luigi Zingales, Friedman's Legacy: From Doctrine to Theorem, ProMarket (Oct. 13, 2020), https://promarket.org/2020/10/13/milton-friedman-legacy-doctrine-theorem/ [https://perma.cc/7QQH-RFGT].

47. Easterbrook & Fischel, supra note 22, at 37–38.

rules of corporate governance exist precisely because of imperfections in markets.[48]

Second, even if a benevolent social planner could theoretically separate and separately optimize measures directed at redistribution and efficiency, actual governments do not do so. This dissonance has implications for reformers' strategy. Reformers following Kaplow and Shavell would focus their efforts on encouraging redistribution through tax and transfer systems, instead of attempting to make changes to ordinary legal rules. In principle, this approach should be the most effective way to achieve a desired outcome: The tax code is an adequate tool, and altering legal rules would damage efficiency in a way that reduces the societal wealth available for redistribution.

However, as Professors Lee Fennell and Richard McAdams have demonstrated, this prescription depends on heroic and contestable assumptions about political action costs.[49] In a variety of contexts, governments may be more willing to adopt legal rules with redistributive aspects than to adopt tax and transfer schemes. Even if a package consisting of an efficient legal rule and a redistributive tax and transfer scheme would theoretically be preferable to a legal rule calibrated to balance efficiency with redistribution, it may not be practically achievable given existing political realities.[50] When offering a broad recommendation on the choices reformers should make, it is necessary to consider features of the real-world political process.

Kaplow and Shavell attempt to neutralize these arguments by suggesting that any attempt to improve distributive outcomes by altering legal rules will be countered by changes to the tax code that preserve the original distribution.[51] This "invariance" principle bears comparison to the stark choice hypothesis: Both claim that any effort to reform an internal set of rules will be balanced out by a change or lack of change in external rules, leaving the public no better off.[52]

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48. See William W. Bratton & Simone M. Sepe, Corporate Law and the Myth of Efficient Market Control, 105 Cornell L. Rev. 675, 705–06 (2020) (discussing how "[t]he law provides for [corporate governance] features to address problems that arise out of market incompleteness").

49. Fennell & McAdams, Distributive Deficit, supra note 5, at 1052–53 (reasoning that "law and economics has neglected a feature of reality that is no less foundational than that of positive transaction costs: the large and variable costs associated with the *political* impediments that must be surmounted to achieve welfare-maximizing distributive results").

50. Id. at 1055.

51. Id. (describing this concept as the "invariance hypothesis"); id. at 1072–78 (documenting use of this concept in the law and economics literature); see also Kaplow & Shavell, supra note 45, at 675 (suggesting that Congress will alter the tax code to counter any attempt at redistribution through the legal system).

52. Admittedly, stark choice arguments are somewhat more optimistic than invariance arguments. Those who advance a stark choice claim seem to believe that positive change is possible; they simply suggest that internal changes will come at the expense of better

But recent research has begun to contest Kaplow and Shavell's invariance principle, noting that governments may not be interested in or capable of countering distributive legal changes.[53] As discussed below, the stark choice hypothesis is open to similar challenge.

II. Evaluating the Stark Choice Hypothesis

This Part considers evidence that the stark choice hypothesis is not true. Section II.A evaluates the premise that reformers are somehow forced to choose between internal and external strategies. It shows that states that adopt stakeholder-oriented internal corporate governance reforms are often willing to defend stakeholder interests through external reforms as well. Section II.B assesses the argument that reformers will fail to properly evaluate internal reforms' effectiveness or external reforms' feasibility. Section II.C considers the political costs of enacting various reforms in a dynamic context, suggesting that successful reforms can make future ones easier to enact.

A. *Capacity to Adopt Multiple Reforms*

The core of the stark choice hypothesis is the idea that some constraint means that policymakers who adopt internal corporate governance reforms to help stakeholders will be less likely to adopt external reforms. But there is little evidence of that effect. Instead, it seems far more likely that policymakers eager to protect particular constituencies will adopt both substantive regulations and stakeholder governance reforms. There are also many separate policymakers acting simultaneously on independent agendas to reform internal rules, and they are unlikely to all choose the same stopping point for reform.

1. *Reforms on Multiple Fronts.* — Reformers appear to be capable of pursuing both external and internal changes simultaneously, with little indication of trading one set of changes against the other. This section considers three examples of simultaneous policy action: (a) the regulatory efforts of states that have adopted "constituency statutes," (b) California's efforts to improve outcomes for women in the workforce, and (c) regulators' efforts to punish and prevent misconduct.

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external changes. Those who advance an invariance claim seem to believe that positive change is impossible; they suggest that changes to legal rules to advance distributive goals will be neutralized by changes to the tax system. But both groups seem to believe that action along a disfavored path to reform will have a negative impact on action along a favored path.

53. See, e.g., Fennell & McAdams, Distributive Deficit, supra note 5, at 1075, 1079–83 (rejecting the claim that Congress will react rapidly to undo or neutralize any efforts at redistributing income through changes to legal rules); Zachary Liscow, Are Court Orders Sticky? Evidence on Distributional Impacts From School Finance Litigation, 15 J. Empirical Legal Stud. 4, 36–38 (2018) (showing that court orders addressing inequalities in school funding are not undone by legislatures through regressive taxes).

a. Constituency Statutes. — During the 1980s, changes in the capital markets launched a "hostile takeover era": An acquirer could launch a tender offer to obtain a targeted company's shares, take over the company, and then generate financial returns at the expense of the targeted company's creditors and workers by increasing corporate debt and shedding jobs.[54] For much of this era, the board of directors of a targeted company was largely powerless to prevent such an acquisition. Delaware's courts suggested that a corporate board had an obligation to maximize returns to shareholders—including by allowing acquirers to purchase shares at a premium price—and could defend constituencies like workers by preventing a takeover only if there were "rationally related benefits accruing to the stockholders."[55] Although later doctrinal developments in Delaware reduced the practical significance of this position,[56] this strict prioritization of the interests of shareholders over other stakeholders seemed to leave workers and others defenseless against the depredations of takeover artists.

Under heavy lobbying by managers and the corporate bar, numerous states responded by enacting constituency statutes. Constituency statutes are an internal corporate governance reform that permits corporate leaders to consider the wellbeing of various stakeholders.[57] For example, New York's statute provides that

> . . . a director shall be entitled to consider, without limitation, (1) both the long-term and the short-term interests of the corporation and its shareholders and (2) the effects that the corporation's actions may have in the short-term or in the long-term upon any of the following: . . . (ii) the corporation's current employees; (iii) the corporation's retired employees and other beneficiaries . . . ; (iv) the corporation's customers and creditors; and (v) the ability of the corporation to provide, as a going concern, goods, services, employment opportunities and employment benefits and otherwise to contribute to the communities in which it does business.[58]

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54. See, e.g., William T. Allen, Our Schizophrenic Conception of the Business Corporation, 14 Cardozo L. Rev. 261, 273–74, 277 (1992).

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

56. See Allen, supra note 54, at 276 (noting that Delaware appeared to have embraced a "social entity conception" of the corporation in Paramount Commc'ns, Inc. v. Time, Inc., 571 A.2d 1140 (Del. 1989)). Chief Justice Strine provides a nuanced account of these developments in Leo E. Strine, Jr., The Story of *Blasius Industries v. Atlas Corp.*: Keeping the Electoral Path to Takeovers Clear, *in* Corporate Law Stories 243 (J. Mark Ramseyer ed., 2009) [hereinafter Strine, Story of *Blasius*].

57. See Bebchuk & Tallarita, Illusory Promise, supra note 1, at 105; id. at 117 (collecting and summarizing statutes).

58. N.Y. Bus. Corp. Law § 717(b) (McKinney 2022).

Under this statute, a director of a New York corporation would be empowered to prevent a hostile takeover that could result in worker layoffs, even if the takeover would generate higher financial returns for the company's shareholders.[59]

The states that have adopted such statutes have thus provided an internal reform to protect constituencies, but they do not seem particularly unwilling to enact external regulations providing other protections. The thirty-two states with constituency statutes that explicitly call for or allow consideration of employees[60] do not appear to have correspondingly reduced minimum wage requirements. Of those thirty-two, twenty states (or 62.5%) have adopted minimum wage requirements that exceed the federal requirement.[61] The pattern of adoption does not suggest that an employee-protective constituency statute makes a state less likely to adopt a minimum wage statute that further protects employees.

TABLE 1: STATES' CONSTITUENCY STATUTES AND MINIMUM WAGE LAWS[62]

	Employees Identified in Constituency Statute	Employees Not Identified in Constituency Statute
Minimum Wage Greater Than Federal Minimum Wage	(20): AZ, CT, FL, HI, IL, MA, MD, ME, MN, MO, NE, NJ, NM, NV, NY, OH, OR, RI, SD, VT	(10): AK, AR, CA, CO, DE, MI, MT, VA, WA, WV
No Minimum Wage or Equal to Federal Minimum Wage	(12): GA, IA, ID, IN, KY, MS, ND, PA, TN, UT, WI, WY	(8): AL, KS, LA, NC, NH, OK, SC, TX

59. There is a serious debate about whether directors and officers actually use this authority to protect stakeholders, or simply use it to extract benefits for themselves and shareholders. See Bebchuk et al., supra note 1, at 1472 (arguing that corporate leaders in states with constituency statutes bargain to obtain benefits for themselves and for shareholders, not for other stakeholders).

60. Bebchuk & Tallarita, Illusory Promise, supra note 1, at 117 tbl.1.

61. This minimum wage information has been collected from the federal Department of Labor. See Consolidated Minimum Wage Table, DOL (Oct. 1, 2022), https://www.dol.gov/agencies/whd/mw-consolidated [https://perma.cc/D42S-EL4J].

62. Id.; see also Bebchuk & Tallarita, Illusory Promise, supra note 1, at 117 tbl.1. Utah's current statute differs from the table shown in Bebchuk and Tallarita's piece. See Utah Code §16-10a-840(5)(b)(ii)(B) (2023) (allowing directors to consider employees' wellbeing).

The timing of adoption also does not suggest that constituency statutes prevent later action to raise the minimum wage, because constituency statutes frequently predated action on minimum wage requirements. Many constituency statutes were adopted as part of a wave that began in 1983, with twenty-nine states having a provision on their books by 1999.[63] The current federal minimum wage was set by statute in 2007;[64] states with a higher minimum wage generally acted later to set those requirements.[65]

There is also no obvious relationship between a state's decision to adopt a constituency statute that protects workers and the generosity of the state's unemployment benefits. Of the thirty-two states that identify employees as a constituency, nineteen states (or 59.4%) replace a higher percentage of wages than the overall U.S. average.[66] Again, the pattern of benefits does not suggest an obvious relationship between adopting a constituency statute and providing generous benefits to unemployed workers.

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63. See Nathan E. Standley, Note, Lessons Learned From the Capitulation of the Constituency Statute, 4 Elon L. Rev. 209, 212 (2012); see also Bebchuk & Tallarita, Illusory Promise, supra note 1, at 105 (describing constituency statutes as a response to "the hostile takeover era of the 1980s and 1990s").

64. See Fair Minimum Wage Act of 2007, Pub. L. No. 110-28, § 8102, 121 Stat. 188, 188 (codified at 29 U.S.C. § 206(a)(1) (2018)).

65. See, e.g., History of the Minimum Wage in New York State, N.Y. Dep't of Lab., https://dol.ny.gov/history-minimum-wage-new-york-state [https://perma.cc/GLA8-FRJT] (last visited Mar. 6, 2023) (noting minimum wage increases in 2009 and several later years).

66. The replacement rate information is from the first quarter of 2019. See UI Replacement Rates Report, DOL, https://oui.doleta.gov/unemploy/ui_replacement_rates.asp [https://perma.cc/3JY6-BZCV] (last updated July 7, 2022).

TABLE 2: STATES' CONSTITUENCY STATUTES AND UNEMPLOYMENT INSURANCE REPLACEMENT RATES[67]

	Employees Identified in Constituency Statute	Employees Not Identified in Constituency Statute
Higher UI Replacement Rate Than U.S. Average	(19): HI, IA, ID, KY, MA, ME, MD, MN, NE, NJ, NM, ND, NV, OR, PA, SD, UT, VT, WY	(7): CA, CO, KS, MT, OK, TX, WA
Lower UI Replacement Rate Than U.S. Average	(13): AZ, CT, FL, GA, IL, IN, MO, MS, NY, OH, RI, TN, WI	(11): AL, AK, AR, DE, LA, MI, NC, NH, SC, VA, WV

States with constituency statutes allowing for internal reform have also adopted other regulations to serve constituencies. New York provides a particularly interesting example. The state does not merely list employees as legitimate stakeholders in its constituency statute. New York also has a minimum wage of $14.20 statewide, well above the federal minimum of $7.25.[68] New York's employment discrimination laws were specifically designed to set a more worker-friendly standard than federal law.[69] And New York makes the largest shareholders in privately held corporations personally liable for wages payable to corporate employees.[70] New York did not adopt stakeholder governance in lieu of more substantive measures; it adopted the approach as one part of an overall regulatory philosophy that is protective of employees.

67. Id; see also Bebchuk & Tallarita, Illusory Promise, supra note 1, at 117 tbl.1. Again, Utah has been moved to reflect current laws. See Utah Code §16-10a-840(5)(b)(ii)(B).

68. Consolidated Minimum Wage Table, supra note 61.

69. See New Legislation Eliminates "Severe or Pervasive" Standard, Lowers Bar for Sexual Harassment and Discrimination Actions in New York State, Levy Ratner (Sept. 10, 2019), https://levyratner.com/new-legislation-eliminates-severe-or-pervasive-standard-lowers-bar-for-sexual-harassment-and-discrimination-actions-in-new-york-state/ [https://perma.cc/TZS9-G2X3] (noting that the state law's lower burden of proof "will make it far easier for employees to pursue mistreatment in New York State").

70. N.Y. Bus. Corp. Law § 630 (McKinney 2022). New York's solicitousness to employees in this respect has been described as making it a less attractive place to incorporate. Marcel Kahan & Ehud Kamar, The Myth of State Competition in Corporate Law, 55 Stan. L. Rev. 679, 732 (2002).

Other states with employee-focused constituency statutes protect workers in similar ways. For example, in addition to naming employees as stakeholders in its constituency statute,[71] Oregon has a minimum wage of at least $12.50 per hour, with higher wages in certain metro areas.[72] It is one of a minority of states to offer paid family leave and one of a minority of states to offer paid sick leave.[73] Oregon has also repeatedly tightened its rules on noncompete agreements, most recently by making nonconforming noncompete agreements void as opposed to voidable, thus making it easier for a worker to leave an employer and find another job in the industry.[74] Like New York and Oregon, Massachusetts has a constituency statute that expressly references employees.[75] But Massachusetts also has a minimum wage of $14.25 per hour.[76] It is also part of the minority of states to offer paid family leave and part of the minority of states to offer paid sick leave.[77] And Massachusetts has updated its law on noncompete agreements to make it easier for workers to move to competing firms.[78] These examples can be multiplied, but the core point is simply that there is no obvious indication that states have treated constituency statutes as a substitute for regulatory action.

71. Or. Rev. Stat. § 60.357(5) (West 2022) ("[T]he directors of the corporation may, in determining what they believe to be in the best interests of the corporation, give due consideration to the social, legal and economic effects on employees . . . .").

72. Oregon Minimum Wage, Or. Bureau of Lab. & Indus., https://www.oregon.gov/boli/workers/pages/minimum-wage.aspx [https://perma.cc/9QHL-WSC9] (last visited Oct. 12, 2022).

73. State Family and Medical Leave Laws, Nat'l Conf. of State Legislatures, https://www.ncsl.org/research/labor-and-employment/state-family-and-medical-leave-laws.aspx [https://perma.cc/TM2D-A89P] (last updated Sept. 9, 2022).

74. See Elizabeth H. White & Jonathan G. Rue, Effective Use of Non-Solicitation and Confidentiality Agreements in Oregon After S.B. 169, K&L Gates (Apr. 1, 2022), https://www.klgates.com/Effective-Use-of-Non-Solicitation-and-Confidentiality-Agreements-in-Oregon-After-SB-169-4-1-2022 [https://perma.cc/9JRQ-BBST] (describing "Oregon's ever-broadening noncompetition statute").

75. Mass. Gen. Laws Ann. ch. 156B, § 65 (West 2022) ("In determining what he reasonably believes to be in the best interests of the corporation, a director may consider the interests of the corporation's employees . . . .").

76. Massachusetts Law About Minimum Wage, Mass. Trial Ct. L. Librs., https://www.mass.gov/info-details/massachusetts-law-about-minimum-wage [https://perma.cc/Q3VE-DYRA] (last visited Oct. 10, 2022).

77. Brendan Williams, The Slow Crawl of Paid Family Leave Laws, 55 Cal. W. L. Rev. 423, 436–37 (2019); State Family and Medical Leave Laws, supra note 73.

78. Michael G. Feblowitz, Note, Repaving Route 128: How New Legislation in Massachusetts Impacts the Noncompete Debate, 61 B.C. L. Rev. 2263, 2263 (2020). Massachusetts previously had a much more employer-friendly body of law on noncompete agreements. See Ronald J. Gilson, The Legal Infrastructure of High Technology Industrial Districts: Silicon Valley, Route 128, and Covenants Not to Compete, 74 N.Y.U. L. Rev. 575, 578–79 (1999) (contrasting Massachusetts's employer-friendly approach with California's employee-friendly approach).

b. *California's Women on Boards Statute.* — Recent years have seen a reinvigoration of interest in curbing sex discrimination and sexual harassment. These problems and the efforts to address them are obviously not a new development.[79] But the reform movement seems to have entered a new phase as a result of high-profile events including the election of Donald J. Trump to the presidency despite the public revelation of an audio recording in which he crudely boasted of engaging in sexual assault,[80] the exposure of serious misconduct by Hollywood mogul Harvey Weinstein;[81] and the confirmation of Brett Kavanaugh to the Supreme Court despite allegations that he had committed sexual assault.[82] Similar revelations also shook corporate America, with misconduct allegations resulting in the forced departure of executives at several high-profile firms.[83]

California's state government responded to these issues with a mix of internal and external measures. On September 30, 2018, California Governor Jerry Brown signed Senate Bill 826, an internal reform designed to ensure a minimal level of female representation on the boards of publicly held corporations chartered or headquartered in California.[84]

The proponents of this "Women on Boards" statute routinely justified the measure by insisting that it would benefit shareholders, perhaps

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79. See, e.g., Catharine A. MacKinnon, Sexual Harassment of Working Women 6 (1979) (documenting sexual harassment and characterizing it as a form of discrimination). The phrase "Me Too" was coined by activist Tarana Burke in 2007 as part of her efforts to help victims of sexual harassment and assault. See Sandra E. Garcia, The Woman Who Created #MeToo Long Before Hashtags, N.Y. Times (Oct. 20, 2017), https://www.nytimes.com/2017/10/20/us/me-too-movement-tarana-burke.html (on file with the *Columbia Law Review*).

80. See, e.g., Alexander Burns, Maggie Haberman & Jonathan Martin, Donald Trump Apology Caps Day of Outrage Over Lewd Tape, N.Y. Times (Oct. 7, 2016), https://www.nytimes.com/2016/10/08/us/politics/donald-trump-women.html (on file with the *Columbia Law Review*).

81. See, e.g., Ronan Farrow, From Aggressive Overtures to Sexual Assault: Harvey Weinstein's Accusers Tell Their Stories, New Yorker (Oct. 10, 2017), https://www.newyorker.com/news/news-desk/from-aggressive-overtures-to-sexual-assault-harvey-weinsteins-accusers-tell-their-stories (on file with the *Columbia Law Review*); Jodi Kantor & Megan Twohey, Harvey Weinstein Paid Off Sexual Harassment Accusers for Decades, N.Y. Times (Oct. 5, 2017), https://www.nytimes.com/2017/10/05/us/harvey-weinstein-harassment-allegations.html (on file with the *Columbia Law Review*).

82. See, e.g., Christine Hauser, The Women Who Have Accused Brett Kavanaugh, N.Y. Times (Sept. 26, 2018), https://www.nytimes.com/2018/09/26/us/politics/brett-kavanaugh-accusers-women.html (on file with the *Columbia Law Review*).

83. For a discussion of the MeToo movement and some of its implications for corporate governance, see generally Daniel Hemel & Dorothy S. Lund, Sexual Harassment and Corporate Law, 118 Colum. L. Rev. 1583 (2018) (analyzing the interaction of corporate and securities law with sexual harassment claims).

84. See An Act to Add Sections 301.3 and 2115.5 to the Corporations Code, Relating to Corporations, S.B. 826, ch. 954, 2018 Cal. Stat. 6263 (increasing the "required minimum number to 2 female directors if the corporation has 5 directors or to 3 female directors if the corporation has 6 or more directors").

because the proponents believed that would be the most compelling justification for a corporate governance measure or would help the statute pass constitutional muster.[85] The bill itself included legislative findings that women on boards improved corporate financial performance.[86] But the statute also had other goals. The legislative findings in the statute spoke to the benefits to women as a class as well as benefits to shareholders as a class.[87] Governor Brown's signing statement also directly tied the measure to the movement against sexual harassment and discrimination. The statement suggested that the measure was necessary because "recent events in Washington, D.C.—and beyond—make it crystal clear that many are not getting the message,"[88] a clear reference to the Kavanaugh confirmation hearings. To ensure the message was not lost, Governor Brown made sure to copy the United States Senate Committee on the Judiciary.[89]

On the same day, Governor Brown also signed a package of external regulations targeting sexual assault, harassment, and discrimination in the employment context.[90] These measures included California Senate Bill 820, prohibiting the use of nondisclosure agreements in settlements of cases of sexual assault, sexual harassment, and sex discrimination;[91] Senate Bill 1300, limiting employers' ability to use liability waivers;[92] and Assembly

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85. Id. § 1(a), 2018 Cal. Stat. at 6264; Emily Stewart, California Just Passed a Law Requiring More Women on Boards. It Matters, Even If It Fails., Vox (Oct. 3, 2018), https://www.vox.com/2018/10/3/17924014/california-women-corporate-boards-jerry-brown [https://perma.cc/DN5R-6BL4].

86. § 1(c), 2018 Cal. Stat. at 6264.

87. § 1(a), 2018 Cal. Stat. at 6264 ("More women directors serving on boards of directors of publicly held corporations will . . . improve opportunities for women in the workplace . . . ."). The leading co-author of the bill, state senator Hannah-Beth Jackson, alluded to this mix of motives when she hailed it as "a giant step forward not just for women but also for our businesses and our economy." See Jorge L. Ortiz, California's 'Giant Step Forward': Gender-Quotas Law Requires Women on Corporate Boards, USA Today (Oct. 1, 2018), https://www.usatoday.com/story/news/2018/09/30/california-law-sets-gender-quotas-corporate-boardrooms/1482883002/ [https://perma.cc/2DB6-4P2G].

88. Letter from Edmund G. Brown, Jr., Governor, California, to the Members of the California State Senate (Sept. 30, 2018), https://ca-times.brightspotcdn.com/89/11/e07e898d40bfa1a532dabef65abe/sb-826-signing-message.pdf [https://perma.cc/A9MP-NA4K].

89. Id.

90. Alexei Koseff, California Bans Secret Settlements in Sexual Harassment Cases, Sacramento Bee (Sept. 30, 2018), https://www.sacbee.com/news/politics-government/capitol-alert/article218830265.html (on file with the *Columbia Law Review*).

91. An Act to Add Section 1001 to the Code of Civil Procedure, Relating to Civil Procedure, S.B. 820, ch. 953, 2018 Cal. Stat. 6262.

92. An Act to Amend Sections 12940 and 12965 of, and to Add Sections 12923, 12950.2, and 12964.5 to, the Government Code, Relating to Employment, S.B. 1300, ch. 955, 2018 Cal. Stat. 6267.

Bill 1619, providing additional time to pursue civil claims for sexual assault.[93]

These internal and external measures can be criticized. Perhaps the minima established by these measures are too weak, or perhaps a different set of reforms would accomplish more for women in the workforce. But there is no indication that robust external measures were traded away for an ineffective internal measure. California appears to have decided to act on gender equity issues and attacked on both the internal and external fronts.

c. *Corporate Prosecutions.* — Government efforts to punish and prevent corporate misconduct may present a more ambiguous example. Prosecutors are eager to deter corporate misconduct and to ensure that crimes are detected and reported. To achieve these objectives, they often settle enforcement actions against corporations with agreements that impose fines and require the companies to make changes to their compliance function.[94] Fines are a classic external strategy—they set a monetary price on socially harmful conduct and thus encourage profit-seeking companies to behave in a socially optimal way. Governance mandates are an internal strategy—they require firms to adopt structures and reporting processes intended to improve their decisions.

It is plausible that prosecutors must trade away external measures to obtain internal measures. Internal mechanisms are costly, both in the sense that they cost money to implement and in the sense that they may raise the likelihood of a corporate crime being detected and punished.[95] A case has some fixed expected value, and a corporation will not agree to pay more than that value to settle it, whether in the form of increased compliance costs or in the form of a fine. If prosecutors demand increased

93. An Act to Add Section 340.16 to the Code of Civil Procedure, Relating to Sexual Assault, A.B. 1619, ch. 939, 2018 Cal. Stat. 6213; see also Press Release, Marc Berman, Assemb., Sexual Assault Survivors Given More Time for Civil Recourse (Sept. 30, 2018), https://a24.asmdc.org/press-releases/20180930-sexual-assault-survivors-given-more-time-civil-recourse [https://perma.cc/JRY4-ASE5].

94. See, e.g., Brandon L. Garrett, Too Big to Jail: How Prosecutors Compromise With Corporations 43 (2014) (documenting the use of penalties and structural reforms in pretrial diversion agreements); Jennifer Arlen & Marcel Kahan, Corporate Governance Regulation Through Nonprosecution, 84 U. Chi. L. Rev. 323, 335 (2017) (noting that pretrial diversion agreements generally "require firms to pay fines and other monetary penalties" and impose mandates regarding compliance).

95. Of course, prosecutors may choose not to punish a corporation if its compliance function is well designed and detects and reports employee misconduct. See DOJ, Just. Manual § 9-28.300 (2020), https://www.justice.gov/jm/jm-9-28000-principles-federal-prosecution-business-organizations#9-28.300 [https://perma.cc/8TZD-D6DN] (establishing that "adequacy and effectiveness of the corporation's compliance program at the time of the offense, as well as at the time of a charging decision" and "the corporation's timely and voluntary disclosure of wrongdoing" are factors to be considered when exercising prosecutorial discretion).

compliance spending, it will in principle decrease the amount of the fine that they can demand.[96]

But this effect is likely to be limited. Prosecutors likely settle cases for far less than their expected value. Prosecutors can plausibly threaten to end businesses with crippling fines or by revoking licenses; but they stay their hand out of concern about effects on innocent stakeholders, such as employees and surrounding communities,[97] and because of an internalized sense of appropriate punishments.[98] As a result, the expected value of the case may not be a binding constraint on the prosecutor's decision: The prosecutor was never going to demand the full value of the case as an external fine. If a prosecutor attaches some new internal condition to a deal, it may not come at the expense of a larger fine.[99]

96. Put differently, a corporation would prefer trial to a negotiated settlement if the fine plus the cost of a revamped compliance program exceeds the expected outcome of a trial. The possibility of reversion to trial operates as a constraint on potential government demands in settlement negotiations. At some point, more extensive demands for the compliance program would require the government to pare back the fine to achieve a settlement. But as discussed, the constraint is unlikely to be binding in the real world because prosecutors are unlikely to push the limits of what they could demand from a defendant corporation. See supra text accompanying notes 91–92.

97. See, e.g., John C. Coffee, Jr., Corporate Crime and Punishment: The Crisis of Underenforcement 12 (2020) ("[H]igh penalties can cause externalities, as creditors, employees, and others closely connected to the corporation are injured."); Jesse Eisinger, The Chickenshit Club: Why the Justice Department Fails to Prosecute Executives 94 (2017) ("Prosecutors and regulators were crippled by the idea that the government could not criminally sanction some companies—particularly large banks—for fear that they would collapse, causing serious problems for financial markets or the economy."); Garrett, supra note 94, at 59 (noting Attorney General Alberto Gonzales's observation that the criminal "conviction of an organization can affect innocent workers and others associated with the organization, and can even have an impact on the national economy" (internal quotation marks omitted) (quoting Alberto R. Gonzales, U.S. Att'y Gen., DOJ, Prepared Remarks at the Press Conference Regarding KPMG Corporate Fraud Case (Aug. 29, 2005))). In response to this problem, Professor John Coffee has proposed that corporate fines should be imposed in the form of equity, thus creating a meaningful financial incentive without affecting the company's operations or non-shareholder stakeholders. See Coffee, supra, at 145.

98. See Dorothy S. Lund & Natasha Sarin, Corporate Crime and Punishment: An Empirical Study, 100 Tex. L. Rev. 285, 335–36 (2021) (showing that recidivist companies pay smaller fines as a percentage of market capitalization and revenue, and suggesting that prosecutors may have internalized some upper bound on fines that they apply regardless of the size of the corporate defendant).

99. To illustrate, suppose that the expected penalty after a trial is $1 billion. In principle, if prosecutors were set to demand $600 million in compliance spending plus a $600 million fine, they would have to pare back the fine before a risk-neutral corporation would agree. But in reality, prosecutors do not appear willing to push the limit, either because they fear hurting workers and other groups or because they believe that such penalties are inappropriate. If prosecutors are set to demand $400 million in compliance spending plus $400 million in fines, they can dial up compliance demands by $200 million before the corporation would rather take its chances with a trial.

Again, there is room to debate the propriety of internal terms in the settlement of enforcement actions against corporations.[100] But the propriety and effectiveness of internal steps is separate from the question of whether they take away from external steps. It is not clear that they do, even in the unique context of prosecutions.

2. *Multiple Reformers Pursuing Internal Reforms.* — The concept of limited capacity also ignores the presence of multiple independent policymakers with the capacity to execute separate policy agendas. An external reform, such as a law against employment discrimination, can be plausibly pursued only by a small set of public actors that face serious constraints on action. By contrast, an internal reform can be pursued by a much broader set of actors, including in the private sector. The diversity of actors who can impose internal reforms means that internal reforms can proceed even where external regulators are satisfied or have exhausted their political capital.

An external reform at the federal level will generally require congressional action. Congress either must enact a statute addressing a problem or must have previously enacted a statute that administrative agencies can use to address that problem. The federal legislative process is characterized by inertia—it takes enormous effort to set it in motion—and it requires an unusually broad national coalition to achieve success.[101] It also has a number of veto gates and procedural idiosyncrasies that can

100. See, e.g., Arlen & Kahan, supra note 94, at 323–24 (urging that regulators generally should not impose corporate governance mandates unless there is an indication of an agency problem). But there are reasons to think that such conditions cause corporations to make real efforts to report misconduct and provide evidence, and that corporations may systematically underinvest in compliance without them. See John Armour, Jeffrey Gordon & Geeyoung Min, Taking Compliance Seriously, 37 Yale J. on Regul. 1, 5–6 (2020) (noting that corporate leaders sensitive to stock prices may systematically underinvest in compliance to avoid signaling to market that the company is at a high risk of violating the law); Aruna Viswanatha & Dave Michaels, Flaws Emerge in Justice Department Strategy for Prosecuting Wall Street, Wall St. J. (July 5, 2021), https://www.wsj.com/articles/flaws-emerge-in-justice-department-strategy-for-prosecuting-wall-street-11625506658 (on file with the *Columbia Law Review*) (recounting anecdotes suggesting that corporations under such mandates vigorously investigate employees suspected of misconduct and turn over evidence to prosecutors).

101. See, e.g., John F. Manning, Lawmaking Made Easy, 10 Green Bag 2d 191, 198 (2007) ("Even the quickest look at the constitutional structure reveals that the design of bicameralism and presentment disfavors easygoing, high volume lawmaking.").

affect the content[102] or success of legislation.[103] And even if a statute is enacted, it must be implemented by regulators, enforced by prosecutors, and survive review by often hostile federal judges. The necessary consensus is frequently lacking at the federal level.[104]

Absent federal leadership, external reform at the state level is difficult. State governments are often prevented from regulating in areas of federal interest by preemption, the dormant commerce clause, and other doctrines.[105] They are also constrained by competitive dynamics. States and local governments vigorously compete to attract investments by large employers.[106] As a result, a single state cannot unilaterally adopt external regulations without consequence.

These forces are also present when federal or state regulators seek to reform internal rules, though sometimes to a lesser degree. It is difficult to pass federal legislation adopting new rules addressed to internal issues,

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102. The Dodd–Frank Wall Street Reform and Consumer Protection Act was intended to address the risk of failure of important financial institutions. Professor David Skeel has suggested that the Act did not use a bankruptcy framework for dealing with failed banks because Senator Dodd and Representative Frank controlled committees focused on financial issues, and a statute using a bankruptcy framework would fall under the jurisdiction of the Judiciary Committees. Using a bankruptcy framework would have required Dodd and Frank to surrender control over the legislation. David Skeel, The New Financial Deal 53–54 (2011).

103. Current Senate rules generally require a sixty-vote supermajority to defeat a filibuster and pass legislation. However, certain legislation on budget matters can be passed by the Senate with a bare majority through the reconciliation process. In 2021, the Senate Parliamentarian ruled that an increase in the minimum wage did not qualify for the reconciliation process; the ruling was widely regarded as dooming the prospects for an immediate increase in the federal minimum wage. See Kristina Peterson, Meet the Senate Parliamentarian, Referee in Minimum-Wage Debate, Wall St. J. (Feb. 26, 2021), https://www.wsj.com/articles/meet-the-senate-parliamentarian-key-figure-in-minimum-wage-debate-11614168008 (on file with the *Columbia Law Review*).

104. For a brief summary of these issues and the failure of regulation to play its required role in constraining corporations, see generally Kovvali & Strine, supra note 7.

105. For example, during the Trump Administration, the Department of Justice investigated four automakers who had attempted to reach agreements with the state of California on tighter fuel economy standards. The subsequent Biden Administration dropped the inquiry. See John M. Newman, The Output-Welfare Fallacy: A Modern Antitrust Paradox, 107 Iowa L. Rev. 563, 587 (2022); Coral Davenport, Justice Department Drops Antitrust Probe Against Automakers That Sided With California on Emissions, N.Y. Times (Feb. 7, 2020), https://www.nytimes.com/2020/02/07/climate/trump-california-automakers-antitrust.html (on file with the *Columbia Law Review*).

106. See, e.g., Strine, Corporate Power, supra note 1, at 183–85 (describing how Delaware communities engaged in a "bidding war" on taxes to retain the operations of DuPont and Dow). This dynamic can sometimes support external regulation. See Susan S. Kuo & Benjamin Means, The Political Economy of Corporate Exit, 71 Vand. L. Rev. 1293, 1295 (2018) ("By making clear that they are unwilling to do business in places that deny equal treatment to LGBT people, corporations have been instrumental in defeating proposed state laws that would restrict transgender bathroom access or permit business owners to refuse services to gay, lesbian, or transgender people.").

just as it is difficult to pass federal legislation adopting new external rules. But there are already important federal statutes on the books that permit administrative agencies to take meaningful action on various governance issues. For example, the Securities and Exchange Commission is already empowered to require or regulate disclosures by public companies and can use that power to mandate disclosures on employee, environmental, social, and governance issues.[107] Likewise, the Department of Labor has the power to regulate important institutional investors that deploy worker funds; the DOL can use that authority to address the way in which those institutional investors use their voting power within corporations.[108]

State governments also arguably face competition in their selection of internal rules. If a Delaware corporation prefers Minnesota corporate law, it can reincorporate in Minnesota. But Delaware's dominance in corporate law raises a real question as to whether that competition is meaningful,[109] and whether it constrains states other than Delaware.[110]

But more importantly, internal reform can proceed without the involvement of the federal and state actors required for external reforms. Quasi-governmental entities like the Financial Industry Regulatory Authority (FINRA) can adopt rules, and stock exchanges like the NYSE and Nasdaq can adopt listing requirements that speak to governance

107. See, e.g., Cynthia Williams, The Securities and Exchange Commission and Corporate Social Transparency, 112 Harv. L. Rev. 1197, 1205–06 (1999) (arguing that the SEC has statutory authority to promote corporate accountability to the public); Press Release, SEC, SEC Proposes Rules to Enhance and Standardize Climate-Related Disclosures for Investors (Mar. 21, 2022), https://www.sec.gov/news/press-release/2022-46 [https://perma.cc/8LXT-UWRZ] (describing proposed rule changes that would require climate-related disclosures).

108. See infra section III.C.3.

109. There is an extensive literature on whether states compete with each other in adopting internal corporate governance rules, and whether that competition is a healthy race to the top or an unhealthy race to the bottom. See, e.g., Roberta Romano, The Genius of American Corporate Law 37–40 (1993) (suggesting that Delaware has succeeded in a competition to charter corporations, leading to a healthy result); Lucian Arye Bebchuk & Assaf Hamdani, Vigorous Race or Leisurely Walk: Reconsidering the Competition Over Corporate Charters, 112 Yale L.J. 553, 555 (2002) (suggesting that Delaware faces relatively little competition for charters); William L. Cary, Federalism and Corporate Law: Reflections Upon Delaware, 83 Yale L.J. 663, 705 (1974) (suggesting that Delaware was leading a race to the bottom); Marcel Kahan & Edward Rock, Symbiotic Federalism and the Structure of Corporate Law, 58 Vand. L. Rev. 1573, 1576 (2005) (observing that federal intervention threatens Delaware's hold only during times of crisis); Mark J. Roe, Delaware's Competition, 117 Harv. L. Rev. 588, 593 (2003) (suggesting that Delaware does not face competition from other states but does face the risk of intervention by the federal government). The existence of meaningful competition is at best uncertain.

110. Chief Justice Strine has suggested that states other than Delaware were free to adopt antitakeover laws like constituency statutes because only managers and employees had political potency in those states. By contrast, Delaware had to maintain a reputation for fairly protecting shareholder interests. See Strine, Story of *Blasius*, supra note 56, at 252.

issues.[111] Fully private entities like institutional investors can also insist on reforms, using their power as shareholders to vote and engage with management on issues of importance. Given the increasingly large stakes held by institutional investors like index funds, they have substantial power to force corporations to follow their preferences: The big three index fund providers, BlackRock, Inc., State Street Global Advisors, and Vanguard Group, collectively cast about 25% of the shareholder votes in the S&P 500 companies.[112] The power of these institutional investors has also empowered the institutions that advise them. Two firms, ISS and Glass Lewis, issue particularly influential advice on how shareholders should cast their proxy votes. Their pronouncements have been so difficult for corporations to resist that one commentator has likened their rulings to a "new civil code" regulating corporate affairs.[113]

Each of these groups has different powers, and some are vulnerable to action by federal or state authorities. For example, if Nasdaq wishes to impose a new listing requirement, it must obtain the Securities and Exchange Commission's approval. And institutional investors may worry that if they are too aggressive in using their power, regulators will take steps to curb them.[114]

But each of these groups also has its own agenda, process, and constituency. If BlackRock wants to take action on some issue, it does not need to mobilize the nationwide coalition required to make the House, Senate, and President act in concert. It simply needs to be mindful of the preferences of its customers and the red lines of its regulators. And BlackRock's narrow purview and focused constituency can make it want to act in circumstances where more generalized institutions like Congress would simply remain inert.[115] As a result, a private actor like BlackRock can take steps that are not approved, or are even actively condemned, by the public actors who would have to approve an external regulation. And a private actor like BlackRock can continue to press forward on an issue even when public actors have exhausted their political capital.

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111. For a broad discussion of the increasingly governmental role of "self-regulatory organizations," see generally William A. Birdthistle & M. Todd Henderson, Becoming a Fifth Branch, 99 Cornell L. Rev. 1 (2013).

112. See, e.g., Lucian Bebchuk & Scott Hirst, Index Funds and the Future of Corporate Governance: Theory, Evidence, and Policy, 119 Colum. L. Rev. 2029, 2033 (2019).

113. Neil Whoriskey, The New Civil Code: ISS and Glass Lewis as Lawmakers, CLS Blue Sky Blog (July 28, 2020), https://clsbluesky.law.columbia.edu/2020/07/28/cleary-gottlieb-discusses-the-new-civil-code-of-iss-and-glass-lewis/ [https://perma.cc/WBJ3-GKH9].

114. See Bebchuk & Hirst, supra note 112, at 2066–71; infra section III.C.

115. Cf. Dhammika Dharmapala, The Congressional Budget Process, Aggregate Spending, and Statutory Budget Rules, 90 J. Pub. Econ. 119, 121 (2006) (showing that small interest groups could lobby focused committees in Congress more effectively than the more generalist Budget Committee, due to the potential for free riding in the latter).

Three simple examples show how internal mechanisms of reform can proceed even where public regulators have refused or lost interest.

a. *Women on Boards.* — As discussed above,[116] California has sought to require public companies chartered or headquartered in the state to have some minimum level of female representation on their boards of directors. But this requirement may be vulnerable to challenge on constitutional grounds, and it is limited in its geographic scope.[117]

Other actors have sought to step in. The Nasdaq stock exchange has sought to impose a similar gender-diversity requirement for the boards of corporations listed on the exchange.[118] And State Street Global Advisors made a high-profile push to require large corporations to include women on their boards.[119] Because of the enormous size of the portfolio State Street manages, the campaign was highly influential.[120]

b. *Classified or Staggered Boards.* — The directors of a corporation must face regular elections in which the shareholders cast votes. The directors can be divided into up to three "classes," with only one class facing an election in a given year.[121] If the board is not classified, all of the directors have one-year terms and all can be voted out in a year.[122] If the board is classified into three groups, all of the directors have three-year terms and only one-third of the directors can be voted out in a given year.[123] As a result, a would-be acquirer can only capture a majority of a classified board by prevailing in two annual shareholder elections. Acquirers can be deterred further by a "poison pill" defense that prevents them from purchasing more than a small fraction of the available shares on the

116. See supra section II.A.1.b.

117. As of this writing, the Ninth Circuit has authorized a shareholder to proceed with a Fourteenth Amendment challenge to the statute based on their allegation that the statute unconstitutionally encouraged the shareholder to discriminate on the basis of sex. Meland v. Weber, 2 F.4th 838, 849 (9th Cir. 2021). And a state court has enjoined enforcement of the law on the ground that the statute violates the equal protection clause of the California constitution. Crest v. Padilla, No. 19STCV27561, 2022 WL 1073294 (Cal. Super. Ct. Apr. 1, 2022).

118. See Press Release, Nasdaq, Nasdaq to Advance Diversity Through New Proposed Listing Requirements (Dec. 1, 2020), https://www.nasdaq.com/press-release/nasdaq-to-advance-diversity-through-new-proposed-listing-requirements-2020-12-01 [https://perma.cc/FX5N-NG2T] [hereinafter Nasdaq, Proposed Listing Requirements]; see also Order Approving Nasdaq Proposed Rule Changes Relating to Board Diversity, Exchange Act Release No. 34-92590, 86 Fed. Reg. 44,424 (Aug. 6, 2021).

119. See Michal Barzuza, Quinn Curtis & David H. Webber, Shareholder Value(s): Index Fund ESG Activism and the New Millennial Corporate Governance, 93 S. Cal. L. Rev. 1243, 1248 (2020).

120. See id. (noting that of the 400 firms targeted by State Street in 2017, over 300 had added a female director by the end of 2018).

121. Del. Code tit. 8, § 141(d) (2022).

122. Id.

123. Id.

market.[124] This tactic prevents a would-be acquirer from simply purchasing a majority of the shares then voting those shares in two consecutive elections—to get control of the board, the acquirer must persuade its fellow shareholders to agree in two consecutive elections.

In *Air Products & Chemicals v. Airgas, Inc.*, the Delaware Court of Chancery approved this potent combination of defenses.[125] In effect, the state of Delaware refused to curb the use of these tactics. But private actors did not simply accept this outcome. Bebchuk and his Harvard Law School Shareholder Rights Project coordinated and assisted a vigorous campaign to declassify corporate boards.[126] The tactics and objective of the effort are hotly debated.[127] But the effectiveness of the effort is not open to serious question: "[C]lassified boards are becoming rare and are on their way toward endangered-species status."[128]

c. *Dual Class Shares.* — A corporation can slice voting and cash-flow rights in different ways. If there is a single class of shares, a person who owns 1% of the shares will receive 1% of corporate dividends and can cast 1% of the votes each year. But a corporation could use multiple classes of shares to divide cash flows and power differently. An owner of high-powered shares may be entitled to cast 10% of the votes despite being entitled to only 1% of the dividends. As a result, a founder can use high-

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124. Air Products & Chemicals, Inc. v. Airgas, Inc., 16 A.3d 48, 94–101 (Del. Ch. 2011) (reaffirming the "legality of the poison pill as a valid takeover defense").

125. Id. at 57.

126. About, S'holder Rts. Project, http://www.srp.law.harvard.edu/index.shtml [https://perma.cc/46HF-4X67] (last visited Oct. 12, 2022).

127. For particularly vigorous criticisms of the effort, and its effect on corporate value, see Daniel M. Gallagher & Joseph A. Grundfest, Did Harvard Violate Federal Securities Law? The Campaign Against Classified Boards of Directors 5–8 (Rock Ctr. for Corp. Governance Working Paper No. 199, 2014), https://ssrn.com/abstract=2536586 [https://perma.cc/2CZK-Z2RT] (suggesting that the Harvard Shareholder Rights Project violated federal law by making misleading claims in support of shareholder resolutions seeking elimination of staggered boards); K.J. Martijn Cremers & Simone M. Sepe, Board Declassification Activism: The Financial Value of the Shareholder Rights Project 6 (June 2, 2017) (unpublished manuscript), https://ssrn.com/abstract_id=2962162 [https://perma.cc/2MN9-L4Z5] (presenting results that "are inconsistent with the entrenchment view of classified boards and support the commitment view that, at least at some firms, classified boards serve a positive governance function by helping to bond directors and shareholders to long-term value creation"); Martin Lipton & Theodore Mirvis, Harvard's Shareholder Rights Project Is Wrong, Harv. L. Sch. Forum on Corp. Governance (Mar. 23, 2012), https://corpgov.law.harvard.edu/2012/03/23/harvards-shareholder-rights-project-is-wrong/ [https://perma.cc/HRF8-B7K4] ("There is no persuasive evidence that declassifying corporate boards enhance[s] stockholder value over the long-term, and . . . the absence of a staggered board makes it significantly harder for a public company to fend off an inadequate, opportunistic takeover bid, and is harmful to companies that focus on long-term value creation.").

128. 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, 497 (2014).

powered shares to retain control of the company and pursue a singular vision while raising cash by selling low-powered shares to others.

In 1988, the SEC adopted Rule 19c-4, sharply discouraging companies from restricting voting rights.[129] The rule was struck down as exceeding the Commission's statutory authority in 1990, and the SEC made no attempt to revive it.[130] But again, private actors did not sit still. Institutional investors urged the stock exchanges to prohibit listings of dual classes of shares.[131] And the S&P Dow Jones Indices prevented companies with multiple classes of shares from joining the S&P 500 Index.[132] This move was highly consequential for companies with multiple classes of shares because the increasingly large investors who seek to passively follow the S&P 500 Index would not have the opportunity to buy shares of those companies.[133] Yet again, private actors were able to press an agenda even where public authorities had been unable to do so.

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These examples are not offered to suggest that private actors will always make the right decisions. Indeed, there are serious reasons for concern that these private actors often share a single and potentially wrongheaded philosophy on corporate governance.[134] The point is that internal reform can proceed on a different track from external reform, and can be pressed by a different set of actors. In order for the stark choice hypothesis to be true, this divergent set of actors must become satisfied or exhausted at the same point. Given their divergent agendas, processes, and constituencies, there is little reason to believe that is the case.

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129. 17 C.F.R. § 240.19c-4 (1990).

130. See Bus. Roundtable v. Sec. & Exch. Comm'n, 905 F.2d 406, 407 (D.C. Cir. 1990).

131. Alexandra Scaggs, Investor Group to Exchanges: Stop Dual-Class Listings, Wall St. J. (Oct. 11, 2012), https://www.wsj.com/articles/SB10000872396390443749204578050431073959840 (on file with the *Columbia Law Review*); see also Gary Shorter, Cong. Rsch. Serv., IF11992, Dual Class Stock: Background and Policy Debate, (2021) (setting out the history of regulation of dual class shares); Stephen M. Bainbridge, The Short Life and Resurrection of SEC Rule 19c-4, 69 Wash. U. L. Q. 565, 625 (1991) (suggesting that control over the issue had shifted back to self-regulatory organizations like the exchanges and to the states).

132. Scott Hirst & Kobi Kastiel, Corporate Governance by Index Exclusion, 99 B.U. L. Rev. 1229, 1232 (2019); see also Chris Dieterich, Maureen Farrell & Sarah Krouse, Stock Indexes Push Back Against Dual-Class Listings, Wall St. J. (Aug. 2, 2017), https://www.wsj.com/articles/stock-indexes-push-back-against-dual-class-listings-1501612170 (on file with the *Columbia Law Review*).

133. See Dieterich et al., supra note 132.

134. See Dorothy S. Lund & Elizabeth Pollman, The Corporate Governance Machine, 121 Colum. L. Rev. 2563, 2575–78 (2021) (arguing that many important players have accepted and act on a "shareholder primacy" agenda).

B. *Reformer Expectations*

The stark choice hypothesis also depends upon the premise that advocates for stakeholder interests misapprehend some critical facts. If reformers correctly evaluate the relative efficacy of internal and external reforms and if they correctly evaluate the political feasibility of potential reforms, then they will not trade away a useful external reform for a useless internal reform.

1. *Reformer Pessimism About Internal Reforms.* — Reformers who are interested in restructuring the American economy plainly have not been mollified by the emergence of stakeholder governance. Until recently, the Business Roundtable, an association of the CEOs of major U.S. companies, took the position that the purpose of the corporation was to generate financial returns to shareholders.[135] As prominent institutional investors like BlackRock began to urge a reorientation of corporate America, the Business Roundtable revised its position, issuing a statement on the purpose of the corporation declaring that corporations shared a fundamental commitment to all of their stakeholders.[136]

After the Business Roundtable published its statement on the purpose of the corporation, conservative commentators reacted by making the easy prediction that political progressives would not be satisfied.[137] Progressives promptly proved them right. Senator Elizabeth Warren issued public letters to signatories of the Business Roundtable statement demanding that they endorse her Accountable Capitalism Act and outline concrete steps they were taking on behalf of stakeholders.[138] Senator Bernie Sanders's presidential campaign website similarly took note of the Business Roundtable's new position on the purpose of the corporation but responded, "Empty words are not enough," and promised an aggressive regulatory program.[139]

The *Wall Street Journal* Editorial Board summarized this reaction in memorable, if exaggerated, terms: "The lesson for the CEOs is that the new progressives won't be satisfied until they effectively own you. The

135. See Bus. Roundtable, supra note 21 (noting that the Business Roundtable's statements on corporate governance had endorsed shareholder primacy from 1997 to 2019).

136. Id.

137. See, e.g., Editorial Board, The 'Stakeholder' CEOs, Wall St. J. (Aug. 19, 2019), https://www.wsj.com/articles/the-stakeholder-ceos-11566248641 (on file with the *Columbia Law Review*) ("Yet these CEOs are fooling themselves if they think this new rhetoric will buy off Ms. Warren and the socialist left.").

138. See Letter from Elizabeth Warren, U.S. Sen., to Jeffrey Bezos, President, Amazon (Oct. 3, 2019), https://www.warren.senate.gov/imo/media/doc/2019-10-03%20Letters%20to%20CEOs.pdf [https://perma.cc/W33G-ZZJQ].

139. Corporate Accountability and Democracy, Bernie, https://berniesanders.com/issues/corporate-accountability-and-democracy/ [https://perma.cc/XPY2-M9JF] (last visited Oct. 13, 2022).

Roundtable statement succeeded mainly in convincing the left that it has business on the run. Ms. Warren is already measuring the length of the rope to hang them."[140]

Given this type of commentary, it is far from obvious that reformers systematically overestimate the impact of internal reforms and drop demands for external reforms in response.

Of course, even if committed reformers are not convinced, relatively disengaged members of the public might be. Political leaders who oppose external reform might cite internal changes as proof that external reform is not required—and voters who lack relevant information may believe them.[141] Political leaders who are hostile to regulatory reform may be happy to have the cover from businesses, even if the internal changes have no real effect.[142] But it is an enormous leap from this possibility to the idea that pivotal policymakers like the median senator or representative would approve an external reform but for an internal reform.

Internal rhetoric could also conceivably allow corporate leaders to change the subject. For example, conservative commentator Vivek Ramaswamy has asserted that Big Tech distracted liberal reformers from a conversation about monopoly power by agreeing to censor content; that Big Pharma distracted from a conversation about drug pricing by discussing subjects like racism and environmentalism; and that Coca-Cola distracted from a conversation about diabetes and obesity by discussing voting laws and racism.[143] These concerns are difficult to credit. Companies often restrict their commentary to areas of operational

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140. Editorial Board, Senator Warren Measures the Rope, Wall St. J. (Sept. 30, 2020), https://www.wsj.com/articles/senator-warren-measures-the-rope-11601507790 (on file with the *Columbia Law Review*). As discussed below, this reaction suggests the potential for dynamic interactions between reforms. See infra section II.C.

141. See Reich, supra note 34, at 40–50 (asserting that Congress's "public scoldings" of corporations are a "diversion from the work of creating rules that balance the interests of consumers and investors with [the] . . . interest of the public," which "allows politicians to maintain good relations with the same companies and industries . . . while showing . . . they're being 'tough' on . . . wrongdoers").

142. See id.

143. Varadarajan, supra note 1. Ramaswamy has since launched an investment fund that urges companies to abandon left-leaning positions on environmental, social, and governance matters in favor of an agenda that "maximiz[es] long-run value for the company's ultimate owners while disregarding social pressure." Letter from Vivek Ramaswamy, Exec. Chairman, Strive Asset Mgmt., to Michael K. Wirth, Chairman of the Bd. and Chief Exec. Officer, Chevron, Inc. 1 (Sept. 6, 2022), https://strive.com/strive-asset-management-letter-to-chevron/ [https://perma.cc/6NQD-ECVS]; see also Amrith Ramkumar, Anti-ESG Activist Investor Urges Chevron to Increase Oil Production, Wall St. J. (Sept. 6, 2022), https://www.wsj.com/articles/anti-esg-activist-investor-urges-chevron-to-increase-oil-production-11662494769 (on file with the *Columbia Law Review*). It is unclear how these claims interact. If left-leaning ESG positions actually help companies to defeat regulations that would destroy value, those positions are arguably value-maximizing for corporations.

concern.[144] The strategy also seems unlikely to succeed: For example, effective censorship by a media company would only call additional attention to its monopoly power. And Ramaswamy's argument seems to reflect a willful misreading of the political environment. Liberals appear to remain committed to issues including attacking monopoly power and addressing drug pricing, despite corporate rhetoric on unrelated issues.[145]

More fundamentally, there would be little reason for optimism about external reforms in general if these diversionary strategies are effective. If corporations and their political allies can readily dupe the public, it is hard to imagine meaningful external reforms ever being enacted: A business that is focused exclusively on maximizing financial returns to shareholders will use precisely the same tactic to defeat external reforms. In other words, to the extent it exists, this phenomenon is not caused by stakeholder governance; it would be a reason for pessimism about external reforms even in a world of pure shareholder primacy.

2. *Reformer Realism About External Processes.* — There is also no evidence that reformers systematically misunderstand the political constraints that they operate under. It is far from obvious that reformers like Senator Warren mistakenly believe that external reforms are not possible and settle for internal corporate reforms as a result. Instead, it is far more common to see would-be reformers criticized for being overly optimistic about the potential for new external rules.

And indeed, much of the demand for internal corporate change has been prompted by reasonable frustration at the processes and prospects for external regulation. As Professor Tim Wu has put it, "[O]ne reason there is so much mounting pressure for corporations to take action today

144. See, e.g., David Gelles, 'Our Menu Is Very Darwinian.' Leading McDonald's in 2021., N.Y. Times (July 2, 2021), https://www.nytimes.com/2021/07/02/business/chris-kempczinski-mcdonalds-corner-office.html (on file with the *Columbia Law Review*) ("Questioned about the company's silence on the issue of voting rights, [McDonald's CEO] Mr. [Chris] Kempczinksi explained it was not a core issue for the company.").

145. For example, Democratic President Joe Biden appointed several serious critics of corporate power to important posts in his administration, including Lina Khan and Tim Wu, see Ryan Tracy, Meet Tim Wu, the Man Behind Biden's Push to Promote Business Competition, Wall St. J. (July 9, 2021), https://www.wsj.com/articles/the-man-behindbidens-push-to-promote-business-competition-11625851555 (on file with the *Columbia Law Review*), and issued an executive order urging efforts to improve competition in the American economy, Exec. Order No. 14036, 86 Fed. Reg. 36,987 (July 9, 2021). And liberal Senator Bernie Sanders continued to urge changes to Medicare that would allow the government to negotiate drug prices down. See Kristina Peterson & Stephanie Armour, Sanders, Progressives Face Split With Centrists Over Plan to Cut Drug Prices in Medicare, Wall St. J. (July 7, 2021), https://www.wsj.com/articles/democrats-split-over-measures-to-cut-drug-prices-11625662801 (on file with the *Columbia Law Review*). A provision authorizing drug price negotiations was ultimately included in the Inflation Reduction Act of 2022. See Press Release, The White House, By the Numbers: The Inflation Reduction Act (Aug. 15, 2022), https://www.whitehouse.gov/briefing-room/statements-releases/2022/08/15/by-the-numbers-the-inflation-reduction-act/ [https://perma.cc/WGX3-GVDA].

is that government has failed to act in many areas that people care about, often by overwhelming margins."[146] This concern about governmental failure is well founded. Scholars in diverse fields like labor law and environmental law have complained about the "ossification" of regulatory schemes, as the government has failed to enact new measures in response to changing circumstances.[147]

Vaccinations for COVID-19 present a salient example. Despite the urgent threat to public health from unvaccinated individuals—and the fact that a substantial majority of American adults have chosen to get vaccinated—government officials have made only fitful progress in requiring the shots. As of this writing, a major part of the federal government's plan to increase vaccination rates is to encourage business leaders to impose mandates on their employees instead of imposing a mandate directly.[148] An attempt to *require* employers to impose mandates on employees through external regulation was defeated in litigation.[149] And the federal government and businesses are at least moving in the same direction. For more than a year, cruise lines and Florida Governor Ron DeSantis were locked in litigation over whether the cruise lines could require passengers to be vaccinated.[150] DeSantis has persisted in his position that

146. Wu, supra note 15.

147. See Cynthia L. Estlund, The Ossification of American Labor Law, 102 Colum. L. Rev. 1527, 1530 (2002) ("The basic statutory language, and many of the intermediate level principles and procedures through which the essentials of self-organization and collective bargaining are put into practice, have been nearly frozen, or ossified, for over fifty years."); Michael P. Vandenbergh, Private Environmental Governance, 99 Cornell L. Rev. 129, 131 (2013) [hereinafter Vandenbergh, Private Environmental Governance] (observing that "no major federal environmental statute has been enacted since the Clean Air Act Amendments of 1990," and that the "period of statutory inaction" exceeded "the period of statutory growth").

148. In one telling exchange, former White House Press Secretary Jen Psaki suggested that a vaccine mandate was "not the role of the federal government; that is the role that institutions, private-sector entities, and others may take." Press Release, The White House, Press Briefing by Press Secretary Jen Psaki (July 23, 2021), https://www.whitehouse.gov/briefing-room/press-briefings/2021/07/23/press-briefing-by-press-secretary-jen-psaki-july-23-2021/ [https://perma.cc/9T8P-CAU4].

149. OSHA issued an Emergency Temporary Standard requiring that employees of large employers either be vaccinated or wear masks and be tested regularly. COVID-19 Vaccination and Testing; Emergency Temporary Standard, 86 Fed. Reg. 61,402 (Nov. 5, 2021) (to be codified at 29 C.F.R. pts. 1910, 1915, 1917, 1918, 1926, 1928). This requirement was stayed by the Fifth Circuit. BST Holdings, L.L.C. v. Occupational Safety & Health Admin., 17 F.4th 604, 609 (5th Cir. 2021). The Sixth Circuit dissolved the stay. See In re MCP No. 165, 21 F.4th 357, 366 (6th Cir. 2021) (summarizing litigation and dissolving Fifth Circuit stay). But the Supreme Court ultimately stayed the rule, finding in an unsigned decision that parties challenging the rule were likely to prevail. Nat'l Fed'n of Indep. Bus. v. Occupational Safety & Health Admin., 142 S. Ct. 661, 662–63 (2022) (per curiam).

150. See Norwegian Cruise Line Holdings Ltd. v. State Surgeon Gen., 50 F.4th 1126, 1130 (11th Cir. 2022) (vacating the preliminary injunction of state law prohibiting plaintiff cruise line from requiring customers to provide proof of vaccination).

unvaccinated individuals should be able to enter confined cruise ships even though an overwhelming majority of Floridians disagree.[151] Businesses appear to be willing to give the public what it wants, even though political actors are paralyzed or actively unhelpful.

This dynamic—a blocked path to external reform, leading to demand for progress along a relatively open path to internal reform—can extend to the legislative arena. Managers have historically been a powerful interest group, and they often have good reasons to support or tolerate internal governance changes while resisting external regulation.[152] Both internal and external rules are likely to reduce corporate profits. But an internal rule will shift the corporation's balance of power away from the stock market so that more of the pain can be offloaded onto shareholders instead of being borne by managers themselves.

There also appears to be more bipartisan support for internal reform than for external rules. For example, conservatives have generally been opposed to external rules intended to address economic inequality or improve working conditions.[153] But prominent conservatives have expressed interest in solutions that are internal in nature, such as codetermination.[154] This interest can be understood as reflecting conservatives' general preference for private ordering, in which parties are empowered to "make tradeoffs tailored to their circumstances and preferences, rendering much bureaucratic oversight superfluous."[155] A similar bipartisan coalition supported the rise of benefit corporation legislation in a majority of states: The legislation allowed private parties to create corporations with purposes other than shareholder value maximization, and this facilitation of private ordering proved congenial to members of both political parties.[156] Given the need for a sizeable coalition

151. See Anthony Man, Poll Shows Vast Majority of Floridians Disagree on DeSantis Policy, Think It's OK to Require COVID-19 Vaccinations for Cruise Passengers, S. Fla. Sun-Sentinel (June 16, 2021), https://www.sun-sentinel.com/news/politics/fl-ne-florida-poll-cruise-ship-theme-park-school-vaccine-requirements-20210616-qaiozhbvurhrplkwh5fuvyeoqa-story.html (on file with the *Columbia Law Review*).

152. See Mark J. Roe, Strong Managers, Weak Owners: The Political Roots of American Corporate Finance 43 (1994) [hereinafter Roe, Strong Managers] (suggesting that managers successfully prevented the emergence of strong American financial institutions that could pressure managers by voting stock and enlarged their power through constituency statutes that weakened shareholder voice); cf. Roe & Shapira, supra note 1, at 269 (describing how unlikely coalitions between groups like employees and executives can form in mutual support of reforms that purport to stymie stock-market short-termism).

153. See, e.g., Conservatives Should Ensure Workers a Seat at the Table, Am. Compass (Sept. 6, 2020), https://americancompass.org/conservatives-should-ensure-workers-a-seat-at-the-table/ [https://perma.cc/VA7J-T3PQ] ("We prefer the private ordering of bargains between workers and management to overbearing dictates from Washington.").

154. See id.

155. Id.

156. Lund & Pollman, supra note 134, at 2616–18.

to overcome the hurdles to federal legislation, conservative opposition to external reform and openness to internal reform may make the difference between impossibility and possibility.

C. *Dynamic Interactions Between Reforms*

The stark choice hypothesis also neglects the potential for dynamic interaction between reforms. A more stakeholder-focused model for corporate decisionmaking can make external reforms more likely by reducing corporate opposition to external reform and causing some corporations to actively support external reform. Corporate attention to an issue can improve electoral dynamics by convincing voters of the need for regulation. And stakeholder-focused models of corporate decisionmaking can make external regulations more valuable while reducing their costs, increasing the likelihood of their adoption.

1. *Corporate Power Over the Political Process.* — Corporations wield extraordinary influence over the political process.[157] If their leaders are instructed to consider only shareholder interests, that influence will generally only be deployed to defeat external reforms. For precisely that reason, numerous commentators have urged that politically powerful corporations must be internally reformed so that they deploy their political power in a manner consistent with social welfare.[158]

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157. Critics of corporate political spending generally start from this premise. But it is also a basic premise of most supporters of corporate political spending. If corporate political spending did not influence political outcomes in a way that expanded corporate profits, it would be an inefficient waste, and tolerating it would be a violation of directors' and officers' fiduciary duties. Cf. Jonathan Macey, Opinion, Using 'Disclosure' to Silence Corporate America, Wall St. J. (Oct. 21, 2013), https://www.wsj.com/articles/using-8216disclosure8217-to-silence-corporate-americausing-8216disclosure8217-to-silence-corporate-america-1382388104 (on file with the *Columbia Law Review*) ("Boards of directors' fiduciary duties to maximize shareholder value often require that companies engage with the politicians who control the competitive and regulatory environment in which they operate.").

Professors Lucian A. Bebchuk, Robert J. Jackson, Jr., and their coauthors chart a potential third course when they suggest that corporations should have to provide additional disclosure of their political spending because of the risk that corporate political spending is unlikely to advance shareholders' interests. See, e.g., Lucian A. Bebchuk & Robert J. Jackson, Jr., Corporate Political Speech: Who Decides?, 124 Harv. L. Rev. 83, 90–93 (2010); Lucian A. Bebchuk & Robert J. Jackson, Jr., Shining Light on Corporate Political Spending, 101 Geo. L.J. 923, 941–45 (2013); Lucian A. Bebchuk, Robert J. Jackson, Jr., James D. Nelson & Roberto Tallarita, The Untenable Case for Keeping Investors in the Dark, 10 Harv. Bus. L. Rev. 1, 2–5 (2020) (responding to critics of proposed SEC disclosure rules). But in a sign of their influence over the political process, corporate lobbyists have repeatedly defeated such disclosure requirements in Congress. Id. at 5 & n.15.

158. See, e.g., Nikolas Bowie, Corporate Personhood v. Corporate Statehood, 132 Harv. L. Rev. 2009, 2014 (2019) (arguing that the norms applicable to democratic governments should also apply to corporations); Jens Dammann & Horst Eidenmüller, Corporate Law and the Democratic State, 2022 U. Ill. L. Rev. 963, 966 (positing that codetermination—that is, allowing employees to elect a specified number of directors—"can serve as a mechanism

Even softer internal changes can have an impact on the way that corporations engage with the political process. The signatories to the Business Roundtable's statement would find it somewhat more awkward to openly advocate for a shareholder-friendly program of deregulation. By raising expectations that they will behave morally, the corporations made it more costly for themselves to do otherwise.[159] ExxonMobil Corporation similarly found itself challenged as a result of a seemingly soft commitment to the Paris Agreement, a global accord focused on reducing carbon emissions. When the company was unable to explain how its lobbying efforts aligned with that commitment, the failure helped persuade major institutional investors to vote to replace Exxon directors.[160] As BlackRock explained, the "misalignment" between Exxon's public positions and lobbying activities created a reputational risk for the company.[161] Simply by publicly committing itself to stakeholder-friendly internal corporate governance, the firm changed its capacity to affect external regulation through lobbying.

Lobbying efforts are only one tool that corporations have for securing legal change. Apart from quietly influencing and supporting political friends, corporations can pick public fights with political adversaries. Internal corporate decisions to protest offensive laws by exiting hostile jurisdictions can affect the external regulatory process. For example, when North Carolina adopted new legislation targeting LGBTQ individuals, corporations pared back investment and spending in the state, costing it "approximately $200 million in lost business."[162] Republican Governor Pat McCrory's popularity plummeted, and he lost the next election despite a

to protect the democratic process by curbing excessive corporate power"); Brett H. McDonnell, Employee Primacy, or Economics Meets Civic Republicanism at Work, 13 Stan. J.L. Bus. & Fin. 334, 335 (2008) (arguing that employee primacy should guide corporate decisionmaking); Leo E. Strine, Jr. & Nicholas Walter, Conservative Collision Course?: The Tension Between Conservative Corporate Law Theory and *Citizens United*, 100 Cornell L. Rev. 335, 340 (2015) (noting how, under the extant corporate law regime, "stockholders are poorly positioned to monitor corporate managers even for their fidelity to a profit-maximization goal," much less their commitment to social welfare or free speech goals); Wu, supra note 15.

159. See, e.g., Kuo & Means, supra note 106, at 1307–09 (noting that corporations are increasingly expected to take political stances and may be penalized by certain stakeholders when they fail to do so).

160. See David A. Katz & Laura A. McIntosh, EESG Activism After ExxonMobil, Harv. L. Sch. Forum on Corp. Governance (July 23, 2021), https://corpgov.law.harvard.edu/2021/07/23/eesg-activism-after-exxonmobil/ [https://perma.cc/P32Q-79F5] (describing positions taken by BlackRock, Vanguard, and State Street). See infra section III.B.1 for a further discussion of the effort to replace Exxon directors.

161. See BlackRock, Vote Bulletin: ExxonMobil Corporation 7 (2021), https://www.blackrock.com/corporate/literature/press-release/blk-vote-bulletin-exxon-may-2021.pdf [https://perma.cc/CP7N-883U].

162. Kuo & Means, supra note 106, at 1324–25.

favorable national political environment.[163] Importantly, this mechanism does not require voters to actually agree with or be persuaded by corporate values. It simply requires that voters prioritize economic issues over cultural issues and that businesses have the power and inclination to force them to make that choice.

More aggressive measures are also possible. As Professor Elizabeth Pollman has noted, corporations can also pick fights with regulators, including by openly flouting their regulations.[164] Such "corporate disobedience" can change facts on the ground in a way that supports regulatory reforms by affecting consumer tastes;[165] can expose limits on regulators' power through litigation that clarifies legal restrictions;[166] and can force regulators to set new priorities by testing how much they are really willing to spend to defend and enforce an existing legal regime.[167] Through such tactics, companies like Uber have reshaped the regulation of entire industries. While intuitions about the normative implications of such actions can vary from case to case, it is clear that corporations can affect external regulatory processes if internal mechanisms cause them to do so.

There are at least four counterarguments to the claim that dynamic interactions mean that internal reforms make external reforms more likely. First, internal corporate governance changes may cause leading companies to clean up their act just enough to avoid the shocking headlines about corporate greed that can overcome legislative inertia and motivate reform.[168] But this argument depends on the idea that the internal rule will actually improve corporate behavior; it also depends on a belief that the political process will not permit action absent some shocking motivation. On those assumptions, it is hard to accept that reformers should avoid internal changes because better external changes are possible. Stakeholder governance could also raise expectations for

163. See id. at 1325; German Lopez, NC's Republican Governor Just Conceded His Election. He Can Probably Blame His Own Anti-LGBTQ Law., Vox (Dec. 5, 2016), https://www.vox.com/policy-and-politics/2016/12/5/13776408/mccrory-cooper-governor-north-carolina-election-lgbtq [https://perma.cc/8R3M-T455].

164. Elizabeth Pollman, Corporate Disobedience, 68 Duke L.J. 709, 712–14 (2019).

165. See id. at 712–13 (noting how Uber "launched operations in cities around the world—often in violation of existing laws" and how ride-hailing companies, in general, have "leverag[ed] consumer support to challenge restrictive taxi regulations and lobbies that had existed for decades").

166. See id. at 714–15.

167. See id. at 713–14 (observing the marijuana industry's growth against a backdrop of a "federal government [that] has taken a variety of positions, from stating that it would not prioritize enforcement of federal law against medical marijuana users and businesses to threatening a federal crackdown").

168. Cf. Reich, supra note 34, at 18–19 (noting the role that exposures of particular corporate abuses have played in encouraging external reforms).

corporate behavior and lead to greater outrage when companies fall short of the public's expectations.[169]

Second, internal changes might increase the clout of corporations by allowing them to claim that they are acting on behalf of stakeholders when they cozy up to political leaders.[170] That clout can then be deployed to defeat external reforms. But these moves are already available to corporations. Corporate leaders regularly lobby against external regulations by saying that they will destroy jobs, positioning themselves as acting on behalf of employees or potential employees instead of shareholders.[171] Financial institutions similarly urge that external regulations will reduce access to credit, positioning themselves as acting on behalf of would-be borrowers instead of shareholders.[172] Internal reforms would only increase the effectiveness of these lobbying tactics if corporations actually began to

169. Hajin Kim, Expecting Corporate Prosociality 6, 24–25 (Oct. 28, 2022) (unpublished manuscript), https://ssrn.com/abstract=4282358 [https://perma.cc/S83M-LBV4].

170. See Gatti & Ondersma, Stakeholder Approach Chimera, supra note 1, at 64–67. Similar mechanisms have been described in India. See Afra Afsharipour, Lessons From India's Struggles With Corporate Purpose, CLS Blue Sky Blog (Feb. 4, 2021), https://clsbluesky.law.columbia.edu/2021/02/04/lessons-from-indias-struggles-with-corporate-purpose/ [https://perma.cc/WF7V-74W5].

China may present a more complex example. Wealthy individuals and important businesses appear to be engaging in social spending in an effort to reduce government pressure. See, e.g., Li Yuan, What China Expects From Businesses: Total Surrender, N.Y. Times (July 19, 2021), https://www.nytimes.com/2021/07/19/technology/what-china-expects-from-businesses-total-surrender.html (on file with the *Columbia Law Review*) (last updated Oct. 8, 2021). But it is not clear how this response to government regulation maps onto an internal versus external divide. The relevant individuals and businesses appear to be demonstrating loyalty to the government and alignment with its policies. Though internal decisions are being taken in an effort to avoid the application of external force, it is not clear that the decisions have the effect of loosening external requirements.

171. See, e.g., Press Release, Neil Bradley, Exec. Vice President & Chief Pol'y Officer, U.S. Chamber of Com., U.S. Chamber Opposes Government Price Controls that Will Destroy Jobs and Threaten Access (Apr. 22, 2021), https://www.uschamber.com/press-release/us-chamber-opposes-government-pricecontrols-will-destroy-jobs-and-threaten-access [https://perma.cc/KE4B-P749] (asserting that the Lower Drug Costs Now Act of 2019 would "destroy American jobs").

172. Stacy Cowley, Payday Lending Faces Tough New Restrictions by Consumer Agency, N.Y. Times (Oct. 5, 2017) https://www.nytimes.com/2017/10/05/business/payday-loans-cfpb.html (on file with the *Columbia Law Review*) (noting that lenders oppose restrictions on pay-day loans on the grounds that "the loans provide financial lifelines to those in desperate need of cash" and that restrictions "will create credit deserts for many Americans who do not have access to traditional banking" (internal quotation marks omitted) (second quotation quoting Edward D'Alessio, Exec. Dir., Fin. Serv. Ctrs. Am.)); see also Ctr. For Cap. Mkts. Competitiveness, U.S. Chamber of Com., Financing Growth: The Impact of Financial Regulation 3 (2016), https://www.centerforcapitalmarkets.com/wp-content/uploads/2018/03/Center-for-Capital-Markets-Competitiveness-Financing-Growth-The-Impact-of-Financial-Regulation-Report.pdf [https://perma.cc/UX6R-RMPX] (asserting that Dodd–Frank is making it more difficult for "companies of all sizes . . . to access the financial services they need").

advocate on behalf of their stakeholders, or if political actors became too credulous about the impact of internal changes. The former possibility would not be a strong argument against internal reform, and the latter possibility seems inconsistent with recent experience.[173]

Third, competitive dynamics can play an important role. Internal corporate rules are often made by entities with limited authority. For example, state governments are constrained by the internal affairs doctrine, which limits their ability to regulate the corporate governance machinery of corporations chartered in other states.[174] This limitation permits states to compete with each other to provide the corporate governance doctrines that will be most appealing to the managers and shareholders who decide where a company will be chartered.[175] As a result, an internal rule that goes too far in protecting stakeholders will be evaded by corporations that can simply reincorporate elsewhere. Similarly, institutional investors and the stock exchanges have enormous capacity to impose policies on public companies, but a company can avoid their power by going or remaining private.

But external rules can be evaded too, as companies can shift operations out of a state or out of the country. Internal rules can also be used to project power—when California imposes internal rules on a California company, it can impact the way that the company treats its employees in Nevada; an external rule would not have that effect. And again, there is a dynamic interaction between external and internal rules.[176] External rules can help limit the impact of competition regarding internal rules—a higher federal minimum wage would limit the competitive impact of greater worker power within corporate governance because firms would not be able to gain as much of a competitive advantage by squeezing workers.[177] And internal rules can help limit the impact of competition regarding external rules—a corporation with genuinely empowered workers is less likely to shift jobs to a state where workers face lower wages or safety protections. As a result, there is little reason to believe that competition among jurisdictions will systematically undermine a healthy dynamic between internal and external rules.

173. See supra section II.B.

174. See, e.g., Restatement (Second) Conflict of L. § 302 & cmt. a (Am. L. Inst. 1971).

175. Cf. Vincent S.J. Buccola, Opportunism and Internal Affairs, 93 Tul. L. Rev. 339, 343–46 (2018) (describing how the internal affairs doctrine prevents shareholders from moving to a jurisdiction with more favorable laws after their investment has been priced and made).

176. See 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. 1325, 1330 (2022).

177. See id. at 1390 (discussing how "[t]he natural forces of competition will generate pressures for companies to shortchange workers to get an advantage").

Fourth, corporations might offer up soft and temporary internal changes strategically to dissipate the force of any drive toward external reform.[178] But this mechanism would only work if reformers and the public systematically overestimate the impact of internal changes. As discussed, there are good reasons to doubt that is the case.[179]

2. *Corporate Influence on the Voting Public.* — Even apart from its influence on the political process, corporate behavior can influence the attitudes of ordinary voters. The issue is an object of current empirical inquiry, and conclusions must be framed carefully and tentatively.[180] But corporate action could help voters accept the need for and feasibility of reform.

Some voters may not believe that a problem exists or that it can be addressed at a realistic cost. To the extent those voters trust business leaders on the issues, corporate action can help persuade them.[181] A voter may not believe the Environmental Protection Agency's pronouncements on the danger of pollution or the feasibility of control mechanisms, out of a sense that the agency is corrupt, disconnected from the practical world of business, or indifferent to effects on employment. For such a voter, a statement by the CEO of Walmart on the dangers of pollution and feasibility of control may carry more weight.

Other voters may not want to believe that a problem exists because they are fundamentally opposed to a governmental solution. If businesses propose a private solution, these voters may be more willing to accept that there is a problem.[182] This type of motivated reasoning can be powerful, and it is understandable: A voter might believe that the threat from a government intervention would far exceed any threat from the underlying problem and simply decline to waste cognitive or emotional resources fretting about the problem. When told that businesses are intervening, they are freed to accept the reality of the issue.

178. See Reich, supra note 34, at 34–35 (providing examples of major companies carrying out slight changes to corporate policy in an attempt to forestall more sweeping external reform).

179. See supra section II.B.

180. See, e.g., David A. Dana & Janice Nadler, Regulation, Public Attitudes, and Private Governance, 16 J. Empirical Legal Stud. 69, 80–82 (2019) (presenting two empirical studies suggesting that corporate action on a problem can cause conservatives to support regulation); Neil Malhotra, Benoit Monin & Michael Tomz, Does Private Regulation Preempt Public Regulation?, 113 Am. Pol. Sci. Rev. 19, 21 (2018) (describing an experiment showing that broad voluntary adoption of a relatively weak environmental program persuaded relevant groups not to press for more draconian regulation); Ash Gillis, Michael Vandenbergh, Kaitlin Raimi, Alex Maki & Ken Wallston, Convincing Conservatives: Private Sector Action Can Bolster Support for Climate Change Mitigation in the United States, 73 Energy Rsch. & Soc. Sci., Mar. 2021, at 1, 6 (finding that business action on climate change persuaded conservatives that the problem was real but tended to reduce concern over the issue).

181. See Dana & Nadler, supra note 180, at 72.

182. See Gillis et al., supra note 180, at 2.

Translating these effects into support for external regulation can be complicated and can depend on the specific issue. Even if voters are persuaded that a problem is real and could be addressed at acceptable cost, they may come to believe that the problem is already being dealt with by businesses and that further action by the government is inadvisable.[183] But the effect is not assured, particularly for low-salience issues.[184] And there may be less danger of dampened enthusiasm for external reforms if only some businesses take action, as a newly mobilized public may demand that the laggards be forced to improve.[185] In any event, convincing a broad swath of the public of the reality of a problem is not a small feat—indeed, it is often outside the reach of public authorities.

3. *Corporate Influence on Costs and Benefits of External Reforms.* — Corporate decisions can also affect the substantive impact of potential regulation, affecting the likelihood that the regulation is adopted. When a firm takes steps to help stakeholders, it changes facts on the ground in a way that affects the potential for future external regulation.[186] For example, suppose that a company invests in retrofitting a facility with a pollution-control technology that brings its emissions significantly below existing legal standards. A regulator weighing the costs and benefits of imposing a more stringent standard will be more likely to take action because the costs would have already been incurred and the feasibility of compliance would have been proven.[187] The firm itself would also have an economic incentive to encourage regulators to take action because it would force competitors to make similar costly investments.[188]

Indeed, effects can operate in a more fundamental way than simple cost–benefit analysis. As Professors Jonathan S. Masur and Eric A. Posner have documented, administrative agencies often survey practices of companies within an industry and adopt a rule somewhere in the middle of the

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183. Malhotra et al., supra note 180, at 20.

184. Dana & Nadler, supra note 180, at 76 (finding that business efforts on cage-free eggs and the use of antibiotics in the food supply increased conservative support for regulation).

185. See Malhotra et al., supra note 180, at 34–35 (finding that when only a few firms participate in a voluntary program, it does not affect support for regulation).

186. See id. at 34–35.

187. Cf. Sarah E. Light & Eric W. Orts, Parallels in Public and Private Environmental Governance, 5 Mich. J. Env. & Admin. L. 1, 57–58 (2015) (noting that "[a]lthough private environmental governance has great potential to be effective, more empirical research is needed" to assess the likelihood of "[p]rivate action . . . spur[ring] eventual public regulation").

188. Cf. Aneil Kovvali, Essential Businesses and Shareholder Value, 2021 U. Chi. Legal Forum 191, 195; Saul Levmore, Interest Groups and the Problem with Incrementalism, 158 U. Pa. L. Rev. 815, 838 (2010) (noting that a firm that has been subjected to regulation may lobby to increase the regulation of its competitors "either to raise their marginal costs or to drive some out of business").

distribution.[189] If managers adopt more stringent practices, agencies that take a norming approach may adopt more stringent regulations in response.

More subtly, internal reforms can work synergistically with external reforms. This effect has long been understood in the opposite direction, as robust external regulation can make internal reforms more plausible: Corporate managers can be made less accountable to shareholders if they will be more accountable to empowered stakeholders and vigorous government regulators.[190] An internal reform can make external interventions more valuable and thus more likely. For example, the federal government should be more willing to engage in a macroeconomic intervention—such as lowering the cost of borrowing—if firms will use that stimulus to create jobs instead of enriching shareholders.[191]

Proposals to increase worker power in corporations can also draw on these effects. An internal corporate governance reform like codetermination—which would place worker representatives on corporate boards of directors—may not succeed without empowered unions and better corporate disclosures on worker issues.[192] But external reforms to empower unions or force companies to disclose information on worker issues may not have the maximum effect if workers are not able to use that power and information to press for change within the corporation.[193] An

189. Jonathan S. Masur & Eric A. Posner, Norming in Administrative Law, 68 Duke L.J. 1383, 1385 (2019).

190. Strine et al., supra note 176, at 1330 (urging that internal measures to increase worker voice at corporations will be more successful if supported by external regulations that facilitate organization and set a robust baseline); see also Bratton & Wachter, supra note 17, at 104–05 (noting that corporate directors can be focused on the public interest that entails being cooperative with a vigorous government). Internal rule changes could also affect the content of external rules for the better by altering corporate lobbying and reducing rent-seeking. See supra section II.C.1.

191. Cf. Aneil Kovvali, Countercyclical Corporate Governance, 101 N.C. L. Rev. 141, 158 (2022) (arguing that changing the way that corporations react can make macroeconomic stimulus more effective); Erica Werner, Seung Min Kim, Rachel Bade & Jeff Stein, Senate Falls Far Short of Votes Needed to Advance Coronavirus Bill, as Clash Between Republicans and Democrats Intensifies, Wash. Post (Mar. 22, 2020), https://www.washingtonpost.com/us-policy/2020/03/22/vast-coronavirus-stimulus-bill-limbo-crunch-times-arrives-capitol-hill/ (on file with the *Columbia Law Review*) (observing that the economic relief package failed to pass in part due to concerns that companies would channel funds to shareholders and managers).

192. Cf. Strine et al., supra note 176, at 1329 n.9 (describing how successful internal corporate governance reform requires "that the corporation focus on stakeholders, particularly workers, and stronger external laws protecting union rights and other important rights vital to workers").

193. See id. at 1328–29 ("[E]xternal reforms . . . are insufficient to restore fair gainsharing with American workers. Thus, advocates for workers and other stakeholders are demanding internal reforms via changes to corporate and securities laws that would require corporations to give more weight to their interests.").

internal reform can create an environment in which external reforms are more effective, thus increasing the likelihood of external reforms.[194]

III. Applications

This Part focuses on concrete applications. Section III.A examines race and social justice. Section III.B considers climate change. Section III.C considers efforts to constrain internal corporate reform and ensure a government monopoly on policymaking.

A. *Race and Social Justice*

Current and past racial discrimination have had a powerful impact on the structure of the American economy. Internal corporate governance reform could play a meaningful role in arresting or reversing these effects, at least relative to likely external reforms.

1. *Capacity to Adopt Multiple Reforms.* — Federal and state regulators have demonstrated limited willingness and capacity to advance external reforms addressing racial justice issues.[195] As of this writing, much of the national political conversation regarding race is consumed with a debate about the teaching of "critical race theory" that has led numerous state governments to enact prohibitions on teaching a broad range of

194. See id.

195. Direct efforts to address past discrimination have been rare. For example, a congressional mandate to use $4 billion to address past lending discrimination against Black farmers was heralded as "unprecedented" when it was enacted. See, e.g., Emma Hurt, The USDA Is Set to Give Black Farmers Debt Relief. They've Heard that One Before, NPR (June 4, 2021), https://www.npr.org/2021/06/04/1003313657/the-usda-is-set-to-give-black-farmers-debt-relief-theyve-heard-that-one-before [https://perma.cc/44TK-WEY5] ("Farmers of color are set to get some unprecedented debt relief starting this month from the U.S. Department of Agriculture."); Laura Reiley, Relief Bill Is Most Significant Legislation for Black Farmers Since Civil Rights Act, Experts Say, Wash. Post (Mar. 8, 2021), https://www.washingtonpost.com/business/2021/03/08/reparations-black-farmers-stimulus/ (on file with the *Columbia Law Review*) (describing the program as "benefiting Black farmers in a way that some experts say no legislation has since the Civil Rights Act of 1964"). The program was halted by lawsuits brought by white farmers. See Holman v. Vilsack, No. 21-1085-STA-jay, 2021 WL 2877915, at *5 (W.D. Tenn. July 8, 2021) (describing suits). But it was ultimately reconfigured by the Inflation Reduction Act of 2022. See Alan Rappeport, Climate and Tax Bill Rewrites Embattled Black Farmer Relief Program, N.Y. Times (Aug. 12, 2022), https://www.nytimes.com/2022/08/12/business/economy/inflation-reduction-act-black-farmers.html (on file with the *Columbia Law Review*) ("The program was frozen as lawsuits worked their way through the courts."). As of this writing, many potential beneficiaries of the program remain skeptical that they will ever see a recovery. See Kristina Peterson, Black Farmers Skeptical About Loan Aid After Discrimination, Wall St. J. (Sept. 25, 2022), https://www.wsj.com/articles/black-farmers-skeptical-about-aid-after-biased-lending-11664107382 (on file with the *Columbia Law Review*).

perspectives on the role of race in American history.[196] Recent years have also seen a shocking rise in racist sentiments in some quarters.[197] Given the need for a broad consensus to overcome legislative inertia, these attitudes are likely enough to prevent meaningful external reform.

There are also doctrinal hurdles to external reform: The modern judiciary's interpretation of the Fourteenth Amendment would seriously complicate many conscious governmental efforts to address racial inequity, and indeed, it has already complicated state government efforts to improve corporate outcomes.[198] Because of this doctrinal difficulty, Congress's rare efforts to address the legacy of racism have become mired in litigation.[199] It would thus be difficult to survey the current environment

196. The quotation marks are used advisedly, as the conversation does not appear to focus on the actual academic critical race theory. A full discussion of this phenomenon would be outside the scope of this Article. For coverage of the origins of the conversation, see Benjamin Wallace-Wells, How a Conservative Activist Invented the Conflict Over Critical Race Theory, New Yorker (June 18, 2021), https://www.newyorker.com/news/annals-of-inquiry/how-a-conservative-activist-invented-the-conflict-over-critical-race-theory [https://perma.cc/4KSD-SEVD]. For examples of state prohibitions on teaching adopted in response, see Cathryn Stout & Thomas Wilburn, CRT Map: Efforts to Restrict Teaching About Racism and Bias Have Multiplied Across the U.S., Chalkbeat (Feb. 1, 2022), https://www.chalkbeat.org/22525983/map-critical-race-theory-legislation-teaching-racism [https://perma.cc/R3N3-2RUB] (collecting bills and other measures).

197. See, e.g., German Lopez, Donald Trump's Long History of Racism, From the 1970s to 2020, Vox (Aug. 13, 2020), https://www.vox.com/2016/7/25/12270880/donald-trump-racist-racism-history [https://perma.cc/YD5H-8FWJ]; Dan Mangan, Hate Crimes Against Asian and Black People Rise Sharply in the U.S., FBI Says, CNBC (Aug. 30, 2021), https://www.cnbc.com/2021/08/30/fbi-says-hate-crimes-against-asian-and-black-people-rise-in-the-us.html [https://perma.cc/Z2ZZ-FX7J]; Steve Peoples, Republican Senate Candidates Promote 'Replacement' Theory, PBS (May 17, 2022), https://www.pbs.org/newshour/politics/republican-senate-candidates-promote-replacement-theory [https://perma.cc/FWH2-ANUY] ("Several mainstream Republican Senate candidates are drawing on the 'great replacement' conspiracy theory once confined to the far-right fringes of U.S. politics to court voters this campaign season, promoting the baseless notion that there is a plot to diminish the influence of white people in America."); Marianna Sotomayor, Stefanik Echoed Racist Theory Allegedly Espoused by Buffalo Suspect, Wash. Post (May 16, 2022), https://www.washingtonpost.com/politics/2022/05/15/stefanik-buffalo-replacement/ (on file with the *Columbia Law Review*). Apart from the rise of straightforwardly racist beliefs, there has also been a collapse in the consensus that racism is a current problem that should be addressed by policy. See, e.g., Nw. Austin Mun. Util. Dist. No. One v. Holder, 557 U.S. 193, 202 (2009) ("Things have changed in the South."); Philip Bump, More Than Half of Republicans Think Minorities Are Favored Over Whites in the United States, Wash. Post (June 29, 2021), https://www.washingtonpost.com/politics/2021/06/29/more-than-half-republicans-think-minorities-are-favored-over-whites-united-states/ (on file with the *Columbia Law Review*).

198. See Chris Brummer & Leo E. Strine, Jr., Duty and Diversity, 75 Vand. L. Rev. 1, 60–65 (2022) (discussing constitutional challenges to state statutes requiring diversity on corporate boards); cf. Meland v. Weber, 2 F.4th 838, 849 (9th Cir. 2021) (permitting suit by a shareholder challenging a state mandate requiring gender diversity on corporate boards).

199. See, e.g., Wynn v. Vilsack, 545 F. Supp. 3d 1271, 1295 (M.D. Fla. 2021) (granting preliminary injunction preventing the Department of Agriculture from implementing a

and find grounds for great optimism about the prospects for meaningful external reform. The actors who could initiate an external reform are either uninterested or are operating in an environment that makes action difficult.

The conversation on the corporate front has been quite different. There has been some governmental action. California adopted a statute analogous to the Women on Boards statute requiring each covered corporation to include some minimum number of directors from underrepresented communities on its board.[200]

But the real action has been driven by purely internal processes. Shareholders have had strong reasons to use their power within corporations to push for better outcomes. First, there is a convergence of interests between shareholders and underrepresented minority groups in terms of encouraging real voice within the corporate power structure: Without such an internal voice, corporations will not be able to manage social risks and may become out of step with the broader society in ways that are dangerous to their bottom line.[201]

As just one telling example,[202] the pizza company Papa John's suffered a substantial stock price decline and considerable volatility as a result of statements by its founder, John Schnatter. The stock lost almost a third of its value after Schnatter commented on the National Football League's handling of player protests against racism and police brutality; the effect of those comments was exacerbated by reports that he had used a racial slur on a company call.[203] A lack of competence and sensitivity on racial

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congressionally authorized program for debt relief for minority farmers); supra note 195 and accompanying text.

200. Cal. Corp. Code § 301.4 (2022), invalidated by Crest v. Padilla, No. 20STCV37513, 2022 WL 1073294 (Cal. Super. Ct. Apr. 1, 2022). An appeal was filed on July 20, 2022. See Defendant's Notice of Appeal, Crest v. Padilla, No. B321726 (BL) (Cal. Ct. App. filed July 20, 2022).

201. See Stavros Gadinis & Amelia Miazad, Corporate Law and Social Risk, 73 Vand. L. Rev. 1401, 1410 (2020). The moment may provide a particularly stark illustration of Professor Derrick A. Bell, Jr.'s interest-convergence thesis. See, e.g., Derrick A. Bell, Jr., *Brown v. Board of Education* and the Interest-Convergence Dilemma, 93 Harv. L. Rev. 518, 523 (1980); Steven A. Ramirez, Games CEOs Play and Interest Convergence Theory: Why Diversity Lags in America's Boardrooms and What to Do About It, 61 Wash. & Lee L. Rev. 1583, 1585 (2004) (suggesting that a coalition in favor of board diversity is possible).

202. Adidas's recent struggles with Ye, formerly known as Kanye West, provide another example. The company's relationship with Ye had been responsible for more than 10% of its profits; by the time the company severed its relationship with Ye over his antisemitic remarks, the company's stock price declined by over 20%. Melissa Eddy, Vanessa Friedman & Michael J. de la Merced, Adidas Ends Partnership With Kanye West at a Considerable Cost, N.Y. Times (Oct. 25, 2022), https://www.nytimes.com/2022/10/25/business/adidas-kanye-west.html (on file with the *Columbia Law Review*).

203. Barzuza et al., supra note 119, at 1298–99; Brummer & Strine, supra note 198, at 45 ("Papa John's, a once-thriving company, suffered massive business harm after its founder was publicly accused of making racist comments."); Tiffany Hsu, Papa John's Founder, John Schnatter, to Leave Board After Nasty Leadership Fight, N.Y. Times (Mar. 5, 2019),

issues did not simply create a moral problem for the company—it created a financial problem for shareholders, which they would have an incentive to solve using the ordinary machinery of corporate governance.

Second, racial discrimination within firms can also sometimes be understood as a form of agency problem, in which directors and officers shortchange shareholders by using discrimination against qualified candidates to gratify themselves or to exclude competitors for their positions. Indeed, the basic premise of disclosure as a strategy for addressing racial issues assumes that shareholders have an interest in curing discrimination at the companies that they own.[204] This convergence of interests likely does not extend to external measures, such as redistributive taxation and spending programs.

Third, there is a body of empirical literature suggesting that diversity improves decisionmaking by eliminating groupthink and enhancing deliberations.[205] These findings are contested.[206] But to the extent the findings are accepted, they would suggest that shareholders benefit from having diverse directors and corporate executives. Again, this convergence of interests is likely to be limited to internal corporate reforms.

Fourth, there are reasons for optimism in social trends among the investor class. It remains the case that shareholders are disproportionately white.[207] But the rising generation of millennial investors is more diverse

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https://www.nytimes.com/2019/03/05/business/papa-johns-john-schnatter.html (on file with the *Columbia Law Review*).

204. See Jessie K. Liu, Susan Saltzstein, Lauren Aguiar & Tansy Woan, Skadden Offers a Scorecard on Diversity in the Corporate Boardroom, CLS Blue Sky Blog (July 14, 2021), https://clsbluesky.law.columbia.edu/2021/07/14/skadden-offers-a-scorecard-on-diversity-in-the-corporate-boardroom/ [https://perma.cc/AAE8-CZ95] (collecting state statutes and showing that disclosure is a common strategy); Courtney Murray & Eric Talley, Racial Diversity and Corporate Governance: Assessing California's New Board Diversity Mandate, CLS Blue Sky Blog (Oct. 28, 2020), https://clsbluesky.law.columbia.edu/2020/10/28/racial-diversity-and-corporate-governance-assessing-californias-new-board-diversity-mandate/ [https://perma.cc/G3NV-TMMZ] (describing disclosure mandates in Illinois and Canada); Nasdaq, Proposed Listing Requirements, supra note 118 (announcing proposed disclosure framework for listed companies).

205. See, e.g., Brummer & Strine, supra note 198, at 33 (surveying the literature and concluding that there is an adequate basis for business judgment that diversity creates shareholder value); Ramirez, supra note 201, at 1587 ("Diversity in the boardroom enhances corporate profitability according to the consensus of scholars of business management, finance, and economics.").

206. See, e.g., Jill Fisch & Steven Davidoff Solomon, *Centros*, California's 'Women on Boards' Statute and the Scope of Regulatory Competition, 20 Eur. Bus. Org. L. Rev. 493, 507 (2019) ("[T]he results of empirical studies evaluating the relationship between female board representation and corporate economic performance have been 'largely inconclusive.'" (quoting Lissa L. Broome, John M. Conley & Kimberly D. Krawiec, Dangerous Categories: Narratives of Corporate Board Diversity, 89 N.C. L. Rev. 759, 765 (2011))).

207. This disproportianately has implications for the racial impact of shareholder primacy, which asks corporations to prioritize the interests of disproportionately white

than any previous American generation, and it holds more progressive views than prior generations.[208] As institutional investors compete for millennial dollars, they will have good reason to deploy engagement and voting power to advance a policy agenda consistent with millennial preferences.[209] Companies themselves are likely to be receptive to such approaches, as they vie with each other to win over millennial customers and recruit millennial employees.

Recent state efforts to restrict voting rights offer a potential test case for these forces. After the 2020 presidential election, various state governments sought to impose new limits on voting.[210] Corporations responding to shareholder, employee, and customer pressure have attacked these measures as oppressive.[211] While the effectiveness of these corporate steps can be debated,[212] it would be difficult to claim that they interfered with the passage of more effective federal laws.[213] It is hard to imagine meaningful voting rights bills passing in the current Congress. And the current Supreme Court has demonstrated serious hostility to

shareholders over the interests of disproportionately Black and Hispanic workers. See, e.g., Lenore Palladino, The Contribution of Shareholder Primacy to the Racial Wealth Gap 2 (Roosevelt Inst. Working Paper No. 202001, 2020), https://rooseveltinstitute.org/wp-content/uploads/2020/07/RI_TheContributionofShareholderPrimacy_Working-Paper_202001.pdf [https://perma.cc/86RF-SP5U].

208. See, e.g., Morgan Stanley Inst. for Sustainable Investing, Sustainable Signals: New Data From the Individual Investor 2 (2017), https://www.morganstanley.com/content/dam/msdotcom/ideas/sustainable-signals/pdf/Sustainable_Signals_Whitepaper.pdf [https://perma.cc/N86D-QHVW] ("Substantial majorities of Millennial investors believe that their own investment decisions can influence climate change (75%) and alleviate poverty (84%).").

209. See Barzuza et al., supra note 119, at 1301 ("[Funds] believe at least one way to reach millennials is through socially responsible investment, and that the time to do so is now, explaining the funds' current activism.").

210. Amy Gardner, Kate Rabinowitz & Harry Stevens, How GOP-Backed Voting Measures Could Create Hurdles for Tens of Millions of Voters, Wash. Post (Mar. 11, 2021), https://www.washingtonpost.com/politics/interactive/2021/voting-restrictions-republicans-states/ (on file with the *Columbia Law Review*).

211. See, e.g., David Gelles, Delta and Coca-Cola Reverse Course on Georgia Voting Law, Stating 'Crystal Clear' Opposition, N.Y. Times (Mar. 31, 2021), https://www.nytimes.com/2021/03/31/business/delta-coca-cola-georgia-voting-law.html (on file with the *Columbia Law Review*); David Gelles, Inside Corporate America's Frantic Response to the Georgia Voting Law, N.Y. Times (Apr. 5, 2021), https://www.nytimes.com/2021/04/05/business/voting-rights-ceos.html (on file with the *Columbia Law Review*) [hereinafter Gelles, Inside Corporate America's Frantic Response] (describing how Georgia-based corporations coalesced in their opposition to restrictive voting rights legislation).

212. See infra section III.A.3.

213. See, e.g., Nicholas Fandos, Republicans Block Voting Rights Bill, Dealing Blow to Biden and Democrats, N.Y. Times (June 22, 2021), https://www.nytimes.com/2021/06/22/us/politics/filibuster-voting-rights.html (on file with the *Columbia Law Review*) (noting that "Republicans never seriously considered the [voting rights] legislation").

federal voting rights legislation.[214] Internal forces driving corporate change did not interfere with external reforms; they have simply continued to operate on a parallel track at a time when external reforms were unlikely to proceed.

2. *Reformer Expectations.* — There is also little reason to believe that reformers are systematically overestimating the value of internal advocacy or underestimating the prospects of external reform. To begin, internal corporate changes can have a real impact. No one corporation can end racial inequality in America, but individual decisions by individual corporations can create actual benefits. Every hiring or governance decision tainted by racism could be improved, and even if no other corporation took comparable action, there would be a benefit for the people who would have been harmed.[215]

Some companies also have an outsized capacity to affect outcomes by shifting the national culture and conversation. When Nike released an advertising campaign embracing Colin Kaepernick, the former professional quarterback who led a protest movement against police brutality and was driven out of the National Football League as a result, the unveiling video was viewed over 80 million times on Twitter, Instagram, and YouTube within the first month of its release.[216] Nike enjoyed substantial benefits from the campaign, obtaining record engagement and hitting a new all-time high on its share price.[217] When player protests restarted, the NFL adopted a far more conciliatory attitude.[218]

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214. For a recent example, see Brnovich v. Democratic Nat'l Comm., 141 S. Ct. 2321 (2021) (adopting a narrow interpretation of the Voting Rights Act). For a broader critical perspective, see also Michael Klarman, Foreword: The Degradation of American Democracy—and the Court, 134 Harv. L. Rev. 1, 195 (2020) ("In no field has the Court's conservative majority done more damage to American democracy than in campaign finance.").

215. These marginal decisions can also be made quickly and in relative secrecy, decreasing the potential for racial backlash. See Deborah C. Malamud, Affirmative Action, Diversity, and the Black Middle Class, 68 U. Colo. L. Rev. 939, 944 (1997) ("Private businesses are private, and so long as the [Equal Employment Opportunity Commission] was on their side, they could work out their [affirmative action] programs in the seclusion of their own headquarters or at the negotiating table with their own unions.").

216. See Julie Creswell, Kevin Draper & Sapna Maheshwari, Nike Nearly Dropped Colin Kaepernick Before Embracing Him, N.Y. Times (Sept. 26, 2018), https://www.nytimes.com/2018/09/26/sports/nike-colin-kaepernick.html (on file with the *Columbia Law Review*).

217. Id.

218. See Ken Belson, N.F.L. Kicks Off Season With Nods to Unrest and Focus on Anthem, N.Y. Times (Sept. 13, 2020), https://www.nytimes.com/2020/09/13/sports/football/nfl-protests.html (on file with the *Columbia Law Review*) (last updated Sept. 5, 2021) (describing NFL-sanctioned demonstrations at football games, including helmet decals, field painting, and warm-up shirts that featured social justice messages).

Of course, the fact that the internal path to reform seems more promising than the external path to reform does not make it a perfect solution. There are meaningful limits on the ability of private law and private entities to undo racial inequity. Legal structures and innovations that help to grow wealth will tend to exacerbate inequality.[219] But there is little indication that reformers are unaware of these points or that they have traded away a feasible external reform because they have misunderstood.

3. *Dynamic Interactions Between Reforms.* — When corporations are mobilized to act on racial issues by internal forces, they can have an effect on external regulation. For example, Delta Airlines claimed to have had this type of impact on Georgia's 2021 law restricting voting.

The company's public approach was initially cautious. In a relatively mild and equivocal statement following the bill's passage, Delta asserted:

> Over the past several weeks, Delta engaged extensively with state elected officials in both parties to express our strong view that Georgia must have a fair and secure election process, with broad voter participation and equal access to the polls. The legislation signed this week improved considerably during the legislative process . . . . Nonetheless, we understand concerns remain over other provisions in the legislation, and there continues to be work ahead in this effort.[220]

But after the initial statement drew criticism, Delta's CEO Ed Bastian issued a less equivocal statement that insisted that the company had successfully lobbied against some voter suppression measures in the bill:

> Last week, the Georgia legislature passed a sweeping voting reform act that could make it harder for many Georgians, particularly those in our Black and Brown communities, to exercise their right to vote.

219. Professor Mehrsa Baradaran starkly illustrates these points. See Mehrsa Baradaran, The Color of Money: Black Banks and the Racial Wealth Gap 4 (2017). Baradaran writes:

> Small community banking has always held a special appeal when applied to poor and marginalized pockets of the economy. The promise is that a beleaguered community, having been left out of the dominant banking industry, could pool its resources and collectively lift itself out of poverty.
> . . . .
> Despite consistent bipartisan support and a few publicized success stories, there was never any evidence that the design would work. The very circumstances that created the need for these banks—discrimination and segregation—permanently limited their effectiveness and would ultimately cause their demise.

Id. As Baradaran describes, the movement to support Black-owned banks lacked the capacity to break down inequality because the Black community had been denied wealth and lacked access to high-quality investment opportunities. Id. at 4–5. Without a government effort to address those broader problems through subsidies and regulations, private institutions could not succeed. Id.

220. Delta Statement on SB202, Delta News Hub (Mar. 26, 2021), https://news.delta.com/delta-statement-sb202 [https://perma.cc/PU96-GB3K].

> Since the bill's inception, Delta joined other major Atlanta corporations to work closely with elected officials from both parties, to try and remove some of the most egregious measures from the bill. *We had some success in eliminating the most suppressive tactics that some had proposed.*
>
> However, I need to make it crystal clear that the final bill is unacceptable and does not match Delta's values.
>
> . . . .
>
> So there is much work ahead, and many more opportunities to have an impact.[221]

Delta's quiet and behind-the-scenes approach before the bill was passed drew substantial criticism.[222] Cynically, the approach may have allowed Delta to reassure stakeholders that it was taking steps without requiring Delta to offend powerful Georgia legislators. But the company's statements after the bill passed suggest that fear of Georgia legislators played a limited role in the company's decisionmaking, and Delta's approach may have reflected a reasonable calculation regarding the most effective strategy.[223] If statements by Delta and other companies are to be believed, the approach also had some impact on the external process.

Corporations motivated by internal concerns may also have had a role in shaping the constitutional doctrine on race. In a landmark decision permitting affirmative action in higher education, the Supreme Court's majority decision explicitly cited arguments from the business community in support:

> [The benefits of student body diversity] are not theoretical but real, as major American businesses have made clear that the skills needed in today's increasingly global marketplace can only be developed through exposure to widely diverse people, cultures, ideas, and viewpoints. Brief for 3M et al. as *Amici Curiae*; Brief for General Motors Corp. as *Amicus Curiae* 3–4.[224]

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221. Ed Bastian, Ed Bastian Memo: Your Right to Vote, Delta News Hub (Mar. 31, 2021), https://news.delta.com/ed-bastian-memo-your-right-vote [https://perma.cc/LS2R-T8AR] (emphasis added).

222. Gelles, Inside Corporate America's Frantic Response, supra note 211.

223. See Chip Cutter, Suzanne Vranica & Alison Sider, With Georgia Voting Law, the Business of Business Becomes Politics, Wall St. J. (Apr. 10, 2021), https://www.wsj.com/articles/with-georgia-voting-law-the-business-of-business-becomes-politics-11618027250 (on file with the *Columbia Law Review*) (quoting Bastian's argument that speaking out before the bill was passed would have meant that the company "lost a seat at the table").

224. Grutter v. Bollinger, 539 U.S. 306, 330–31 (2003). A group of American businesses has advanced similar arguments in the affirmative action cases currently pending before the Supreme Court. Brief for Major American Business Enterprises as Amici Curiae Supporting Respondents at 31, Students for Fair Admissions, Inc. v. President & Fellows of Harvard Coll., Nos. 20-1199 & 21-707 (U.S. filed Aug. 1, 2022), 2022 WL 3130774 ("Amici's . . . organizations are strengthened when their team members and leaders have rich and

These effects should not be overstated. But corporations do have substantial influence over the legislative and judicial processes. When internal forces cause corporations to recognize the importance of progress on race, that muscle can be put to real use.

B. *Climate Change*

Climate change has also been an important area for debate by internal and external reformers. While external regulations are critical to driving changes, internal reforms may play a constructive role by supplementing and accelerating the effect of the external measures.

1. *Capacity to Adopt Multiple Reforms.* — Federal regulatory progress on carbon emissions has been frustrating and fitful.[225] Enacting new legislation is difficult. Among other hurdles, most legislation must attract sixty votes in the Senate in order to overcome a filibuster. A majority of that size is extremely difficult to achieve, particularly on a contentious issue like climate change. While narrow pathways for avoiding this requirement do exist, they have important limitations. The landmark Inflation Reduction Act of 2022 was passed through a reconciliation process that did not allow it to include regulatory provisions.[226] The Act included subsidies that are projected to shift the trajectory of American carbon emissions, but it could not take steps like reversing a recent hostile Supreme Court decision.[227] More fundamentally, the replicability and durability of the legislation are open to serious question. The Act came as something of a surprise, with its likelihood of success and its content uncertain until late in the process.[228] It is also unclear whether the policies will prove durable. The subsidies in the package will likely attract

individualized experiences with people from different racial and ethnic backgrounds. University education remains an essential environment for fulfilling that need.").

225. See Coral Davenport & Lisa Friedman, Five Decades in the Making: Why It Took Congress So Long to Act on Climate, N.Y. Times (Aug. 7, 2022), https://www.nytimes.com/2022/08/07/climate/senate-climate-law.html (on file with the *Columbia Law Review*) (describing decades of fitful progress).

226. See Patrick Parenteau, The Inflation Reduction Act Doesn't Get Around the Supreme Court's Climate Ruling in *West Virginia v. EPA*, but It Does Strengthen EPA's Future Abilities, Conversation (Aug. 24, 2022), https://theconversation.com/the-inflation-reduction-act-doesnt-get-around-the-supreme-courts-climate-ruling-in-west-virginia-v-epa-but-it-does-strengthen-epas-future-abilities-189279 [https://perma.cc/5R3S-5LC9].

227. See West Virginia v. Env't Prot. Agency, 142 S. Ct. 2587, 2616 (2022) (holding that the EPA lacked authority to issue generation-shifting regulations, a key pillar of the Obama Administration's Clean Power Plan); Parenteau, supra note 226 ("[A]s groundbreaking as it is, the Inflation Reduction Act does not change the impact of the Supreme Court's determination in *West Virginia v. EPA* that the EPA lacks the authority to require a systematic shift to cleaner sources of electricity generation.").

228. See Emily Cochrane, Sinema Agrees to Climate and Tax Deal, Clearing the Way for Votes, N.Y. Times (Aug. 4, 2022), https://www.nytimes.com/2022/08/04/us/politics/sinema-inflation-reduction-act.html (on file with the *Columbia Law Review*).

constituencies that will have a vested interest in seeing the policies continue. But policy oscillation is normal in this area.[229] In the meantime, states can only make limited progress because of legal doctrine and competitive dynamics.[230] These realities suggest that any optimism about the external path must be guarded.

The internal path is more complicated. There are two basic avenues for internal reforms to affect corporate behavior: Companies might anticipate external regulation and change their behavior accordingly, and companies might act independently of external regulation.

a. *Anticipating External Reforms.* — When internal forces compel a company to take action in anticipation of an external regulation, the internal reform ultimately depends on the capacity of public actors to take action. If the federal government is known to be completely unable to enact meaningful reform, this mechanism of action would be disabled.

But internal mechanisms can have important effects. Imagine that a company was considering making an investment in 2017 and that the profitability of the investment would depend on carbon regulations: Examples of such investments might include a pipe or rail line transporting fossil fuels, a mine or well extracting fossil fuels, an electric plant burning fossil fuels, or a factory manufacturing a product that will burn fossil fuels. If the regulatory environment is favorable, the project will have operating profits and break even in six years. If the regulatory environment is unfavorable, the project will operate at a loss and will not break even. The company anticipates a favorable environment until the next presidential election; if the incumbent is reelected, the favorable environment will continue, but if a Democratic challenger wins, the environment will become unfavorable.

The internal machinery of corporate decisionmaking can have at least three effects. First, cautious management can smooth or even amplify the expected effect of regulation. Instead of swinging wildly from an approach calibrated for one regulatory regime to an approach calibrated for a different regulatory regime based on the outcome of an election, a firm can anticipate potential changes and chart a middle course.[231] Second,

229. For example, the Obama Administration sought to reduce carbon emissions in the electricity industry with the Clean Power Plan; the Trump Administration sought to reverse course with the Affordable Clean Energy Rule; the Court of Appeals for the District of Columbia Circuit struck down the Trump rule on the final day of the administration; and the Supreme Court substantially limited the EPA's authority in the space during the Biden Administration. See Am. Lung Ass'n v. Env't Prot. Agency, 985 F.3d 914, 930 (D.C. Cir. 2021) (striking down the Trump Administration's Affordable Clean Energy Rule and its embedded repeal of the Obama Administration's Clean Power Plan), rev'd sub nom. West Virginia v. Env't Prot. Agency, 142 S. Ct. 2587 (2022).

230. See supra notes 105–106 and accompanying text.

231. Internal firm decisionmaking can also amplify the impact of an expected regulation. If the expected impact of regulation—that is, the average impact of favorable

preemptive action by firms can accelerate the impact of potential regulation. The firm's decisions in 2017 would have been based in part on its guesses about the potential for new regulation in 2021. For an urgent problem like climate change, changing behavior today may be extremely valuable. Third, changes in corporate decisions can affect the likelihood of stringent regulation.[232]

The mechanisms of corporate governance will have an important role to play in channeling these effects when markets are not perfect. Markets may not properly evaluate the likelihood of regulatory reforms.[233] And firms may have important inside information about the impact of a potential regulation—the company may uniquely be in possession of information about the likely emissions from the project and its profitability. In such an environment, managers may be able to temporarily boost stock prices and annual bonuses by investing in the dirty project, even if the expected value of the project is negative: In effect, corporate managers would be signaling to shareholders that they believe regulations are unlikely or that the project is unusually clean or profitable.[234] The internal mechanisms of corporate governance are essential in countering these effects, addressing the basic agency problem and focusing attention on long-term problems.[235]

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and unfavorable regulations weighted for the likelihood of Republican and Democratic victory—makes the expected profits of the project negative, the firm may avoid the project. That outcome would be indistinguishable from the firm treating a Democratic victory as a certainty.

232. See infra section III.B.3.

233. Financial markets have often struggled to predict Washington's behavior, particularly under crisis conditions. See, e.g., Andrew Ross Sorkin, Too Big to Fail 3 (2009) (describing collapse in financial markets after Congress initially failed to pass a rescue package in response to the subprime mortgage crisis); Anna Hirtenstein & Paul Vigna, Stocks Slide on Coronavirus Uptick, Fading Stimulus Hopes, Wall St. J. (Oct. 26, 2020), https://www.wsj.com/articles/global-stock-markets-dow-update-10-26-2020-11603706439 (on file with the *Columbia Law Review*) (describing market correction "after Congress and the White House failed to agree on a much-anticipated fiscal stimulus deal").

234. See Madison Condon, Market Myopia's Climate Bubble, 2022 Utah L. Rev. 63, 86–87 [hereinafter Condon, Market Myopia] (observing how "executives sometimes spend money on investments that are not net-present-value justified, just to keep up the appearance of growth and the promise of future profits" in the face of restrictive regulations or market uncertainty); see also Armour et al., supra note 100, at 5 (noting that managers may avoid making efficient investments in compliance measures because large investments would signal to the market that the firm faces a high risk of liability).

235. See Condon, Market Myopia, supra note 234, at 125 (noting, for instance, that "[s]hareholders, as monitors of corporate management, should examine the metrics by which executive compensation is determined and push for the removal of those that distort managers away from long-term stewardship"). Government regulation can have an important role in facilitating these processes. For example, mandating securities disclosures on "stranded assets" or the anticipated effects of regulation would help markets evaluate projects more accurately and limit the need for corporate governance to take special account of these problems. Id. at 114–17.

The recent success of activist hedge fund Engine No. 1 in unseating members of Exxon's board of directors may be a useful example. The company's strategy of doubling down on fossil fuels by making large investments in production had resulted in major losses, particularly during the coronavirus pandemic—the company took a loss in excess of $20 billion in 2020 alone.[236] Engine No. 1 was able to persuade a coalition of shareholders to vote out various directors and replace them with new candidates focused on transitioning the company to cleaner technologies that would succeed when oil prices were low and regulators were more aggressive.[237] Shareholder votes are usually a routine rubber stamp for management-approved directors. But with shareholders expecting new regulations, this normally predictable internal process became an avenue for change.[238]

Not all paths have been so straightforward. For example, during most of the Trump Administration, General Motors and its CEO Mary Barra advocated against tough standards on vehicle emissions.[239] Shortly after now-President Joseph R. Biden defeated Trump in the 2020 presidential election, Barra reversed course on regulations.[240] And shortly after the Biden Administration took office, Barra announced that General Motors would phase out traditional automobiles in favor of electric vehicles by 2035.[241] If General Motors anticipated tougher external regulatory action on climate change and sought to position itself as a leader, the anecdote does not show that internal corporate reform is a more promising path

236. See Exxon Mobil Corp., Annual Report (Form 10-K) 70 (Feb. 24, 2021), https://www.sec.gov/Archives/edgar/data/34088/000003408821000012/xom-20201231.htm [https://perma.cc/P54C-PL82]; Clifford Krauss, Exxon Mobil Lost $22 Billion in 2020, Its Worst Performance in Four Decades, N.Y. Times (Feb. 2, 2021), https://www.nytimes.com/2021/10/29/business/exxon-mobil-lost-22-billion-in-2020-its-worst-performance-in-four-decades.html (on file with the *Columbia Law Review*) (last updated Oct. 29, 2021).

237. For one account, see Justin Baer & Dawn Lim, The Hedge-Fund Manager Who Did Battle With Exxon—and Won, Wall St. J. (June 12, 2021), https://www.wsj.com/articles/the-hedge-fund-manager-who-did-battle-with-exxonand-won-11623470420 (on file with the *Columbia Law Review*).

238. See id.

239. See Paul A. Eisenstein, GM Turns on Trump, Now Supports California's Tough Emissions Rules, NBC News (Nov. 24, 2020), https://www.nbcnews.com/business/autos/gm-turns-trump-now-supports-california-s-tough-emissions-rules-n1248799 [https://perma.cc/JLC5-T8HB].

240. Id. ("General Motors . . . reversed course and no longer supports President Donald Trump's plan to prevent California from setting its own automotive emissions standards. . . . The GM announcement [in support of] California's mandate also happened to come on the day the White House all but formally conceded the 2020 presidential election . . . .").

241. See Mike Colias, GM to Phase Out Gas- and Diesel-Powered Vehicles by 2035, Wall St. J. (Jan. 28, 2021), https://www.wsj.com/articles/gm-sets-2035-target-to-phase-out-gas-and-diesel-powered-vehicles-globally-11611850343 (on file with the *Columbia Law Review*).

than external reform. The company's back and forth also suggests limited success in smoothing or accelerating the impact of external regulation.

b. Independent Internal Reform. — Internal reforms can proceed even without the potential for external reforms. For example, General Motors might have been reacting to internal forces, such as shareholder preferences, that are entirely separate from potential government regulation. There are good reasons to think that might be the case. The electric vehicle and clean energy company, Tesla, Inc., currently trades at a much higher share-price-to-earnings ratio than General Motors; shareholders apparently believe that Tesla is worth more than General Motors, even though Tesla currently manufactures far fewer cars and makes far less money.[242] Even if General Motors was not concerned about external regulations, it would have good internal reasons to service its shareholders by attempting to tap into Tesla's share price magic.

And indeed, some scholars have suggested that shareholders would benefit from corporate action to reduce carbon emissions, even absent the prospect of external regulation. Professor Madison Condon has argued that climate change presents a systemic risk that investors cannot avoid through diversification.[243] A diversified investor is thus forced to take on the full risk associated with climate change and has a real incentive to use their voting power to encourage companies in their portfolio to reduce carbon emissions.[244] And index funds, which have the perspective of a diversified investor, do in fact seem to be signaling a desire to see portfolio companies cut down on carbon emissions.[245]

At some companies, working on climate issues can also contribute to traditional drivers of shareholder value. Walmart's Gigaton Project seeks to avoid one billion tons of greenhouse gas emissions in the company's supply chain by 2030. Although Walmart's environmental efforts have had an impact on a scale comparable to a major government program, they began when an activist convinced company leadership that environmental

242. See Andrew Nusca & David Z. Morris, Teslanomics: How to Justify Being the Most Valuable Car Company on Earth, Fortune (Aug. 10, 2020), https://fortune.com/2020/08/10/tesla-most-valuable-car-company-in-the-world-electric-vehicles-evs/ (on file with the *Columbia Law Review*) (noting that at the time, Tesla was worth "more than quadruple the combined value of American icons General Motors and Ford Motor, even though the California company sold just 4% of the vehicles the Detroit duo did last year").

243. See Madison Condon, Externalities and the Common Owner, 95 Wash. L. Rev. 1, 6, 9, 11 (2020).

244. See id. at 7–10.

245. See, e.g., Larry Fink, Letter to CEOs: A Fundamental Reshaping of Finance, BlackRock (2020), https://www.blackrock.com/corporate/investor-relations/2020-larry-fink-ceo-letter [https://perma.cc/3AU8-BYZ9] [hereinafter Fink, 2020 CEO Letter]. BlackRock was one of the institutional investors to back changes at Exxon. See Baer & Lim, supra note 237.

work was closely aligned with the company's core focus on controlling cost and eliminating waste.[246]

Admittedly, there are some good reasons to doubt the strength of any alliance between shareholders and social interests in the area of climate change. First, shareholders will not internalize the full effects of climate change. Most obviously, someone who holds a portfolio of public American companies will not have any exposure to the losses experienced by a farmer in Bangladesh.[247]

Second, to the extent that an American public company does have exposure to climate change, it is likely to have access to adaptation strategies that will help insulate shareholders from loss. A firm that sources a key input from a country that will experience climate change devastation will find an alternate supplier. Capital is mobile and can flee from the effects of climate change, often in ways that actual human beings cannot.[248] Indeed, climate change may actually create profitable opportunities for capital to exploit. As a simple example, there may be opportunities to buy land that will be more productive because of climate change: A vineyard in Germany may be underpriced today relative to its potential productivity over the next few decades.[249] General Motors' transition to electric vehicles may be a similar phenomenon. Society as a whole will not profit from climate change, but smart companies may find a way.

Third, a diversified investor in America's public markets will have a larger stake in established players in old industries (e.g., oil giants) than in the pioneers building things that will benefit from a complete transition away from carbon (e.g., startups developing new technologies or lithium miners in China).[250] Many pioneers are not publicly traded on American markets. Even if an investor could buy shares in them, it would be impossible to predict in advance which pioneers will succeed and which

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246. See Edward Humes, Force of Nature: The Unlikely Story of Wal-Mart's Green Revolution 2–4 (2011); Kim, supra note 169, at 5 ("Walmart's Project Gigaton is set to abate more greenhouse gases (1 billion metric tons) than the Clean Power Plan (700 million tons).").

247. See Roberto Tallarita, The Limits of Portfolio Primacy, 76 Vand. L. Rev. (forthcoming 2023) (manuscript at 24), https://ssrn.com/abstract=3912977 [https://perma.cc/95EJ-JEXA].

248. See id. (discussing the option to relocate production and invest in climate change–mitigating technologies that "do not . . . alleviate the consequences of climate change for the general population").

249. See Christopher F. Schuetze, 'Disgusting to Say, but It's the Truth': German Winemakers See Boon in Climate Change, N.Y. Times (Jan. 19, 2019), https://www.nytimes.com/2019/01/19/world/europe/germany-wine-climate-change.html (on file with the *Columbia Law Review*) (explaining that rising global temperatures will expand the amount of land in Germany suitable for wine growing).

250. See Tallarita, supra note 247 (manuscript at 39, 42).

will fail.[251] As a result, a diversified investor may have a vested interest in business as usual, instead of disruption. Even if a regulation that would reduce carbon emissions would be socially beneficial, it could be opposed by shareholders holding large stakes in established fossil fuel companies and small stakes in pioneering green companies.

Fourth, action at the margins is not likely to have any effect. One marginal ton of carbon emissions would have little impact on the magnitude of climate change. Only a small handful of companies operate at such a scale that their decisions could have a meaningful impact on the phenomenon.[252] As a result, even if an investor expects to suffer from climate change, it is not clear that they would want a company to spend shareholder money to reduce carbon emissions.

Finally, even if shareholders wanted effective action against climate change, they would likely prefer external action to internal action. External action on racial inequity would likely be painful for a rich, white shareholder, who therefore would have an incentive to support alternative internal measures that could maintain social stability. But aggressive government action to address climate change would not be especially painful for a diversified investor, who would be able to offload some of the costs of the transition away from carbon onto society while potentially

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251. Making those predictions is not simply a matter of having an appropriate time horizon or vision. Many car companies went broke in the early years of the automotive industry. Ford Motor Company was Henry Ford's *third* attempt at starting a successful car company. See M. Todd Henderson, The Story of *Dodge v. Ford Motor Company*: Everything Old Is New Again, *in* Corporate Law Stories 37, 39 (J. Mark Ramseyer ed., 2009) ("Henry Ford['s] . . . first two companies, the Detroit Automobile Company and the Henry Ford Company, made no cars and no profits."); cf. Warren Buffett & Carol Loomis, Mr. Buffett on the Stock Market, Fortune (Nov. 22, 1999), https://www.berkshirehathaway.com/1999ar/FortuneMagazine.pdf (on file with the *Columbia Law Review*) ("All told, there appear to have been at least 2,000 car makes . . . . After corporate carnage that never let up, we come down to three U.S. car companies . . . . You could have grasped the importance of the auto when it came along but still found it hard to pick companies that would make you money.").

252. This is not to say that there are *no* companies that could have an impact. Walmart's Project Gigaton seeks to avoid one billion metric tons of greenhouse gas emissions in its supply chain by 2030. See Michael P. Vandenbergh, The New Wal-Mart Effect: The Role of Private Contracting in Global Governance, 54 UCLA L. Rev. 913, 927–28 (2007) (describing the scale of Walmart and other firms and the impact of their adoption of environmental standards); Dieter Holger, Walmart Makes Progress on Emissions Target by Winning Over Suppliers, CSO Says, Wall St. J. (Apr. 12, 2022), https://www.wsj.com/articles/walmart-makes-progress-on-emissions-target-by-winning-over-suppliers-cso-says-11649782501 (on file with the *Columbia Law Review*) (describing Walmart's progress toward eliminating one billion metric tons of greenhouse gas emissions). Groups of firms can also improve outcomes through concerted action coordinated through private governance mechanisms like certification schemes. See Vandenbergh, Private Environmental Governance, supra note 147, at 137 ("A recent comprehensive review of empirical research on private environmental certification systems . . . finds evidence of substantial positive impacts on corporate environmental behavior at the global and local levels.").

profiting from new government projects and subsidies. Indeed, despite urging from Republican politicians, oil and gas companies did not energetically lobby against the climate provisions of the Inflation Reduction Act, and executives offered statements that ranged from ambivalent to supportive.[253]

But while these factors may reduce the likelihood that purely internal processes will yield adequate results, they do not suggest that internal changes would cannibalize or prevent external changes. Indeed, the existence of a broad ecosystem of private actors encouraging progress on environmental issues—often using forms of action traditionally associated with government policymaking, but for private reasons[254]—suggests that there is a valuable role for thoughtful internal interventions. Reformers can travel along both the internal and external paths simultaneously.

2. *Reformer Expectations.* — Reformers do not appear likely to trade away an effective external regulation for an ineffective internal reform. Commentators on corporate issues are already attentive to the threat of "greenwashing," in which companies mouth platitudes about the environment without making changes to their operations.[255] Regulators have also taken note.[256] Groups that are focused on environmental issues are not likely to be satisfied by empty promises.

There is also little evidence that reformers are ignoring the potential for external regulation. It would be difficult to criticize political progressives for a lack of ambition on climate change. The "Green New Deal" package championed by Representative Alexandria Ocasio-Cortez and Senator Edward J. Markey set bold targets, including the goal of "meeting 100 percent of the power demand in the United States through clean, renewable, and zero-emission energy sources."[257] The stimulus and infrastructure legislation pursued by Democrats after President Biden's election also calls for extensive efforts on climate change.[258] It is hard to

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253. See Timothy Puko, GOP Lawmakers Lobby Oil Industry to Denounce Tax-and-Climate Bill, Wall St. J. (Aug. 6, 2022), https://www.wsj.com/articles/gop-lawmakers-lobby-oil-industry-to-denounce-tax-and-climate-bill-11659778202 (on file with the *Columbia Law Review*).

254. Light & Orts, supra note 187, at 10.

255. See, e.g., Paul Polman, Corporate Greenwashing Is All the Rage. How Can We Stop It?, Fortune (Apr. 11, 2021), https://fortune.com/2021/04/11/greenwashing-esg-businesses-corporations-climate-change/ [https://perma.cc/9EA6-9F3F].

256. See, e.g., Press Release, Rohit Chopra, Comm'r, FTC, Statement of Commissioner Rohit Chopra Regarding the FTC EnergyGuide Rule 1, 4–5 (Dec. 22, 2020), https://www.ftc.gov/system/files/documents/public_statements/1585238/20201222_final_chopra_statement_on_energyguide_rule.pdf [https://perma.cc/A6T8-A4ZW].

257. See Recognizing the Duty of the Federal Government to Create a Green New Deal, H.R. Res. 109, 116th Cong. § 2(c) (2019).

258. See, e.g., Lisa Friedman & Jim Tankersley, Biden's Recovery Plan Bets Big on Clean Energy, N.Y. Times (July 11, 2021),

see how reformers could obtain more powerful external measures by abandoning efforts to encourage corporations to behave better.

3. *Dynamic Interactions Between Reforms.* — Internal changes may also make external changes more likely. First, if a few key corporations start to move toward greener behavior, it may substantially improve the prospects for external regulations by changing the cost–benefit ratio.[259] General Motors' voluntary move toward an all-electric vehicle lineup will make it cheaper for the government to require car companies to make the transition, much as the energy industry's natural transition away from coal made it cheaper to impose tighter emission standards. The move would also make it impossible to claim that tighter requirements were technically or economically infeasible.

Second, if a major corporation is a leader, it would also have good reason to put its political muscle into seeking regulations that force its competitors to meet standards of conduct that its competitors do not want to meet.[260] This effect can be amplified by a major corporation's capacity to enlist stakeholders. When Ford announced plans to build an electric truck using union labor in plants in the Midwest, it effectively recruited important constituencies to the project of electric vehicle manufacturing.[261]

Third, action by major companies can change cultural meanings. Ford kicked off its electrification plans by announcing an electric version of the Ford F-150 pickup truck—a vehicle associated with tough, utilitarian applications.[262] When electric vehicles were only for environmentalists looking to curb emissions or wealthy people looking for a flashy toy, they could easily be rejected by a substantial portion of the American population. A savvy bit of marketing, backed by Ford's scale and industrial

https://www.nytimes.com/2021/03/23/climate/biden-infrastructure-stimulus-climate-change.html (on file with the *Columbia Law Review*).

259. Supra section II.C.

260. See Levmore, supra note 188, at 838.

261. See Neal E. Boudette, Ford's Electric F-150 Pickup Aims to Be the Model T of E.V.s, N.Y. Times (May 19, 2021), https://www.nytimes.com/2021/05/19/business/ford-electric-vehicle-f-150.html (on file with the *Columbia Law Review*) (last updated May 28, 2021); Ted Cannis, Tough Goes Electric, Ford, https://corporate.ford.com/articles/electrification/tough-goes-electric.html [https://perma.cc/PF9Q-XH6Y] ("Ford trucks provide the global backbone of work, built on a foundation of toughness. . . . Tough starts and ends with F-Series, our bread and butter. . . . The all-electric F-150 will be a new and exciting kind of Built Ford Tough.") (last visited Oct. 13, 2022).

262. See, e.g., Brian C. Black, Why Ford's Electric F-150 Pickup Is a Turning Point for Car Culture, Fast Co. (June 17, 2021), https://www.fastcompany.com/90647325/ford-electric-f-150-lightning-truck-of-the-future [https://perma.cc/7EDE-R74N]. The auto industry has been the site of other shifts in cultural meanings. Cf. Tom Ginsburg, Jonathan S. Masur & Richard H. McAdams, Libertarian Paternalism, Path Dependence, and Temporary Law, 81 U. Chi. L. Rev. 291, 320, 347 (2014) (noting that seatbelt usage was once uncommon, with the result that wearing a seatbelt sent an undesirable signal). For further elaboration on industry nudging cultural change, see Cass Sunstein, Why Nudge? The Politics of Libertarian Paternalism 60 (2014); Light & Orts, supra note 187, at 63.

might, has the potential to change the cultural meaning of electric vehicles in a way that would make for a more congenial environment for pro-electric vehicle regulation.

Finally, political actors seem to think the internal process is a threat. As discussed in section III.C below, Republicans have sought to curtail internal processes for addressing environmental and social issues. The most straightforward explanation is that Republican officials wanted to ensure that reform could only happen through the external regulatory process, because they believed that they could control and limit the external process in a way that they could not control the internal process. If that is right, savvy figures that benefit politically from a lack of reform believe that the internal pathway is a serious threat.

C. *Constraining Internal Reform*

Groups that have the ability to veto external reforms have an obvious interest in ensuring that their power cannot be evaded through internal processes. In recent years, conservative forces have sought to use perches in government to prevent internal processes from operating. This opposition strongly suggests that internal processes for reform can have advantages,[263] while indicating that there are limits on how far they will be allowed to go. Four recent examples demonstrate the phenomenon.

1. *Managing the Federal Reserve's COVID-19 Portfolio.* — In response to the economic crisis prompted by COVID-19, the Federal Reserve embarked on a massive program under the CARES Act to purchase billions of dollars of bonds. To handle the program, the Federal Reserve hired asset manager BlackRock.[264]

Just a few months before the Federal Reserve engagement, BlackRock and its CEO, Larry Fink, had taken a prominent role in the movement toward sustainable investing. Fink released a letter which stated in part that "climate risk is investment risk" and that "climate-integrated portfolios can

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263. While opposition to the *results* of internal processes seems to be the most plausible explanation for these positions, opposition can also be founded on legitimacy concerns. If the external political process is the uniquely legitimate way to resolve disputes about environmental or social matters, internal processes necessarily must be prevented from intruding on those matters. Cf. Light & Orts, supra note 187, at 65 (noting legitimacy concerns with private action but suggesting that in present context, "something less than ideal is needed"); Reich, supra note 34, at 21 (arguing that unless answers are supplied by the "political process," the "answers are completely arbitrary").

264. See Matthew Goldstein, Fed Releases Details of BlackRock Deal for Virus Response, N.Y. Times (Mar. 27, 2020), https://www.nytimes.com/2020/03/27/business/coronavirus-blackrock-federal-reserve.html (on file with the *Columbia Law Review*); Cezary Podkul & Dawn Lim, Fed Hires BlackRock to Help Calm Markets. Its ETF Business Wins Big., Wall St. J. (Sept. 18, 2020), https://www.wsj.com/articles/fed-hires-blackrock-to-help-calm-markets-its-etf-business-wins-big-11600450267 (on file with the *Columbia Law Review*).

provide better risk-adjusted returns to investors."[265] This belief led Fink to commit to "making sustainability integral to portfolio construction and risk management[] [and] exiting investments that present a high sustainability-related risk, such as thermal coal producers . . . ."[266]

Apparently concerned that BlackRock would consider climate risk as it managed the Federal Reserve program, a group of seventeen Republican senators sent a letter to the Treasury Secretary and the Chairman of the Federal Reserve expressing their reservations:

> Industries, like the energy and transportation sectors[,] are facing significant economic challenges as the demand for products and services have dropped with the constraints on the economy. We urge you to ensure that the financial relief offered under the CARES Act is fully available to companies throughout the economy.
>
> Some outside groups have already advocated that certain sectors of the economy be excluded from the loans made available under the CARES Act. Acquiescing to these demands would be contrary to Congressional intent and would arbitrarily harm certain American workers. Both are unacceptable.
>
> . . . .
>
> Earlier this year, BlackRock announced that it would remove from its discretionary active investment portfolios the public securities (both debt and equity) of certain companies. This was a decision made solely by BlackRock as an individual business decision. However, we believe that the Federal Reserve should emphasize that, in carrying out its fiduciary duties . . . BlackRock must act without regard to this or other investment policies BlackRock has adopted for its own funds.[267]

As Condon has noted, the letter was probably unnecessary in a narrow sense—BlackRock was never likely to apply its climate risk tools to the Federal Reserve engagement—but it was part of a broader partisan effort to use political power to prevent markets from realigning to account for climate risk.[268] It could also have a chilling effect if financial institutions

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265. See Fink, 2020 CEO Letter, supra note 245.

266. Id.

267. Letter from Kevin Cramer, James M. Inhofe, Shelley Moore Capito, John Barrasso, Steve Daines, Ted Cruz, Dan Sullivan, John Hoeven, John Cornyn, Joni K. Ernst, James Lankford, Michael B. Enzi, Thom Tillis, Bill Cassidy, David A. Perdue, Mike Braun & M. Michael Rounds, U.S. Sens., to Steven Mnuchin Sec'y U.S. Dep't of the Treasury, & Jerome Powell, Chairman, Bd. of Governors of the Fed. Rsrv. Sys. (Apr. 7, 2020), https://senatorkevincramer.app.box.com/s/981sfgn44nmkr8fq5hhf6xryxro6fyvp [https://perma.cc/6M3W-4P24].

268. See Madison Condon, The Firm Administering the Coronavirus Rescue Considers Climate Risks in Its Ordinary Investments: Republicans Told Them Not to This Time, Slate (Apr. 20, 2020), https://slate.com/news-and-politics/2020/04/republicans-block-blackrock-climate-risk-assesment.html [https://perma.cc/CU2R-LDTU].

reasonably infer that being outspoken on climate change could cost them profitable opportunities to participate in government programs.

2. *Managing Federal Workers' Retirement Savings*. — About six million active and retired federal workers save for retirement through the Thrift Savings Plan, a 401(k)-like defined contribution program overseen by the Federal Retirement Thrift Investment Board (FRTIB). Congress has taken steps to limit the FRTIB's ability to use the $700 billion Thrift Savings Plan portfolio to exercise power. The FRTIB is statutorily directed to provide specific offerings to savers, with each offering either passively tracking an index or allowing the use of mutual funds.[269] The FRTIB is also statutorily barred from "exercis[ing] voting rights associated with the ownership of securities" within the portfolio.[270]

As a result, the FRTIB has adopted a largely passive stance. Unlike its counterparts in Japan, Sweden, and the United Kingdom, the FRTIB has not taken steps to assess the risks associated with climate change.[271] But the FRTIB relies on two outside asset management firms—BlackRock and State Street—to manage the portfolio. And the FRTIB does not read the statutory bar on voting to extend to BlackRock and State Street, instead expecting them to vote based on their established proxy voting guidelines.

In June 2021, two Republican senators sent a letter to the acting chairman of the FRTIB expressing alarm at this state of affairs and demanding a briefing:

> [W]hile [BlackRock and State Street's] proxy voting guidelines are ostensibly focused on the investor's fiduciary advantage, both entities are increasingly incorporating left-leaning environmental, social, and corporate governance ("ESG") priorities into these guidelines. For example, BlackRock announced that in 2021 "key changes" in its voting guidelines "address board quality; the transition to a low-carbon economy; key stakeholder interests; diversity, equity and inclusion; alignment of political activities with stated policy positions; and shareholder proposals." Not to be outdone, [State Street's] CEO stated "our main stewardship priorities for 2021 will be the systemic risks associated with climate change and a lack of racial and ethnic diversity."[272]

269. 5 U.S.C. § 8438(b) (2018).

270. Id. § 8438(f).

271. See U.S. Gov't Accountability Office, GAO-21-327, Retirement Savings: Federal Workers' Portfolios Should Be Evaluated for Possible Financial Risks Related to Climate Change 28–34, 40 (2021), https://www.gao.gov/assets/gao-21-327.pdf [https://perma.cc/BN39- 3G6A]. The report urged the FRTIB to evaluate, among other issues, the scope of the climate-related financial risk posed to the federal Thrift Savings Plan, which contains around $700 billion of assets for roughly six million active and retired federal workers recommended changes. Id. at 39.

272. Letter from Pat Toomey & Ron Johnson, U.S. Sens., to David A. Jones, Acting Chairman, Fed. Ret. Thrift Inv. Bd. (June 30, 2021),

The letter again reflects concern that the internal mechanisms of shareholder voting could be used to achieve policy outcomes that the senators disfavor—and would be in a position to prevent if reformers sought change through external processes. The letter is also a clear shot across the bow of major asset managers, suggesting that outspoken support of a "left-leaning" agenda could damage their ability to do lucrative work with the government.

3. *Rules for Fiduciaries of Retirement Accounts.* — The Trump Administration similarly sought to deploy its regulatory muscle to prevent institutional investors from using environmental, social, or governance criteria when making investments or casting votes. A Department of Labor rule issued in November 2020 stated that fiduciaries of retirement and pension funds were only permitted to make investment decisions based on "pecuniary" factors and could not consider "non-pecuniary" factors except as a tie-breaker.[273] A companion rule issued in December 2020 provided that fiduciaries could only use their rights as shareholders to advance the pecuniary interests of the retirement or pension plan and that they could choose not to vote on matters that did not have a material financial impact on the plan's assets.[274] In support of these changes, Trump Administration Secretary of Labor Eugene Scalia stressed his view that "[p]rivate employer-sponsored retirement plans are not vehicles for furthering social goals or policy objectives that are not in the financial interest of the plan."[275]

The Biden Administration put these regulatory changes on hold. In a March 2021 statement, the Department of Labor stated that it intended to revisit the rules and that it would not enforce the rules in the interim.[276] The moves were explained as part of a larger effort to revisit Trump Administration decisions on matters that relate to climate change.[277]

At an abstract level, it is not obvious that the Trump Administration's rules would have prevented fiduciaries from trying to increase the value of an overall portfolio by limiting climate change or other undesirable social or environmental problems. But, at a minimum, the rules were plainly

https://www.banking.senate.gov/imo/media/doc/toomey_johnson_letter_to_frtib.pdf [https://perma.cc/VQW3-KNZA].

273. Financial Factors in Selecting Plan Investments, 85 Fed. Reg. 72,846, 72,846 (Nov. 13, 2020) (codified at 29 C.F.R. pts. 2509, 2550).

274. See Fiduciary Duties Regarding Proxy Voting and Shareholder Rights, 85 Fed. Reg. 81,658, 81,672 (Dec. 16, 2020) (codified at 29 C.F.R. pts. 2509, 2550).

275. See U.S. Department of Labor Proposes New Investment Duties Rule, DOL (June 23, 2020), https://www.dol.gov/newsroom/releases/ebsa/ebsa20200623 [https://perma.cc/L58C-Q4KH].

276. See U.S. Department of Labor Statement Regarding Enforcement of Its Final Rules on ESG Investments, Proxy Voting by Employee Benefit Plans, DOL (Mar. 10, 2021), https://www.dol.gov/newsroom/releases/ebsa/ebsa20210310 [https://perma.cc/FY53-J6BF] [hereinafter DOL, ESG Investments].

277. Id.

intended to inject uncertainty on that score.[278] The Biden Administration suggested that in the few months that they had been in force, the rules had achieved their intended effect and had "already had a chilling effect on appropriate integration of ESG factors in investment decisions, including in circumstances that the rules can be read to explicitly allow."[279]

These regulatory developments are readily understood as part of a competition between internal and external modes of reform. People with power over the external mode are seeking to either limit the internal mode or authorize it to move forward. On the whole, the dynamic vindicates the thesis of this Article and suggests its limits—the regulatory developments implicitly recognize that corporate reform through internal governance mechanisms could proceed more easily than reform through external government regulation on certain hot-button topics, while suggesting that the government will act in some cases to protect its exclusive hold on power.

But the limits are unlikely to be too constricting for the processes of internal corporate reform. There are specific contexts in which governmental bodies have extensive control over the processes that drive internal corporate reform. For example, the Securities and Exchange Commission has power over listing requirements that exchanges may want to impose on issues like board diversity.[280] But many mechanisms do not require active involvement from the federal government. The federal government also may not be able to maintain a consistent and effective opposition to an internal reform. Congressional inertia may prevent the introduction of new legislation. As evidenced by the Biden Administration's reversal of the Trump Administration's policy, different administrations may have different views, preventing effective executive action. Any regulation will also have limited scope. If climate risk will impact actual financial returns, or if ESG-focused investors raise the cost of capital for polluters, even the Trump rules would not prevent consideration of pollution in investment decisions.

As a result of these dynamics, the unavailability of an external reform may not mean that the government will intervene to prevent an internal reform. Political actors in Congress and the executive branch may not be willing to adopt appropriate external regulations, but they likely also lack the will and capacity to fully defend the status quo by preventing internal action.

278. See Financial Factors in Selecting Plan Investments, 85 Fed. Reg. at 72,850 (rejecting the view that "fiduciaries should be permitted to consider the potential for an investment to create jobs for workers who in turn would participate in the plan"); id. at 72,860 (asserting that "the fact that an investment promotes ESG factors, or that it arguably promotes positive general market trends or industry growth" does not imply that it "is a prudent choice for retirement or other investors").

279. DOL, ESG Investments, supra note 276.

280. See supra notes 111–113 and accompanying text.

4. *State-Level Responses to Stakeholderism.* — There has been a marked increase in the volume and intensity of state-level efforts to punish corporations acting on stakeholder interests. West Virginia has threatened to bar BlackRock, Goldman Sachs, JPMorgan, Morgan Stanley, and Wells Fargo from doing business with the state in response to the companies' reluctance to finance coal companies and projects.[281] Texas barred financial firms from its lucrative municipal bond market if they "discriminate" against the firearm industry[282] or the oil industry.[283] State lawmakers have suggested that they will use similar bans to punish banks that provide abortion-related travel benefits or cover abortion-related expenses for employees.[284] Perhaps most strikingly, Florida sought to punish Walt Disney Co. for its opposition to the "Parental Rights in Education" bill, also known as the "Don't Say Gay" bill, by revoking the special district status of Disney World.[285]

A full analysis of this trend would be beyond the scope of this Article. But the developments do interact with key claims. To begin, it is hard to see how corporate action in these areas could reduce the likelihood of external reforms. No one concerned about the environment, firearm deaths, abortion rights, or homophobia could possibly have believed that the corporate action was a complete (or even partial) solution to the problem. As a result, the corporate action could not have meaningfully dampened desire for more direct political change.

At the same time, it does suggest limits on corporate influence. Disney employs dozens of lobbyists in Florida and is used to having an outsized

281. See David Gelles, West Virginia Punishes Banks That It Says Don't Support Coal, N.Y. Times (July 28, 2022), https://www.nytimes.com/2022/07/28/business/west-virginia-fossil-fuel-banks.html (on file with the *Columbia Law Review*).

282. See Amanda Albright & Danielle Moran, Two Dozen Banks Sidestep Texas Law Punishing Gun, Oil Policies, Bloomberg (Oct. 8, 2021), https://www.bloomberg.com/news/articles/2021-10-08/two-dozen-banks-sidestep-texas-law-punishing-gun-oil-policies (on file with the *Columbia Law Review*); Stephen Gandel, The Texas Law That Has Banks Saying They Don't 'Discriminate' Against Guns, N.Y. Times (May 28, 2022), https://www.nytimes.com/2022/05/28/business/dealbook/texas-banks-gun-law.html (on file with the *Columbia Law Review*).

283. See Albright & Moran, supra note 282; Ross Kerber, BlackRock, JPMorgan, Others Tell Texas They Don't Boycott Energy Companies, Reuters (May 19, 2022), https://www.reuters.com/business/finance/blackrock-jpmorgan-others-tell-texas-they-dont-boycott-energy-companies-2022-05-19/ [https://perma.cc/LFW3-J7CF].

284. See Taylor Telford, Companies Offer to Help Employees Seeking Abortions. It'll Be Tricky., Wash. Post (July 2, 2022), https://www.washingtonpost.com/business/2022/07/02/abortion-healthcare-insurance-coverage-dobbs-roe/ (on file with the *Columbia Law Review*).

285. See Andrew Atterbury, DeSantis Revokes Disney's Special Status After 'Don't Say Gay' Opposition, Politico (Apr. 22, 2022), https://www.politico.com/news/2022/04/22/desantis-disney-special-status-dont-say-gay-00027302 [https://perma.cc/6TNM-774Z].

influence over the political process in the state.[286] The fact that Florida's state government not only defied Disney by enacting the Parental Rights in Education Act, but went on to retaliate, suggests real limits on Disney's capacity to shape the political process or voting outcomes.

But there are reasons to suspect that this phenomenon may be limited. The principal targets are telling: Media and finance companies are easily painted as outside elites. Indeed, there is a long history in the United States of political skepticism of financial companies exercising power.[287] The maneuvers are also costly for the states and may prove extremely costly if they actually induce companies to exit.[288] States and companies may simply be testing each other's limits, searching for a new equilibrium. Whether that equilibrium entails balkanization—in which companies must choose whether to operate in blue states or red states—or convergence, it seems unlikely that corporate efforts to satisfy stakeholders will push politics in an unhelpful direction.

CONCLUSION

Shareholder primacy theorists have begun to assert that advocacy for internal corporate reforms is dangerous because it has the potential to interfere with better external reforms. But these claims are undertheorized and difficult to square with recent experience. Internal and external reforms have historically proceeded in parallel, in part due to the presence of multiple actors with their own agendas, powers, processes, and constituencies. Reformers themselves are reasonably savvy and are unlikely to accept a weak internal reform as a substitute for a better external reform. Internal corporate governance reforms can also support external reforms by leveraging corporate power over the political process and changing facts on the ground in a way that supports external regulation. These dynamics are reflected in the current debates over racial justice, climate change, and the power of institutional investors. At present, there is little evidence that reformers face a stark choice between internal and external reforms to improve corporate conduct.

286. See Todd C. Frankel, How Disney Fell Flat in Fight Over LGBTQ Talk in Florida's Schools, Wash. Post (Apr. 1, 2022), https://www.washingtonpost.com/business/2022/04/01/disney-dont-say-gay-bill/ (on file with the *Columbia Law Review*).

287. See Roe, Strong Managers, supra note 152.

288. See Daniel Garrett & Ivan Ivanov, Gas, Guns, and Governments: Financial Costs of Anti-ESG Policies 21 (Jan. 13, 2023) (unpublished manuscript), https://ssrn.com/abstract=4123366 [https://perma.cc/5365-YDDX] (suggesting that barring banks with ESG policies will result in Texas entities incurring an extra $303 to $532 million in interest).