The Legitimation of Shareholder Primacy

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I am grateful for the comments of Usha Rodrigues, the participants in the Michigan Law and Economics Workshop, the Tulane Corporate and Securities Roundtable, the Seattle University Faculty Development Workshop, and the National Business Law Scholars Conference, as well as for the research assistance of Zach Stevenson.

Abstract

We are living in a particularly polarized era, and corporate governance is no exception. With controversies raging over "environmental, social, governance" (ESG) investing, diversity, equity, and inclusion initiatives, climate change as an investment concern, and even Elon Musk's pay package at Tesla, it seems as though corporate governance has never been so starkly divided along partisan lines. The divisions have threatened to spill over to Delaware, the preferred jurisdiction for incorporation in the United States. Several high profile cases-including those involving Elon Musk-have called Delaware's neutrality into question. Commenters have argued that Delaware's newly-politicized approach threatens to splinter the corporate governance universe, driving corporations to other states that are more reliable (or that follow different corporations' preferred politics). This Article argues that, in some ways, the critics are correct: Delaware law is on a path toward politicization. But it is not because of any particular bias of its judges or its law; to the contrary, the pressures toward politicization are inherent in any system that purports to guide how vast aggregations of capital will be deployed. What is unique about the current moment is that the trends toward politicization result from tensions inherent in shareholder primacy. Shareholder primacy was conceived, in large part, as a compromise to keep politics out of business management; what the modern controversies reveal is the futility of that effort.

Keywords: corporations, delaware, esg, corporate social responsibility

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by Ann M. Lipton*

Abstract

We are living in a particularly polarized era, and corporate governance is no exception. With controversies raging over "environmental, social, governance" (ESG) investing, diversity, equity, and inclusion initiatives, climate change as an investment concern, and even Elon Musk's pay package at Tesla, it seems as though corporate governance has never been so starkly divided along partisan lines.

The divisions have threatened to spill over to Delaware, the preferred jurisdiction for incorporation in the United States. Several high profile cases – including those involving Elon Musk – have called Delaware's neutrality into question. Commenters have argued that Delaware's newly-politicized approach threatens to splinter the corporate governance universe, driving corporations to other states that are more reliable (or that follow different corporations' preferred politics).

This Article argues that, in some ways, the critics are correct: Delaware law is on a path toward politicization. But it is not because of any particular bias of its judges or its law; to the contrary, the pressures toward politicization are inherent in any system that purports to guide how vast aggregations of capital will be deployed. What is unique about the current moment is that the trends toward politicization result from tensions inherent in shareholder primacy. Shareholder primacy was conceived, in large part, as a compromise to keep politics out of business management; what the modern controversies reveal is the futility of that effort.

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I. Introduction

We are living in a particularly polarized era, and corporate governance is no exception. Though corporate law has always been deployed to promote various preferred policies,[1] it has rarely been as blatantly partisan as it is today. Specifically, with controversies raging over "environmental, social, governance" (ESG) investing,[2] diversity, equity, and inclusion initiatives,[3] climate change as an investment concern,[4] and even Elon Musk's takeover of Twitter[5] and his pay package at Tesla,[6] it seems as though corporate governance has never seemed so starkly divided along partisan lines.[7]

The divisions have threatened to spill over to Delaware, the preferred jurisdiction for incorporation in the United States. For over a century, Delaware has dominated the market for corporate charters, in large part – it is argued – because of its commitment to nonpartisanship in the development of its law.[8] Nonetheless, several high profile cases – including those involving Elon Musk – have called Delaware's neutrality into question.[9] Commenters have warned that Delaware's newly-politicized approach threatens to splinter the corporate governance universe,

[1] *E.g.*, William W. Bratton & Michael L. Wachter, *Shareholder Primacy's Corporatist Origins: Adolf Berle and the Modern Corporation*, 34 J. Corp. L. 99 (2008); Kent Greenfield, *Proposition: Saving the World With Corporate Law*, 57 Emory L.J. 948 (2008); David G. Yosifon, *The Public Choice Problem in Corporate Law: Corporate Social Responsibility After* Citizens United, 89 N.C. L. Rev. 1197 (2011).
[2] Saijel Kishan, *What Is ESG Investing and Why Is It Under Fire?*, Bloomberg (Apr. 22, 2024), https://www.bloomberg.com/news/articles/2024-04-22/what-is-esg-investing-what-are-the-risks-and-why-is-it-facing-a-backlash.
[3] Joseph Pisani & Chip Cutter, *The Activist Pushing Companies to Ditch Their Diversity Policies*, Wall St. J. (Aug. 3, 2024), https://www.wsj.com/business/the-activist-pushing-companies-to-ditch-their-diversity-policies-aeb82873.
[4] David Gelles, *How Republicans Are 'Weaponizing' Public Office Against Climate Action*, N.Y. Times (Aug. 5, 2022), https://www.nytimes.com/2022/08/05/climate/republican-treasurers-climate-change.html.
[5] Ann M. Lipton, *Every Billionaire is a Policy Failure*, 18 Va. L. & Bus. Rev. 327, 344-45 (2024).
[6] Anan Ashraf, *Investor Naval Ravikant Threatens To Sell All Tesla Holdings If CEO Musk's Pay Plan Is Rejected But Says He'll Buy More If Approved*, Benzinga Newswire (June 10, 2024).
[7] Stephen M. Bainbridge, *Corporate Purpose in a Populist Era*, 98 Neb. L. Rev. 543 (2020)
[8] Ofer Eldar & Gabriel Rauterberg, *Is Corporate Law Nonpartisan?*, 2023 Wis. L. Rev. 177; Brian D. Feinstein & Daniel J. Hemel, *The Market Value of Partisan Balance*, Nw. U. L. Rev. (forthcoming), https://papers.ssrn.com/sol3/papers.cfm?abstract_id=4890129.
[9] *See, e.g.*, William P. Barr & Jonathan Berry, *Delaware Is Trying Hard to Drive Away Corporations*, Wall St. J. (Nov. 24, 2023), https://www.wsj.com/articles/delaware-is-trying-hard-to-drive-away-corporations-business-environmental-social-governance-investing-780f812a; Robert Anderson, https://x.com/ProfRobAnderson/status/1752703982169104656 (arguing that "the Chancellor's seeming feud with Musk" has "injected "ideological 'culture wars'" into Delaware's law); Robert Anderson, https://x.com/ProfRobAnderson/status/1803893416360554648; Erica Grieder, *5 reasons why Elon Musk might want to incorporate Tesla in Texas*, Houston Chron. (Feb. 1, 2024), https://www.houstonchronicle.com/business/article/tesla-musk-incorporation-18641875.php.

driving corporations to other states that are more reliable (or that follow different corporations' preferred politics[10]).

This Article argues that, in some ways, the critics are correct: Delaware law is on a path toward politicization. But it is not because of any particular bias of its judges or its law; to the contrary, the pressures toward politicization are inherent in any system that purports to guide how vast aggregations of capital will be deployed. What is unique about the current moment is that the trends toward politicization result from tensions inherent in shareholder primacy – which is a doctrine that was developed and championed to *avoid* corporate governance politicization in the first place. Shareholder primacy was conceived, in large part, as a compromise to keep politics *out* of business management; what today's controversies reveal is the futility of that effort.

Ever since the rise of the great corporations in the early 20th century, the question of corporate purpose has bedeviled corporate theory, namely, what goals corporate managers should aspire to attain.[11] Our legal system facilitates the concentration of resources within state-chartered entities, whose managers then are permitted to wield great power over our economic landscape, our political system, and our day to day lives as consumers and employees and citizens. For that kind of power to be accepted as legitimate – and for businesses to retain their social license to operate[12] – there must be the perception that his power is channeled in a prosocial direction, which is to say, with due regard for the multiple constituencies – shareholders, creditors, employees, consumers, and communities – who may be affected by corporate behavior.

In the period following World War II, the legitimating narrative that justified the exercise of managerial power was a faith in the skill, expertise, and character of the men who held these positions.[13] At the time, it was expected that business leaders would manage their companies for the benefit of the community at large, as living proof of capitalism's superiority to communism in terms of providing for the general welfare.[14] That vision faltered, however, with the business

[10] Anthony Rickey, *Politics as a New Differentiator Between American Business Courts: A View on the Debate Between Former Attorney General Barr and Vice Chancellor Laster*, Bus. L. Prof. Blog (Dec. 21, 2023), https://lawprofessors.typepad.com/business_law/2023/12/guest-post-politics-as-a-new-differentiator-between-american-business-courts-a-view-on-the-debate-be.html.

[11] C.A. Harwell Wells, *The Cycles of Corporate Social Responsibility: An Historical Retrospective for the Twenty-First Century*, 51 U. Kan. L. Rev. 77, 77-79 (2002); *see also* A.A. Berle, Jr., *Corporate Powers as Powers in Trust*, 44 Harv. L. Rev. 1049 (1931); E. Merrick Dodd, Jr., *For Whom Are Corporate Managers Trustees?*, 45 Harv. L. Rev. 1145, 1160 (1932); Adolf A. Berle, Jr., *For Whom Corporate Managers Are Trustees: A Note*, 45 Harv. L. Rev. 1365, 1367 (1932).

[12] It has frequently been recognized that the power wielded by corporate managers must be recognized as legitimate in order for businesses to function effectively. *See, e.g.*, Hillary A. Sale, *The Corporate Purpose of Social License*, 94 S. Cal. L. Rev. 785 (2021); Cary Coglianese, *Legitimacy and Corporate Governance*, 32 Del. J. Corp. L. 159 (2007); Patrick Jahnke, *Asset Manager Stewardship and the Tension Between Fiduciary Duty and Social License* (Jan. 30, 2019), https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3307172/

[13] Dalia T. Mitchell, *Proceduralism: Delaware's Legacy*, 2 U. Chi. Bus. L. Rev. 333 (2023); James J. Park, *From Managers to Markets: Valuation and Shareholder Wealth Maximization*, 47 J. Corp. L. 435, 446-47 (2022).

[14] Dalia T. Mitchell, *Proceduralism: Delaware's Legacy*, 2 U. Chi. Bus. L. Rev. 333, 345-46 (2023); William W. Bratton & Michael L. Wachter, *Shareholder Primacy's Corporatist Origins*, 34 J. Corp. L. 99, 141 (2008); Jeffrey N. Gordon, *The Rise of Independent Directors in the United States, 1950–2005: Of Shareholder Value and Stock*

scandals of the 1960s and 1970s.[15] As belief in managers' superior judgment declined, the doctrine of shareholder primacy – the principle that corporate governance should orient around encouraging managers to maximize profits for the equity holders – became the preferred source of constraint on the exercise of managerial power.[16]

This does not mean a shareholder primacist system has no concern for nonshareholder constituencies; rather, under shareholder primacy, these constituencies are believed to be better protected through contracts (markets) and external regulation, rather than through the internal levers of corporate governance.[17] The expectation is that market mechanisms, as well as regulatory penalties, will make it expensive for corporations to exploit nonshareholder constituencies. If corporations pollute their surroundings, or make unsafe products, or abuse employees, they will pay a price, via governmental sanction, consumer aversion, and employee attrition. Therefore, simply as a result of natural profit seeking, corporations will engage in prosocial behavior. Markets, coupled with governmental regulation, will sufficiently align the interests of shareholders and nonshareholders to ensure that corporations responsive to shareholder interests will serve society as a whole.[18]

In large part, this system has become the default for lack of a viable alternative.[19] Shareholder primacy, it is contended, offers a simple, clear metric for assessing managerial performance: shareholder returns. Any other system would grant managers nearly unchecked discretion to balance the interests of multiple competing constituencies with no comparably

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Market Prices, 59 Stan. L. Rev. 1465, 1512 (2007); *see also* A.P. Smith Manufacturing Co. v. Barlow, 98 A.2d 581, 582-83 (N.J. 1953).

[15] Dalia T. Mitchell, *Proceduralism: Delaware's Legacy*, 2 U. Chi. Bus. L. Rev. 333, 349-51 (2023); Jeffrey N. Gordon, *The Rise of Independent Directors in the United States, 1950–2005: Of Shareholder Value and Stock Market Prices*, 59 Stan. L. Rev. 1465, 1514-15 (2007).

[16] Dalia T. Mitchell, *Proceduralism: Delaware's Legacy*, 2 U. Chi. Bus. L. Rev. 333, 369 (2023); *see also* Milton Friedman, *A Friedman Doctrine — The Social Responsibility of Business Is to Increase Its Profits*, N.Y. Times (Sept. 13, 1970), https://www.nytimes.com/1970/09/13/archives/afriedman-doctrine-the-social-responsibility-of-business-is-to.html. I have previously explained that "shareholder primacy" can also be defined to mean that shareholders select corporate goals other than wealth maximization. *See* Ann M. Lipton, *What We Talk About When We Talk About Shareholder Primacy*, 69 Case W. Res. L. Rev. 863 (2019). For the purposes of this Article, however, I use the phrase in its traditional sense, to mean that corporate managers are obligated to maximize value for the equity.

[17] Henry Hansmann & Reinier Kraakman, *The End of History for Corporate Law*, 89 Geo. L.J. 439 (2001).

[18] Henry Hansmann & Reinier Kraakman, *The End of History for Corporate Law*, 89 Geo. L.J. 439 (2001); Daniel R. Fischel, *The Corporate Governance Movement*, 35 Vand. L. Rev. 1259, 1269-71 (1982); Frank H. Easterbrook & Daniel R. Fischel, The Economic Structure of Corporate Law 37–39 (1991); Kent Greenfield, *Proposition: Saving the World With Corporate Law*, 57 Emory L.J. 948, 966-67 (2008); Marcel Kahan & Edward B. Rock, *Corporate Governance Welfarism*, 15 J. Legal Analysis 108, 110 (2023). The argument goes back at least as far as Adam Smith, who claimed that "By pursuing his own interest [an individual] frequently promotes that of the society more effectually than when he really intends to promote it." Adam Smith, An Inquiry into the Nature and Causes of The Wealth of Nations 293 (R.H. Campbell, A.S. Skinner & W.B. Todd eds., Clarendon Press, Oxford 1976) (1776).

To be sure, part of our system relies on enforcement against individual actors within corporations, who incur penalties personally for lawbreaking. Shareholders do not suffer when specific officers are jailed or fined; instead, the assumption is that those individuals will be personally deterred regardless of the benefits to the firm. However, because of the difficulty of identifying guilty individuals, our system threatens penalties against the corporation itself unless the entity takes steps to detect and prevent wrongdoing. *See generally* Jennifer Arlen & Reinier Kraakman, *Controlling Corporate Misconduct: An Analysis of Corporate Liability Regimes*, 72 N.Y.U. L. Rev. 687 (1997).

[19] Henry Hansmann & Reinier Kraakman, *The End of History for Corporate Law*, 89 Geo. L.J. 439 (2001).

determinate goal. The result would be to enable America's CEOs to deploy the vast resources of the corporation to serve their own notion of the social good, a task for which they have neither expertise nor democratic legitimacy.[20] Shareholder primacy, by contrast, does not rely on the moral instincts of America's business elite. Contested political choices about how corporate surplus should be distributed are instead left to the democratic process and the invisible hand of a market that reflects popular sentiment. Shareholder primacy, in other words, is championed as the better system because it is the only one that offers a meaningful, societally-determined constraint on managerial behavior.[21]

Slotting neatly into this system is the state of Delaware. Corporate managers can select any jurisdiction in which to incorporate, and that jurisdiction's law will control its internal governance; for over a century, Delaware has been the preferred jurisdiction for incorporators.[22] As a result, Delaware – home to only 0.3% of America's population – exerts outsized influence over the country's corporate law and, consequently, the principles that guide the allocation of billions or trillions of dollars of capital. Delaware's legitimacy to serve this inescapably political function rests, ironically, on its fierce commitment to keeping political concerns out of its law.[23] Among other things, it has enshrined party balance into its courts via its state constitution, and has adopted special procedures to keep amendments to its business code in the hands of technocrats rather than politicians.[24] Delaware is able to position itself as apolitical because shareholder primacy itself is treated as apolitical; just as shareholder primacy is supposed to take corporations out of the business of making social policy, enforcing shareholder primacy keeps Delaware out of the business of making social policy, which allows Delaware to stay above the partisan fray.

Especially in recent years, Delaware judges have aggressively communicated the shareholder-centric nature of its law. Delaware courts have explicitly referred to nonshareholder constituencies as mere "instrument[s]" for the achievement of stockholder wealth,[25] and declared

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[20] Adolf A. Berle, Jr., *For Whom Corporate Managers Are Trustees: A Note*, 45 Harv. L. Rev. 1365, 1367 (1932); Robert T. Miller, *How Would Directors Make Business Decisions Under Stakeholder Model?*, 77 Bus. Law. 773 (2022); Stephen M. Bainbridge, The Profit Motive: Defending Shareholder Value Maximization 114-17 (2023).
[21] Lucian A. Bebchuk & Roberto Tallarita, *The Illusory Promise of Stakeholder Governance*, 106 Cornell L. Rev. 91 (2020); Lucian A. Bebchuk & Roberto Tallarita, The Perils and Questionable Promise of ESG-Based Compensation, 48 J. Corp. L. 37 (2022); Robert P. Bartlett & Ryan Bubb, *Corporate Social Responsibility through Shareholder Governance*, 97 S. Cal. L. Rev. 417 (2024).
[22] Ofer Eldar & Gabriel V. Rauterberg, *Is Corporate Law Nonpartisan?*, 2023 Wis. L. Rev. 177.
[23] McRitchie v. Zuckerberg, 315 A.3d 518, 573 (Del. Ch. 2024) ("Reformers who look to Delaware law to address externalities must acknowledge the larger political environment. Delaware is one of fifty states…Among the fifty states, Delaware has one of the smaller human populations …Delaware must identify niches where it has a comparative advantage—like corporate law—so that entrepreneurs want to use its corporations, legal practitioners want to choose its law, and parties want to litigate in its courts. Delaware has traditionally filled the corporate law niche by taking a distinctively nonpartisan, technocratic approach…. Depending on an observer's political leanings, there are any number of salient issues that Delaware might use its corporate law to address. But to the extent the General Assembly sought to intervene on any of them, entrepreneurs who did not like the answer could incorporate their firms elsewhere.").
[24] Ofer Eldar & Gabriel V. Rauterberg, *Is Corporate Law Nonpartisan?*, 2023 Wis. L. Rev. 177.
[25] *In re* Toys "R" Us, Inc. S'holder Litig., 877 A.2d 975, 999 (Del. Ch. 2005) ("stockholders are the only corporate constituency whose best interests are an end, rather than an instrument, of the corporate form"); *In re* Rural Metro Corp., 88 A.3d 54, 80 (Del. Ch. 2014) ("Stockholders' best interest must always, within legal limits, be the end.

that the "shareholder franchise" is "the ideological underpinning upon which the legitimacy of directorial power rests."[26] Decontextualized, the elevation of shareholder wealth maximization above all other values seems almost sociopathic; in fact, it is best read as something like a cry for help, to be provided in the form of generalized acknowledgment that Delaware's corporate law cannot be relied upon to exercise social control over corporations, and in fact, regulation among those lines must occur externally.[27]

That said, for shareholder primacy to serve its legitimating function, it must not only channel corporate and managerial behavior in a prosocial direction, but it must be *seen* to do so. The corporate governance system must *visibly* operate along two dimensions: first, procedurally, it must be seen to constrain corporate managers, and second, substantively, these constraints must be perceived to produce prosocial outcomes.[28] Corporate governance must, in other words, perform prosociality – which of course requires that the social concerns that shareholder primacy excised now be imported back into the system. The paradox is one that has come under increasing pressure, culminating in perhaps the gravest threat to Delaware's dominance in decades.

I. The Tesla Trap

As above, the first purported virtue of shareholder primacy is that it meaningfully constrains the behavior of corporate managers. These constraints are theoretically enforced through a variety of procedures around which regulators, courts, and commenters have coalesced as representing "good" corporate governance. They include a corporate board that is majority independent,[29] with key committees that are entirely independent,[30] and procedures to facilitate responsiveness to shareholders, such as a single-class board,[31] access to the corporate proxy,[32] and commitments to modesty when fending off hostile acquirers (such as poison pills that require

Other corporate constituencies may be considered only instrumentally to advance that end." (citations and alterations omitted)).

[26] Blasius Industries, Inc. v. Atlas Corp., 564 A.2d 651, 659 (Del. Ch. 1988).

[27] Then-Chancellor Leo Strine was fairly explicit on this point in his article, *Our Continuing Struggle with the Idea that For-Profit Corporations Seek Profit*, 47 Wake Forest L. Rev. 135 (2012), where he argued that "plain acknowledgment that corporate managers' primary duty is to seek as much profit as can be achieved within the limits of the law," also requires acknowledgment of the "importance of the law in channeling corporate behavior." *Id* at 152.

[28] *Cf.* Cary Coglianese, *Legitimacy and Corporate Governance*, 32 Del. J. Corp. L. 159 (2007) (arguing that legitimacy comes from two places: procedural and substantive).

[29] Mariana Pargendler, *The Corporate Governance Obsession*, 42 J. Corp. L. 359, 377 (2016); ISS, *Proxy Voting Guidelines Benchmark Policy Recommendations* 9, at https://www.issgovernance.com/file/policy/active/americas/US-Voting-Guidelines.pdf

[30] 15 U.S.C. § 78j–1; 17 CFR § 240.10C-1; NYSE Listed Company Manual §303A.04; Glass Lewis, *2024 Benchmark Policy Guidelines* 15, https://www.glasslewis.com/wp-content/uploads/2023/11/2024-US-Benchmark-Policy-Guidelines-Glass-Lewis.pdf.

[31] Lucian Bebchuk, Alma Cohen, & Allen Ferrell, *What Matters in Corporate Governance?*, 22 Rev. Fin. Studies 783 (2009);); ISS, *Proxy Voting Guidelines Benchmark Policy Recommendations* 15, at https://www.issgovernance.com/file/policy/active/americas/US-Voting-Guidelines.pdf.

[32] ISS, *Proxy Voting Guidelines Benchmark Policy Recommendations* 23, at https://www.issgovernance.com/file/policy/active/americas/US-Voting-Guidelines.pdf.

shareholder approval after some period of time).[33] "Good" boards might separate the chair and CEO roles,[34] adopt ethics codes,[35] oversee and minimize related party transactions,[36] and avoid purchasing non audit services from firms that conduct financial audits.[37]

Many of these structures have been imposed on corporations via the federal securities laws, either as a requirement for all public companies, or as a requirement for all companies listed on registered stock exchanges.[38] Still others have been advocated by shareholders, and adopted by companies more or less voluntarily, as a result of investor pressure.[39] Under state (Delaware) corporate law, deployment of these devices is not mandatory, but is strongly encouraged, via favorable judicial treatment in the event of a stockholder challenge to board action. For example, the fact that an independent rather than inside board employed a takeover defense will contribute to a finding that the defense was reasonable[40]; similarly, independent board approval, or disinterested shareholder approval, will cleanse most board action from the specter of self-dealing or disloyalty.[41] Even when ideal procedures are not used – and the court is forced to evaluate the substantive fairness of a decision – the procedural path by which it was reached contributes to the court's analysis of its correctness.[42] In other words, one way or another, the procedures deployed in corporate decisionmaking heavily influence a court's evaluation of the merits of that decision.[43]

At the same time, there is a longstanding debate as to whether these "good" governance provisions do, in fact, protect shareholder interests.[44] There are some obvious reasons why they

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[33] ISS, *Proxy Voting Guidelines Benchmark Policy Recommendations* 14, at https://www.issgovernance.com/file/policy/active/americas/US-Voting-Guidelines.pdf.
[34] Yaron Nili, *Successor CEOs*, 99 Boston U. L. Rev. 737, 833 (2019).
[35] Sean O'Neill, *What is a code of conduct?*, https://www.thecorporategovernanceinstitute.com/insights/lexicon/what-is-a-board-code-of-conduct/
[36] NYSE Listed Company Manual §314.00.
[37] John C. Coffee, Jr., *Understanding Enron: "It's About the Gatekeepers, Stupid,"* 57 Bus. Law. 1403, 1410-1411 (2002).
[38] 15 U.S.C. § 78j–1; 17 CFR § 240.10C-1; NYSE Listed Company Manual §303A.04; 17 CFR §229.406; 15 U.S. Code § 78n–2.
[39] Assaf Hamdani & Kobi Kastiel, *Superstar CEOs and Corporate Law*, 100 Wash. U. L. Rev. 1353, 1363 (2023).
[40] Unocal v. Mesa Petroleum Co., 493 A.2d 946 (Del. 1985).
[41] Corwin v. KKR Fin. Holdings LLC, 125 A.3d 304 (Del. 2015).
[42] William Penn P'ship v. Saba, 13 A.3d 749, 756 (Del. 2011); *see also* Dell v. Magnetar Global Event Driven Master Fund, 177 A.3d 1 (Del. 2017) (valuation for appraisal purposes depends in part on the integrity of the process by which the deal was negotiated).
[43] Dalia T. Mitchell, *Proceduralism: Delaware's Legacy*, 2 U. Chi. Bus. L. Rev. 333 (2023).
[44] Michael Klausner, *Fact and Fiction in Corporate Law and Governance*, 65 Stan. L. Rev. 1325, 1358 (2013); Mariana Pargendler, *The Corporate Governance Obsession*, 42 J. Corp. L. 359, 396 (2016); Stephen M. Bainbridge, *Dodd Frank: Quack Federal Corporate Governance Round II*, 95 Minn. L. Rev. 1779 (2011); Roberta Romano, *The Sarbanes-Oxley Act and the Making of Quack Corporate Governance*, 114 Yale L.J. 1521 (2005); Yakov Amihud, Markus Schmid & Steven Davidoff Solomon, *Settling the Staggered Board Debate*, 166 U. Pa. L. Rev. 1475 (2018); K.J. Martijn Cremers, Lubomir P. Litov & Simone M. Sepe, *Staggered Boards and Long-Term Firm Value, Revisited*, 126 J. Fin. Econ. 422 (2017); Urska Velikonja, *The Political Economy of Board Independence*, 92 N.C. L. Rev. 855 (2014); Zohar Goshen & Doron Levit, *Irrelevance of Governance Structure*, at https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3340912; Yaron Nili & Claire Hill, *Independence Reconceived*, 2023 Colum. Bus. L. Rev. 589, 625. A recent study concluded that the data set most researchers have used to determine whether particular governance provisions are wealth-enhancing is itself inaccurate, which calls into

would fail: independent directors, for example, are frequently uninformed about corporate operations,[45] and are likely to feel generally beholden to others in their circle even without identifiable personal ties.[46] And, as it turns out, the evidence that these measures contribute to higher shareholder returns is sufficiently ambiguous that some have argued that they are not intended to benefit shareholders at all. Instead, these provisions are intended to legitimate the exercise of corporate power in the eyes of society as a whole.[47] When firms adopt a certain level of formality and transparency with respect to their decisionmaking, the control of a staggering aggregation of financial and human resources, concentrated in the hands of a small number of unelected private citizens, becomes acceptable in the eyes of the general public.[48] The "good governance" requirements civilize firms by cloaking their decisionmaking with a veneer of professionalism.[49] This would explain, for example, why many of the more voluntary "good" governance provisions seem only to be adopted at the largest companies.[50] If they increase shareholder value, one would expect more companies to select them; if they are intended to legitimate corporate power, however, they would only be needed at the most powerful and visible firms.[51]

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question any number of previous findings about the value of "good" governance provisions. *See* Jens Frankenreiter, Cathy Hwang, Yaron Nili, & Eric Talley, *Cleaning Corporate Governance*, 170 U. Pa. L. Rev. 1 (2021).

[45] Usha Rodrigues, *A Conflict Primacy Model of the Public Board*, 2013 U. Ill. L. Rev. 1051, 1061

[46] Yaron Nili & Claire Hill, *Independence Reconceived*, 2023 Colum. Bus. L. Rev. 589; Julian Velasco, *Structural Bias and the Need for Substantive Review*, 82 Wash. U. L.Q. 821 (2004); Nicola Faith Sharpe, *Process, Not Structure: An Organizational Behavior Approach to Improving Corporate Boards*, 85 S. Cal. L. Rev. 261 (2012).

[47] Robert Charles Clark, Corporate Law 95 (1986) (shareholder voting is "a mere ceremony designed to give a veneer of legitimacy to managerial power"); Dalia T. Mitchell, *Proceduralism: Delaware's Legacy*, 2 U. Chi. Bus. L. Rev. 333, 354, 368 (2023); Urska Velikonja, *The Political Economy of Board Independence*, 92 N.C. L. Rev. 855 (2014); Donald C. Langevoort & Robert B. Thompson, "*Publicness" in Contemporary Securities Regulation After the JOBS Act*, 101 Geo. L.J. 337 (2013); Claire Hill & Yaron Nili, *Independence Reconceived*, 2023 Colum. Bus. L. Rev. 589, 625; Donald C. Langevoort, *The Social Construction of Sarbanes-Oxley*, 105 Mich. L. Rev. 1817, 1831 (2007).

[48] Marcel Kahan & Edward Rock, *Symbolic Corporate Governance Politics*, 94 B.U. L. Rev. 1997, 2034 (2014) ("we need to believe that in even—and especially—the largest corporations, there are individual shareholders who collectively own and control those corporations. Because shareholders exercise control over managers, perhaps mediated through markets, it is acceptable that a small group of managers control huge concentrations of capital for which they are paid princely sums"); Donald C. Langevoort & Robert B. Thompson, *"Publicness" in Contemporary Securities Regulation After the JOBS Act*, 101 Geo. L.J. 337 (2013).

[49] An additional data point suggesting that these standards add little value *for shareholders* comes from the fact that scholars have not been able to identify any shareholder benefit arising from incorporation in Delaware versus incorporation in any other state. *See, e.g.*, Robert Anderson & Jeffrey Manns, *The Delaware Delusion: An Empirical Analysis*, 93 N.C. L. Rev.101 (2015); Lucian A. Bebchuk & Alma Cohen, *Firms' Decisions Where to Incorporate*, 46 J. L. & Econ 383 (2003); Robert J. Rhee, *The Irrelevance of Delaware Corporate Law*, 48 J. Corp. L. 295 (2023). To be fair, that is a messy signal; states' laws trend in similar directions and so many states look to Delaware that there may not be much variation for comparison. Still, the lack of detectable differences is suggestive.

[50] Kobi Kastiel & Yaron Nili, *The Corporate Governance Gap*, 131 Yale L.J. 782 (2022).

[51] I am perhaps overstating. Just because some idiosyncratic companies may benefit from more individualized corporate governance standards does not mean the standards are merely cosmetic across the board. If they add value at a critical mass of firms, it may be simplest and cheapest to require them at all firms, rather than have diversified shareholders incur the costs of investigating the precise standards that would suit each firm individually. *Cf.* Marcel Kahan & Edward B. Rock, *Index Funds and Corporate Governance: Let Shareholders Be Shareholders*, 100 Boston U. L. Rev. 1771 (2020); *see also* Jeffrey N. Gordon, *The Rise of Independent Directors in the United States, 1950–2005: Of Shareholder Value and Stock Market Prices*, 59 Stan. L. Rev. 1465 (2007) (arguing that the benefits of independent boards operate systemically, by requiring companies to either adopt the practice or substantively improve their businesses to compete). That said, shareholders have tolerated such extraordinary variance in

These two conceptions of "good" corporate governance – substantively for investors, or as a performance for society as a whole – are not entirely at odds. Even if the presence of independent directors, for example, does not directly improve operational functioning, it may still maximize shareholder wealth systemically, by contributing to corporations' social license to operate and thereby staving off more robust regulation of corporate behavior.[52] Still, these measures are adopted – ostensibly – because they benefit shareholders by controlling managerial agency costs[53]; if they do not, if their real purpose is to cleanse corporate action in society's eyes, that only begs the question regarding the merit of an economic system that relies on pantomime in order to garner public acceptance.

Which brings us to Tesla. By any conceivable measure of "good" corporate governance, Tesla's is abysmal. In addition to having a staggered board and a two-thirds majority vote requirement to amend the entrenching provisions of its charter, board members have comically close financial, personal, and even familial ties to its "superstar" CEO, Elon Musk.[54] Musk runs Tesla along with five other companies, and reallocates resources among them at will, with – according to the eventual findings of Chancellor McCormick of the Delaware Court of Chancery, (and contrary to representations in Tesla's SEC filings) – almost no board oversight.[55] Tesla's auditor, PwC, also performs significant consulting work for Musk's other companies.[56] Until a settlement with the SEC in late 2018**,** Musk was both Chair and CEO,[57] and even after he was forced to relinquish the chair position, he openly boasted that the new chair had no power over him.[58] In 2016, Musk was the driving force behind Tesla's purchase of another of his companies, SolarCity, after SolarCity ran into serious financial trouble; shareholders voted in favor of that deal just after Musk staged a presentation of its "solar roof" product. It was eventually revealed that the solar roof was nonfunctional.[59]

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corporate governance arrangements in recent years that it no longer seems plausible that they find value in a stable, familiar form. *See, e.g.*, Gabriel Rauterberg & Eric Talley, *Contracting Out of the Fiduciary Duty of Loyalty: An Empirical Analysis of Corporate Opportunity Waivers*, 117 Colum. L. Rev. 1075 (2017); Elizabeth Pollman, *Startup Governance*, 168 U. Penn. L. Rev. 155 (2019); Gabriel V. Rauterberg, *The Separation of Voting and Control: The Role of Contract in Corporate Governance*, 38 Yale J. on Reg. 1124 (2021); Gladriel Shobed & Jarrod Shobe, *The Dual-Class Spectrum*, 39 Yale J. on Reg. 1343 (2022); Jill Fisch & Steven Davidoff Solomon, *The Problem of Sunsets*, 99 B.U. L. Rev. 1057 (2019).

[52] Donald C. Langevoort, *The Human Nature of Corporate Boards: Law, Norms, and the Unintended Consequences of Independence and Accountability*, 89 Geo. L.J. 797, 802 (2001) (one board function is to "assist the company in claiming and protecting its shares of external resources. Carefully chosen board members help make the company more legitimate in the eyes of key resource providers such as governments, customers, labor, and so on.").

[53] Adam B. Badawi, *Influence Costs and the Scope of Board Authority*, 39 J. Corp. L. 675, 702 (2014).

[54] Kimbal Musk, Elon Musk's brother, is a Tesla board member.

[55] Tornetta v. Musk, 2024 WL 343699, *49 (Del. Ch. 2024); Tesla, Schedule 14A (Apr. 6, 2023), https://www.sec.gov/Archives/edgar/data/1318605/000119312523094075/d451342ddef14a.htm.

[56] Lora Kolodny, *Tesla whistleblowers filed a complaint to the SEC in 2021, but the agency never interviewed them. Here's what the complaint said*, CNBC (Oct. 12, 2023), https://www.cnbc.com/2023/10/12/tesla-whistleblowers-filed-complaint-to-sec-in-2021-what-it-said.html.

[57] Tornetta v. Musk, 2024 WL 343699, *11 (Del. Ch. 2024).

[58] Lesley Stahl, *Tesla CEO Elon Musk: The 60 Minutes Interview* (Dec. 9, 2018), *available at* https://www.cbsnews.com/news/tesla-ceo-elon-musk-the-2018-60-minutes-interview/.

[59] Bethany McLean, *"He's Full of Shit": How Elon Musk Fooled Investors, Bilked Taxpayers, and Gambled Tesla to Save Solarcity*, Vanity Fair (Aug. 25, 2019), https://www.vanityfair.com/news/2019/08/how-elon-musk-gambled-tesla-to-save-solarcity.

Despite these facts, Musk has built an army of investor fans who believe fiercely in his engineering skills and visions for the future. Tesla shareholders have expressed confidence in his leadership through their dollars, triggering financial losses for any number of doubting short sellers along the way.[60]

In 2018, the Tesla board awarded Musk a new compensation package that would pay him a maximum of $55.8 billion in stock options – "250 times larger than the contemporaneous median peer compensation plan and over 33 times larger than the plan's closest comparison, which was Musk's prior compensation plan,"[61] but only if he was able to increase Tesla's market capitalization from $50 billion to $650 billion, a feat generally perceived to be "laughably impossible."[62] Shareholders holding 73% of Tesla's votes (excluding those held by Musk and his brother) approved the package, after being fully informed of its financial terms. Showing up the naysayers, Musk was able to meet those goals well ahead of the 10 year timeline for completion. Nonetheless, a Tesla shareholder sued, claiming that the pay package – negotiated by Musk's captured board – was unfair to public Tesla investors.

Tornetta v. Musk presented a fundamental problem for the Delaware courts. On the one hand, it is difficult to argue with success: Musk had led the company to an astronomical value that most shareholders would be glad to pay $56 billion to achieve. On the other, the pay package had not been negotiated in accordance with best practices: the board members were, in various ways, beholden to Musk personally, and the affirming shareholder vote had been marred by incomplete disclosures regarding the process by which it had been negotiated. Chancellor McCormick thus had the unenviable choice of either affirming the package – thus conceding the lack of importance of procedural safeguards – or striking it down, despite the obvious benefits shareholders had enjoyed. On January 30, 2024, she issued a decision rescinding the entirety of the options grant, about a quarter of Musk's total wealth, largely reasoning that because of the absence of procedural protections that would render board and shareholder judgment reliable, she would have to substitute her own. In her judgment, given that Musk already owned 21% of Tesla at the time the grant had issued, there could be no assurances that the board could not have wrung a similar performance out of him for a much smaller price tag.[63]

For sure, there were always legitimate arguments that the 2018 options grant was not, in fact, ideal for shareholders. The grant, predicated on the temporary achievement of stock price milestones, largely disconnected from actual increases in profit,[64] may have encouraged Musk to make wild projections, and cut manufacturing and regulatory corners,[65] in a manner that could

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[60] Carmen Reinicke, *Short Sellers Lost $195 Billion in 2023 Despite Wins on Regional Banks*, Bloomberg (Jan. 4, 2024), https://www.bloomberg.com/news/articles/2024-01-04/shorts-lost-195-billion-in-2023-despite-wins-on-regional-banks.
[61] Tornetta v. Musk, 2024 WL 343699, *1 (Del. Ch. 2024).
[62] Andrew Ross Sorkin, *Tesla's Elon Musk May Have Boldest Pay Plan in Corporate History*, N.Y. Times Dealbook (Jan. 23, 2018), https://www.nytimes.com/2018/01/23/business/dealbook/tesla-elon-musk-pay.html.
[63] Tornetta v. Musk, 2024 WL 343699, *75 (Del. Ch. 2024).
[64] Tornetta v. Musk, 2024 WL 343699, *77 (Del. Ch. 2024).
[65] Geoffrey A. Fowler, *Elon Musk's road to Twitter is paved with broken promises*, Wash. Post (Apr. 15, 2022), https://www.washingtonpost.com/technology/2022/04/15/elon-musk-promises; Walter Isaacson, Elon Musk 249-50, 334 (2023); Hyunjoo Jin, Kevin Krolicki, Marie Mannes, & Steve Stecklow, *Tesla blamed drivers for failures of parts it long knew were defective*, Reuters (Dec. 20, 2023), https://www.reuters.com/investigates/specialreport/tesla-musk-steering-suspension; Steve Stecklow & Norihiko

hurt Tesla's stock in the long term.[66] Moreover, the inconceivable wealth that the grant bestowed upon Musk may have fueled his recklessness, inspiring and enabling his ill-advised takeover of Twitter, which not only has apparently distracted him from Tesla, but also may be damaging the brand in the eyes of potential consumers.[67] Indeed, in 2022, after Musk's acquisition of Twitter, Tesla's stock price plummeted, reducing its market capitalization to under $400 billion in January 2023. And though Tesla's stock price soared on Musk's promises that its future was AI, he has recently begun to develop AI in a separate, privately-held company – relying, in part, on data generated by Tesla cars[68] (two potential breaches of his fiduciary obligations of loyalty under Delaware law.). Certainly, then, a case could be made that – especially in hindsight – the options grant traded short term gains for long term viability.[69]

But the gains to Tesla have been undeniable, as has been the continuing support of Tesla shareholders (many of whom wrote to the court to express their unhappiness with the ruling[70]). Board member Antonio Gracias testified that the compensation plan was designed to give Musk "dopamine hits," with incremental options awards doled out every time Musk achieved a particular milestone on the journey to the $650 billion market capitalization.[71] Given Musk's known preference for risk taking, it seems plausible that by gameifying his pay package – presenting him with impossible goals and then, when he met them, ringing bells and showering confetti and gold coins – the board really did extract maximum performance. Under these

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Shirouzu, *Tesla created secret team to suppress thousands of driving range complaints*, Reuters (July 27, 2023), https://www.reuters.com/investigates/special-report/tesla-batteries-range/; Ronan Farrow, Elon Musk's Shadow Rule, The New Yorker (Aug. 21, 2023).

[66] Faiz Siddiqui, Rachel Lerman, & Jeremy B. Merrill, *Teslas running Autopilot involved in 273 crashes reported since last year*, Wash. Post (June 15, 2022), https://www.washingtonpost.com/technology/2022/06/15/tesla-autopilot-crashes/; Steve Stecklow & Norihiko Shirouzu, *Tesla created secret team to suppress thousands of driving range complaints*, Reuters (July 27, 2023), https://www.reuters.com/investigates/special-report/tesla-batteriesrange/; Kirsten Korosec, *Feds expand Tesla investigation to include vehicle range, personal benefits*, TechCrunch (Oct. 23, 2023), https://techcrunch.com/2023/10/23/feds-expand-tesla-investigation-toinclude-vehicle-range-personal-benefits/.

[67] Kurt Wagner, Battle for the Bird 281 (2024). Of course, as of this writing, it is anticipated that Elon Musk's manipulation of the Twitter platform to support the election Donald Trump will result in a series of regulatory changes that ultimately benefit Tesla. *See, e.g.*, David Ingram, Dan De Luce, & Laura Strickler, *Elon Musk could be the biggest winner of a second Trump term*, NBC News (Nov. 5, 2024), https://www.nbcnews.com/tech/tech-news/elon-musk-trump-endorses-pac-administration-cabinet-connection-rcna178549. In that sense, then, the takeover of Twitter may have been wealth maximizing for Tesla after all, by increasing Musk's political influence.

[68] Tim Higgins, *Tesla Was Once About Climate Change, Driverless Cars, AI. Now What?*, Wall St. J. (Feb. 10, 2024), https://www.wsj.com/business/autos/tesla-has-long-been-a-hope-stock-but-what-are-investors-hoping-for-now-7031171f; Layan Odeh, Gillian Tan, & Kurt Wagner, *Musk's Track Record, OpenAI Success Are Focus of Potential xAI Investors*, Bloomberg (Feb. 5, 2024), https://www.bloomberg.com/news/articles/2024-02-05/xai-potential-investors-focus-on-muskonomy-openai-success; Lora Kolodny, *Elon Musk plans Tesla and Twitter collaborations with xAI, his new startup*, CNBC (July 14, 2023), https://www.cnbc.com/2023/07/14/elon-musk-plans-tesla-twitter-collaborations-with-xai.html.

[69] *Cf.* Bryce Elder, *What Might Explain Tesla's Night Moves?*, Fin. Times (Jan. 31, 2025), https://www.ft.com/content/9cc311b7-676b-4539-a682-b3533a76b0fc (explaining how Tesla trades more on "vibes" and shareholder support than fundamentals).

[70] Jef Feeley & Dana Hull, *Tesla investors are flooding judge who threw out Elon Musk's $56bn pay package with complaints about winning lawyers' request for $6bn in company stock*, Fortune (Mar. 13, 2024), https://fortune.com/2024/03/13/tesla-investors-flooding-judge-threw-out-elon-musk-56bn-pay-package-complaints-winning-lawyers-demand-6bn-stock/.

[71] Tornetta v. Musk, 2024 WL 343699, *77 (Del. Ch. 2024).

circumstances, to fault the pay package for sacrificing Tesla's "long term" value in favor of "short term" stock price boosters is, fundamentally, to argue that state authorities (in this case, the Delaware Court of Chancery) should substitute their judgment as to how to manage a company for the judgment of actual investors who hold the company's stock. It positions shareholder primacy as a form of government regulation as to how capital should be deployed.[72] If Delaware's version of shareholder primacy is viewed through that lens, it explodes the myth that the doctrine of shareholder primacy removes contested allocative choices from the law of corporate governance (and from the State of Delaware). From a lay perspective, then, the *Tornetta* decision must have seemed inexplicable: Musk had delivered tremendous value, against all odds, and a court had declared it knew better than the board or the market or Tesla investors themselves.

One particular aspect of the decision stood out. In recounting the evidence that the Tesla board was incapable of acting independently of Musk, Chancellor McCormick highlighted that in March 2021, Musk had unilaterally created for himself the new official title of "TechnoKing," without prior board approval. The title, which he announced by adding to his Twitter profile,[73] undoubtedly amused many of Tesla's customers and retail investors, and was exactly the kind of behavior that inspired their admiration. But notwithstanding this shareholder approval – or at least indifference – McCormick wrote, "Musk testified that the title was intended as a joke, but that is a problem in itself. Organizational structures, including titles, promote accountability by clarifying responsibilities. They are not a joke."[74]

The scold was striking, and not only because of its emphasis on procedural formalities that shareholders themselves apparently did not value. Given the insignificance of the "TechnoKing" title – it had no effect on Tesla's actual operations or organizational structure, and no one suggested it created any confusion about responsibilities – there was almost an aesthetic quality to the rebuke. Musk had hung a clown face on the very corporate governance standards that Delaware has spent over a century perfecting, and his open disrespect defied one of their signature purposes: to polish corporate *manners*. Musk's refusal to perform his duties with sufficient gravitas undermined the legitimating function of corporate governance.

But Delaware does not, and to some extent cannot, recognize the social role that its own law plays in civilizing corporate behavior in the eyes of the broader public, because the foundation of Delaware's law – and the source of its own legitimacy – is its focus on the welfare of shareholders alone. At the same time, the more that Delaware courts insist that its law concerns shareholder value alone, the more difficult that is to square with corporate governance rules that are unnecessary to protect shareholder interests, as the *Tornetta* case perhaps unwittingly revealed.

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[72] See Ann M. Lipton, *What We Talk About When We Talk About Shareholder Primacy*, 69 Case W. Res. L. Rev. 863, 881 (2019).
[73] https://twitter.com/melaniemadri/status/1371558267567099904. There was also an 8-K filing.
[74] Tornetta v. Musk, 2024 WL 343699, *49 (Del. Ch. 2024).

At least in some corners, the decision to strike Musk's compensation was greeted with approval if not glee.[75] And many of those commenters would likely justify their reaction by reference to Tesla's shareholders – McCormick had shown, they would perhaps argue, that the grant had been a pure wealth transfer from the company to Musk. But one cannot help but suspect that, to those who celebrated the decision, their reaction was less about concern for Tesla's shareholders than concern for *society*. A pay package of that size was simply irresponsible from a *societal* standpoint, as its practical effect was to confer on Musk sufficient material resources as to largely free him from any legal or social constraints on his behavior. Since becoming the richest person on the planet (on some days), Musk not only bought a social network with global influence and turned it into a hotbed of misinformation, harassment, and conspiracy theorizing,[76] but he has publicly adopted increasingly anti-immigrant stances that code as racist[77] while advocating for appeasement of dictators opposed to America's interests.[78] He has become infamous for defying regulations intended to keep employees, consumers, and the general public safe,[79] and his financial support of Donald Trump's presidential campaign –

[75] Timothy Noah, *How Elon Musk's Zany Compensation Arrangement Got Blown Up in Court*, The New Republic (Jan. 31, 2024), https://newrepublic.com/article/178631/elon-musk-tesla-compensation-ruling; Scott Lemieux, *There's no dealing like self-dealing*, Lawyers, Guns, & Money (Jan. 30, 2024), https://www.lawyersgunsmoneyblog.com/2024/01/theres-no-dealing-like-self-dealing; Maxwell Zeff, *Relatable: Elon Musk Is Mad About His Paycheck*, Gizmodo (Feb. 1, 2024), https://gizmodo.com/elon-musk-tesla-mad-about-his-paycheck-1851211791; Michael Hiltzik, *A judge voids Musk's huge Tesla pay package as dishonest, and hoo boy, is Musk steamed*, L.A. Times (Jan. 31, 2024), https://www.latimes.com/business/story/2024-01-31/elon-musk-pay-package-tesla-delaware-judge; Slate Money with Felix Salmon, Feb. 3, 2024, https://slate.com/podcasts/slate-money/2024/02/elon-musk-tesla-ceo-court-judgment-texas-delaware.

[76] Jim Rutenberg & Kate Conger, *Elon Musk Is Spreading Election Misinformation, but X's Fact Checkers Are Long Gone*, N.Y. Times (Jan. 25, 2024), https://www.nytimes.com/2024/01/25/us/politics/elon-musk-election-misinformation-x-twitter.html; Sarah Ellison, Amy Gardner, & Clara Ence Morse, *Elon Musk's misleading election claims reach millions and alarm election officials*, Wash. Post (Sept. 10, 2024), https://www.washingtonpost.com/politics/2024/09/10/elon-musk-illegal-immigrant-voting-misinformation/.

[77] Miles Klee, *Elon Musk All but Endorses the Great Replacement Conspiracy Theory*, Rolling Stone (Jan. 5, 2024), https://www.rollingstone.com/culture/culture-news/elon-musk-great-replacement-conspiracy-theory-1234941337/; Aimee Picchi, *Elon Musk faces growing backlash over his endorsement of antisemitic X post*, CBS News (Nov. 20, 2023), https://www.cbsnews.com/news/elon-musk-actual-truth-antisemitic-post-backlash-advertisers/; Max Boot, *Musk is a MAGA megaphone and a federal contractor. That's a problem.*, Wash. Post (Mar. 18, 2024), https://www.washingtonpost.com/opinions/2024/03/18/elon-musk-defense-contractor/; Jamelle Bouie, *Elon Musk Is Preoccupied With Something He Doesn't Understand*, N.Y. Times (March 23, 2024), https://www.nytimes.com/2024/03/23/opinion/elon-musk-great-replacement.html.

[78] Steven T. Dennis & John Harney, *Musk Says Putin Can't Lose in Ukraine, Opposes Senate Bill*, Bloomberg (Feb. 13, 2024), https://www.bloomberg.com/news/articles/2024-02-13/musk-predicts-putin-can-t-lose-in-ukraine-opposes-senate-bill; David Ingram, *Musk suggests Ukraine should cede Crimea, draws rebuke from Zelenskyy*, NBC News (Oct. 4, 2022), https://www.nbcnews.com/tech/tech-news/musk-suggests-ukraine-cede-crimea-draws-rebuke-zelenskyy-rcna50528; Max Boot, *Musk is a MAGA megaphone and a federal contractor. That's a problem.*, Wash. Post (Mar. 18, 2024), https://www.washingtonpost.com/opinions/2024/03/18/elon-musk-defense-contractor/; Andrew Stanton, *NATO Ally Leader Confronts Elon Musk on Claim About Alliance*, Newsweek (March 3, 2024), https://www.newsweek.com/nato-ally-leader-confronts-elon-musk-claim-about-alliance-1875362.

[79] *See* Jacob Bogage & Faiz Siddiqui, *California sues Tesla, alleging racial discrimination and harassment*, Wash. Post (Feb. 10, 2022), https://www.washingtonpost.com/business/2022/02/09/tesla-california-lawsuit/; Stephen Rodrick, *How Many Women Were Abused to Make That Tesla?*, Rolling Stone (Sept. 19, 2022), https://www.rollingstone.com/culture/culture-features/tesla-sexual-harassment-lawsuitinvestigation-elon-musk-1234590697; Josh Eidelson & Dana Hull, *Tesla's safety data in doubt; Some work injuries were omitted from reports sent to state*, L. A. Times at C2 (Mar. 7, 2020), https://www.latimes.com/business/story/2020-03-06/tesla-left-injuries-out-of-reports-california-safety-regulator-says; Matthew Field, *Musk accused of polluting German rivers with Tesla gigafactory*, The Telegraph, https://www.telegraph.co.uk/business/2024/02/27/musk-

trivial in light of Musk's overall wealth, but massive in terms of resources provided to the candidate, and unprecedented in terms of political involvement by a public company CEO[80] – may well have changed the course of American history. It is very hard to believe these are not the knockon effects of a supine board willing to confer unimaginable wealth on a single individual based on metrics that incentivize the worst kind of short-term manipulative behavior.

Senator Elizabeth Warren is among those who have repeatedly called upon Tesla's board to police Elon Musk's conflicts more vigorously. She has written multiple letters on the subject, each time extolling the need to protect Tesla shareholders.[81] But it is very hard to believe that Senator Warren is dissatisfied with the returns to Tesla shareholders; she is almost certainly far more concerned about the *public* power that Musk is able to exercise as a result of a pliant board. Tesla's corporate governance *failed*, but it did not fail *Tesla* – it failed everyone else. But *that* reasoning was impossible to relate via Delaware corporate law; to maintain shareholder primacy's legitimacy, rejection of the pay package had to be cloaked in the language of shareholder protection. In a perverse sense, then, the decision might be viewed as an *affirmation* of shareholder primacy's utility: one takeaway might be that shareholder interests and societal interests *are in fact* aligned, and that by vindicating shareholder interests, society's interests are also protected. But the jarringly poor fit between the ruling's shareholder-protective rationale, and the actual outcomes shareholders had experienced under Musk's stewardship, only laid bare the ceremonial nature of "shareholder primacist" procedure. No wonder, then, accusations of "politicized" decisionmaking flew.[82]

Other recent decisions from Delaware courts have a similar flavor, in that they impose constraints on corporate managers that may appeal to public sensibilities but do not necessarily offer corresponding benefits to shareholders. These decisions share a theme: they concern governance arrangements that became commonplace among private companies, but suddenly

accused-polluting-german-rivers-tesla-gigafactory; Susan Pulliam, Emily Glazer, & Becky Peterson, *Musk Says He Wants to Save the Planet. Tesla's Factories Are Making It Dirtier*, Wall St. J. (Nov. 24, 2024), https://www.wsj.com/business/autos/elon-musk-tesla-environment-1263cd60; Ronan Farrow, *Elon Musk's Shadow Rule*, The New Yorker (Aug. 21, 2023).

[80] *See* Brian Slodysko, Thomas Beaumont, & Tom Krisher, *Musk tests the role of money in U.S. politics as he backs Trump with at least $119 million*, AP News (Nov. 1, 2024), https://apnews.com/article/elon-musk-donald-trump-election-2024-28d023d2ea2d06a8be99add994feb4aa; Whizy Kim, *Elon Musk and the age of shameless oligarchy*, Vox (Nov. 25, 2024), https://www.vox.com/money/387348/elon-musk-trump-president-billionaire-oligarchy.

[81] *See* Letter from Elizabeth Warren, United States Senator, to Dr. Robyn Denholm, Chairman of the Board, Tesla, Inc. (Dec. 18, 2022), https://www.warren.senate.gov/oversight/letters/senator-warren-questions-tesla-board-chairman-on-conflicts-of-interest-with-elon-musks-takeover-of-twitter; Letter from Elizabeth Warren, United States Senator, to The Honorable Gary Gensler, Chair, U.S. Securities and Exchange Commission (July 17, 2023), https://www.warren.senate.gov/oversight/letters/warren-calls-on-sec-to-investigate-tesla-board-of-directors-for-failures-to-manage-elon-musks-conflicts-of-interest-in-his-dual-role-as-ceo-of-tesla-and-twitter; Letter from Elizabeth Warren, United States Senator, to Dr. Robyn Denholm, Chairman of the Board, Tesla, Inc. (Aug. 8, 2024), https://www.warren.senate.gov/imo/media/doc/final_-_warren_letter_to_tesla_board_re_musk_conflicts_of_interest.pdf.

[82] Robert Anderson, https://x.com/ProfRobAnderson/status/1752703982169104656 (arguing that "the Chancellor's seeming feud with Musk" has "injected "ideological 'culture wars'" into Delaware's law); Anan Ashraf, *Investor Naval Ravikant Threatens To Sell All Tesla Holdings If CEO Musk's Pay Plan Is Rejected But Says He'll Buy More If Approved*, Benzinga Newswire (June 10, 2024); Michael Toth, *Why the corporations are fleeing Delaware*, The Hill (June 12, 2024), https://thehill.com/opinion/finance/4715117-why-the-corporations-are-fleeing-delaware/mlite.

found themselves under attack when adopting firms began to sell shares to the public, and became subject to public scrutiny.

Beginning in 1996, a series of changes to the securities laws made it possible for companies to raise enormous amounts of capital while remaining privately held, meaning, with shares held by a small number of investors who rarely litigate against each other, and without the scrutiny that accompanies public disclosure of their financials.[83] In this space, Silicon Valley firms, backed by private equity and venture capital, adopted an idiosyncratic set of governance practices. First, they rely heavily on thick social networks and a small cadre of repeat players to develop their businesses,[84] and second, they liberally use shareholder agreements – personal contractual arrangements – to grant founders and significant investors any number of management rights, including the right to nominate specific directors, and to review and approve major corporate transactions.[85] Operating out of public view, these firms (and their managers) apparently saw little need to design their governance structures with an eye toward appealing to public sensibilities.

Once these firms started to become public, however – and the extraordinary wealth and political and social influence wielded by this sector of the economy became more visible – their governance practices collided with the performative constraints of shareholder primacy. For example, just as these firms were becoming public, Delaware courts reinvigorated their general analysis of director independence. Whereas previously courts tended to focus solely on family ties and direct financial relationships,[86] in a series of decisions, the Delaware Supreme Court signaled that longstanding personal friendships and professional networks should also factor into the independence inquiry.[87] Given the obvious *political* power wielded by Silicon Valley firms, then-Delaware Chief Justice Strine may very well have been correct that Delaware decisions would be viewed with "skepticism" if courts accorded corporate directors too much leeway, and that to maintain the "integrity" of Delaware's law, courts needed to be "cautious about according deference to directors unable to act with objectivity."[88] Yet, given the paucity of evidence that director independence does, in fact, contribute to shareholder wealth in the first place, it is unclear that the shift materially advances shareholder interests. What it may accomplish,

[83] Ann M. Lipton, *Not Everything is About Investors: The Case for Mandatory Stakeholder Disclosure*, 37 Yale J. on Reg. 499, 520 (2020); Danielle A. Chaim & Asaf Eckstein, *A Theory of Trust-Based Governance in Startups*, https://papers.ssrn.com/sol3/papers.cfm?abstract_id=4952630, at 7
[84] *E.g.*, Abraham J.B. Cable, *Does* Trados *Matter?*, 45 J. Corp. L. 311, 324 n. 100 (2020); Anat Alon-Beck, *Unicorn Stock Options – Golden Goose or Trojan Horse?*, 2019 Colum. Bus. L. Rev. 107, 122 n.47; Ronald J. Mann, *An Empirical Investigation of Liquidation Choices of Failed High Tech Companies*, 82 Wash. U. L.Q. 1375, 1421 (2004); Jennifer Kay, *Judge Leaves Top Business Court Legacy of 'Glasscockian Prose'*, Bloomberg Law News (Aug. 26, 2024), https://news.bloomberglaw.com/litigation/judge-leaves-top-business-court-legacy-of-glasscockian-prose.
[85] Gabriel V. Rauterberg, *The Separation of Voting and Control: The Role of Contract in Corporate Governance*, 38 Yale J. on Reg. 1124 (2021); Jill E. Fisch, *Stealth Governance: Shareholder Agreements and Private Ordering*, 99 Wash. U. L. Rev. 913 (2021).
[86] *E.g.*, Beam v. Stewart, 845 A.2d 1040 (Del. 2004).
[87] Del. Cty. Emps. Ret. Fund v. Sanchez, 124 A.3d 1017 (Del. 2015); Sandys v. Pincus, 152 A.3d 124 (Del. 2016); Marchand v. Barnhill, 212 A.3d 805 (Del. 2019).
[88] Sandys v. Pincus, 152 A.3d 124 (Del. 2016).

however, is to contribute to a public narrative that a shareholder primacist approach professionalizes and meaningfully constrains managerial behavior.[89]

Shareholder agreements, as well, became a point of contention. Delaware law has historically centered the board of directors as the managing body of the corporation,[90] and while specific areas of board authority may be carved out in the corporate charter,[91] boards are otherwise granted overweening discretion to make decisions on the corporation's behalf as they see fit. In *West Palm Beach Firefighters' Pension Fund v. Moelis*,[92] Vice Chancellor Laster held that the shareholder agreements that had become de rigueur among private equity and venture capital backed firms functionally usurped the board's authority and therefore were inconsistent with Delaware law.

Though Laster's analysis was firmly grounded in Delaware precedent,[93] it is worth contemplating how shareholders are *actually* served by prohibiting these agreements. Theoretically, of course, the *Moelis* rule ensures that boards – who have fiduciary obligations to all shareholders – have the freedom to exercise their business judgment in the best interests of the corporation rather than act on behalf of the desires of a single shareholder alone. In reality, however, as even Laster admitted, many if not all of the same powers granted in the prohibited agreements could be conferred upon the favored stockholders through charter provisions or even preferred share issuances – the latter of which may be issued at board discretion without shareholder input.[94] Moreover, firms have increasingly adopted dual-class share structures,

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[89] The Delaware Supreme Court recently exhibited unusual frankness in its acknowledgement of how public perception shapes Delaware law. In *In re Dell Technologies Inc. Class V Stockholder Litigation*, certain stockholders objected to the $266.7 million fee sought by plaintiffs' attorneys for securing a $1 billion settlement. In approving the fee, the court noted, "it is also legitimate to ask, outside our somewhat insular legal universe, whether the public would ever believe that lawyers must be awarded many hundreds of millions of dollars in any given case to motivate them to pursue representative litigation or to discourage counsel from settling cases for less than they are worth." 2024 WL 3811075, *12 (Del. Aug. 14, 2024).
[90] Abercrombie v. Davies, 123 A.2d 893 (Del. Ch. 1956); Stephen M. Bainbridge, *Director Primacy: The Means and End of Corporate Governance*, 97 Nw. U. L. Rev. 547 (2003).
[91] Del. Code tit. 8, § 141(a).
[92] 311 A.3d 809 (Del. Ch. Feb. 23, 2024).
[93] 311 A.3d 809, 831-855; *see also* Sujeet Indap, *The battle over who makes the rules for US companies*, Fin. Times (Aug. 4, 2024), https://www.ft.com/content/9effb213-6ec7-4f3a-9f81-b235bfc0c108 (reporting that "[f]ew believed [Laster's] reasoning — that boards of directors cannot give up certain powers through contract — was technically incorrect."); Joel Edan Friedlander, *Former Chancellor Chandler's Unjust Criticism of Chancellor McCormick and Vice Chancellor Laster: What Does it Signify?*, J. Corp. L. (forthcoming) at 36 ("*Moelis* was widely viewed as having been decided correctly on the merits."), https://papers.ssrn.com/sol3/papers.cfm?abstract_id=4901375.
[94] *See* 311 A.3d 809, 822 ("Although some might find it bizarre that the [Delaware General Corporation Law] would prohibit one means of accomplishing a goal while allowing another, that is what the doctrine of independent legal significance contemplates."); Del. Code tit. 8, §§ 102(a)(4); 151(a). A shareholder agreement might be easier to amend than a preferred share or charter provision, as by default, the charters and preferred shares can only be amended with a shareholder vote. *See* Del. Code tit. 8 § 242(b). That said, a charter could also provide that common shareholders are not entitled to vote on amendments to preferred share issuances, and that written consent of the rights holder is all that is required for amendment. *See* C Stephen Bigler & Jennifer Veet Barrett, *Words that Matter: Considerations in Drafting Preferred Stock Provisions* (Jan. 23, 2014), https://www.americanbar.org/groups/business_law/resources/business-law-today/2014-january/words-that-matter-considerations-in-drafting; Akin, *Avoiding Common Pitfalls in Preferred Stock Transactions* (Nov. 19, 2014), https://www.jdsupra.com/legalnews/avoiding-common-pitfalls-in-preferred-st-97436/. In the end, while the two perhaps would not be entirely equivalent, careful drafting could render them reasonably similar. *Cf.* Matt Levine,

which often confer functionally the same rights on insiders.[95] Thus, though there may be some additional benefits to ordinary shareholders by prohibiting the transfer of control rights through agreements – for example, in private companies, agreements may be less transparent[96] – the protections championed in *Moelis* could also be viewed as an exercise in elevating form over substance.[97]

Why bother with the formalities, then? One possibility is that they construct nominal procedural guardrails on the raw exercise of power by single individuals over large, important companies, in a manner that satisfies the public. When decisions remain in the hands of a board – even a board that remains practically beholden to particular stockholders through dual class share structures – there are formal records of their meetings, and public disclosures regarding their deliberations, all of which contribute to the display of constraints on managerial discretion (and may even substantively provide an avenue for popular influence and input).[98] And that is true even if those constraints actually confer minimal benefits on the shareholders they are intended to protect.[99]

Viewed through that lens, it is perhaps unsurprising that *Tornetta*, *Moelis*, and the general shift in standards for evaluating independence have all led to enormous outcry,[100] with the corporate bar and corporate managers accusing Delaware courts of being "skeptical of the governance of venture-backed private companies and many Silicon Valley-based companies,"

The Board of Directors Is in Charge, Bloomberg (Feb. 29, 2024), https://www.bloomberg.com/opinion/articles/2024-02-29/the-board-of-directors-is-in-charge ("Now, at some level, none of this matters. As a 40% shareholder (by voting rights), and the founder, CEO, chairman of the board and namesake of the firm, Ken Moelis probably can get the board to do most of what he wants, with or without a contract.")

[95] Jill Fisch & Steven Davidoff Solomon, *The Problem of Sunsets*, 99 B.U. L. Rev. 1057 (2019). Dual class rights do not directly confer interference with managerial decisionmaking but may have the same effect, especially when the rights holder is also a director and CEO, as was the case in *Moelis*, and is frequently true for other companies with dual-class shares, such as Meta.

[96] Jill E. Fisch, *Stealth Governance: Shareholder Agreements and Private Ordering*, 99 Wash. U. L. Rev. 913 (2021).

[97] This is particularly so if the objection VC Laster voiced in *Moelis* could be avoided by simply including a "fiduciary out" in the relevant shareholder agreement, explicitly giving the board the right to refuse to honor the contract if it believed its fiduciary duties so required. The language of the opinion – which criticized the fact that boards were *entirely* constrained by the agreement – would suggest a fiduciary out would indeed remedy the problem. *Cf.* Transcript of Hearing on a Motion to Expedite and for a TRO Held via Zoom, Miller v. Bartolo, 2024-0176-JTL (Del. Ch. Mar. 8, 2024) (allowing for the possibility that a fiduciary out might save an otherwise illegal shareholder agreement). Yet such an "out" would do substantive work only in the rarest of circumstances; most boards would be hesitant to buck an influential blockholder, especially one who also held an officer and board role. Its role, then, would be to create the appearance of preserving board discretion.

[98] Ann M. Lipton, *Beyond Internal and External: A Taxonomy of Mechanisms for Regulating Corporate Conduct*, 2020 Wisc. L. Rev. 657.

[99] *Cf.* Donald C. Langevoort, *The Social Construction of Sarbanes-Oxley*, 105 Mich. L. Rev. 1817, 1829-30 (2007) (arguing that the reforms passed in the wake of the Enron scandal were described as investor protection measures but designed to increase transparency and formalize decisionmaking procedures for the benefit of the general public).

[100] David Marcus, *Tulane: Discussing the Delaware Dilemma*, The Deal (March 12, 1994), https://pipeline.thedeal.com/article/0000018e-2f0d-de92-a3ee-3fed441b0000/deal-news/law/tulane-discussing-the-delaware-dilemma; Sujeet Indap, *The battle over who makes the rules for US companies*, Fin. Times (Aug. 4, 2024), https://www.ft.com/content/9effb213-6ec7-4f3a-9f81-b235bfc0c108.

and "adopt[ing] an increasingly suspicious or negative tone toward corporate boards and management, and toward the corporate bar."[101] Critics accused Delaware of "activist" and politicized decisionmaking,[102] implicitly recognizing the rightward shift of the firms whose governance structures were most impacted by these decisions. There have been open discussions about corporations organizing in other states,[103] to the point where the Delaware State Bar Association's Corporation Law Section quickly proposed, and the Delaware legislature almost immediately adopted, statutory amendments to overrule the *Moelis* decision and legalize governance via shareholder agreement.[104]

Most striking about these amendments was the relatively minimal pushback they received from investor-aligned groups[105] – and they even garnered some investors' limited support.[106] But investors' acquiescence was perhaps not surprising, when one recalls that, not long ago, major index providers proposed to exclude dual-class firms from their indices, purportedly to protect shareholders and yet, almost immediately, most providers dropped or watered-down the requirement,[107] because the reality was, many investors valued access to opportunities over whatever benefits "good governance" structures provide.[108]

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[101] Wilson Sonsini, *Delaware's Status as the Favored Corporate Home: Reflections and Considerations* (Apr. 23, 2024), https://www.wsgr.com/en/insights/delawares-status-as-the-favored-corporate-home-reflections-and-considerations.html; Stephen M. Bainbridge, *DExit Drivers: Is Delaware's Dominance Threatened?*, J. Corp. L. (forthcoming), https://papers.ssrn.com/sol3/papers.cfm?abstract_id=4909689 ("concerns about both the application of the law and the tone of the opinions are mounting").

[102] *See supra* text accompanying notes ___; Joel Edan Friedlander, *Former Chancellor Chandler's Unjust Criticism of Chancellor McCormick and Vice Chancellor Laster: What Does it Signify?*, J. Corp. L. (forthcoming), at 51, https://papers.ssrn.com/sol3/papers.cfm?abstract_id=4901375; Robert Anderson, https://x.com/ProfRobAnderson/status/1780616990471966978.

[103] Sujeet Indap, *Why the Tesla shareholder vote won't be the end of Elon Musk's Delaware fight*, Fin. Times (June 9, 2024), https://www.ft.com/content/70d99ef8-fa1a-4b4f-9f7b-7964f40ee1f8; Stephen M. Bainbridge, *DExit Drivers: Is Delaware's Dominance Threatened?*, J. Corp. L. (forthcoming), https://papers.ssrn.com/sol3/papers.cfm?abstract_id=4909689.

[104] Jeff Montgomery, *Delaware's Corporate Law Debate Left 'Blood On The Floor'*, Law360 (June 21, 2024), https://www.law360.com/articles/1850449.

[105] The Council of Institutional Investors, an advocacy group that largely consists of pension funds, wrote two letters objecting to the amendments. *See* Letter from Jeffrey P. Mahoney, General Counsel, Council of Institutional Investors, to Kate Harmon, President, Delaware State Bar Association (May 14, 2024), https://www.cii.org/files/issues_and_advocacy/correspondence/2024/Moelis_CII%20letter.pdf; Letter from Jeffrey P. Mahoney, General Counsel, Council of Institutional Investors, to The Honorable John C. Carney, Governor of Delaware (July 10, 2024), https://www.cii.org/files/issues_and_advocacy/correspondence/2024/July%2010,%202024%20CII%20letter%20to%20Delaware.pdf. No other investor groups, such as the Investment Company Institute (the trade association for mutual funds) took a public position.

[106] Jason Geeves-Booth, *Boards make more settlements with activists amid rising legal opposition*, Diligent (July 17, 2024), https://www.diligent.com/resources/blog/in-depth-boards-make-more-settlements-with-activists-amid-rising-legal-opposition.

[107] Council of Institutional Investors, *Index Providers and Dual-Class Stock*, https://www.cii.org/index-providers-dual-class-stock.

[108] Notably, the London Stock Exchange recently lifted its ban on dual-class listings. Though certain pension and sovereign wealth funds objected, their concerns did not carry the day at least in part because these investors did not hesitate to invest in other markets that offered fewer formal shareholder protections. *See* Tom Inchley, The Introduction of Multiple Class Share Structures to the UK Market, ISS Insights (Aug. 8, 2024), https://insights.issgovernance.com/posts/the-introduction-of-multiple-class-share-structures-to-the-uk-market/. *Cf.* Danielle A. Chaim & Asaf Eckstein, *A Theory of Trust-Based Governance in Startups*,

But the most dramatic pushback against Delaware's corporate governance formalities came when Tesla put Musk's pay package to a *second* shareholder vote, along with a proposal to redomesticate the company out of Delaware to Texas, where – the perception was – courts were less likely to second-guess Tesla's decisions.[109] Both resolutions passed by a significant margin, reflecting the support of major institutional investors such as BlackRock and Vanguard.[110] Commenters observed that Tesla had, fundamentally, rejected Delaware's standards of good governance[111] – and, it turned out, shareholders rejected them as well.

Now, one potential interpretation of the second vote was that it was not, in fact, entirely free and fair; at the time, Musk made clear that if shareholders bucked his wishes, he would develop AI in his outside ventures, using – as above – Tesla resources to do so. Shareholders may have believed that the only way to prevent these potential breaches of fiduciary duty was to acquiesce to his demands. But, even if shareholders were reacting to these threats, they must have believed that these fiduciary breaches could *not* be cured by additional Delaware litigation – as at least three groups of shareholders are currently attempting[112] – leaving an affirming shareholder vote as their only option to protect Tesla's value. In other words, however you slice it, the vote suggests shareholders did not believe that Delaware's formal legal standards were providing them many benefits at all.

Certainly, this is not the first time in Delaware's history that the state has been caught in this kind of dilemma.[113] During the hostile takeover era of the 1980s, for example, corporate raiders offered to buy out public shareholders at a healthy premium, with the intention of breaking up larger conglomerates.[114] These buyouts often ended in bankruptcy for the targeted

https://papers.ssrn.com/sol3/papers.cfm?abstract_id=4952630, at 25-27 (noting that large investors do not demand strong control rights when investing in private companies).

As above, the only shareholders to object to the DGCL amendments were also pension funds. *See supra* n. ___. As I have observed elsewhere, it is likely that pension funds (and sovereign wealth funds), as representatives of labor, have regulatory concerns that go beyond shareholder wealth maximization. *See* Ann M. Lipton, *Beyond Internal and External: A Taxonomy of Mechanisms for Regulating Corporate Conduct*, 2020 Wisc. L. Rev. 657, 676.

[109] Matt Levine, *Texas Tempts Tesla*, Bloomberg (Feb. 1, 2024), https://www.bloomberg.com/opinion/articles/2024-02-01/texas-tempts-tesla ("the bet here for Elon Musk is reasonable… is the Texas business court, in its first real high-profile case, going to say 'actually it's illegal to pay Elon Musk that much'? It absolutely is not."); Michael Hiltzik, Elon Musk thinks Tesla's investors love him. He's very wrong, L.A. Times (June 18, 2024), https://www.latimes.com/business/story/2024-06-18/elon-musk-thinks-teslas-investors-love-him-hes-very-wrong ("The Tesla board instantly executed the change of incorporation, which is evidently rooted in Musk's conviction that Texas courts, which have little experience in adjudicating corporate governance issues, will be more pliant in his hands than the very experienced Delaware judiciary.").

[110] Ross Kerber, *Vanguard vote switch helped pass Tesla CEO Elon Musk's $56 billion pay package*, Reuters (June 14, 2024), https://www.reuters.com/business/autos-transportation/vanguard-vote-switch-helped-pass-tesla-ceo-elon-musks-56-billion-pay-package-2024-06-14; BlackRock, *Vote Bulletin: Tesla, Inc.*, https://www.blackrock.com/corporate/literature/press-release/vote-bulletin-tesla-june-2024.pdf.

[111] Lucian Bebchuk, *Tesla Should Take the Court Decision Seriously*, Not Dismissively, Harv. L. Sch. F. Corp. Gov. (June 10, 2024), https://corpgov.law.harvard.edu/2024/06/10/tesla-should-take-the-court-decision-seriously-not-dismissively/ ("the Board seems to be following an approach of dismissal and defiance").

[112] Ball v. Tesla, 2024-0621 (Del. Ch. June 6, 2024); Cleveland Bakers & Teamsters Pension Fund v. Musk, 2024-0646 (Del. Ch. June 13, 2024); Employees' Ret. Sys. Rhode Island v. Musk, 2024-0631 (Del. Ch. June 10, 2024).

[113] *See* Michael Barzuza, *Nevada v. Delaware: The New Market for Corporate Law*, at https://papers.ssrn.com/sol3/papers.cfm?abstract_id=4746878.

[114] John C. Coffee, Jr., *Shareholders vs. Managers: The Strain in the Corporate Web*, 85 Mich. L. Rev. 1 (1986).

firm, and layoffs of substantial numbers of employees.[115] Delaware became trapped in the crosshairs, faced with a choice between corporate governance rules that would either *enable* these takeovers (which would benefit shareholders financially while harming everyone else), or inhibit them, by giving corporate boards tools to resist unwanted takeover bids.[116] At the time, Delaware defused that tension by insisting that boards consisting of independent directors – i.e., ones that adhered to procedural formalities – could legitimately employ antitakeover devices to protect the corporation's "long term" value, which just so happened to coincide with the interests of nonshareholder constituencies.[117] In other words, Delaware adopted a legal standard that protected societal interests while purporting to favor shareholders – or, rather, the board's expertise in determining what would be good for shareholders.

But in those hostile takeover disputes, the interests of incumbent corporate managers, concerned with maintaining their jobs, were aligned with those of employees and creditors, and arrayed against the demands of shareholders. Because, ultimately, managers alone are responsible for selecting where to incorporate, in the 1980s, managerial interests prevailed. Since that era, however, managerial contracts have come to include stock awards and "golden parachutes" that provide windfall financial benefits in response to a change in control, thus loosening resistance to takeovers.[118] Meaning, in today's disputes, managerial and shareholder interests are more likely in accord, while other corporate stakeholders stand on the other side of the table. That raises the question how long Delaware can maintain its formalist stance. As of this writing, just in the past few weeks, Meta, Dropbox, and Pershing Square Capital Management have all announced they are moving out of Delaware, or at least considering such moves.[119]

But if it is true that the *performance* of the formalities provides firms with the intangible benefit of societal acceptance, while only mildly curtailing managerial behavior, a question arises: Why are we now seeing a rebellion?

One possibility is that the prospect of new regulation – the kind that a social license to operate is meant to forestall – has dimmed. Delaware lawmakers – and, presumably, managers of Delaware-chartered corporations – have long understood that Delaware operates in the shadow of federal law. When corporate governance externalities create major catastrophes, the

[115] John C. Coffee, Jr., *Shareholders vs. Managers: The Strain in the Corporate Web*, 85 Mich. L. Rev. 1 (1986).
[116] Lyman P.Q. Johnson, *The Delaware Judiciary and the Meaning of Corporate Life and Corporate Law*, 68 Tex. L. Rev. 865 (1990).
[117] Lyman P.Q. Johnson, *The Delaware Judiciary and the Meaning of Corporate Life and Corporate Law*, 68 Tex. L. Rev. 865 (1990).
[118] Jeffrey N. Gordon, *The Rise of Independent Directors in the United States, 1950–2005: Of Shareholder Value and Stock Market Prices*, 59 Stan. L. Rev. 1465, 1534 (2007); Peer C. Fiss, Mark T. Kennedy, & Gerald F. Davis, *How Golden Parachutes Unfolded: Diffusion and Variation of a Controversial Practice*, 23 Org. Sci. 1077, 1080 (2012); Edward B. Rock, *Adapting to the New Shareholder-Centric Reality*, 161 U. Pa. L. Rev. 1907, 1917-18, 1924 (2013).
[119] Katie Balevic, *Billionaire hedge fund manager Bill Ackman says he will move management company out of Delaware*, Business Insider (Feb. 1, 2025), https://www.businessinsider.com/bill-ackman-pershing-square-capital-management-delaware-nevada-2025-2; Hannah Murphy, Stephen Morris, Sujeet Indap, & Patrick Temple-West, *Facebook parent Meta in talks to reincorporate outside Delaware*, Fin. Times (Jan. 31, 2025), https://www.ft.com/content/b4d136a2-c4b3-4b49-bfc7-3b5c0a1f7b49.

federal government steps in with new, mandatory rules that preempt Delaware's standards.[120] Delaware has in the past offered its own (milder) regulation as an alternative to more intrusive proposed federal rules,[121] and, so long as the state's oversight is recognized as sufficiently robust, federal regulators avoid invading Delaware's domain.[122] The prospect of federal preemption presumably limits the accommodations that Delaware can offer managers, and that managers demand of the Delaware legal system.

Today, however, political gridlock has made it very difficult for Congress to pass new legislation, and a conservative judiciary has dramatically curtailed the powers of the regulatory state.[123] The incoming Trump administration – backed by private equity and venture capital,[124] is likely to be particularly averse to imposing new constraints on corporate internal governance structures. Without the threat of federal preemption looming, neither Delaware lawmakers, nor managers of Delaware companies, have a use for modesty.[125]

But if that's right, there is a final irony. The more freedom Delaware accords corporate managers, and the less scrutiny it applies to their transactions, the less there is for Delaware to, well, actually do. That threat is particularly stark in light of the recent amendments to Delaware law, because shareholder agreements – unlike Delaware charters – are not subject to the internal affairs doctrine and may not be governed by Delaware law.[126] In other words, these newly-authorized shareholder agreements may be interpreted, and enforced, according to a law *other than* Delaware's. The more that corporate governance moves into personal contracts (and other states are likely to follow Delaware's lead) the less important the state of incorporation may become, which erodes Delaware's dominance. And, as if to bring that point home more clearly, disputes regarding these contracts may be decided in non-Delaware courts, including arbitral courts, where Delaware will be powerless to control the standards applied.[127]

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[120] Mark J. Roe, *Delaware's Competition*, 117 Harv. L. Rev. 588 (2003); Mark J. Roe, *Is Delaware's Corporate Law Too Big to Fail?*, 74 Brook. L. Rev. 75 (2008).

[121] Mark J. Roe, *The Corporate Shareholder's Vote and Its Political Economy, in Delaware and in Washington*, 2 Harv. Bus. L. Rev. 1, 31 (2012); William W. Bratton & Joseph A. McCahery, *The Equilibrium Content of Corporate Federalism*, 41 Wake Forest L. Rev. 619 (2006).

[122] For example, the federal Securities Litigation Uniform Standards Act of 1998, Pub. L. No. 105-353, 112 Stat. 3227, requires certain stockholder actions to be litigated exclusively in federal court, but contains a provision colloquially known as the "Delaware carve-out" to except the types of actions that Delaware traditionally hears. *See* Cecilia A. Glass, Note, *Sword or Shield? Setting Limits on SLUSA's Ever-Growing Reach*, 63 Duke L.J. 1337, 1347 (2014). During the debates over the recent amendments to Delaware law, Professor Charles Elson warned that the changes might invite federal intrusion. *See* Senate Judiciary Debate (June 11, 2024), 152nd Delaware General Assembly.

[123] Loper Bright Enterprises v. Raimondo, 144 S.Ct. 2244 (2024); West Virginia v. EPA, 597 U. S. 697 (2022); Nat'l Assoc. of Private Fund Mgrs v. SEC, 103 F.4th 1097 (5th Cir. 2024); Chamber of Commerce v. SEC, 88 F.4th 1115 (5th Cir. 2023).

[124] William A. Birdthistle, *How Private Funds Could Hurt Americans Under Trump*, N.Y. Times (Dec. 3, 2024), https://www.nytimes.com/2024/12/03/opinion/trump-presidency-billionaires.html.

[125] For example, the Business Roundtable – an association of Chief Executive Officers – endorse independent director requirements when regulatory threats loom, and pull back when the threat recedes. Mariana Pargendler, *The Corporate Governance Obsession*, 42 J. Corp. L. 359, 377-78, 385 (2016).

[126] *See* Ann M. Lipton, *Inside Out (or, One State to Rule Them All): New Challenges to the Internal Affairs Doctrine*, 58 Wake Forest L. Rev. 321 (2023).

[127] The reason for this is twofold. First, the statutory amendments authorizing stockholder agreements explicitly permit signatories to select any forum, including an arbitral forum, for resolving disputes, *see* Del. Gen. Assembly,

II. The Stewardship Solution

If the first premise of shareholder primacy is that it offers meaningful constraints on corporate managers, the second is that, in a properly functioning system, those constraints channel corporate behavior in a prosocial direction. That creates a curious dilemma for proponents of shareholder primacy, because its logic requires them to continually equate societal interests with shareholder interests. The effort only ends up replicating the problems that shareholder primacy was intended to solve.

The contradictions surfaced at least as far back as the 1970s, with the waning of the managerial era. The country was rocked by a series of corporate scandals, some of which were financial and directed at investors, but others of which involved political bribery and other forms of illegal behavior that were intended to – and possibly had the effect of – benefitting shareholders.[128] The SEC quickly moved to render management more "accountable" by improving corporate governance, namely by increasing shareholder voice, indirectly via independent directors, and directly by increasing both the power and responsibilities of institutional shareholders.[129] The initiatives were of a piece with the SEC's general approach of the era, which was to assume that managerial ethics and character factor in to investor decisonmaking, and seek disclosure of information relevant to those qualities.[130]

The SEC's views were controversial and opposed by many shareholder primacists, who argued that the Commission's mission was to protect investors, and not society at large.[131] For example, Professor Daniel Fischel, writing in 1982, criticized the SEC's corporate governance reforms, on the ground that the Commission had conflated harms to investors with harms to society more generally.[132] But in the same article, not two pages later, Professor Fischel defended a core premise of shareholder primacy: that, in fact, investor interests *are* coextensive with society's interests, because corporations are forced to internalize the costs of the harms they

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S.B. 313 Bill, and second, the Federal Arbitration Act prohibits states from limiting agreements to arbitrate in ordinary contracts, *see* Ann M. Lipton, *Manufactured Consent: The Problem of Arbitration Clauses in Corporate Charters and Bylaws*, 104 Geo. L.J. 583 (2016).

[128] Jeffrey N. Gordon, *The Rise of Independent Directors in the United States, 1950-2005: Of Shareholder Value and Stock Market Prices*, 59 Stan. L. Rev. 1465, 1511-17 (2007); Lewis D. Solomon, *Restructuring the Corporate Board of Directors: Fond Hope - Faint Promise?*, 76 Mich. L. Rev. 581 (1978); Daniel R. Fischel, *The Corporate Governance Movement*, 35 Vand. L. Rev. 1259, 1267 (1982).

[129] Div. of Corp. Fin., U.S. SEC & Exch. Comm'n, Staff Report on Corporate Accountability: A Re-Examination of Rules Relating to Shareholder Communications, Shareholder Participation in the Corporate Electoral Process and Corporate Governance Generally 31 (Sept. 4, 1980) (printed for the use of S. Comm. on Banking, Housing, and Urban Affairs, 96th Cong., 2d Sess.) [hereinafter "Staff Report"]; *see also* Daniel R. Fischel, *The Corporate Governance Movement*, 35 Vand. L. Rev. 1259 (1982); Mariana Pargendler, *The Corporate Governance Obsession*, 42 J. Corp. L. 359, 376 (2016).

[130] *See* Ann M. Lipton, *Not Everything is About Investors: The Case for Mandatory Stakeholder Disclosure*, 37 Yale J. on Reg. 499, 549 (2020).

[131] *See, e.g.*, Bevis Longstreth, *SEC Disclosure Policy Regarding Management Integrity*, 38 Bus Law. 1413, 1423-27 (1983); Milton Freeman, *The Legality of the SEC's Management Fraud Program*, 31 Bus. Law. 1295 (1976).

[132] Daniel R. Fischel, *The Corporate Governance Movement*, 35 Vand. L. Rev. 1259, 1267 (1982) ("questionable foreign payments and noncompliance with environmental laws, in all probability are explainable as attempts by managers to boost profitability, shareholders are far more likely to be beneficiaries of these practices rather than victims.")

inflict.[133] In other words, what Professor Fischel unwittingly revealed is that once shareholder primacy's fundamental axioms are accepted, it is difficult to avoid the full implications, such as an expectation that reforms of corporate governance – and in particular, reforms that focus managerial attention more tightly on shareholder interests – work as a corrective to general corporate malfeasance.

From there, the next logical step is to turn to corporate governance as an all-purpose regulatory tool. And so politicians have done, regularly filtering reforms intended for the general public through the language of investor protection, such as combatting income inequality by giving shareholders an advisory vote on corporate pay packages and requiring disclosure of the ratio of CEO pay to median worker pay,[134] requiring disclosure of how diversity considerations factor in to director nominations,[135] and requiring disclosure of how risk-taking factors in to compensation decisions.[136] The 2010 Dodd-Frank Act, passed in the wake of the Great Financial Crisis, limited the ability of brokers to cast ballots on behalf of shareholders who did not vote themselves; as brokers default to voting with management, the move was intended to enhance shareholder oversight.[137] Frequently, independent directors – who, with their lack of ties to corporate management, are one of the procedural mechanisms employed to (purportedly) render corporate management more responsive to shareholders – are enlisted to the project of making corporations more socially responsible.[138] Businesses, of course, enthusiastically insist that shareholder profits are unattainable absent prosocial behavior,[139] while accepting or even advocating for independent directors as a substitute for more robust regulation.[140] The popular press plays into the same narrative, laying the blame for corporate scandals at the feet of captured boards.[141]

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[133] Daniel R. Fischel, *The Corporate Governance Movement*, 35 Vand. L. Rev. 1259, 1269 (1982) ("Although potential conflict exists between profit maximization and pursuit of other goals, far more consistency is present between the two than generally assumed…. Substantial overlap exists, therefore, between the pursuit of profit maximization and other social goals.").

[134] Mariana Pargendler, *The Corporate Governance Obsession*, 42 J. Corp. L. 359, 391 (2016); Ann M. Lipton, *Not Everything is About Investors: The Case for Mandatory Stakeholder Disclosure*, 37 Yale J. on Reg. 499, 558 (2020).

[135] 17 CFR § 229.407.

[136] 17 CFR § 229.402. This type of disclosure is of especially questionable benefit for equity holders, who are likely diversified and therefore prefer risk-taking. *See* Daniel J.H. Greenwood, *Fictional Shareholders: For Whom are Corporate Managers Trustees, Revisited*, 69 S. Cal. L. Rev. 1021, 1073 (1996).

[137] Mariana Pargendler, *The Corporate Governance Obsession*, 42 J. Corp. L. 359, 388 (2016).

[138] Mariana Pargendler, *The Corporate Governance Obsession*, 42 J. Corp. L. 359, 376 (2016); Urska Velikonja, *The Political Economy of Board Independence*, 92 N.C. L. Rev. 855, 904 (2014); Donald C. Langevoort, *The Social Construction of Sarbanes-Oxley*, 105 Mich. L. Rev. 1817, 1829, 1831 (2007) (explaining that shareholders were not the main beneficiary of post-Enron reforms, including director independence requirements); Daniel R. Fischel, *The Corporate Governance Movement*, 35 Vand. L. Rev. 1259, 1266-67 (1982) (arguing that the SEC's 1980 report on corporate governance reforms – which included a call for greater directorial independence – were intended for the public despite claims they would benefit shareholders); Yaron Nili & Claire Hill, *Independence Reconceived*, 2023 Colum. Bus. L. Rev. 589, 597-99, 629-30.

[139] Bus. Roundtable, Redefined Purpose of a Corporation: Welcoming the Debate, Medium (Aug. 25, 2019), https://bizroundtable.medium.com/redefined-purpose-of-a-corporation-welcomingthe-debate-8f03176f7ad8 ("for corporations to be successful, durable and return value to shareholders, they must consider the interests and meet the fair expectations of a wide range of stakeholders in addition to shareholders").

[140] *See supra* n. ___; Urska Velikonja, *The Political Economy of Board Independence*, 92 N.C. L. Rev. 855, 906 (2014).

[141] *See, e.g.*, Douglas MacMillan, *'Safety was just a given': Inside Boeing's boardroom amid the 737 Max crisis*, Wash. Post (May 5, 2019), https://www.washingtonpost.com/business/2019/05/06/safety-was-just-given-inside-

The flaw in this logic is that shareholder primacy is not self-executing; the theory posits that the regulatory system will render antisocial behavior unprofitable, not that antisocial behavior will be curbed by shareholders as a substitute for regulation. To the contrary, absent regulation, an empowered institutional shareholder base may very well urge equity-price maximizing actions that do significant damage to other corporate constituencies, such as creditors, employees, customers.[142] But that inconvenient truth tends to be skipped over in favor of regulatory moves that imply the system *already works*, such that the only problem to be solved is a corporate governance apparatus that does not make the appropriate calculus.[143]

No doubt, the choice to filter regulation intended to benefit society through an "investor protection" rationale represents a political compromise, in situations where more direct regulation may not be politically feasible.[144] And that compromise may serve some limited purpose; for example, independent directors, with fewer ties to the corporation, may be more responsive to legal guardrails, and more concerned about their own – and consequently the firm's – image in the eyes of the public (which is precisely why more independent directors at Tesla might have restrained Elon Musk's compensation package).[145] But of course, that line of

boeings-boardroom-amid-max-crisis/; Matt Egan, *Boeing has a 'crisis of confidence.' It's time for the board to step up*, CNN (May 16, 2019), https://www.cnn.com/2019/05/16/business/boeing-737-max-crisis-faa/index.html; James B. Stewart, *Problems at Volkswagen Start in the Boardroom*, N.Y. Times (Sept. 24, 2015), https://www.nytimes.com/2015/09/25/business/international/problems-at-volkswagen-start-in-the-boardroom.html; Russell Adams & Joann S. Lublin, *News Corp. Board Challenged*, Wall St. J. (July 26, 2011), https://www.wsj.com/articles/SB10001424053111903591104576468332122262092; David Carr, *The Cozy Compliance of the News Corp. Board*, N.Y. Times (May 6, 2012), https://www.nytimes.com/2012/05/07/business/media/the-cozy-compliance-of-the-news-corp-board.html; Geoff Colvin, *Who's to blame at BP? The board*, CNN (July 28, 2010), https://money.cnn.com/2010/07/28/news/companies/bp_board_to_blame.fortune/index.htm. This has also been true in some private companies. *See, e.g.*, Reuters, *A Challenge to Finding Uber's New COO: Its CEO*, Fortune (Apr. 13, 2017), http://fortune.com/2017/04/13/ceo-kalanick-coo-search-culture; Jennifer Reingold, *Theranos' board: Plenty of political connections, little relevant expertise*, Fortune (Oct. 15, 2015), https://fortune.com/2015/10/15/theranos-board-leadership/.

[142] Mariana Pargendler, *The Corporate Governance Obsession*, 42 J. Corp. L. 359, 386-87 (2016); Leo E. Strine, Jr., *Our Continuing Struggle with the Idea that For-Profit Corporations Seek Profit*, 47 Wake Forest L. Rev. 135 (2012); Edward B. Rock, *Adapting to the New Shareholder-Centric Reality*, 161 U. Pa. L. Rev. 1907, 1917-18, 1924 (2013).

[143] Frequently, the claim is something like "short-termism," namely, an insistence that companies engage in socially harmful behavior because their governance structures prevent them from rationally identifying the superior profits to be gained longer term by prosocial behavior. In fact, the evidence of an irrational "short-term" market focus is mixed at best. Mark J. Roe, *Stock Market Short-Termism: What the Empirical Evidence Tells Policymakers*, https://papers.ssrn.com/sol3/papers.cfm?abstract_id=4087746; Michal Barzuzaa & Eric Talley, *Long-Term Bias*, 2020 Colum. Bus. L. Rev. 104.

[144] Urska Velikonja, *The Political Economy of Board Independence*, 92 N.C. L. Rev. 855, 906 (2014); Mariana Pargendler, *The Corporate Governance Obsession*, 42 J. Corp. L. 359, 366 (2016).

[145] *See* Yaron Nili & Claire Hill, *Independence Reconceived*, 2023 Colum. Bus. L. Rev. 589, 629-30 (independent directors associated with fewer incidents of corporate misconduct); Jeffrey N. Gordon, *The Rise of Independent Directors in the United States, 1950–2005: Of Shareholder Value and Stock Market Prices*, 59 Stan. L. Rev. 1465, 1509 (2007) ("Independent directors may be more likely to promote the firm's compliance with legal norms."); Edward B. Rock, *Saints and Sinners: How Does Delaware Corporate Law Work?*, 44 UCLA L. Rev. 1009, 1103-04 (1997) (arguing that professionalized directors are more responsive to public shaming via exposure of misconduct than are entrepreneurs who run businesses on a day to day basis); Donald C. Langevoort, *The Human Nature of Corporate Boards: Law, Norms, and the Unintended Consequences of Independence and Accountability*, 89 Geo. L.J. 797, 804 (2001) (independent directors protect their reputations with regulators).

thinking posits that the value of independent directors comes from their *lack* of responsiveness to shareholders, rather than their alignment with them, which contradicts the entire premise of shareholder primacy. Thus, the overt rationale for these kinds of regulatory responses is that independent directors will be more vigorous in their pursuit of shareholder interests.[146]

All of which has culminated in the recent push toward, and controversy surrounding, "environmental, social, governance" ("ESG") investing. As I have explained elsewhere,[147] "ESG" sometimes describes a values or impact-based style of investing, but other times, especially among the professional investment community, refers to a financial strategy that posits prosocial corporate behavior is ultimately more profitable for investors.[148] In that form, ESG can be understood as gesture of profound faith in shareholder primacy's viability. After all, if shareholder primacy is operating as expected, it is only natural that profit-seeking investors should go further and make prosociality the actual investment thesis – indeed, it is *necessary* that they do so. To demand otherwise is to concede that shareholder primacy has failed, and that external regulation has not, in fact, aligned the interests of shareholders with the interests of the general public at all.[149] And because most investors are institutions, with fiduciary obligations toward their natural-person beneficiaries, the next step is for the regulatory apparatus surrounding these institutions to encourage or even require that they affirmatively demand prosocial behavior from their portfolio firms.

The seeds of this were again sown in the 1970s, when the public company shareholder base began to transform from retail shareholders – natural persons – to institutions, such as pension and mutual funds.[150] In the wake of the corporate scandals of the era, the SEC's push for greater corporate accountability included a new emphasis on the fiduciary obligations of institutional shareholders to use their voting power to influence the behavior of their portfolio companies.[151] From there, shareholder power – and institutional shareholder responsibilities – have only ramped up, largely through the securities laws, but also through labor law, in the form of oversight of private pension plan investors. In the 1990s and 2000s, the SEC and the Department of Labor promulgated rules requiring that institutional investors disclose their policies for proxy voting.[152] In 2003, the SEC began to require disclosure of how mutual funds exercise their votes, explaining:

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[146] *E.g.*, Staff Report, *supra*, at 428.
[147] *See* Ann M. Lipton, *ESG Investing, or, If You Can't Beat 'Em, Join 'Em*, in Research Handbook on Corporate Purpose and Personhood (Elizabeth Pollman & Robert Thompson, eds. 2021).
[148] Elizabeth Pollman, *The Making and Meaning of ESG*, Harv. Bus. L. Rev. (forthcoming), https://papers.ssrn.com/sol3/papers.cfm?abstract_id=4219857; Max M. Schanzenbach & Robert H. Sitkoff, *Reconciling Fiduciary Duty and Social Conscience: The Law and Economics of ESG Investing by a Trustee*, 72 Stan. L. Rev. 381, 398 (2020); Robert T. Miller, *How Would Directors Make Business Decisions Under Stakeholder Model?*, 77 Bus. Law. 773, 776 n.8 (2022); Pitchbook, Sustainable Investment Survey 24 (2024).
[149] David G. Yosifon, *The Citizens United Gambit in Corporate Theory: A Reply to Bainbridge on Strine and Walter* 2 (Santa Clara Univ. Sch. of L., Working Paper No. 4-14, 2014), https://ssrn.com/abstract=2510967; Leo E. Strine, Jr. & Nicholas Walter, *Conservative Collision Course?: The Tension Between Conservative Corporate Law Theory and* Citizens United, 100 Cornell L. Rev. 335, 379-82 (2015).
[150] Amy Deen Westbrook & David A. Westbrook, *Unicorns, Guardians, and the Concentration of the U.S. Equity Markets*, 96 Neb. L. Rev. 688, 730 (2018); Staff Report, *supra*, at 381.
[151] Staff Report, *supra*, at 390-91.
[152] Ann M. Lipton, *Family Loyalty: Family Loyalty: Mutual Fund Voting and Fiduciary Obligation*, 19 Tenn. J. Bus. L. 175, 185-85 (2017).

> Recent corporate scandals have … underscored the need for mutual funds and other institutional investors to focus on corporate governance. The increased equity holdings and accompanying voting power of mutual funds place them in a position to have enormous influence on corporate accountability. As major shareholders, mutual funds may play a vital role in monitoring the stewardship of the companies in which they invest.[153]

The Supreme Court even got into the act when it relied on shareholder "voice" to control corporate political spending.[154] Thus, when the United Nations developed the concept of ESG investing (originally as a means to encourage responsible industrialization of the developing world[155]), the infrastructure was in place to enlist large asset managers as stewards of the *social* behavior of their portfolio companies. Mutual fund companies leaned in to the idea – much like operating companies embraced independent directors – likely because they believed it would forestall more intrusive regulation of their activities.[156] Certainly, their commitment to ESG did not smack of true belief; evidence of "greenwashing," both in portfolio assembly and voting behavior, abounded.[157] Nonetheless, the *logic* of shareholder primacy – that ultimately profitability is achieved via prosociality – lent the project a veneer of legitimacy.[158] Political activists leaped on the bandwagon, almost certainly because of the potential for policy wins that an unresponsive federal bureaucracy made difficult to achieve via substantive regulation.[159] And

[153] Disclosure of Proxy Voting Policies and Proxy Voting Records by Registered Management Investment Companies, Securities Act Release No. 8188, Exchange Act Release No. 47,304, Investment Company Act Release No. 25,922, 2003 WL 215451 (Jan. 31, 2003).
[154] Citizens United v. Federal Election Comm'n, 558 U.S. 310, 361-62 (2010).
[155] Elizabeth Pollman, *The Making and Meaning of ESG*, Harv. Bus. L. Rev. (forthcoming), https://papers.ssrn.com/sol3/papers.cfm?abstract_id=4219857.
[156] Jeff Schwartz, *Stewardship Theater*, 100 Wash. U. L. Rev. 393, 432 (2022); Amanda M. Rose, *A Response to Calls for SEC-Mandated ESG Disclosure*, 98 Wash. U. L. Rev. 1821, 1824-25 (2021).
[157] *E.g.*, Shane Shifflet, *Funds Go Green, but Sometimes in Name Only*, Wall St. J. (Sept. 9, 2021), https://www.wsj.com/articles/funds-go-green-but-sometimes-in-name-only-11631179801; Roni Michaely, Guillem Ordonez-Calafi, & Silvina Rubio, *Mutual funds' strategic voting on environmental and social issues*, Rev. Fin. (forthcoming), https://doi.org/10.1093/rof/rfae017.

A recent contretemps involving the Exxon Corporation stands out. The shareholder proposal mechanism, created by federal Rule 14a-8, 17 CFR § 240.14a-8, is one of the key avenues by which shareholders express a preference for ESG initiatives. Recently, Exxon brought a lawsuit against two shareholders who filed a proposal pertaining to climate change, alleging that the proposal violated the proxy rules. *See* Exxon Mobil Corp. v. Arjuna Capital, 2024 WL 3075862 (N.D. Tex. June 17, 2024). The case was widely viewed as an attempt to deter future proposals, and, in response, a handful of institutional shareholders – and one proxy advisory firm – publicly argued that investors should punish Exxon for attempting to minimize shareholder voice by voting against various Exxon directors at the next annual meeting. *See* Ross Kerber, *Glass Lewis recommends votes against Exxon director Hooley, citing lawsuit*, Reuters (May 13, 2024), https://www.reuters.com/sustainability/boards-policy-regulation/glass-lewis-recommends-votes-against-exxons-hooley-citing-lawsuit-2024-05-13/. Despite the campaign, few shareholders withheld their votes, *see* Report on Form 8-K, Exxon Mobil (May 31, 2024), https://www.sec.gov/ix?doc=/Archives/edgar/data/34088/000003408824000036/xom-20240529.htm, suggesting many were not interested in defending shareholder voice on ESG topics after all.
[158] This is why some of the most vigorous defenders of shareholder wealth maximization as the sole corporate purpose concede that ESG is simply an expression of shareholder primacy *See* Stephen M. Bainbridge, The Profit Motive: Defending Shareholder Value Maximization 104 (2023); Robert T. Miller, *How Would Directors Make Business Decisions Under Stakeholder Model?*, 77 Bus. Law. 773, 776 n.8 (2022).
[159] Ann M. Lipton, *Every Billionaire is a Policy Failure*, *Every Billionaire is a Policy Failure*, 18 Va. L. & Bus. Rev. 327, 422-23 (2024).

they, too, could emphasize the shareholder primacist logic – that shareholder wealth maximization can only be achieved via prosociality – that at this point had been woven into the system.[160] Climate change, gun violence, racial, gender, and sexual orientation diversity, have all become corporate governance concerns, promoted by advocates ostensibly for the financial value they add to firms,[161] while opponents insist they represent the pet political concerns of corporate "elites" rather than any sincere strategy for maximizing profits.[162]

The issue soon escalated into regulatory warfare, with Democrats and Republicans ping ponging back and forth about how much leeway – if any – asset managers should be given to consider these issues when making investment decisions.[163] Nineteen Republican state attorneys

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[160] *See, e.g.*, Letter from Amazon Watch & First Peoples Worldwide, to The Honorable Gary Gensler, Chair, U.S. Securities and Exchange Commission (June 16, 2022), https://www.sec.gov/comments/s7-10-22/s71022-20131665-302054.pdf (arguing that investors need corporations to disclose the risks their activities pose to indigenous communities); As You Sow, Coca-Cola Co: Mitigation of Risks Related to Restrictive Public Health Care Policies (Nov. 2023), https://www.asyousow.org/resolutions/2023/11/9-coca-cola-mitigation-risks-reproductive-healthcare-policies (arguing that investors need the company to disclose its strategy to ameliorate employee harm caused by restricted access to reproductive healthcare); Trinity Wall Street v. Wal-Mart Stores, 792 F.3d 323 (3d Cir. 2015) (addressing a shareholder proposal seeking that Wal-Mart develop a policy for oversight of gun sales, out of concern for the firm's reputation and brand).

[161] *E.g.*, Testimony of James Andrus, Investment Manager, Board Governance and Sustainability California Public Employees' Retirement System, Before the United States House of Representatives Committee on Financial Services Subcommittee on Investor Protection, Entrepreneurship and Capital Markets (Feb. 25, 2021), https://www.congress.gov/117/meeting/house/111245/witnesses/HHRG-117-BA16-Wstate-AndrusJ-20210225.pdf; Testimony of Andy Green, Senior Fellow, Center for American Progress, Before the United States House of Representatives Committee on Financial Services Subcommittee on Investor Protection, Entrepreneurship and Capital Markets (Feb. 25, 2021), https://democrats-financialservices.house.gov/uploadedfiles/hhrg-117-ba16-wstate-greena-20210225.pdf; Notice of Filing of Proposed Rule Change to Adopt Listing Rules Related to Board Diversity, Release No. 34-90574, 85 Fed. Reg. 80,472 (Dec. 11, 2020); Jeffrey S. Davis, Senior Vice President, Senior Deputy Counsel, Nasdaq, Response to Comments and Notice of Filing of Amendment No. 1 of Proposed Rule Change to Adopt Listing Rules Related to Board Diversity (Feb. 26, 2021), https://www.sec.gov/comments/sr-nasdaq-2020-081/srnasdaq2020081-8425992-229601.pdf.

[162] James Call, Gov. *Ron DeSantis moves to prohibit state investments in 'woke' agenda*, Tallahassee Democrat (Aug. 23, 2022); Vivek Ramaswamy, Woke, Inc.: Inside Corporate America's Social Justice Scam (2021); Lawrence Cunningham et al., *The SEC's Misguided Climate Disclosure Rule Proposal* (Jan. 5, 2023), https://papers.ssrn.com/sol3/papers.cfm?abstract_id=4256724; Jay Ashcroft, *Opinion: It's Time to Rein In ESG*, Missouri Times (July 18, 2023), https://themissouritimes.com/opinion-its-time-to-rein-in-esg/ ("ESG and the Corporate Equality Index (CEI) are part of the so-called 'ethical investing' movement being pushed by progressives, activist shareholders, and proxy voters, driving investments toward liberal priorities that are in conflict with investors' interests").

[163] Dep't of Labor, Interpretive Bulletin Relating to Exercise of Shareholder Rights (Oct. 17, 2008), 2008 WL 4600732; Dep't of Labor, Interpretive Bulletin Relating to the Fiduciary Standard Under ERISA in Considering Economically Targeted Investments (Oct. 26, 2015), 2015 WL 6438622; Dep't of Labor, Interpretive Bulletin Relating to the Exercise of Shareholder Rights and Written Statements of Investment Policy, Including Proxy Voting Policies or Guidelines (Dec. 29, 2016), 2016 WL 7453352; Dep't of Labor, Field Assistance Bulletin No. 2018-01 (Apr. 23, 2018), 2018 WL 2387479; Financial Factors in Selecting Plan Investments, 85 Fed. Reg. 39113 (proposed June 30, 2020); Fiduciary Duties Regarding Proxy Voting and Shareholder Rights, 85 Fed. Reg. 55219 (proposed Sept. 4, 2020); Financial Factors in Selecting Plan Investments, 85 Fed. Reg. 72846-01 (Nov. 13, 2020); Fiduciary Duties Regarding Proxy Voting and Shareholder Rights, 85 Fed. Reg. 81658 (Dec. 16, 2020); Prudence and Loyalty in Selecting Plan Investments and Exercising Shareholder Rights, 87 Fed. Reg. 73822 (2022) (codified at 29 C.F.R. pt. 2550); Diego Areas Munhoz & Ben Biller, *Anti-ESG 401(k) Republican Bills Package Passed by the House*, Bloomberg Law (Sept. 18, 2024), https://news.bloomberglaw.com/daily-labor-report/anti-esg-401k-republican-bills-package-passed-by-the-house.

general accused asset manager BlackRock of violating its fiduciary obligations by encouraging portfolio companies to combat climate change,[164] and five Democratic Senators accused BlackRock of violating its fiduciary obligations by opposing efforts to encourage portfolio companies to combat climate change.[165] A Republican-appointed federal district judge in Texas concluded after a bench trial that American Airlines violated its fiduciary obligations to 401(k) plan members by including BlackRock funds with ESG voting policies on the investment menu.[166] The SEC amended its rules to require more granular public disclosure of mutual funds' proxy votes, including on issues pertaining to environmental matters, human rights, and diversity,[167] and four Republican-led states petitioned to vacate the rule, arguing that disclosure would enable activists to pressure asset managers into violating their fiduciary obligations.[168]

The controversy has mostly raged with respect to regulation of institutional investors, both at the federal and state levels,[169] but has also expanded to the realm of corporate governance. A proxy contest at Disney was waged in part over whether the company had gone "woke" by developing films with women and nonwhite leads.[170] Writing as the investment adviser to the New York City Retirement Systems pension funds, Comptroller Brad Lander urged Walmart and other retailers to begin dispensing the abortion drug mifepristone, arguing that the failure to take advantage of a "market opportunity" threatened "long-term shareholder value."[171] In response, a consortium of religious investors urged Walmart *not* to dispense mifepristone, in order to avoid "alienating its diverse customers and potential customers" for its remaining products.[172] And the whole mess has landed in Delaware's lap, via accusations over whether corporations do – or do not – violate fiduciary duties to shareholders when they adopt diversity

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[164] Letter from Mark Brnovich, Arizona Attorney General et al, to Laurence D. Fink, CEO, BlackRock Inc. (Aug. 4, 2022), https://www.texasattorneygeneral.gov/sites/default/files/images/executive-management/BlackRock%20Letter.pdf.

[165] Letter from Brian Schatz, U.S. Senator, at al., to Larry Fink, Chairman & CEO, BlackRock (Oct. 8, 2020), https://www.schatz.senate.gov/imo/media/doc/Letter%20to%20BlackRock%20on%202020%20proxy%20voting%20record_2020.10.08.pdf.

[166] Spence v. American Airlines, 2025 WL 225127 (N.D. Tex. Jan. 10, 2025).

[167] Enhanced Reporting of Proxy Votes by Registered Management Investment Companies; Reporting of Executive Compensation Votes by Institutional Investment Managers, 87 Fed. Reg. 78770-01 (Dec. 22, 2022).

[168] *See* Brief for Petitioners, Texas et al. v. Securities & Exchange Comm'n, No. 23-60079 (5th Cir. filed Sept. 5, 2023). The challenge was rejected by the Fifth Circuit. Texas et al. v. Securities & Exchange Comm'n, 2024 WL 2106183 (5th Cir. May 10, 2024).

[169] In addition to the controversies described above, various states have restricted their public pension funds from adopting ESG investing strategies, *see, e.g.*, David Hood, *DeSantis Signs Sweeping Anti-ESG Bill Targeting Funds, Banks*, Bloomberg Law (May 2, 2023), https://news.bloomberglaw.com/esg/desantis-signs-sweeping-anti-esg-bill-targeting-funds-banks, prompting at least one lawsuit, *see*, Brenna Goth, *Oklahoma Judge Blocks Anti-ESG Law Targeting Financial Firms*, Bloomberg Law (July 22, 2024), https://news.bloomberglaw.com/esg/oklahoma-judge-blocks-anti-esg-law-that-targets-financial-firms. Meanwhile, New York pensioners (unsuccessfully) sued various city retirement plans, alleging that the plans' ESG investments threatened the plans' financial health. Wong v. N.Y. City Employees' Ret. Sys., 2024 WL 3276803 (N.Y. Sup. July 2, 2024).

[170] Rebecca Alter & Savannah Salazar, *Nelson Peltz Lost the Battle for Disney*, Vulture (Apr. 3, 2024), https://www.vulture.com/article/disney-proxy-fight-shareholder-meeting-nelson-peltz.html.

[171] *See* New York City Comptroller Brad Lander, *NYC Comptroller Presses Pharmacy Giants To Provide Abortion Medication or Risk Losing Investor Confidence* (July 17, 2024), https://comptroller.nyc.gov/newsroom/nyc-comptroller-presses-pharmacy-giants-to-provide-abortion-medication-or-risk-losing-investor-confidence.

[172] *See* Letters from Robert Netzly, CEO, Inspire Investing et al to CEOs of Walmart, Costco, Kroger, Albertsons, and McKesson (Aug. 2, 2024), https://storage.googleapis.com/vds_storage/document/Investor%20Mifepristone%20Letters%20080524.pdf.

programs and other political stances. In *Kiger v. Mollenkopf*, a shareholder (unsuccessfully) alleged that Qualcomm violated its fiduciary duties to investors by overstating its efforts to diversify its board.[173] In *Simeone v. Walt Disney Corporation*,[174] a shareholder sought internal corporate documents to investigate then-Disney CEO Bob Chapek's opposition Florida's parental rights law, colloquially known as "Don't Say Gay," which had goaded Florida's governor into revoking certain Disney corporate privileges. The claim was denied due to Delaware's well-established deference to corporate managers,[175] but that only fueled charges that Delaware had become politicized and was bowing to liberal pressure.[176] Other high profile disputes – such as Target's marketing of Pride merchandise and Bud Light's courting of a transgender influencer, both of which resulted in boycotts and stock price drops[177] – have drawn additional claims of breach of fiduciary duty (though those companies are not incorporated in Delaware).[178] The upshot of all of this is that shareholders have now been drawn into the precise political thicket that an emphasis on "stewardship" over direct regulation was intended to avoid in the first place.[179]

There is no obvious escape from the trap, because, ultimately, under shareholder primacy, profitability is treated as proof market preferences, and market preferences are taken as a kind of

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[173] Transcript of Oral Argument and Rulings of the Court on Defendants' Motion to Dismiss the Class Action Complaint, Kiger v. Mollenkompf, No. 2023-0444-JTL (Del. Ch. May 9, 2024). In another case, a shareholder settled claims that a healthcare trust refused to appoint Black individuals to top management roles and directorships. *See* Katryna Perera, *Healthcare Co. To Pay Atty Fees In Suit Over Board Diversity*, Law360 (Aug. 12, 2024), https://www.law360.com/securities/articles/1868867.

[174] 302 A.3d 956 (Del. Ch. 2023).

[175] *Id.* at 971.

[176] Michael Toth, *Why the corporations are fleeing Delaware*, The Hill (June 12, 2024), https://thehill.com/opinion/finance/4715117-why-the-corporations-are-fleeing-delaware/mlite/; William P. Barr & Jonathan Berry, *Delaware Is Trying Hard to Drive Away Corporations*, Wall St. J. (Nov. 24, 2023), https://www.wsj.com/articles/delaware-is-trying-hard-to-drive-away-corporations-business-environmental-social-governance-investing-780f812a; Anthony Rickey, *Politics as a New Differentiator Between American Business Courts: A View on the Debate Between Former Attorney General Barr and Vice Chancellor Laster*, Bus. L. Prof. Blog (Dec. 21, 2023), https://lawprofessors.typepad.com/business_law/2023/12/guest-post-politics-as-a-new-differentiator-between-american-business-courts-a-view-on-the-debate-be.html.

[177] *See* Nick Halter, *Target, in the crosshairs, is taking a beating on Wall Street*, Axios (June 2, 2023), https://www.axios.com/local/twin-cities/2023/06/02/target-stock-prices-tumble-pride-boycotts; Emily Stewart, *The Bud Light boycott, explained as much as is possible*, Vox (June 30, 2023), https://www.vox.com/money/2023/4/12/23680135/bud-light-boycott-dylan-mulvaney-travis-tritt-trans.

[178] *See* Letter from Ron DeSantis, Governor of Florida, to Lamar Taylor, Interim Executive Director, State Board of Administration (July 20, 2023), https://flvoicenews.com/wp-content/uploads/2023/07/SGS_BIZHUB23072011270.pdf (asking the head of Florida's state pension system to investigate potential breaches of fiduciary duty by the directors of InBev, Bud Light's parent company, to investors); Letter from Todd Rokita, Attorney General of Indiana, et al., to Brian C. Cornell, Chairman and CEO, Target Corporation (July 5, 2023) (accusing Target's management of breaching fiduciary duties to shareholders by marketing Pride merchandise), https://content.govdelivery.com/attachments/INAG/2023/07/06/file_attachments/2546257/Target%20Letter%20Final.pdf. Though no shareholder sued either company for breach of fiduciary duty, a securities fraud lawsuit alleging that Target's management falsely described the risks associated with its ESG practices survived a motion to dismiss. *See* Craig v. Target, 2024 WL 4979234 (M.D. Fla. Dec. 4, 2024).

[179] *See* David A. Cifrino, *The Politicization of ESG Investing*, Harvard ALI Social Impact Review (Jan. 24, 2024), https://www.sir.advancedleadership.harvard.edu/articles/politicization-of-esg-investing.

popular vote. Profitability, in other words, becomes a proxy for the *mainstream* of America.[180] And, especially in highly polarized times, a claim to represent the mainstream enjoys an enormous amount of political currency.[181] Political actors are thus incentivized to establish that particular business strategies are, or are not, profitable – which transforms the adoption or abandonment of those strategies into both an investment, and a corporate governance, concern.

In sum, the shareholder primacist conceit that profitability will ultimately align with prosociality invites politicians to treat antisociality as a problem of corporate governance. And when the very definitions of prosociality and antisociality are contested, corporate governance itself becomes the new political battlefield, with Delaware's role now squarely in the crosshairs.

III. The *Caremark* Conundrum

The shareholder primacist system posits that corporations will be incentivized to engage in prosocial behavior because antisocial behavior is rendered *expensive*, either through regulatory penalties or rejection by the market.[182] For many proponents, that is sufficient; the only role for corporate law, then, is to protect investors and ensure that corporate management is sufficiently focused on maximizing shareholder wealth.[183] Yet state corporate law contains an additional stricture: corporations – as state created organizations, enjoying state-conferred privileges (such as legal personhood, unlimited life, and limited liability) – are authorized only to engage in "lawful" activity.[184] That is, states do not generally treat it as sufficient that profit-seeking corporations are already incentivized by the external regulatory system to avoid expensive antisocial behavior; state corporate law itself conditions the grant of a charter on legal compliance.[185] As Elizabeth Pollman has explained, corporate law's internal prohibition on illegality is another legitimating principle.[186] It is one of the visible ways that the corporate law system can publicly communicate its prosociality; after all, it would be intolerable to suggest that

[180] The point is obvious for product markets, such as the markets for merchandise marketed as trans-inclusive, but applies equally, if more subtly, to aspects of corporate functioning such as diversity of the workforce or the management team. If profitably is tied to demographic diversity, that fact demonstrates the importance of fostering an inclusive environment, either because diverse teams are inherently more innovative, or because a diverse team has more social legitimacy with an increasingly diverse American population. *See* Transcript of Oral Argument and Rulings of the Court on Defendants' Motion to Dismiss the Class Action Complaint at 43-44, Kiger v. Mollenkompf, No. 2023-0444-JTL (Del. Ch. May 9, 2024) (hypothesizing that because "[t]he United States has a diverse population," then "When people look at a group, whether it be a company, a board, or a group of judges, then if they don't see anyone who looks like them, or maybe they only see very few people who look like them, they can lose confidence in the organization.").
[181] Jamelle Bouie, *The Real Reason Trump and Vance Hate Being Called 'Weird'*, N.Y. Times (Aug. 9, 2024), https://www.nytimes.com/2024/08/09/opinion/trump-vance-harris-walz-weird.html.
[182] Daniel R. Fischel, *The Corporate Governance Movement*, 35 Vand. L. Rev. 1259, 1269 (1982); Frank H. Easterbrook & Daniel R. Fischel, The Economic Structure of Corporate Law 37–39 (1991).
[183] *E.g.*, Stephen M. Bainbridge, *Don't Compound the Caremark Mistake by Extending it to ESG Oversight*, 77 Bus. Law. 651 (2022).
[184] Del. Code tit. 8, § 101(b); Model Bus. Corp. Act § 3.01(a).
[185] *See* McRitchie v. Zuckerberg, 315 A.3d 518, 572-73 (Del. Ch. 2024) ("By explicitly rejecting the notion that a board of directors can act loyally when consciously deciding to violate positive law in pursuit of greater profits, Delaware ensures that positive laws and regulations have bite. Through those laws and regulations, governments can impose meaningful restrictions on externalities. Through its corporate law, Delaware supports those efforts.").
[186] Elizabeth Pollman, *Corporate Oversight and Disobedience*, 72 Vand. L. Rev. 2013, 2028-29 (2019).

the state-conferred privileges of the corporate form do not carry with them some basic obligation of legal compliance.

As a result, state corporate regulators are empowered to dissolve the charters of any organization found to have abused its privileges.[187] A corollary principle has been that shareholders may bring derivative actions against corporate directors for damages and expenses incident to intentional lawbreaking, even if that lawbreaking was undertaken for the purpose of increasing profits.[188] Some earlier cases recognized a degree of tension in allowing shareholders to bring such actions, given that the conduct was for their benefit and they may even have acquiesced in it,[189] but nonetheless allowed the claims to proceed on the grounds of public policy.

In *In re Caremark International Derivative Litigation*,[190] Chancellor Allen expanded that principle with a further corollary: that directors may be liable to shareholders for a breach of fiduciary duty not only if they intentionally break the law, but also if they fail to properly oversee compliance with the law (by, for example, failing to adopt an internal reporting system or failing to monitor that system for signs of illegal activity). *Caremark* however, was subtly different than what came before: as Jennifer Arlen points out, the *Caremark* decision assumed that in an age of increased penalties for corporate criminality, the costs of ignoring potential lawbreaking would exceed the profits to be gained, and therefore a failure of oversight would, in fact, harm shareholders themselves.[191] Similar to the stewardship displays in Part II, then, Allen's legitimating assumption in *Caremark* was that *corporate lawbreaking is unprofitable*, and therefore that shareholders' interest in preventing corporate criminality is roughly equivalent to society's interest. Allen did not entertain the possibility that directors may set up sub-par oversight systems because, given mild penalties and the low risk of detection, corporate lawbreaking *is wealth maximizing* from an ex ante perspective. Thus, in the view of Chancellor Allen, there was no tension or irony in the fact that shareholders themselves would be permitted to bring such claims. The *Caremark* decision, then, reframed the issue of corporate lawbreaking to bring it back within the traditional shareholder primacist framework.

It would not remain there long, however, because when it comes to corporate illegality, boards are not permitted to offer the usual defense of their actions, namely, that they made a calculated decision to assume a risk.[192] Thus, the typical *Caremark* scenario involves some kind

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[187] Del. Code tit. 8, § 284.

[188] Roth v. Robertson, 64 Misc. 343 (N.Y. Sup. Ct. 1909); Miller v. American Tel. & Tel. Co., 507 F.2d 759 (3rd Cir. 1974); Abrams v. Allen, 74 N.E.2d 305 (N.Y. 1947).

[189] Roth v. Robertson, 64 Misc. 343 (N.Y. Sup. Ct. 1909); Miller v. American Tel. & Tel. Co., 507 F.2d 759 (3rd Cir. 1974). *Miller*, which concerned illegal corporate campaign donations, justified the lawsuit by recognizing that prohibitions on corporate political spending were intended to protect shareholders.

[190] 698 A.2d 959 (Del. Ch. 1996).

[191] Jennifer Arlen, *Evolution of Director Oversight Duties and Liability Under* Caremark*: Using Enhanced Information-Acquisition Duties in the Public Interest*, *in* Research Handbook on Corporate Liability (Martin Petrin and Christian Anton Witting eds., Edward Elgar Publishing, 2023).

[192] For example, in *In re Citigroup Shareholder Derivative Litigation,* 964 A.2d 106, 129-31 (Del. Ch. 2009), shareholders attempted to advance a *Caremark* claim that Citigroup board members were aware of, but failed to respond to, "red flags" of overexposure to the subprime mortgage market. In rejecting the claim, Chancellor Chandler explained that boards have discretion to take business risks – and thus are permitted to decide how to respond to signs of brewing problems – but do not have discretion to take *legal* risks. *See also In re* Goldman Sachs

of corporate criminality that is intended to boost profits but ultimately results in a disaster for the firm, such as the defects in the design of Boeing's 737 Max.[193] The harm to shareholders is obvious; however, what is less obvious, and *cannot even be the focus of inquiry*, is whether the directors made a rational ex ante calculation that the profits to be gained from lawbreaking outweighed the foreseeable harms to the corporation.[194] Nor can any inquiry be made into whether the firm gained more financially during the period of criminality than it later lost due to exposure of the wrongdoing. Even if the claim is that *no* system was in place to monitor for illegal activity (or that monitoring was "woefully inadequate"[195]), there is not (and cannot be) any interrogation of whether the expected penalties from lawbreaking exceeded the expected gains from failing to adopt a detection system. The fact that there can be no evaluation along these lines demonstrates that *Caremark* has very little to do with protecting shareholders, and shareholder harm in the traditional sense is not its focus.

Thus, though Delaware courts have recognized the distinction between intentional illegality and failure to monitor,[196] the claims are often brought in the alternative, with plaintiffs using a single set of facts, such as the Board's inaction in the face of signs of criminality, to argue multiple theories, blurring the line between a failure to monitor for criminal activity and acquiescence in its commission.[197] That line was finally erased in *In re Transunion Derivative Stockholder Litigation*,[198] where Vice Chancellor Will collapsed the different theories into a single "fundamental rule that Delaware corporations operate lawfully."[199] Nonetheless, though Delaware courts commonly recognize that the "true" victims of corporate illegality are the injured members of the public rather than the shareholders,[200] little remains of the direct confrontation – seen in earlier cases – with the fact that, if lawbreaking was intended to benefit shareholders, shareholders may not be best positioned to challenge it.[201] That conflation of

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Group Inc. S'holder Litig., 2011 WL 4826104, *20-23 (Del. Ch. Oct. 12, 2011); Ontario Provincial Council of Carpenters' Pension Trust Fund v. Walton, 2023 WL 3093500, at *34 (Del. Ch. Apr. 26, 2023).

[193] *In re* The Boeing Co. Deriv. Litig., 2021 WL 4059934 (Del. Ch. Sept. 7, 2021).

[194] Ontario Provincial Council of Carpenters' Pension Trust Fund v. Walton, 2023 WL 3093500, at *34 (Del. Ch. Apr. 26, 2023).

[195] Rich ex rel. Fuqi Int'l, Inc. v. Yu Kwai Chong, 66 A.3d 963 (Del. Ch. 2013).

[196] *E.g.*, City of Detroit Police & Fire Ret. Sys. v. Hamrock, 2022 WL 2387653, at *17 (Del. Ch. June 30, 2022).

[197] *E.g.*, Ontario Provincial Council of Carpenters' Pension Trust Fund v. Walton, 2023 WL 3093500, at *31-34 (Del. Ch. Apr. 26, 2023).

[198] 324 A.3d 869 (Del. Ch. 2024).

[199] *Id.* at 887.

[200] Marchand v. Barnhill, 212 A.3d 805, 807 (Del. 2019); *In re* The Boeing Co. Deriv. Litig., 2021 WL 4059934, *1 (Del. Ch. Sept. 7, 2021); Teamsters Local 443 Health Services & Ins. Plan v. AmerisourceBergen, 2020 WL 5028065, *1 (Del. Ch. Aug. 24, 2020).

[201] One exception to this principle came in *In re Massey Energy Co.*, where the court opined, in a footnote, "It may well be that the corporate law does not make stockholders whole in situations like this when it is alleged that corporate managers skirted laws protecting other constituencies in order to generate higher profits for the stockholders. … [I]f stockholders come out a bit worse, then justice is in fact done. Remember that to the extent that Massey kept costs lower and exposed miners and the environment to excess dangers, Massey's stockholders enjoyed the short-term benefits in the form of higher profits. The very reason for laws protecting other constituencies is that those who own businesses stand to gain more if they can keep the operation's profits and externalize the costs. Thus, the stockholders of corporations, especially given the short-term nature of holding periods that now predominate in our markets, have poor incentives to monitor corporate compliance with laws protecting society as a whole and may well put strong pressures on corporate management to produce immediate profits." 2011 WL 2176479, at *29 n.185 (Del. Ch. May 31, 2011).

shareholder harm and societal harm renders the doctrine unstable and, increasingly, difficult for Delaware courts to navigate.

A. Standards for Liability

Traditionally, the standards for liability under *Caremark* are quite high: *Caremark* has been described as "possibly the most difficult theory in corporation law" for a plaintiff to advance,[202] because the plaintiff must either establish that the board completely failed to exercise oversight, or that the board engaged in intentional lawbreaking. As a result, the potential additional penalties that corporate managers may realistically incur are slight compared to the penalties offered by the external regulatory system (and likely covered entirely by insurance in most cases[203]). *Caremark*'s functional "irrelevance" [204] is precisely what has given rise to the accusation of symbolism.[205] Some have speculated that much like the *procedural* aspects of shareholder primacy – which function by making constraints on managerial visible – shareholder claims for legal violations are also communicative. Shareholders obtain access to internal documents, which are then aired in court, and judicial opinions detail corporate failings even if those fall short of what is required for liability.[206] *Caremark* therefore functions as a kind of soft discipline by exposing corporate misconduct to public scrutiny.

That impression is buttressed by some of the doctrinal oddities introduced by *Caremark*'s poor fit within the shareholder-primacist framework. For example, *Caremark* claims are derivative actions, which means, they are brought by shareholders to remedy an offense against the corporate entity.[207] A fundamental principle of derivative actions is that the litigation right belongs to the entity itself, and therefore the board of directors would ordinarily be in charge of whether and how to file a claim. Thus, if the claim is to be brought by shareholders (over board objection) the shareholders must first demonstrate to the court that the board cannot fairly make a decision on the company's behalf. Typically, this is accomplished by demonstrating that the board is likely implicated in the wrongdoing, and therefore too conflicted to make a determination as to the corporate best interests.[208] Boards, however, can defeat a shareholder claim by demonstrating either that the board is not majority-conflicted – i.e., that only a minority of the board is conflicted, and the majority of members can therefore act on the company's behalf – or by forming a special litigation committee that investigates the claim and evaluates whether it would be in the corporate best interests to pursue it.[209]

These lines of inquiry, however, make no sense in the context of a claim for lawbreaking, especially one that resulted in net gains to shareholders. Even untainted board members should perceive no *corporate* interest in pursuing a claim that resulted in a positive gain to shareholders, or even one that represented a rational ex ante calculation that benefits exceeded costs. Untainted boards would also likely perceive no *corporate* interest in litigation that might uncover

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[202] *In re* Caremark Int'l Inc. Deriv. Litig., 698 A.2d 959, 967 (Del. Ch. 1996).
[203] Angela N. Aneiros & Karen E. Woody, *Caremark's Butterfly Effect*, 72 Am. U. L. Rev. 719, 770 (2023).
[204] Mercer Bullard, *Caremark's Irrelevance*, 10 Berkeley Bus. L.J. 15, 23 (2013).
[205] Elizabeth Pollman, *Corporate Oversight and Disobedience*, 72 Vand. L. Rev. 2013, 2035 (2019).
[206] Roy Shapira, *A New Caremark Era: Causes and Consequences*, 98 Wash. U. L. Rev. 1857, 1883-85 (2021).
[207] United Food & Com. Workers Union v. Zuckerberg, 262 A.3d 1034 (Del. 2021).
[208] *E.g.*, *In re* Boeing Co. Deriv. Litig., 2021 WL 4059934, at *24 (Del. Ch. Sept. 7, 2021).
[209] *E.g.*, Teamsters Loc. 443 Health Servs. & Ins. Plan v. Chou, 2023 WL 7986729 (Del. Ch. Nov. 17, 2023).

additional lawbreaking and result in further regulatory penalties.[210] In other words, notwithstanding Chancellor Allen's efforts, the typical analysis to determine whether a *Caremark* claim should proceed fits poorly within the shareholder primacist framework. As a result, courts have issued opinions that identify serious potential lawbreaking while barring any (corporate law) remedy.[211]

The difficulty that arises, then, is the same one that plagued courts in the context of determining director independence: if *Caremark* claims exist as a public display of corporate law prosociality, that display is weakened if they also are demonstrably toothless. Which is to say, if *Caremark* claims expose corporate wrongdoing while offering weak justifications for allowing directors to escape liability, its legitimating function is undermined.

That dynamic may explain the Delaware Supreme Court's recent decision in *Marchand v. Barnhill*,[212] which has largely been read as reinvigorating *Caremark* claims.[213] Though the *Caremark* doctrine ordinarily gives boards wide discretion to design compliance systems, in *Marchand*, the Delaware Supreme Court made clear that boards have a duty to monitor for "mission critical" legal risks that cannot be delegated to officers at lower levels of the company.[214] *Marchand* has been widely interpreted as relaxing the standards plaintiffs need to meet to bring a *Caremark* claim, and, sure enough, since it was decided, a remarkable number of *Caremark* claims have survived initial motions to dismiss.[215]

That newly-reinvigorated approach to *Caremark*, however, now pressures Delaware corporate law, in large part because of the distance between the justifying assumption – that corporate criminality is a harm to shareholders – and the reality that shareholders may benefit from and encourage such behavior. And if compliance with the legal system is treated as an

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[210] Roy Shapira, *Conceptualizing Caremark*, Ind. L.J. (forthcoming), at 49, 53 https://papers.ssrn.com/sol3/papers.cfm?abstract_id=4778827 (discussing the problem in the context of special litigation committees and claims against corporate officers).

[211] For example, in *Bricklayers Pension Fund of Western Pennsylvania v. Brinkley*, 2024 WL 3384823 (Del. Ch. July 12, 2024), the company settled over $1 billion worth of claims by multiple states for violation of Medicaid rules. The scheme had been orchestrated by the company's CEO. Out of 13 board members, the plaintiffs alleged wrongdoing by 8. Of those 8, three had only joined the board after the scheme was well underway. The court therefore focused solely on whether the newly-added board members could be said to have violated their *Caremark* duties, and concentrated its analysis on the relatively limited information that they had received. The court concluded that those board members were not at risk of liability, and therefore, a majority of the board was not at risk – without an inquiry into the complicity of the remaining directors.

[212] 212 A.3d 805 (Del. 2019).

[213] Roy Shapira, *Conceptualizing Caremark*, Ind. L.J. (forthcoming), at 10 https://papers.ssrn.com/sol3/papers.cfm?abstract_id=4778827. Notably, *Marchand* was authored by then-Chief Justice Leo Strine. Two years earlier, Strine had faulted his colleagues for dismissing a *Caremark* claim against Duke Energy, hinting that public suspicions of wrongdoing by Duke Energy's board demanded a judicial response. *See* City of Birmingham Ret. & Relief System v. Good, 177 A.3d 47, 69 (Del. 2017) (Strine, C.J., dissenting) ("It may be that after the daylight of discovery shines for some time, the rancid whiff that arises from the pled facts dissipates and turns into the bracing freshness of a new Carolina day. But, without that, the off-putting odor will linger and so too will rational suspicions that the defendants caused the smell.")

[214] Jennifer Arlen, *Evolution of Director Oversight Duties and Liability Under* Caremark*: Using Enhanced Information-Acquisition Duties in the Public Interest*, *in* Research Handbook on Corporate Liability (Martin Petrin and Christian Anton Witting eds., Edward Elgar Publishing, 2023).

[215] Roy Shapira, *A New Caremark Era: Causes and Consequences*, 98 Wash. U. L. Rev. 1857, 1866 (2021).

aspect of corporate law, it draws corporate law itself – and, consequently, the (Delaware) courts that adjudicate corporate law issues – back into the political thicket they were trying to avoid.

B. Identifying the Victim

Because *Caremark* claims are at least as much about protecting society as protecting shareholders, it is not clear what kinds of harms give rise to a claim. As above, Chancellor Allen's formulation placed harm to shareholders front and center; yet, because of the hard prohibition on even wealth maximizing illegal conduct, courts cannot inquire whether the gains to shareholders exceeded eventual losses (such as profits earned that dwarfed any eventual regulatory penalties), or whether boards made a rational ex ante calculation that the benefits of lawbreaking outweighed the risks. The lack of a requirement of *shareholder* harm has begun to encourage lawsuits with an openly political agenda, such as against Starbucks for implementing allegedly discriminatory diversity policies,[216] and Smith & Wesson for allegedly illegally marketing its AR-15.[217] (Neither of these are Delaware companies, but, in both cases, the shareholders alleged that the organizing state's law is similar to Delaware's). The *Starbucks* court dismissed the case on the ground that the plaintiff's nakedly partisan agenda was at odds with the interests of other shareholders,[218] but that is exactly what these sorts of claims envision: holding directors accountable for lawbreaking that is intended to profit the entity.[219] As a result, the current state of *Caremark* doctrine encourages the shift of highly contestable political disputes into the realm of corporate governance. Even when no lawsuit is filed, the possibility of one provides an opening for intrusive document requests.[220]

To be sure, Delaware courts have emphasized that a *Caremark* claim must include some sort of realized corporate trauma before shareholders can bring a lawsuit,[221] often traceable to public exposure of the wrongdoing and subsequent financial damage. But that requirement not only fits poorly with the general prohibition on even *wealth-maximizing* illegal behavior – *Caremark* does not serve its legitimating function if shareholders suing over lawbreaking are told that their claims must be dismissed because shareholders were not harmed by it – but, in the absence of a requirement of *shareholder* harm, there are no doctrines for assessing what kind of trauma is sufficient; presumably, even the legal expenses incurred by a corporation defending itself should count.

Moreover, it is not clear how far the doctrine extends: *Caremark* claims have been brought against Fox News, alleging that it committed a common law tort, namely, defamation of Dominion Voting Systems, for the purposes of preserving a conservative audience disappointed with Donald Trump's electoral loss, i.e., in order to *maximize wealth* by *preserving market*

[216] Nat'l Ctr. for Pub. Policy Rsch. v. Schultz, 2023 WL 5945958 (E.D. Wash. Sept. 11, 2023).
[217] Complaint, Adrian Dominican Sisters of Bon Secours USA v. Smith et al., A-23-882774-B (Clark Cty, Nev.. filed Nov. 6, 2023). The district court dismissed the complaint against Smith & Wesson, and the plaintiff filed an appeal. *See* Adrian Dominican Sisters v. Smith, Docket No. 88980 (Nev. Sup. Ct. Jul 15, 2024).
[218] Nat'l Ctr. for Pub. Policy Rsch. v. Schultz, 2023 WL 5945958 (E.D. Wash. Sept. 11, 2023).
[219] Indeed, one Delaware case upheld *Caremark* claims while acknowledging that shareholders had known about, and acquiesced in, misconduct for years before disaster struck. *See supra* n. __.
[220] Mike Leonard, *Investor Scrutiny Lawsuits Snarl Business Court's Breakneck Norm*, Bloomberg Law News (Nov. 12, 2024).
[221] Firefighters' Pension System v. Foundation Building Materials, 2024 WL 2795026 (Del. Ch. May 31, 2024).

share.[222] The overtly political nature of that case has already drawn further challenges that Delaware has abandoned political neutrality,[223] and expanding *Caremark* to these kinds of torts only invites political cherry picking of lawsuits.[224] Yet there is no obvious way out: the legitimating function of *Caremark* would be at odds with an open declaration that corporations are permitted consciously to choose to injure people for stockholders' benefit, let alone a declaration that such an action *would in fact* benefit stockholders more than it would harm them through subsequent penalties, i.e., that shareholders' interests are not, in fact, aligned with those of the public.

C. Delaware as Regulator

The final morass created by the *Caremark* line of cases concerns the role of Delaware vis a vis the primary regulators who have responsibility for making initial determinations of lawbreaking. In most cases, *Caremark* claims are brought after such determinations are made, and there is no conflict, but not always. For example, in *Lebanon County Employees' Retirement Fund v. Collis*,[225] AmerisourceBergen (ABC) settled various federal and state enforcement actions concerning its role in the opioid crisis and its failure to comply with DEA regulations for handling controlled substances. At least two congressional reports also singled out the company for its mishandling of opioids. In addition to those cases, two cases in West Virginia alleged that the company had caused a public nuisance by fueling the opioid epidemic. After a bench trial, one court decided the matter in favor of the defendants, concluding they had "substantially complied with their duties" under federal law.

Shareholders of ABC sued the company on a *Caremark* theory, alleging that the company had ignored red flags of misconduct. A Delaware Court of Chancery concluded that the complaint stated a claim *but for* the conclusions in the West Virginia action, which had been reached after a thorough review of the facts. On appeal, the Delaware Supreme Court reversed, holding that it was improper for the Chancery court to functionally adopt the factual findings of another court as its own.

As a matter concerning preclusion and the rules of evidence, the decision was likely correct. As a matter of practicality, though, the decision further threatens to draw Delaware into hot button regulatory issues – and contested political disputes – as its courts are now authorized to decide not only whether corporate directors violated their fiduciary duties by authorizing legal

[222] Verified Amended S'holder Deriv Complaint, In re Fox News Deriv. Litig, Docket No. 2023-0418 (Del. Ch. Apr 11, 2023).
[223] Michael Toth, *Why the corporations are fleeing Delaware*, The Hill (June 12, 2024), https://thehill.com/opinion/finance/4715117-why-the-corporations-are-fleeing-delaware/mlite/. Significantly, the stockholder plaintiffs selected by the court to lead the case – New York and Oregon retirement funds – both are led by public officials who had previously offered political criticism of Fox News's programming. Nonetheless, they were selected to lead the case in part because the court believed their status as public officials rather than private investors lent "legitimacy" to the lawsuit. *See In re* Fox Corp. Deriv. Litig., 307 A.3d 979, 995-97 (Del. Ch. 2023).
[224] William P. Barr & Jonathan Berry, *Delaware Is Trying Hard to Drive Away Corporations*, Wall St. J. (Nov. 24, 2023), https://www.wsj.com/articles/delaware-is-trying-hard-to-drive-away-corporations-business-environmental-social-governance-investing-780f812a ("It is no coincidence that the board-level Caremark 'risks' that both the plaintiffs' bar and companies' legal advisers stress correspond to du jour ESG issues like climate change, DEI, and #MeToo—or even the 2020 presidential election.").
[225] 2023 WL 8710107 (Del. 2023).

violations, but also whether such violations actually took place in the first instance, regardless of the findings of other regulators. The shareholder lawsuit against Fox News exemplifies the problem: there, Fox settled with Dominion before a court could decide whether Fox had committed the tort of defamation; therefore, if the case in Delaware proceeds that far, the Court of Chancery will have to decide whether defamation did in fact occur in the context of a shareholder lawsuit. And even if the technical standards for defamation were not met, shareholders will likely argue that Fox executives walked *close enough to the line* of lawbreaking to endanger the company, in breach of fiduciary duty, which will present another opportunity for *Caremark* creep.

Caremark has been championed as a means by which flaws in the regulatory process can be corrected,[226] but this is exactly the problem. It turns state corporate courts – and Delaware courts in particular – into a secondary regulator for the United States (and, potentially, the world, to the extent violations of *foreign* law are alleged).[227] There is no possibility that Delaware can adopt such a regulatory function while avoiding the appearance of taking a political – and partisan – bent, which once again undermines the justification for shareholder primacy in the first instance, as well as Delaware's role in the system.

Conclusion

If cosmetic corporate governance is used as a tool to stave off more robust regulation of corporate behavior, there seem to be two possibilities. The *most* benign explanation is that shareholder primacy *genuinely is* the most efficient mechanism for arranging economic affairs, but that its virtues are not fully appreciated by the general public. As a result, special efforts must be made to appeal to public sensitivities via a performance of sobriety and professionalism. That explanation, however, is not only inherently dishonest, but antidemocratic as well; it assumes the public cannot comprehend the issues at stake.

The *less* benign explanation, of course, is that shareholder primacy is *not*, in fact, the most efficient economic arrangement, and that the public would be better served by a corporate law designed more for the benefit of all stakeholders. In that alternative, legitimacy-washing is a tool to maintain a system that benefits a few at the expense of the many.

The open question is how long profit-maximizing corporations will tolerate incurring real expenses as the price of public acceptance. If they reincorporate out of Delaware, as they currently threaten to do, or if they even shift governance to contractual arrangements that are litigated out of view of the Delaware courts, the pitchforks – via more robust federal regulation, if nothing else – may in fact reveal themselves. Or, more unsettlingly, corporate managers may

[226] Roy Shapira, *Conceptualizing Caremark*, Ind. L.J. (forthcoming), at 62 https://papers.ssrn.com/sol3/papers.cfm?abstract_id=4778827; Jennifer Arlen, *Evolution of Director Oversight Duties and Liability Under* Caremark*: Using Enhanced Information-Acquisition Duties in the Public Interest*, *in* Research Handbook on Corporate Liability (Martin Petrin and Christian Anton Witting eds., Edward Elgar Publishing, 2023); William J. Moon, *Transnational Corporate Litigation*, Duke L.J. (forthcoming), https://papers.ssrn.com/sol3/papers.cfm?abstract_id=4734519.
[227] William J. Moon, *Transnational Corporate Litigation*, Duke L.J. (forthcoming), https://papers.ssrn.com/sol3/papers.cfm?abstract_id=4734519.

reach the rational calculation that they have amassed enough political influence and power so as to no longer need legitimizing symbols to maintain their dominance after all.

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