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William Wilson Bratton

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Reuven Avi-Yonah's "Citizens United and the Corporate Form": Still Unuseful

William W. Bratton

Abstract

I welcome Avi-Yonah's new deployments of descriptive theories of the corporation. But I traversed this territory years ago and came away with a skeptical view of the enterprise. Although Avi-Yonah's interventions are compelling in the encounter, I remain unconvinced that the theories have important lessons to teach us.

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Reuven Avi-Yonah (2011; Avi-Yonah hereafter) wants to revive historical theories of corporate personality and persuade us that they possess descriptive and normative traction.¹ "*Citizens United* and the Corporate Form" is the second in what looks to be a series papers in this pursuit.

Avi-Yonah describes the history of the corporation as a four stage evolution: (1) the long trip from Roman times to the appearance of the membership corporation in the late middle ages; (2) the emergence of for-profit corporations in England and the United States in the late eighteenth and early nineteenth centuries; (3) the rise of public corporations with limited liability and jurisdictional choice in the United States at the end of the nineteenth century; and (4) the late twentieth century appearance of multinationals.

He situates descriptive theories of the corporation in this evolutionary account as follows:

Each of these four transformations was accompanied by changes in the legal conception of the corporation. What is remarkable, however, is that throughout all of these changes spanning two millennia, the same three theories of the corporation can be discerned. Those theories are the aggregate theory, which views the corporation as an aggregate of its members or shareholders; the artificial entity theory, which views the corporation as a creature of the State; and the real entity theory, which views the corporation as neither the sum of its owners nor as an extension of the state, but as a separate entity controlled by its managers.

Each of the three theories came to the fore at each point of transformation, but, says Avi-Yonah, but "the real entity view always won and was the established view during periods of stability."

I welcome Avi-Yonah's new deployments of descriptive theories of the corporation. But I traversed this territory years ago and came away with a skeptical view of the enterprise.² Although Avi-Yonah's interventions are

¹ See also Reuven S. Avi-Yonah, The Cyclical Transformations of the Corporate Form: A Historical Perspective on Corporate Social Responsibility, 30 Del. J. Corp. L. 767 (2005).

² See William W. Bratton, The "Nexus of Contracts" Corporation: A Critical Appraisal, 74 Cornell L. Rev. 407 (1989); William W. Bratton, The New Economic Theory of the Firm: Critical Perspectives from History, 41 Stan. L. Rev. 1471 (1989).

compelling in the encounter, I remain unconvinced that the theories have important lessons to teach us.

When once again confronting these theories, the first thing I do is reread John Dewey's *The Historic Background of Corporate Legal Personality*,³ which for me serves as the definitive text on the subject matter. Dewey, like Avi-Yonah, addressed a long series of philosophical and legal debates on the question whether associations are in essence artificial or natural. Dewey claimed a consequentialist justification for his intervention. The whole line of inquiry, he said, was causing perverse effects in legal practice. Philosophical ideas and dogma had found their way into law with obstructive results.⁴ Dewey administered a strong dose of realist critique. The discussants, he said, wrongheadedly tried to "induce unity into a conception where the facts show utmost divergence."⁵ They deployed theories that, first, yielded no determinate results (each theory "has been used to serve the same ends, and each has been used to serve opposing ends"⁶), and, second, figured into policy debates largely as *ex post* rationalizations for the discussants' positions.⁷ At a descriptive level the debate was not even particularly interesting: Corporations and other associations had an obvious social reality.⁸ That point being established, the thing to do was analyze the facts respecting given specimens of the breed, identifying "whatever specific consequences flow from the right-and-duty bearing units."⁹

Dewey's analysis implied a devastating critique of a theory of the firm much in circulation at the time. That theory, "corporate realism," drew on European ideas¹⁰ about the spiritual reality of group life to assert that the corporate entity was real and group dynamics were more significant in practice than individual contributions. Important implications had followed for the large, mass-producing corporations that had suddenly appeared in the American economy around the turn of the century. The new management-dominated corporations had reconstituted the profit-maximizing individual of classical economic theory in a collective form. Since individuals and not the state supplied the creative force that brought corporate groups into existence, respect for individuals counselled against regulation. Corporate realism, a theory of group

³ John Dewey, *The Historic Background of Corporate Legal Personality*, 35 Yale L.J. 655 (1926).

⁴ Id. at 655-56, 657.

⁵ Id. at 671.

⁶ Id. at 669.

⁷ Id. at 663.

⁸ Id. at 673.

⁹ Id. at 661.

¹⁰ See Otto Gierke, *Political Theory of the Middle Age* i-xlv (F.W. Maitland trans. 1900). In the United States, the theory's most prominent advocate was Ernst Freund. Ernst Freund, *The Legal Nature of Corporations* (1884).

production without state control, provided an important source of intellectual justification for the mass production firm.¹¹

Yet corporate realism disappeared without a trace after the publication of Dewey's essay. Henceforth, with Dewey, legal theory would treat corporations as reifications and address itself to their economic and social consequences. Thus did corporate legal theory spend the succeeding half century focusing on Berle and Means,¹² the separation of ownership and control, and project of grappling with corporate economic and social power.¹³

Avi-Yonah has read his Dewey and so reconstitutes the real entity even as he revives it. We hear nothing of the spiritual reality of group life and instead get the corporation as Dewey left it to us and Berle and Means described it, an institution with important economic and social consequences. Avi-Yonah takes the additional step of folding managerialism into the real entity thus constituted, much as Morton Horwitz did twenty five years ago.¹⁴ The emerging concept is notably capacious. Where the corporate realism rejected by Dewey remains in eclipse, we can identify Avi-Yonah's new version of realism in contemporary decisions and commentaries, just as we also can identify aggregate and artificial entity notions.

I stick with Dewey even so. In fact, it is hard to see any break with Dewey here. It is unsurprising that the real entity, as Avi-Yonah describes it, wins out today. We are all realists now and social and economic consequences accordingly have a way of trumping juridical notions. The managerialist corporation also persists, even as it undergoes constant attack.

But I do not it helpful to attribute the managerialist corporation's persistence to the fact that it is "more real," and then to point to the limitations of the aggregate and artificial entity notions. Surely something else must be going on.

In my view, that something else is a post-Dewey discussion about economic and social consequences. To see this discussion in action, consider the one moment post-Dewey when descriptive theory of the firm became an issue. That was the "nexus of contract" interval in which Chicago law professors¹⁵ took

¹¹ See Morton J. Horwitz, *Santa Clara Revisited: The Development of Corporate Theory*, 88 W.Va.L.Rev. 173, 176, 224 (1985).

¹² Adolf A. Berle, Jr. & Gardiner C. Means, *The Modern Corporation and Private Property* (Macmillan reissue 1933).

¹³ See William W. Bratton, *Berle and Means Reconsidered at the Century's Turn*, 26 J. Corp. L. 737 (2001).

¹⁴ See Horwitz, *supra* note 10.

¹⁵ See Frank H. Easterbrook & Daniel R. Fischel, *The Economic Structure of Corporate Law* (1991).

Jensen and Meckling's agency cost theory¹⁶ and attempted to assert an aggregate description on an absolute basis. Now, strictly speaking, Chicago did not peddle the aggregate theory of centuries past, under which there is no reality in and around corporations other than that incident to the human beings. Chicago cared less about the individual subjects than the contracts they make and the markets in which the contracts are traded, and the implications that contracts and markets had for progressive and regulatory notions inherited from Berle and Means. These normative motivations led the Chicagoans to proceed with their case in the teeth of manifest descriptive short-comings: They argued that corporations were just voluntary contracts even as anybody could open a law book and identify mandates and outline a juridical entity. Viewed narrowly, the debate accordingly did present an issue of aggregate versus artificial entity. But the outcome was not determined in that framework.

The question was normative: Even if the juridical corporation is not presently a nexus of contracts, should corporate law be reconstituted to make it so? The answer was "no" by reference to economic factors – management power and the shareholder collective action problem prime among them. At this stage, Avi-Yonah fairly could insert his revised real entity characterization – the management corporation beat back the nexus of contracts. I do not find the characterization helpful, however. Reality – continued management dominance – matters little *per se* in these normative discussions. The question goes to functionality and counterfactual possibilities for enhanced productivity, and the answer is contestable. Indeed, the contest has continued ever since. And even if the juridical management corporation has survived unscathed, shareholder empowerment has been a growth proposition at the level of practice.¹⁷ I would not call this a shift to an aggregate corporation. The legal artifice is still with us, as is the salient institution.

The same observation applies to the methodological outcome of the nexus of contracts debate. Even as the corporation turned out to be something more complex than a nexus of contracts, Chicago won its point at a methodological level – microeconomic analysis and agency theory gained general currency. This happened because individual incentives rose to descriptive prominence and market controls were thought more effective than government controls as means to the end of wealth creation. One certainly could characterize this as a shift to an aggregate view, but the motivations would get lost in the translation.

I also continue to accept Dewey's indeterminacy point. Yes, social and economic consequences control, but once one takes the various descriptive

¹⁶ Michael Jensen & William H. Meckling, Theory of the Firm: Managerial Behavior, Agency Costs and Ownership Structure, 3 J Fin. Econ. 305 (1976).

¹⁷ See William W. Bratton & Michael L. Wachter, The Case Against Shareholder Empowerment, 158 U. Pa. L. Rev. 653 (2010).

perspectives on corporations and translates them into doctrinal statements, an ambiguous mess always results. Avi-Yonah's presentation of recent Supreme Court cases and the comings and going of the theories within them nicely bears out this point. However persuasive his account, I tend to find myself adding a gloss of further complication, case by case. Where Avi-Yonah finds one theory motivating a given opinion, I tend to find two; if he finds two, I can find three.

For example, Avi-Yonah sees *Citizens United*¹⁸ as a rare case in which both sides devolve on real entity theory, fighting not over the description but its divergent implications for the first amendment. But I see multiple descriptive theories cropping up in both of the lead opinions.

I read Justice Kennedy's opinion less as a description of the corporation with first amendment implications, than as an aggressive description of first amendment values with implications for the constitutional treatment of corporations. And, since the values import the motivation, the less said about corporate reality the better, because the more detailed the description of what corporations do and the power and money they possess, the less persuasive the presentation. In any event, this is a two-out-of-three, with all three acknowledged. Artificial entity is explicitly rejected, as it must be.¹⁹ Corporations are indeed seen as real, fully personified entities with "voices and viewpoints."²⁰ But there is also an emphasis on individual association, the statue in question being seen as a "ban on the political speech of millions of associations of citizens."²¹ Now, technically, mention of "associations" can be cabined into conceptual framework of early twentieth century corporate realism. But the exercise makes little sense here. Those early twentieth century theories figured into the larger super structure of corporatism and a state built on group rather than individual participation. In contrast, methodological individualism dominates in contemporary Supreme Court opinions respecting first amendment rights. Thus does the majority opinion cite associations with a view to the individual right to associate, an aggregate move. The opinion wants to cover both bases – the collective and the individual.

As for the dissent, there certainly is plenty of economic and social reality on offer. But Justice Stevens also makes a classic artificial entity move in the very excerpt from which Avi-Yonah quotes – campaign finance distinctions "based on corporate identity tend to be less worrisome because the 'speakers' are not natural persons, much less members of our political community, and governmental interests are of the highest order."²² Alternatively, try this passage from the dissent: "...[C]orporations have no consciences, no feelings, no thoughts, no

¹⁸ *Citizen United v. Federal Election Comm'n*, 130 S.Ct. 876 (2010).

¹⁹ 130 S.Ct. at 900.

²⁰ 130 S.Ct. at 907.

²¹ *Id.*

²² *Id.* at 947.

desires. Corporations help structure and facilitate the activities of human beings, to be sure, and their 'personhood' often serves as a useful legal fiction."²³

The shareholders also show up in the dissent, when it makes the familiar point that shareholders "who disagree with the corporation's electoral message may find their financial investments being used to undermine their political convictions."²⁴ Strictly speaking, this is not aggregate theory, because aggregate theory asserts that there is no there, there other than the people, and Justice Stevens is making no such assertion. But Avi-Yonah deploys the aggregate concept more loosely, enough so as to pick up this bit of argumentation.

We see this in his discussion of takeover era cases. He sees the shareholder protective line taken by Justice White in *Edgar v. MITE Corp.*²⁵ as a reflection of an aggregate view, and carries the characterization over to the choice posed in *Paramount Communications, Inc. v. Time Inc.*,²⁶ with anti-takeover argumentation falling on the real entity side and pro-takeover on the aggregate side. It is a valid characterization, but a broad one. Outside of the Chicago School, no one during the takeover era thought the shareholder side of the issue implied a denial of the salience of the corporate entity. The stakes instead went to value, agency costs, and juridical structure. And juridical structure figures importantly in the Delaware courts' management-favorable responses, which accordingly stand for artificial entity as well as real entity. The Delaware courts finessed important and largely intractable questions about management and shareholder power and values at stake by reference to the doctrinal framework. The doctrine vested the business plan with management and the law was the law, whatever the contrary implications of agency theory. Forced to choose between the artificial and the real in their opinions of the era, I would go with the artificial as the motivating theory.

However, as noted earlier, I would just as soon omit the inquiry altogether and proceed directly to a more particular description of the factors in play.

²³ Id. at 972.

²⁴ Id. at 977.

²⁵ 457 U.S. 624 (1982).

²⁶ 571 A.2d 31.

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Lawrence E. Mitchell, *George Washington University*

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