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NEW OWNERS AND OLD MANAGERS: LESSONS FROM THE SOCIALIST CAMP

By Richard M. Buxbaum*

It is an honor to be asked to deliver this third Francis G. Pileggi Lecture at Widener University School of Law. It is a further privilege to be addressing members of the Delaware courts in this audience, especially since their cases and articles comprise so much of my own reading matter. They have looked at me from the bench before, but not from the audience; all in all, this arrangement is more to my liking.

My topic today is taken from the comparative-law corner of corporation law, but bears on the future of American corporation law. It is based, further, on recent practical experiences and events, but bears on the theory, not the practice, of corporation law. Corporations, as anyone reading the major law reviews over this past decade cannot help but recognize, have become the darlings of legal theory, rivaling the administrative agencies of the thirties and the automobile guest statutes of the sixties in the affection of scholars.

Recent international upheavals indirectly have confirmed this privileged position of corporations in academic discourse. Societies with economies organized along liberal principles and on the basis of market-based institutions have, in these past couple of years, demonstrated their superiority over their state-socialist rivals. The superior organization of a market-based economy rests largely on those economic productive units called "corporations," as we in the

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1. The original format of the paper, given as a lecture, has been retained and citations held to a minimum. I would like to thank Jennifer Lew, Boalt class of 1994, for her able research assistance.

OECD\textsuperscript{3} West know them. This in itself is a further reason for paying more attention to the structure and laws governing these organizations. Thus, it should not surprise us that corporations have become the objects of academic attention not only in law but also in economics,\textsuperscript{4} in political science,\textsuperscript{5} in sociology,\textsuperscript{6} and even in anthropology\textsuperscript{7} and philosophy.\textsuperscript{8}

This academic change from the previous situation in as little as twenty years is remarkable. Most of you will recall Bayless Manning's winged words of that period to the effect that corporation codes and, by implication, corporation law scholarship resembled nothing so much as the rusted skeleton of an empty skyscraper with its girders slowly creaking in the wind.\textsuperscript{9} Today we find an entire new generation of mostly younger scholars, at major law faculties, tearing up this track and making corporation law the hottest game in town. If you will forgive me the academic vanity, I dare say that some members of this roster are known even to the bench and bar; certainly the Delaware courts' citations to the works of some of the most visible among them suggest this new state of affairs.\textsuperscript{10} Underlying this

\begin{itemize}
\item \textsuperscript{3}Organization of Economic Cooperation and Development.
\item \textsuperscript{6}See, e.g., Neil Fischl, The Transformation of Corporate Control (1990).
\item \textsuperscript{8}See, e.g., Elizabeth Wolgast, Ethics of an Artificial Person: Lost Responsibility in Professions and Organizations (1992).
\item \textsuperscript{9}Bayless Manning, The Shareholder's Appraisal Remedy: An Essay for Frank Coker, 72 Yale L.J. 223, 245 n.37 (1962).
\end{itemize}
reinvigoration of legal scholarship is the similar surge of interest with corporations among social scientists, as I have just indicated.

What has brought most of my fellow academics to this field of the law is what seems to many observers of the American corporate economy to be its most inherent and perhaps even its most important feature; namely, the fact that it is through markets, especially the market for shares and the market for control, that we in the United States express the relationship between private ownership and corporate management.11 Most of these academics, of course, have found their home in economics, specifically in that wing of the discipline that shares the triumphalism of our society over the vindication of a liberal economy within a democratic state structure against the pretensions of a socialist economy within a non-democratic state structure.

The real-world game that confirmed—though most recently it seems to disprove—this corporate-capital version of product markets was the takeover "game."12 The real-world phenomenon that intensified this takeover wave and, through it, the rise and possible fall of these two corporate-capital markets was, of course, the rise of institutional investment.13 It is no coincidence that, when public and private leaders of Western opinion argued for the superiority of a free-market over a state-socialist economy, they implicitly, and often explicitly, included these two capital markets within the pantheon of necessary virtues.14 Certainly much of the academic cohort of that group did so.

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12. For a view of the history of this phenomenon with an emphasis on the political economy of the takeover movement, see Mark J. Roe, Takeover Politics (Center for Law and Economic Studies Working Paper No. 74, 1991).
14. See, e.g., Christian Kirchner, Privatization Plans of Central and Eastern European States, 148 JITE 4, 17 (1992) (posing the possible role of institutional investors in the privatization process and noting their major role in Western capital markets).
Back in the real world, however, something happened to the United States, the supposed big winner, on its way to collect at the teller’s window. We are now told that the stake has been picked up by the real winners of this Cold War race, the German and the Japanese economies and their firms.¹⁵

Now, whatever else might be our reaction to this news—whether we look for the cause of this unexpected development within the stars or within ourselves—we are resilient losers and willing to check out how the winners did it.¹⁶ Certainly American academics are flexible enough, and hold their theories lightly enough, to shift gears rather quickly.¹⁷ Thus, it will not surprise you to learn that we all are now becoming scholars of comparative corporation and capital market law,¹⁸ and are paying more and more attention to the institutional investor, even occasionally looking at them within the same context.¹⁹

And that—looking at comparative corporation and capital market law with a special emphasis on institutional investment—is what I propose to do in this brief talk. To be true to the announced title, I will look specifically at the emerging fragile economies of the former state-socialist regimes; though I will warn you now that the lessons I expect to take from that camp are not the obvious ones.

My thesis is this: As the current winner of the inter-systemic war, but the current loser of many intra-systemic battles, we need to recognize that capitalism is not one but a spectrum of phenomena, and that the differences between these species, within the genus of

¹⁶. Some were willing to make this effort before the results, that now seem so apparent were in. See especially Alfred Conard’s discussion of the emergence of effective capital and labor participation in corporate decision-making within European countries. Alfred F. Conard, The Supervision of Corporate Management: A Comparison of Developments in European Community and United States Law, 82 Mich. L. Rev. 1459 (1984).
¹⁸. See especially the cross-country studies, including several by American scholars, in Theodor Baums et al., Comparative Problems of Institutional Investment and Corporate Governance (forthcoming 1993).
capitalism, are rapidly becoming more important than their common
difference from state-socialism. There are several ways to view this
more differentiating assertion, and I shall briefly take us through
three of them.

Let me begin with the elegantly phrased, if hardly scholarly,
line of a recent book, *Capitalisme Contre Capitalisme*,\(^2\) that dichotomizes
capitalism into an Anglo-American or “casino capitalism” and a
Rhineland or “social-market capitalism,” or, though the French
author’s Eurocentric vision prevents him from adding it, the obvious
Japanese variant of this second category. The author, Michel Albert,
prominent in European business and government circles, argues that
our version, the casino version, is characterized by certain behavior
patterns and results: a highly individualistic concept of success, that
success being measured by financial profit concepts alone, and that
profit being defined within a short-term perspective. He identifies
the Rhenish version by its social, relatively egalitarian concept of
success, that success being measured by the achievement of collective
goals through the means of collective, rather than individual capa-
bilities, and those collective goals being defined, as a result of this
social-consensus approach, within a long-term perspective.

Now admittedly, one person’s meat is another’s poison, and an
American observer could as easily turn this French version of the
dichotomy of capitalism on its head. We would define the Anglo-
American version of capitalism as having an open-ended nature,
with the principal social collective good being a “liberty” that pro-
vides scope for autonomy and opportunity—of course, with failure
being as likely or as possible an outcome of this opportunity as
success. The Rhenish version, by contrast, may seem to an American
observer to reserve opportunity to a club characterized by its powerful
symbiotic interaction with the state, an interaction that joins gov-
ernmental and private actors in a tight, reciprocal web of identity
of interests; in short, a club that leaves non-members in a passive,
dependent condition, and, most of all, stifles the initiative that au-
tonomy and opportunity provide through open markets.

This battle of descriptions, however, is not in itself particularly
interesting. Interesting is the question of the cause and of the con-
ditions for the maintenance or change of these apparently divergent
species of the genus capitalism. Only if we understand the causal
factors of either condition can we even begin to predict future de-

velopments in each setting, let alone prescribe policies to help us attain desirable future states. The critical issue for theory is how to understand and thus to reflect on this apparently dichotomous reality. Are these respective present states of capitalism the result of voluntary, willed structures and behavior, or are they the exigent result of objective and more or less inevitable causal conditions? If the former were the case, these divergent forms indeed may continue to flourish and we will have competition between structures and behavioral patterns in the future. If the latter were the case, are not our respective present states of capitalism then only transitional ones, stages on the road to a necessarily uniform state of capitalism, a state defined, as to the critical relations of ownership and management, by public markets in shares and in control that will look suspiciously like our current, somewhat idealized version of American stock and control markets?

This latter approach is one which Marxism and the dominant form of Chicago-School Economics have in common. The first sees in the relations of production and ownership the basis from which all future states of economic life will evolve; the other sees the same universal in the relations of markets and ownership. The important point is that both, at least in their strong, reductionist forms, would see both law and even the state as superstructural variables only, impotent over the long run to halt the objectively determined evolutionary march to these respectively desired end states.

Yet, to many European legal scholars, as well as to economists and other social scientists, these currently triumphant American mainstream economics are no science at all, but, as labelled by some, simply an Anglo-ideology. 21 It almost seems as if, like the disputing washerwomen in the well-known pun, we cannot agree since we argue from different premises. The real dichotomy between these polar extremes of capitalism, and of theories of capitalism (including legal theories about corporations and markets), arises from different views of the role of structure. That is to say, it arises from differing evaluations of the ability of both private and governmental actors to define their field of operations rather than be defined by it. Another way to understand this concept of structure is to look at the role of the state and of law. Let us test this differentiating approach by reference to some American social-science views of corporations and

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21. See generally Albert, supra note 20 (comparing and critiquing the American form of capitalism).
markets that respect the insights of our dominant economic science, but are not dominated by it.

The business-history, business-sociology school of thought associated with Alfred Chandler has produced a view of American corporations and corporation law that allows for a more voluntaristic, less determinist path to their development. At bottom, his argument about that evolution, in *Strategy and Structure*, still rests on objective and exigent forces of technology as the shaping determinants of corporations and of corporate owner-manager relations. In addition, however, it emphasizes the ability of business leaders to seize their destiny and at least wrestle with these external forces, in large part by harnessing law and the state to their purposes even while they are affected by the law and the state as well as by other more objective forces.

Recent work has refined and revised this approach, and in doing so has further emphasized the role of persons and power in grappling with a supposedly intractable external reality. At the same time, this type of work suggests that much richer insights may be gleaned if we dare compare American and European organizations along this work's paradigms. Let me use Neil Fligstein's recent book, *The Transformation of Corporate Control*, as the principal exemplar of this scholarly development. He deals both with the relationship of corporations to external society, and of corporate management to its external society, the collectivity of shareholders. Fligstein argues that these relationships can best be explained (and predicted) by looking at the efforts of top management to stabilize their corporate environment in an equilibrium that is perturbed from time to time by both natural and social external forces. An element of that struggle for equilibrium is the ability of management to interact with, not just passively accept, these external forces, especially the social (i.e., the state and law) forces. "The structures that are in place now are not the products of some pure process of competition... Instead, what has come into existence is the result of a social and political process that defines and redefines markets."25

25. *Id.* at 32.
More specific, and for my purposes more interesting, is his identification of a limited number of types of corporate leadership. These types are identified by the evolution, to date, of three types of specializations suitable to the recapture of an equilibrium; namely, the production-oriented manager, the sales-oriented manager, and the finance-oriented manager. Each evolved at a specific point in time, in a social-Darwinian sense, from the effort of the enterprise to stabilize vis-à-vis a particular set of external destabilizing impulses. The production-oriented manager evolved first, the consequence of the struggle to combat ruinous competition arising from endemic overproduction during the first stages of organized capitalism in the post-Civil War era. This was a struggle that led from a first, natural stage of predatory price warfare, through cartelization and other forms of so-called loose combinations, to the tight combination of mergers. This, the period of "direct control of competition," did not succeed because governmental antitrust policies chased each substage to the next. Only with the move to a control mechanism that did not rely on direct control of competition but instead "relied on the size, integration, and relative effectiveness of the large firm as a potential threat to competitors"—in other words, only with the evolution of a production-oriented management—did a first genuine equilibrium develop during the second decade of the twentieth century. For the first time, this equilibrium was based on the creation of a shared belief among the leaders of major firms, a belief that this type of structure was the most promising one with which to achieve some control over the external environment. The relative stability of this equilibrium depended on the ability of this corporate leadership to create what organization theorists call an "organizational field of force"—that is, a surrounding ambience among the wider reaches of the business community and, to an attenuating degree, within the society at large—that accepts and even supports this pattern of corporate structure and behavior.

The important point of this business, rather than economic science-oriented analysis, is that it identifies the clash of real interests—government using antitrust weapons versus corporate leaders acting and reacting with a succession of strategies—as the motive to find a new equilibrium, and as almost sufficient to sustain it.

26. Id. at 75.
27. Id.
A similar story can be told for Stage Two, albeit in briefer form. The sales-oriented or marketing-oriented CEO emerged in response to the failure of the production-oriented leadership of American corporations to pull out of the Depression by the use of low production and stable prices. Some outsiders in the twenties had already begun to see in product differentiation, advertising, and other marketing tactics a superior strategy for recreation of a stable equilibrium in this turbulent time. This new leadership came to the fore toward the end of the Depression. Already in the ascendancy before the outbreak of World War II, this sales-oriented CEO universe dominated the corporate scene in the first post-war decades. Among its most enduring legacies was the shift to diversification of firms and away from single-sector lines of production, a step that presaged the third stage of corporate organization.  

Diversification led to a new merger wave. The horizontal and vertical aspects of this new wave soon fell afoul of the strong antitrust-enforcement climate of the period, both in its implementation by the Truman and Eisenhower administrations and in the specific effects of the passage of the Celler-Kefauver Act of 1950. This, in turn, led the way to the one path to growth that was not significantly inhibited by these constraints: the pure conglomerate aggregation. This strategy called for a different type of chief executive officer, the finance-oriented leader—the Royal Little of Textron and the James Ling of LTV. With the ascendancy of this cohort, a totally new view of the firm emerged. This view paid little attention to product or sector specificity but combed all units over the same raster of financial performance, which even in internal, let alone stock-market terms, necessarily meant relatively short-term performance. To Fligstein, both the conglomerate-merger wave of the sixties and its frenzied hostile takeover culmination of the late eighties are

28. Id. at 117-18.


30. An ironic demonstration of the ongoing search of corporate leadership for new paradigms is that the Vought Corporation, one of the linchpins of that first pure conglomerate empire, was recently reestablished as an independent firm! See Thomas Hayes, Company News; LTV to Sell 2 Divisions to Venture, N.Y. Times, Feb. 4, 1992, at D1.
simply the beginning and ending chronological markers of this stage of American industrial organization.\footnote{See Fligstein, supra note 6, at 226-30, 238-58.}

I am sure that this sequence, and perhaps even the reasons for it, are known to you, and yet I submit that this review is neither banal nor irrelevant. Each of these dominant forms of corporate organization and managerial structure carries its specific visions and capabilities of interaction with government and society, and its specific value orientation and consequent discourse with that government and that society. If we accept the correctness of this time line and causal correlation, then we accept, even for the United States, a political model of corporations, of corporation law, and of economic processes. This political reality permits the contention of real social forces, even—and this is the crux of the issue—to the point of influencing, if not determining, markets. To emphasize the obvious: It is not that Chicago-School Economics ignores political and social forces; indeed, its “rational-actor” explanations of political behavior are an important component of its analytical strength.\footnote{See, e.g., Jonathan R. Macey, Promoting Public-Regarding Legislation Through Statutory Interpretation: An Interest Group Model, 86 COLUM. L. REV. 223 (1986).} It is, rather, that that school views market processes as autonomous from and superior to social processes, and as autonomous from and superior to the role of social institutions consciously shaped to support certain social processes and suppress others. The sounder view of the world, I argue, is one that views the role of politics as the shaper of markets. This view provides an entirely different perspective from which to understand and to predict the course of economic life. Especially of note is the course of the competition between different real structures of what we too blithely assume to be “the” form of capitalistic organization of both the national and the global economy.

Let me conclude this portion of my review with an extended quotation from Kligstein’s book that drives this point home. I find it especially telling because it points toward the intra-systemic comparisons that legal scholars are beginning to undertake.

\begin{quote}
[E]conomic accounts have to downplay the social and political search for stability. . . . They also have to ignore the role of the state in defining what behavior is acceptable from firms. . . . The interpretation of the history of the corporation that stresses efficiency ignores the central fact
\end{quote}
that managers and entrepreneurs were constantly trying to escape or control competition, not engage in it. These actors were also well aware that markets were social constructions that revolved around systems of power, both private and public. As such, the rules of markets could be changed by powerful corporate actors and the government. [The market as the driving force of economic history is replaced by the variety of constructions of institutional arrangements in the economic and political spheres and by the dynamics of those arrangements. The market and the rules that govern it are the product of those interactions. This point of view] does not assume the rationality of action or some absolute standard of efficiency. There is not one most efficient mode of organization, nor is there only one way in which organizational goals can be pursued.

If the economists are right, the most efficient form will emerge in every market society either because the market will select that form or because managers will adopt it. There should be convergence in form across societies of roughly equal levels of development in the conceptions of control and the strategies and structures of the largest firms. In contrast, if the view that markets are constructed in the context of strategic interactions between firms and states is correct, such convergence should not be observed.33

Let me try to accept this challenge of comparison by briefly remarking on a few salient features of that so-called Rhenish capitalism that Albert identifies as the polar opposite of our so-called casino capitalism. It is beyond the scope of this discussion to describe the history of today’s major European corporate-sector firm structures and resultant social interaction processes, but if we focus on the principal methods of societal monitoring of those firms’ behavior and performance (their analogues to our overtouted two markets for stock and for control), we necessarily focus on the relationship of what I will call the corporate sector on the one hand and the financial sector on the other. The French state-controlled banking sector, the Japanese keiretsu arrangement of banks and firms, and the German Grossbank and Hausbank involvement with their client firms all display an

33. Fligstein, supra note 6, at 301-05.
intimate, social web of networks that seems leagues away from the robust and impersonal American style of business-society-state interaction that the Chicago School both apotheosizes and caricatures.

I turn now to some specifics of corporate governance in these systems. The principal test of the durability or at least adaptability of Rhenish capitalism will necessarily be found in the durability or at least adaptability of those networks. Therefore, a brief look at the future of that financial sector is essential, for it is that sector’s structure, and that sector’s part in this enterprise-society-state relationship, that will be the crucial determinant of the European version of our enterprise future. Not surprisingly, it is on this terrain that proponents of the Anglo-American form of modern capitalism are trying to force through Brussels and the European Community liberal directives and regulations, like the still-pending Thirteenth Draft Directive on Takeovers that would enshrine that form. It is likewise on this terrain that the individual member states and their firms are still successfully resisting.

If the world of corporations were nationally bounded, it would be easier to predict an outcome close to Fliistain’s thesis of non-convergence. But it is not, at least not in relative terms. The great anomaly is the difference between these nationally bounded product and (traditional) service markets, and the increasingly global nature of the most important modern service market, the financial market. I have argued that private firm actors and public governmental actors have the will and the way to maintain corporate structures in a mutually desired, typically national economic setting. The evidence suggests current success in doing so despite the movement towards a larger European regional market identified with “Europe 1992.” However, current financial markets—and in American terms that

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34. For examples of recent scholarship focusing on these institutions and their relationship to corporate governance, see Theodor Baums, Corporate Governance in Germany: The Role of the Banks, 40 Am. J. Comp. L. 503 (1992); Gilson & ‘Roe, supra note 19. See also Roe, supra note 12, at 6-13 (briefly discussing the role of the German banks).


36. See supra note 30 and accompanying text.
includes capital markets if not also markets in corporate control—not only are already regional, they are now global. The new fund transfer technologies mock national boundaries, and the new institutional investors have the means and certainly the appetite to graze abroad almost as readily as at home. It hardly seems possible that a nationally specific form of corporate organization can withstand the levelling power of international financial flows through international financial intermediaries.

On the other hand, the premise on which that anomaly is founded may be wrong, or at least eroding. Compared with those of the United States, the national financial firms of Europe are much fewer in number, much more oligopolistically organized, and, paradoxically, because of the prevalence of universal banking and its merger of investment and commercial banking functions, much less exposed to so-called outsider competition. Indeed, my economist colleague Albert Fishlow has suggested that one of the more important consequences, and therefore perhaps intentions, of the Cooke Committee and the Basle Accord’s setting of stringent and uniform standards of capitalization for the banking sector world-wide, is the maintenance of traditional discipline among banks as they continue or at most carefully adapt their traditional governance relations with the private firm sector.

Of course, the jury is still out on the success of this effort to hold the financial sector to the same minimal structural conditions necessary to permit firm-state interaction to function as continue to hold in the corporate sector. Not all major banks are maintaining this discipline, a feature particularly noticeable in the case of some of the smaller East Asian countries’ banking sectors. Furthermore,

37. The directives of the European Community in this sector, in contrast to the corporate sector, have done their share to create a transnational, liberal structure. On the banking directives, see Uwe Schneider, The Harmonization of E.C. Banking Laws: The Euro-Passport to Profitability and International Competitiveness of Financial Institutions, 22 LAW & POL’Y Intr’L Bus. 261 (1991).

On the more troubled and still incomplete effort to enact the analogous directives liberalizing the financial services industry (e.g., investment banking, underwriting, funds creation, and management), see Gerhard Wegen, Transnational Financial Services—Current Challenges for an Integrated Europe, 60 FORDHAM L. REV. 91 (1992); Roberta Karmel, The Market 2000 Study, N.Y.L.J., Oct. 15, 1992, at 3.

it is doubtful whether the totally different American commercial and investment banking sector, still more or less internally segregated despite the erosion of the Glass-Steagall barrier,\textsuperscript{39} will evolve to a similar structural situation. The inevitable merger wave now consolidating the United States financial sector has a long way to go before it can possibly fit the minimum conditions for the imposition of that kind of discipline, even assuming our cultural and historical conditions would generate the mind-set that would readily entertain such a sea change in habits and practices.\textsuperscript{40} Further some barely noticed European developments may also militate against the capture of the new financial world by the old. For example, the modern German economy’s amazing ability to operate with only a fraction of its firms exposed to capital markets—a special feature of its niche economy and a necessary, indeed critical feature of Albert’s Rhenish capitalism—may be in jeopardy as the first generation of heirs with much wealth excessively concentrated in their founders’ family firms pushes for greater liquidity and diversification. But all in all, the possibility certainly exists for European business organizations to weather current liberalization and globalization tendencies, and to maintain the kind of symbiotic state-private sector relationship that marks that version of capitalism.\textsuperscript{41}

We have now surveyed these two major regional bloc economies to determine whether the American picture is timeless and inevitable, or is changeable and changing. We have seen that even within the American setting rival explanations of this picture are credible, explanations with quite different predictions for the future. We have looked at some of the evidence supporting the view that private firms have more power to maintain themselves against the supposed exigencies of markets, or at least to buy the time to try to adapt and create new equilibria. (I should add, digressing, that, obviously, defending against the market in takeover or other efficiency-monitoring terms by reincorporating in Pennsylvania,\textsuperscript{42} is not the same

\textsuperscript{39} Ch. 84, 48 Stat. 162 (1933) (codified as amended in scattered sections of 12 U.S.C.).


\textsuperscript{41} See, e.g., Gutachten der Monopolkommission 1988/1989, Hauptgutachten Nr. 8 (Bundestag Drucksache 11/7582) (underlying information suggesting this result), and the astute analysis in Roe, supra note 40.

\textsuperscript{42} Pennsylvania is a popular state for reincorporation because of its extreme antitakeover statute. 15 PA. CONS. STAT. ANN. § 2571 (Purdon Supp. 1991).
thing as being forever immune from market reaction to your goods and services; even General Motors cannot face too many years of multi-billion dollar losses without changing radically or going under). Finally, we have noted that the single most critical variable in this story is likely to be the degree of separation between the directions and rates of change of corporate sectors and of financial sectors. The reason why that is important is not that one type of financial sector would monitor corporations and another would not, but because changes in the financial sector's organizational patterns may disrupt older forms of relationships between corporations and their financial (and monitoring) institutions.

This brings me to the second of the new legal scholarship's concerns—the new institutional ownership. It is this last point, this role of financial markets and financial actors as corporate monitors, that makes the role of institutional investment in this story so important and so fascinating. As I have pointed out elsewhere, the portfolio ownership of firms by institutional investors as such is not new.43 What is new is the further transfer of ownership from traditional intermediaries like banks directly to the beneficiaries or ultimate owners of these financial assets. Alternatively, if ownership is not vested with these ultimate beneficiaries, then it is vested with other types of intermediaries whose relationships with the corporations in which they invest are less symbiotic and less intimate than are these traditional relationships. From the perspective of this discussion, then, we need to ask whether this major, indeed predominant new form of portfolio investment in equities (and for that matter, given their potential use in corporate governance situations, in debt securities) may be a major influence on the current efforts of the leadership of the corporate sector to create a new equilibrium in the relation of firms and firm management with firm owners and society.

I will not belabor the point that the new institutional investment is a major if not predominant component of all investment in the equity and debt securities issued by private firms. The figures are sufficiently well known. Using the most recent compilation from the

43. See Buxbaum, supra note 13.
Columbia Law School Institutional Investor Project, we find institutional investors holding over $6.5 trillion in assets in 1990, and controlling over fifty percent of United States-issued equities and over twenty percent of all financial-paper assets issued by United States firms. We find the largest of them, the public-sector pension funds, which comprise approximately twelve percent of all institutional investments and fourteen of the top twenty pension funds, moving heavily to indexation strategies of investment. Because of that strategy, public-sector pension funds are taking a considerable position in the equities of foreign issuers to the tune of $4 billion in 1990 for TIAA-CREF and almost that much for CalPERS. We find not only a huge but also, in certain ways, a highly concentrated form of institutional investment. Thus, the top twenty pension funds (fourteen of them public) hold nearly forty-five percent of all pension fund assets; the actual management of these funds, because of the structure of the financial-advisor industry, is even more concentrated.

In short, at least in the United States, and to a growing degree elsewhere, wherever capital markets are open and large enough to absorb the investment, these new types of institutional investors, the public-sector and the private-trusteed pension funds, have entered the ranks of ownership of corporations with a weight and in a manner that was bound to disturb preexisting owner-manager relations. After all, what matters is not the amount of equity owned by owners—a quick calculation suggests this is 100%—but the relative specificity and individual proportionality of ownership in both its direct and its variously intermediated forms.

So we come to what I believe is the critical issue: How will America’s corporate-sector leaders, in their understandable and in-

45. See Buxbaum, supra note 13, at 14.
46. Id. at 16, 17 n.60.
evitable effort to reestablish stability and control over this newly perturbed external environment, respond to this new ownership? My guess, and it is a guess, is that the corporate sector, just as it has triumphed over or at least reached a favorable accommodation with America’s traditional investment and commercial banking sectors, will reach an accommodation with the new institutional investment sector. It will confirm the political rather than the economic version of the theories I have sketched in this talk, but it will move to a new form of stability and control over its fractious environment that is subject to both old and new constraints. The old constraints arise from the particular economic and social condition of this nation, both historically and culturally expressed; namely, the size and diversity of the country and its markets, the demographic structure of its population and workforce (especially in its racially specific context), the fading remnants of its populist, anti-power ideology, and—I dare not ignore this in front of a Delaware audience—its federal form of government. All these old constraints will set specific limits on the shape of the next stage of this search for stability. 47

Of at least equal relevance, but harder for both actors and observers to factor in specifically, are the new constraints; namely, our new global environment and our new global competition. More exigent and of less affinity to the American corporate-sector setting than are our domestic governmental and societal pressures, these new elements demand more innovative corporate structures, culturally more difficult to achieve than any of the production-driven, marketing-driven, or finance-driven structures we have experienced during the past century.

I submit that our search for them not only is to a great extent compelled by developments in Europe and Asia, it can to some extent learn from those foreign developments. If the closer business-state relationships of those societies make them more suitable to the kind of economic structure the new international environment and the new international economy require, then our own search for a new structure, which in any event is tending towards these more symbiotic relationships, is bound to be influenced by that success. In this search for a new stability, an accommodation by old managers with their new, institutional owners, one consonant with our cultural context

and at least not dysfunctionally imitative of the European or Asian cultural context, will be critical.

Professor Garfield recently examined the problem of worker dislocation in our society. This problem is alleged to arise particularly from "bustup" takeovers; the reality is that it is caused by a much larger and deeper set of problems.48 Addressing labor interests directly, he pointed to the virtues of Rhenish Capitalism in creating a kinder and gentler economy.49 Whatever one may believe about the accuracy of that correlation, it can only fit our setting, if it fits at all, through the medium of, and with the cooperation of, pension-based institutional investors. Indeed, one could argue, and I have tiptoed towards that argument elsewhere, that both the private-trusteed and the public-pension fund comprise today's union sector, but are less adversary and more intermeshed with today's management sector than its fading prototype.50

We know the first arguments about that sector's participation in corporate structure and decision-making processes. Indeed, a recent contributor to this journal, our esteemed colleague Al Sommer, foresaw, though abhorring rather than welcoming them, some operationalized versions of that accommodation, such as constituency directorships.51 We know of the increasing interest in shareholder advisory committees,52 and we have seen recent efforts to obtain some modest proxy reforms for institutional investors53 (whose recent

48. Alan E. Garfield, Helping the Casualties of Creative Destruction: Corporate Takeovers and the Politics of Worker Dislocation, 16 J. CORP. L. 249 (1991). Professor Garfield argues that takeover dislocation is no different than employee dislocation in general. Id. at 276. The problem, he asserts, stems not from takeovers, but from managerial decisions that adversely affect employees. Id. at 276-77.

49. Id. at 297-98 (quoting commentary of Robert Reich, Marketplace (American Public Radio, July 2, 1990) (cassette)).

50. Buxbaum, supra note 13, at 40-41, 53.


52. See William Taylor, Can Big Owners Make a Big Difference?, 68 HARV. Bus. Rev. 70 (Sep.-Oct. 1990). Taylor argues that although this mechanism of collective action may improve public elections by fostering informal communication among shareholders, it would likely be ineffective in improving corporate performance due to a lack of expertise among its members. Id. at 80-81.

defeat by the Business Roundtable,\textsuperscript{44} incidentally, is a wonderfully ambivalent bit of evidence as to the validity of the political version of a theory of corporations). We also have seen a specific effort to permit the use of the federal shareholder proposal channel to allow nomination of a minority of candidates for the board of directors.\textsuperscript{55} In short, though I can hardly go into this in any detail here, this effort to recreate a stable environment is underway, and institutional investors are both a major target and a major player in that effort.\textsuperscript{55}

Before closing with my long-deferred turn to the former Socialist Camp, let me mention one component of this political version of enterprise-state accommodation that is unique to the United States. It is—I can hardly avoid this in Delaware—the role of the courts. In the United States, that country of courts and parties,\textsuperscript{57} courts more than any other governmental institution expressed the state’s response to the corporate sector’s drive for stability.\textsuperscript{53} When antitrust was the state’s response to the first effort to stabilize via cartels and mergers, it was the courts, not the relatively empty generalizations

\textsuperscript{54} Business Roundtable v. SEC, 905 F.2d 406 (D.C. Cir. 1990). The court struck down a SEC rule which would have barred national securities exchanges and associations from providing lists of corporations which impinged on the per-share voting rights of common shareholders.


A separate but critical issue concerns the motives and modalities of the monitoring of corporate managers by institutional investors. For a first effort actually to identify efforts and results, see Bernard S. Black, \textit{The Value of Institutional Investor Monitoring: The Empirical Evidence}, 39 UCLA L. Rev. 895 (1992). His conclusion is that institutional oversight may be a useful tool in correcting various shortcomings in corporate performance. \textit{Id.} at 931-32.

\textsuperscript{57} STEPHEN SKOWRONEK, \textit{BUILDING A NEW AMERICAN STATE} 24 (1982). The author discusses the central role of courts and political parties in the formation of the national state. \textit{Id.}

of the Sherman Act itself, that defined the state’s response.\textsuperscript{59} Now that the state has responded to the flood of hostile takeovers, it is the courts that have defined that response. It was neither the Illinois statute of \textit{Edgar v. MITE Corp.}\textsuperscript{60} nor the Indiana statute of \textit{CTS Corp. v. Dynamics Corp.},\textsuperscript{61} but rather the Supreme Court’s legislative use of the commerce clause that set the stage for state supremacy in this area. Similarly, it was not the generalizations of the Delaware takeover statute\textsuperscript{62} but the Delaware Supreme Court’s common-law legislation in \textit{Paramount-Time}\textsuperscript{63} that awarded round one in this new stage to management over shareholders.

I am sure most of you have been if not fully convinced, then at least intrigued, by Professor Gordon’s recent socio-historical stab at psychoanalyzing your supreme court.\textsuperscript{64} Even if he intimates that the Delaware Bar must view the \textit{Paramount-Time} decision much as dentists viewed the development of fluoride, I am glad he disparages the old saw that the courts decide as they do in order to serve the interests of the bar. I am, admittedly, not sure that this audience likes his explanation of the court’s decision any better; but whether or not you agree with his theory that only their recoil from Gordon Gekko explains its members’ decision in that case,\textsuperscript{65} I share with him the belief that to the senior executives of our important corporations the Delaware court is as much an addressee of their efforts to regain their control over this turbulent environment as are other governmental and social actors and institutions.

What is unique about this particular addressee, and what complicates the political resolution of this search for a new stability, is the accident that the internal affairs doctrine accidentally allows the Delaware courts to exercise what, with all due respect, one must

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\item See, e.g., United States v. Trans Mo. Freight Ass’n, 166 U.S. 290 (1897) ("rule of reason" inapplicable to Sherman Act § 1 violations); United States v. E.C. Knight Co., 156 U.S. 1 (1895) (manufacturing not commerce under Sherman Act). See generally HANS B. THORELLI, \textit{THE FEDERAL ANTITRUST POLICY: ORIGINATION OF AN AMERICAN TRADITION} (1955) (discussing the origins and development of American antitrust policy). On the analogous more recent experience with the Anti-Merger Act of 1950, see the cases and materials cited supra note 29.
\item 457 U.S. 624 (1982).
\item 481 U.S. 69 (1987).
\item Paramount Communications, Inc. v. Time, Inc., 571 A.2d 1140 (Del. 1989).
\item See, e.g., Roe, supra note 12.
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call a kind of squatter sovereignty in this enormously important political arena.\textsuperscript{66} With both federal and other large and populous states' vital interests at stake, this accidental doctrinal feature can serve our mutual search for stability only so long as the Delaware courts can divine and express the barely emerging and by no means settled societal consensus on these issues. What is even more daunting is that they must do so without disclosing this search.\textsuperscript{67} That is indeed a challenge, and I envy you for your participation in its conquest.

Are the lessons from the former Socialist Camp now clear? In the previously mentioned article, Professor Garfield concludes with this observation: "In light of the recent collapse of communist systems in Eastern Europe, it may seem strange that this Article would recommend increased social intervention into the labor market."\textsuperscript{65} Hopefully, my review of Rhenish Capitalism and of the political/sociological explanation of the American corporate sector has been persuasive. If so, it will not surprise you if, in their emergence into the light of capitalism, these societies will quickly learn the critical lesson: that a new democracy cannot survive a state attempt to impose Anglo-American casino capitalism on a fragile economic system. Of course, new energies are unleashed with the turn to a liberal economic order, and, of course, the first act of the new regimes is to turn the former Central Committee Headquarters into the stock exchange. However, those new liberal/economic and democratic/political orders will only collapse into a landrush chaos followed by authoritarian government if their private and state sectors do not reach accommodation along the Rhenish model of capitalism. This is 1992 not 1875, and neither our post-Civil War nor Europe's post Franco-Prussian War developments can be replicated in an Eastern Europe situated among advanced Rhenish capitalist societies.

Western Europe's political and business leadership assumes as much, even if some of its private-sector players are among the first ranks of the landrush contingent. Indeed, Western Europe may see to it that the Rhenish model is implanted to its East for very good

67. The political-science literature concerned with the United States Supreme Court's expenditure of the currency of political legitimacy might now, for the first time, be relevant to the situation of a state court with this much common-law discretion within the nominal framework of an open-textured statute. See Melvin Eisenberg, The Nature of the Common Law 8 (1988).
68. Garfield, supra note 48, at 296-97.}
geopolitical and global economic reasons. Only recently the *New York Times* published an excerpt from a book by, of all people, Jacques Attali, president of the Group of Paris's European Bank for Reconstruction and Development. The excerpt reads as follows: "If Western Europe is able to link Eastern Europe with its development, an integrated Europe has a chance to assume the role of the center of the world economy."\(^{69}\) To drive the point home, this reference was intended to serve as a blueprint for the contingency that the Uruguay Round GATT talks would fail. With that failure, the last chance for the imposition of the Anglo-American vision of a liberal global economic order on the world trade in goods and services—*nota bene* in financial services—would disappear.

Given this news from the Eastern Front, it behooves us to take seriously the argument that we should understand the economic organization of the United States in political terms. In my academic corner of public debate, explanations and investigations that pay due attention to this side of theory and less attention to its ahistorical and abstract side are on the ascendant.\(^{70}\) I hope they also will be more useful to policymakers, bench, and bar as they confront these turbulent and uncertain times.

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70. See Roe, *supra* note 12; and Roe, *supra* note 41.