Stakeholder Impartiality: A New Classic Approach for the Objectives of the Corporation

Law Working Paper N° 476/2019
December 2019

Amir N. Licht
Interdisciplinary Center Herzliya and ECGI

ECGI Working Paper Series in Law

Stakeholder Impartiality: A New Classic Approach for the Objectives of the Corporation

Working Paper N° 476/2019
December 2019

Amir N. Licht

For helpful comments I am grateful to Richard Brooks, Lior Frank, Jennifer Hill, Lyman Johnson, Arthur Laby, Amnon Lehavi, Paul Miller, Asaf Raz, Jacob Russell, Steven Schwarcz, Andrew Tuch, and Julian Velasco. Special thanks to Chief Justice Leo E. Strine, Jr. for his comments on an earlier draft. Accountability for all errors remains with me.

Abstract

The stockholder/stakeholder dilemma has occupied corporate leaders and corporate lawyers for over a century. In addition to the question whose interests should managers prioritize, the question how those interests could or should be balanced has proven equally difficult. To address the latter challenge, this paper advances a doctrinal innovation that is both new and time-honored - to implement a duty of impartiality with regard to directors' discretion over stakeholder interests. A sub-component of trustees' duty of loyalty, the duty of impartiality regulates settings in which several beneficiaries have conflicting interests without dictating substantive outcomes, especially not equal treatment. This paper proposes an analogous process-oriented impartiality duty for directors to consider the interests of relevant stakeholders. Stakeholder impartiality is a lean duty whose main advantage lies in its being workable. It can be implemented in legal systems that have different positions on the objectives of the corporation, from Canada's and India's open-ended stakeholderist approaches to Delaware's staunch shareholderism.

Keywords: corporate governance, fiduciary duties, stakeholders, loyalty, impartiality

JEL Classifications: K22

Amir N. Licht*
Professor of Law
Interdisciplinary Center Herzliya, Harry Radzyner School of Law
Kanfe Nesharim Street
Herzliya 46150, Israel
phone: +972 995 273 32
e-mail: alicht@idc.ac.il

*Corresponding Author

Stakeholder Impartiality: A New Classic Approach for the Objectives of the Corporation

Amir N. Licht*

[A chapter for Fiduciary Obligations in Business (Arthur Laby & Jacob Hale Russell, eds, Cambridge University Press, forthcoming)]

The stockholder/stakeholder dilemma has occupied corporate leaders and corporate lawyers for over a century. In addition to the question whose interests should managers prioritize, the question *how* those interests could or should be balanced has proven equally difficult. To address the latter challenge, this paper advances a doctrinal innovation that is both new and time-honored - to implement a duty of impartiality with regard to directors' discretion over stakeholder interests. A sub-component of trustees' duty of loyalty, the duty of impartiality regulates settings in which several beneficiaries have conflicting interests without dictating substantive outcomes, especially not equal treatment. This paper proposes an analogous process-oriented impartiality duty for directors to consider the interests of relevant stakeholders. Stakeholder impartiality is a lean duty whose main advantage lies in its being workable. It can be implemented in legal systems that have different positions on the objectives of the corporation, from Canada's and India's open-ended stakeholderist approaches to Delaware's staunch shareholderism.

This version: 30 November 2019
First version: 8 September 2019
JEL codes: K22
Keywords: corporate governance, fiduciary duties, stakeholders, loyalty, impartiality

---

* Professor of Law, Harry Radzyner Law School, Interdisciplinary Center Herzliya, Israel. alicht@idc.ac.il. For helpful comments I am grateful to Richard Brooks, Lior Frank, Jennifer Hill, Lyman Johnson, Arthur Laby, Amnon Lehavi, Paul Miller, Asaf Raz, Jacob Russell, Steven Schwarcz, Andrew Tuch, and Julian Velasco. Special thanks to Chief Justice Leo E. Strine, Jr. for his comments on an earlier draft. Accountability for all errors remains with me.

Stakeholder Impartiality: A New Classic Approach for the Objectives of the Corporation

I. INTRODUCTION

Chief Justice Leo Strine, Jr. recently argued extra-judicially that "[d]espite attempts to muddy the doctrinal waters, a clear-eyed look at the law of corporations in Delaware reveals that, within the limits of their discretion, directors must make stockholder welfare their sole end, and that other interests may be taken into consideration only as a means of promoting stockholder welfare."[1] For many years, the semi-official position of the U.S. business community, reflected in the Business Roundtable's Statement on Corporate Governance, has espoused a similar principle - that "the paramount duty of management and of boards of directors is to the corporation's stockholders."[2]

In direct response to this position, U.S. Senator Elizabeth Warren (D-Mass.) in 2018 introduced her Accountable Capitalism Act. Inspired by the "the thriving benefit corporation model", the Act would require very large American corporations to consider the interests of all corporate stakeholders - including employees, customers, shareholders, and communities - with a view to balance their interests.[3] In a complete turnaround of its prior position, the Business Roundtable in 2019 promulgated a new statement on the purpose of a corporation, in which prominent

---

[1] Leo E. Strine, Jr., *The Dangers of Denial: The Need for a Clear-Eyed Understanding of the Power and Accountability Structure Established by the Delaware General Corporation Law*, 50 WAKE FOREST L. REV. 761, 768 (2015). In tandem, Strine recently advanced a reform proposal that, *inter alia,* would ensure that large companies consider worker concerns through dedicated board committees. Leo E. Strine Jr., Toward Fair and Sustainable Capitalism. U. of Penn. Inst. for L. & Econ. Research Paper No. 19-39 (2019), https://ssrn.com/abstract=3462454.

[2] THE BUSINESS ROUNDTABLE, STATEMENT ON CORPORATE GOVERNANCE 3 (1997).

[3] Press Release, Office of Senator Elizabeth Warren, Warren Introduces Accountable Capitalism Act (Aug. 15, 2018), https://www.warren.senate.gov/newsroom/press-releases/warren-introduces-accountable-capitalism-act.

corporate leaders announced that they "share a fundamental commitment to all of our stakeholders."[4] As reporters noted, however, the Business Roundtable did not provide specifics on *how* it would carry out its newly stated ideals.[5]

A duty to consider stakeholder interests is already a pressing reality for large companies in the United Kingdom. Section 172 of the Companies Act 2006 requires directors to act in a way they consider, in good faith, would be most likely to promote the success of the company for the benefit of its members (i.e., shareholders) as a whole. In doing so, directors are *required* to have regard, among other things, to the interests of the company's employees, business partners, the community, and the environment. Government regulations promulgated in 2018 require large companies, whether listed or non-listed, to include in their strategic reports a new statement on *how* the directors have considered stakeholders' interest in discharging their duty under section 172.[6]

The new U.K. provision brings a major twist to a plot that has been unfolding - in circles, in must be said - at least since Lord Bowen in 1883 famously stated in *Hutton v. West Cork Ry.*:

> A railway company, or the directors of the company, might send down all the porters at a railway station to have tea in the country at the expense of the company. Why should they not? It is for the directors to judge … The law does not say that

[4] The Business Roundtable, Statement on the Purpose of a Corporation (2019), https://opportunity.businessroundtable.org/ourcommitment/.

[5] David Gelles & David Yaffe-Bellany, *Shareholder Value Is No Longer Everything, Top C.E.O.s Say*, The New York Times (Aug 19, 2019), https://www.nytimes.com/2019/08/19/business/business-roundtable-ceos-corporations.html. Echoing decades-old concerns about such position, Joseph Stiglitz has questioned the statement's ingenuity. *See* Joseph Stiglitz, *Can we Trust CEOs' Shock Conversion to Corporate Benevolence?*, The Guardian (Aug. 29, 2019), https://www.theguardian.com/business/2019/aug/29/can-we-trust-ceos-shock-conversion-to-corporate-benevolence?.

[6] The Companies (Miscellaneous Reporting) Regulations 2018, Regulation 414CZA.

> there are to be no cakes and ale, but there are to be no cakes and ale except such as are required for the benefit of the company.[7]

From Lord Bowen to Chief Justice Strine (and/or Senator Warren and/or Mr. Jeff Bezos & co.), the debate over the objectives of the corporation has been oscillating between two polar positions, dubbed "monistic" and "pluralistic" in the business management parlance. The monistic position endorses a single maximand (that which is to be maximized) - invariably, shareholder interest - while the pluralistic position supports a multiple-objective duty that would balance the interests of several stakeholder constituencies, shareholders included. With few glaring exceptions, this debate was limited to the substantive question whether non-shareholder stakeholders *deserve* consideration in their own right. The practical question of *how* to perform this balancing act has virtually never been addressed until now. As we shall see below, when the Supreme Court of Canada discussed it in an *obiter dictum* in *BCE Inc. v. 1976 Debentureholder*s, it explicitly eschewed giving it an answer.[8] Lawyers are similarly at sea with regard to a multiple-stakeholder-objective provision in India's Companies Act, 2013.

This paper advances a new, yet classical, approach for the task of considering the interests of various stakeholders by directors and other corporate fiduciaries. I argue that for lawfully accomplishing this task, while also complying with their standard duties of loyalty and care, directors should exercise their discretion impartially. Respectively, judicial review of directors' conduct in terms of treating different stakeholders should implement the concomitant doctrine of impartiality.

---

[7] Hutton v. West Cork Ry. Co. (1883) 23 Ch.D. 654, 672. *Hutton* was followed, with extensive quotes, in Parke v. The Daily News Ltd [1962] Ch 927.

[8] BCE Inc. v. 1976 Debentureholders, 2008 SCC 69. *See below* text to note 35.

This approach is new, as it has not yet been implemented in this context.[9] At the same time, this approach is also classical, even orthodox. The duty of impartiality (or even-handedness, or fairness; courts use these terms interchangeably) has evolved in traditional trust law mostly during the nineteenth century. In recent years, it has been applied in trust cases in several common law jurisdictions. More importantly, this duty has been applied during the latter part of the twentieth century in modern, complex settings of pension funds, where fund trustees face inescapable conflicts between subgroups of members. These conflicts resemble the tensions between different stakeholders in business corporations - a feature that renders this doctrine a suitable source of inspiration for the task at hand.

In a nutshell, the duty of impartiality accepts that there could be irreconcilable tensions and conflicts among several trust beneficiaries who in all other respects stand on equal footing vis-à-vis the trustee. Applying the rule against duty-duty conflict (dual fiduciary) in this setting would be ineffective, as it would disable the trustee - and consequently, the trust - without providing a solution to the conundrum. The duty of impartiality calls on the trustee to consider the different interests of the beneficiaries impartially, even-handedly, fairly, etc.; it does not impose any heavier burden on the good-faith exercise of the trustee's discretion. Crucially, the duty of impartiality does not imply equality. All that it requires is that the different interests be considered within very broad margins.

The upshot is a light though not hollow regime whose main advantage is that it is workable. This is precisely where impartiality holds a promise for advancing the discourse and actual legal regulation of shareholder-stakeholder relations through

---

[9] For an early version of some of the present ideas *see* AMIR LICHT, FIDUCIARY LAW 203-210 (2013) (in Hebrew).

fiduciary duties. A normatively appealing legal regime is unlikely to satisfy even its proponents if it does not lend itself to practical implementation; *a fortiori* for its opponents. For legal systems and for individual lawyers that champion a pluralistic stakeholder-oriented approach for the objective of the corporation, having a workable doctrine for implementing that approach is crucial - an absolute necessity. Stakeholder impartiality is thus particularly suitable for legal systems that endorse a pluralistic stance on the objectives of the corporation, such as Canada's and India's open-ended stakeholderist approaches. Such a doctrinal framework might also prove useful for systems and individuals who endorse a monistic, shareholder-focused approach. That could be the case in the United Kingdom and Australia, for instance, where directors could face liability if they did not consider creditors' interest in a timely fashion even before the company reaches insolvency. Moreover, this approach could be helpful where the most extreme versions of doctrinal shareholderism arguably rein, such as Delaware law post- *NACEPF v. Gheewalla*[10] - in particular, with regard to tensions between common and preferred stockholders post-*Trados*.[11]

II. *E PLURIBUS UNUM?* MONISM AND PLURALISM IN THE CORPORATE OBJECTIVE

This Part lays the ground for introducing impartiality as a workable legal framework for considering multiple stakeholders in strategic decisions aimed for promoting the best interest of the corporation. My goal is neither to justify nor to debunk a pluralistic approach to strategic management. In fact, there is reason to

[10] North American Catholic Educational Programming Foundation, Inc. v. Gheewalla, 930 A2d 92 (Del. 2007).

[11] In re Trados Inc. Shareholder Litigation, 73 A.3d 17 (Del. Ch. 2013).

believe that this debate cannot be resolved, as it is values-laden and political in essence. This Part therefore begins with a comparative overview of the positive legal regimes that govern this subject, primarily in common law jurisdictions. Next, it deals briefly with the normative aspect of the subject and points out the implementation challenge that bedevils it.

A. A Positive Comparative Overview

1. The World

A superficial observation might lead one to think that corporate laws around the world have converged to shareholder value as the single maximand of corporate governance. When Henry Hansmann and Reinier Kraakman announced "the end of history for corporate law", they argued that "there is convergence on a consensus that the best means to … the pursuit of aggregate social welfare is to make corporate managers strongly accountable to shareholder interests and, at least in direct terms, only to those interests."[12] Some ten years later, they insisted that their ideological or normative claim (which was stated quite positively) "is holding up extremely well."[13]

The OECD's Principles of Corporate Governance convey a similar impression.[14] In their third edition since 1999, now published together with the G20 forum of the world's largest economies and after consultation with business and labor representatives, the Principles purport to reflect a universal consensus. Moreover, they guide international financial institutions and countries in assessing corporate governance reforms. Principle VI on the responsibilities of the board states that "[t]he

---

[12] Henry Hansmann & Reinier Kraakman, *The End of History for Corporate Law*, 89 GEO. L.J. 439, 441 (2001).

[13] Henry Hansmann & Reinier Kraakman, *Reflections on the End of History for Corporate Law*, in THE CONVERGENCE OF CORPORATE GOVERNANCE: PROMISE AND PROSPECTS 32 (Abdul A. Rasheed & Toru Yoshikawa eds., 2012).

[14] Organisation for Economic Co-operation and Development, G20/OECD PRINCIPLES OF CORPORATE GOVERNANCE 51 (2015), https://www.oecd.org/daf/ca/Corporate-Governance-Principles-ENG.pdf.

corporate governance framework should ensure … the board's accountability to the company and the shareholders."[15] On the role of stakeholders the Principles state that "[t]he corporate governance framework should recognise the rights of stakeholders established by law or through mutual agreements…"[16] Despite their claim for universality, the Principles adopt a very American approach. By declaring the board accountable to the company and the shareholders, the Principles closely follow the ruling in *Guth v. Loft*, that "[c]orporate officers and directors … stand in a fiduciary relation to the corporation and its stockholders."[17] Other stakeholders only have the protection of other laws or contracts but not of directors' fiduciary accountability.

This appearance of uniformity is misleading, however. Legal systems vary considerably on the objectives of the corporation and the board's mission. The following sections present glimpses into a number of common law systems in this regard. Fiduciary law constitutes an important segment of private law in all of these systems, exhibiting the same basic principles of fiduciary loyalty, yet they differ significantly in the ways they address this issue.[18]

2. The United States

U.S. law - in particular, Delaware law - represents the strongest doctrinal version of shareholder primacy. To begin, only shareholders have the power to appoint directors, such that one way or another, directors are bound to serve their interest both practically and, one could argue, also deontologically. As just noted,

---

[15] *Id.*, at 51.

[16] *Id.*, at 37 (Principle IV).

[17] Guth v. Loft, Inc., 5 A.2d 503, 510 (Del. 1939).

[18] Some scholars argue that common law systems are shareholder-oriented while civil law systems are stakeholder-oriented. *See* Michael Bradley et al., *Challenges to Corporate Governance: The Purposes and Accountability of the Corporation in Contemporary Society: Corporate Governance at a Crossroads*, 62 L. & CONTEMP. PROBS. 9 (1999); Hao Liang & Luc Renneboog, *On the Foundations of Corporate Social Responsibility*, 72 J. FIN. 853 (2017). A full discussion of this hypothesis, which still awaits a rigorous empirical confirmation, exceeds the present scope.

Guth directs the directors' fiduciary obligations to the company and to shareholders, implicitly implying that the interests of the two overlap. This doctrine has been solidified in a number of recent cases. In *eBay Domestic Holdings, Inc. v. Newmark*, the Delaware Chancery Court stated that "[d]irectors of a for-profit Delaware corporation cannot deploy a rights plan to defend a business strategy that openly eschews stockholder wealth maximization - at least not consistently with the directors' fiduciary duties under Delaware law."[19] In a more broadly applicable and prominent context, the Delaware Supreme Court in *Gheewalla* ruled that -

> When a solvent corporation is navigating in the zone of insolvency, the focus for Delaware directors does not change: directors must continue to discharge their fiduciary duties to the corporation and its shareholders by exercising their business judgment in the best interests of the corporation for the benefit of its shareholder owners.[20]

Gheewalla is particularly noteworthy because the Court goes to great lengths "to provide the directors with clear signal beacons and brightly lined channel markers as they navigate with due care, good faith, and loyalty on behalf of a Delaware corporation and its shareholders."[21] So much so, that by drawing a sharp distinction between solvency and insolvency, it effectively denies, as a matter of law, the existence of a murky zone of insolvency. In reality, however, vagueness and uncertainty characterize this setting, as the Court itself notes.

In *Trados*, the Delaware Chancery took shareholder primacy to its logical extreme, when it distinguished between common stockholders as residual claimants and thus ultimate beneficiaries of the firm's value, who are protected by fiduciary duties, and preferred stockholders with contractual rights, who are not owed fiduciary

---

[19] eBay Domestic Holdings, Inc. v. Newmark, 16 A.3d 1, 35 (Del. Ch. 2010).

[20] *Gheewalla, supra* note 10, at 101 (Del. 2007). *See* also Quadrant Structured Prods. Co. v. Vertin, 102 A.3d 155 (Del. Ch., 2014).

[21] *Gheewalla, id.*

duties on the basis of such rights.[22] By holding the contractual element to be dominant, *Trados* relegates the preferred to the stakeholder category in the OECD Principles framework. While doctrinally and economically sound, this distinction, too, has a certain air of denial to it, since preferred stocks are actually a hybrid of debt and residual-claim-type equity.

The legal landscape in the United States is broader and more varied than Delaware law. For one, scholars still debate shareholder primacy in fiduciary duties in U.S. corporations.[23] In addition to case law, there is a substantial body of statutory law in numerous states - including, in particular, "constituency statues" and benefit corporation statues. The effect of these statutes on the content and exercise of fiduciary duties in regular business corporations is at best unclear.[24]

3. The United Kingdom

U.K. law is more loyal to the classical formula of fiduciary loyalty by making the company alone the beneficiary of directors' fiduciary duties. Moreover, it has traditionally taken a comprehensive approach to the best interests of the company by referring to "the company as a whole".[25] The Companies Act 2006 preserves this

---

[22] *Trados, supra* note 11, at 63; *see* also Frederick Hsu Living Trust v. ODN Holding Corp., 2017 Del. Ch. LEXIS 67 (Del. Ch. 2017) (same).

[23] *See* Robert J. Rhee, *A Legal Theory of Shareholder Primacy*, 102 MINN. L. REV. 1951 (2018) for a recent survey.

[24] *See*, e.g. and respectively, Brett H. McDonnell, *Corporate Constituency Statutes and Employee Governance*, 30 WM. MITCHELL L. REV. 1227 (2004); Jonathan D. Springer, *Corporate Constituency Statutes: Hallow Hopes and False Fears*, 1999 ANN. SURV. AM. L. 85 (1999); Julian Velasco, *Shareholder Primacy in Benefit Corporations*, in this volume; Brett McDonnell, *Benefit Corporations and Public Markets: First Experiments and Next Steps*, 39 SEATTLE U. L. REV. 263 (2017); David G. Yosifon, *Opting out of Shareholder Primacy: Is the Public Benefit Corporation Trivial?*, 41 DEL. J. CORP. L. 461 (2017). One may note that the Model Benefit Corporation Legislation only requires that directors consider the interests of other stakeholders, not unlike the present proposal. *See* William H. Clark, Jr. et al., White Paper: The Need and Rationale for the Benefit Corporation 17 (2013), https://benefitcorp.net/sites/default/files/Benefit_Corporation_White_Paper.pdf.

[25] *See* Greenhalgh v. Arderne Cinemas [1951] Ch. 286, 291 (C.A.); Allen v. Gold Reefs of West Africa Ltd [1900] 1 Ch 656, 671.

approach.[26] Section 172 of the Act is explicit in designating shareholders as the ultimate beneficiaries of the company. Crucially, this section requires directors to consider other stakeholders, yet stakeholders' interests are subordinated to the interests of shareholders.[27] In tandem, the manner in which this consideration is to be carried out - e.g., as between shareholder value and combating climate change and promoting human rights - is left to the discretion of the directors.[28]

The relations between shareholders' and creditors' interests as the subject of directors' good-faith judgment as to the best interest of the company are more nuanced in U.K. law than in Delaware law. Section 172 preserves prior statutory and case law "requiring directors, in certain circumstances, to consider or act in the interests of creditors of the company" - namely, in the vicinity of insolvency.[29] In those circumstances, the contours of which are decidedly fuzzy,[30] the director must "have proper regard for the interest of [the company's] creditors and prospective creditors."[31] In *BTI 2014 v. Sequana*, the Court of Appeal acknowledged that "the interests of creditors are identified as interests different from, and potentially in conflict with, the promotion of the success of the company for the benefit of its

[26] Companies Act 2006, s. 170(1).

[27] For discussions, *see*, e.g., Andrew Keay, *Tackling the Issue of the Corporate Objective: An Analysis of the United Kingdom's Enlightened Shareholder Value Approach*, 27 SYDNEY L.R 577 (2007); Georgina Tsagas, *Section 172 of the Companies Act 2006: Desperate Times Call for Soft Law Measures*, in SHAPING THE CORPORATE LANDSCAPE: TOWARDS CORPORATE REFORM AND ENTERPRISE DIVERSITY (Nina Boeger & Charlotte Villiers, eds) 131 (2018).

[28] *See* R (on the application of People & Planet) v. HM Treasury (2009) EWHC 3020 (Admin), [35].

[29] *See* West Mercia Safetywear Ltd (Liq.) v. Dodd (1988) 4 BCC 30; Kristin van Zwieten, *Director Liability in Insolvency and Its Vicinity*, 38 OXFORD J. L. STUD. 382 (2018).

[30] *See*, recently, BTI 2014 LLC v. Sequana S.A. [2019] EWCA Civ 112.

[31] Jetivia SA v. Bilta (UK) Ltd [2015] UKSC 23, [123].

members as a whole."[32] The Court further indicated that these interests are mutually exclusive, suggesting that they should dominate directors' discretion sequentially.[33]

4. *Canada*

At first glance, Canadian law closely resembles U.K. law on the present subject, as section 122 of the Canada Business Corporations Act, 1985 renders the corporation the nominal beneficiary of directors and officers' fiduciary duties. A seemingly small difference in the provision on oppression, which refers to creditors,[34] has led to a radical departure of the Canadian approach to the treatment of stakeholders from the traditional rule. In considering a petition by institutional bondholders in 2008, the Supreme Court of Canada in *BCE* said:

> [T]he duty of the directors to act in the best interests of the corporation comprehends a duty to treat individual stakeholders affected by corporate actions equitably and fairly. There are no absolute rules. In each case, the question is whether, in all the circumstances, the directors acted in the best interests of the corporation, having regard to all relevant considerations, including, but not confined to, the need to treat affected stakeholders in a fair manner, commensurate with the corporation's duties as a responsible corporate citizen.
>
> Directors may find themselves in a situation where it is impossible to please all stakeholders… There is no principle that one set of interests - for example the interests of shareholders - should prevail over another set of interests.[35]

The Court thus put on the table what many have swept under the carpet. By using fairness rather than loyalty as the framework of analysis, *BCE* allows for conflicting interested to be weighted against one another. However, as the Court candidly acknowledges, it gives directors no guidance as to how they should resolve this dilemma, and in fact notes that "the court looks beyond legality to what is fair,

---

[32] *BTI 2014 v. Sequana, supra* note 30, at [198].

[33] *Id.*, at [199].

[34] Canada Business Corporations Act, 1985, s. 241(2). *Compare* the parallel provision on unfair prejudice in s. 994 of the Companies Act 2006 (U.K.).

[35] *BCE*, *supra* note 8, at [82]-[84].

given all of the interests at play."[36] A 2019 amendment to section 122 (re-)locates the issue within fiduciary duties, as it authorizes directors and officers to consider the interests of shareholders, employees, retirees and pensioners, creditors, consumers, and governments; the environment; and the long-term interests of the corporation. Consistent with *BCE*, this new provision does not prioritize any of these interests.[37]

5. Israel

In line with other modern corporate law statutes, the Israeli Companies Law, 1999 includes a specific provision on the objective of the corporation, stating that "[t]he purpose of a company is to operate in accordance with business considerations for maximizing its profits, and within the scope of such considerations, the interests of its creditors, its employees and the public may *inter alia* be taken into account."[38] Bearing in mind that only shareholders are entitled to profits when dividends are paid out, this section thus reads like a stronger version of its U.K. counterpart. Both provisions implement a shareholder primacy approach, but while in the U.K. statute considering the interests of other stakeholders is mandatory, the Israeli provision renders it discretionary.

Despite the relatively clear language of the statute, the Israeli Supreme Court in *Mishmar HaEmek v. Manor* - a case dealing with equitable subordination of shareholder loans - interpreted it as requiring the company at all times to balance the

---

[36] *BCE*, *id.*, at [71].

[37] The new section 122(1.1) resembles Peoples Department Stores Inc. (Trustee of) v. Wise, 2004 SCC 68, [42] ("[I]n determining whether they are acting with a view to the best interests of the corporation it may be legitimate, given all the circumstances of a given case, for the board of directors to consider, inter alia, the interests of shareholders, employees, suppliers, creditors, consumers, governments and the environment.").

[38] Companies Law, 1999, s. 11(a).

interests of all stakeholders, especially creditors.[39] The Court reasoned that such balancing is called for in light of the duty of good faith that governs the company's relations with all of its commercial counterparts.[40] It stands to reason that in discharging their fiduciary duty to act in the interest of the company,[41] directors and officers should implement such balancing, although the manner for doing so remains elusive, much like in Canada.

6. India

India's Companies Act, 2013 presents the most dedicated attempt to date to implement a formal pluralistic, stakeholder-oriented duty. Section 166 of the Indian Act provides that "[a] director of a company shall act in good faith in order to promote the objects of the company for the benefit of its members as a whole, and in the best interests of the company, its employees, the shareholders, the community and for the protection of environment." The language and the legislative history of this provision are clear, that the intention was to put the interests of all stakeholder constituencies on the same level as constitutive elements of the interest of the company.[42]

On the one hand, the Indian provision echoes the parallel Israeli and U.K. provisions in terminology and style. On the other hand, its content bears substantial resemblance to the Canadian ruling in *BCE* and section 122(1.1). Specifically, there

---

[39] C.A. 4263/04 Mishmar HaEmek v. Manor, Adv., as Liquidator of Efrochei HaZafon Ltd., 63(1) P.D. 458 (2009).

[40] *Id.*, at [18] (Procaccia J).

[41] S. 254(a) of the Companies Law. This section codifies the traditional duty of loyalty, which was formerly recognized in case law. *See* Mo. 100/52 Hevra Yerushalmit LeTaasiya Ltd v. Aghion, 6 P.D. 887, 889 (1952), citing *Cook v. Deeks*, [1916] UKPC 10.

[42] *See*, e.g., Afra Afsharipour, *Redefining Corporate Purpose: An International Perspective*, 40 SEATTLE U. L. REV. 465 (2017); Umakanth Varottil, *The Evolution of Corporate Law in Post-Colonial India: From Transplant to Autochthony*, 30 AM U. INT'L L. REV. 253 (2016). On a related obligation of corporate philanthropy under Section 135 of the Act *see*, e.g., Arjya B. Majumdar, *India's Journey with Corporate Social Responsibility: What Next*, 33 J.L. & COM. 165 (2014-2015).

is no hint in it (or in related materials) as to *how* directors should balance the potentially conflicting interests of different stakeholders. Moreover, as Mihir Naniwadekar and Umakanth Varottil powerfully argue, this provision suffers from additional implementation problems, as stakeholders lack any means for enforcing whatever rights they may have.[43] "Arguably," they aver, "the magnanimity of its verbiage and rhetoric in favour of stakeholders merely pays lip service to them and obscures any real teeth or legal ammunition available to non-shareholder constituencies to assert those rights as a matter of law."[44]

B. Some Normative Aspects

Let us now move from the positive to the normative. In the seminal dialogue between Adolf Berle and E. Merrick Dodd in the 1930s, Berle actually sided with Dodd on the principled normative desirability of a pluralistic approach.[45] He nonetheless rejected it for being unworkable:

> Now I submit that you can not [sic] abandon emphasis on 'the view that business corporations exist for the sole purpose of making profits for their shareholders' until such time as are to be prepared to offer a clear and reasonably enforceable scheme of responsibilities to someone else.[46]

Arguments for the monistic, shareholder-centered approach are diverse. One strand invokes shareholder sovereignty and ownership of the corporation, manifested in shareholder voting, to support this view.[47] Another invokes the agency problem

---

[43] *See* Mihir Chandrashekhar Naniwadekar & Umakanth Varottil, The *Stakeholder Approach Towards Directors' Duties Under Indian Company Law: A Comparative Analysis*, in THE INDIAN YEARBOOK OF COMPARATIVE LAW 2016 95 (Mahendra Pal Singh, ed, 2017).

[44] *Id.*, at 97.

[45] For a detailed analysis *see* Amir N. Licht, *The Maximands of Corporate Governance: A Theory of Values and Cognitive Style*, 29 DEL. J. CORP. L. 649, 690-698 (2004).

[46] Adolf A. Berle, Jr., *For Whom Corporate Managers Are Trustees: A Note*, 45 HARV. L. REV. 1365, 1367 (1932); *see* also Victor Brudney, *Contract and Fiduciary Duty in Corporate Law*, 38 B.C. L. REV 595, 645-46 (1997).

[47] *See*, e.g., Lawrence A. Hamermesh & Leo E. Strine Jr., *Fiduciary Principles and Delaware Corporation Law: Searching for the Optimal Balance by Understanding that the World is not*, in

and economic efficiency more generally. The former argument, from agency, holds that allowing corporate insiders to shift among several maximands of different stakeholders will dilute the accountability of those insiders. Pointing to shareholders as the residual financial claimants in the corporation, the argument from efficiency holds that maximizing profits in the interest of shareholders promotes the interest of all other (financial) claimants, whose interests are largely fixed.[48]

Some proponents of the pluralistic approach marshal ethical and political arguments in support of that view.[49] Another strand of the literature draws on insights about pro-social motivations from psychology and behavioral economics in support of entrusting insiders with discretion to consider all the stakeholders who participate the firm's team production.[50]

Economists who have interjected into this debate tend to uphold the shareholderist approach.[51] Vikas Mehrotra and Randall Morck underscore the danger that "[e]xpanding the corporate objective function to include non-equity stakeholders

---

OXFORD HANDBOOK OF FIDUCIARY LAW (Evan J. Criddle, Paul B. Miller & Robert H. Sitkoff eds., forthcoming 2019), https://ssrn.com/abstract=3044477; Julian Velasco, *Shareholder Ownership and Primacy*, 2010 U. ILL. L. REV. 897.

[48] FRANK H. EASTERBROOK AND DANIEL R. FISCHEL, THE ECONOMIC STRUCTURE OF CORPORATE LAW 38 (1991).

[49] *See*, e.g., Lyman Johnson, *The Delaware Judiciary and the Meaning of Corporate Life and Corporate Law*, 68 TEX. L. REV. 865 (1990); Ronald M. Green, *Shareholders as Stakeholders: Changing Metaphors of Corporate Governance*, 50 WASH. & LEE L. REV. 1409 (1993); Symposium, *Corporate Irresponsibility: America's Newest Export?*, 70 GEO. WASH. L. REV. 890 (2002); Robert J. Rhee, *Fiduciary Exemption for Public Necessity: Shareholder Profit, Public Good, and the Hobson's Choice During a National Crisis*, 17 GEO. MASON L. REV. 661 (2010); David Millon, *Radical Shareholder Primacy*, 10 U. ST. THOMAS L.J. 1013 (2013).

[50] *See*, e.g., Margaret M. Blair & Lynn A. Stout, *A Team Production Theory of Corporate Law*, 85 VA L. REV. 247 (1999); LYNN STOUT, THE SHAREHOLDER VALUE MYTH: HOW PUTTING SHAREHOLDERS FIRST HARMS INVESTORS, CORPORATIONS, AND THE PUBLIC (2012). Bainbridge, however, supports shareholder-centered "director primacy". *See*, e.g., Stephen M. Bainbridge, *Director Primacy: The Means and Ends of Corporate Governance*, 97 NW. U. L. REV. 547 (2003).

[51] *See*, most famously, Milton Friedman, *A Friedman Doctrine - The Social Responsibility of Business Is to Increase Its Profits*, N.Y. Times, Sept. 13, 1970, § 6 (Magazine); *see* also MILTON FRIEDMAN, CAPITALISM AND FREEDOM 133 (1962) (same).

has the side effect of magnifying top mangers' scope for opportunism"; they therefore wryly conclude that "shareholder value maximization might be the worst option save all the others."[52] Acknowledging this risk, Roland Bénabou and Jean Tirole nonetheless aver that investors and other stakeholders could have some demand for corporate managers to adopt socially responsible strategies on their behalf notwithstanding profit sacrifice.[53] Hart and Luigi Zingales argue that given that in reality many investors are prosocial, managers should be tasked with the former.[54] This approach seems to suffer from a implementation problem, too, however. Entrusting corporations with promoting prosocial preferences could run into the impossibility of forming a consensus among investors and/or stakeholders.[55]

Empirical evidence on the desirability of these approaches is equivocal. A number of meta-analyses find a weak but significantly positive correlation between firms' social performance and financial performance.[56] What remains unclear is the mechanism that engenders these results: Does maximizing shareholder value

---

[52] Vikas Mehrotra & Randall Morck, *Governance and Stakeholders*, in 1 THE HANDBOOK OF THE ECONOMICS OF CORPORATE GOVERNANCE 637, 673, 638 (Benjamin E. Hermalin & Michael S. Weisbach eds., 2017). *See* also Richard M. Frankel, S.P. Kothari, and Luo Zuo, Why Shareholder Wealth Maximization despite Other Objectives, working paper (2019), https://ssrn.com/abstract=3165085.

[53] Roland Bénabou & Jean Tirole, *Individual and Corporate Social Responsibility*, 77 ECONOMICA 1 (2010).

[54] Oliver Hart & Luigi Zingales, *Companies Should Maximize Shareholder Welfare Not Market Value*, 2 J.L. FIN. & ACCT. 247 (2017).

[55] *See* Mehrotra & Morck, *supra* note 52, citing Kenneth J. Arrow, *A Difficulty in the Concept of Social Welfare*, 58 J. POL. ECON. 328 (1950); Frankel *et al.*, *supra* note 52 (same).

[56] *See* Mahfuja Malik, *Value-Enhancing Capabilities of CSR: A Brief Review of Contemporary Literature*, 127 J. BUS. ETHICS 419 (2015); Gunnar Friede et al., *ESG and Financial Performance: Aggregated Evidence from More than 2000 Empirical Studies*, 5 J. SUSTAINABLE FIN. & INV. 210 (2015); Joshua Margolis et al., Does it Pay to Be Good … And Does it Matter? A Meta-Analysis of the Relationship between Corporate Social and Financial Performance, (2009) (unpublished manuscript), https://ssrn.com/abstract=1866371; Joshua Margolis & Hillary A. Elfenbein, *Do Well by Doing Good? Don't Count on It*, 86 HARV. BUS. REV. 19 (Jan. 2008); Marc Orlitzky et al., *Corporate Social and Financial Performance: A Meta-Analysis*, 24 ORG. STUD. 403 (2003). While the methodology for assessing financial performance is well-established, the methodology for assessing social performance is still developing. *See* generally Amir Amel-Zadeh, Social Responsibility in Capital Markets: A Review and Framework of Theory and Empirical Evidence, working paper (2018), https://ssrn.com/abstract=2664547.

incidentally help other stakeholders, or can better managers handle several stakeholder constituencies simultaneously to the benefit of all?[57]

Whether or not one is persuaded by the empirical evidence, the normative debate probably cannot be resolved because of another, more fundamental difficulty. I have argued that the two polar positions in this debate express different values, where values are defined according to social psychological theories as conceptions of the desirable.[58] In a joint study with Renée Adams and Lilach Sagiv, we have shown that board members and CEOs of Swedish public corporations exhibited a systematic approach to different shareholder-stakeholder conflict that map onto a dimension of shareholderism versus stakeholderism, that in turn is linked to personal value preferences.[59] In a subsequent study with Adams, we confirm this relationship in a multinational sample of directors and also observe robust relations between shareholderism and cultural orientations.[60] These findings indicate that directors address the issue with an intention to "do the right thing", the law notwithstanding.

---

[57] *See* Larry Fauver, Michael B. McDonald, & Alvaro Taboada, *Does it Pay to Treat Employees Well? International Evidence on the Value of Employee Friendly Culture*, 50 J. CORP. FIN. 84 (2018). *Compare* Lea Cassar & Stephan Meier, Intentions for Doing Good Matter for Doing Well: The Negative Effects of Prosocial Incentives, Columbia University Working Paper (2018); Agne Kajackaite & Dirk Sliwka, Prosocial Managers, Employee Motivation, and the Creation of Shareholder Value. IZA Discussion Paper No. 11789 (2018), https://ssrn.com/abstract=3249903. *See*, generally, Wolfgang Breuer *et al.*, *Corporate Social Responsibility, Investor Protection, and Cost of Equity: A Cross-Country Comparison*, 96 J. BANK'G FIN. 34 (2018); Allen Ferrell *et al.*, *Socially Responsible Firms*, 122 J. FIN. ECON. 585 (2016); Philipp Krüger, *Corporate Goodness and Shareholder Wealth*, 115 J. FIN. ECON. 304 (2015); Jan Schmitz & Jan Schrader, *Corporate Social Responsibility: A Microeconomic Review of the Literature*, 29 J. ECON. SURV. 27 (2015); Patricia Crifo & Vanina Forget, *The Economics of Corporate Social Responsibility: A Firm-Level Perspective Survey*, 29 J. ECON. SURV. 112 (2015); Ronald W. Masulis & Syed Walid Reza, Private Benefits and Corporate Investment and Financing Decisions: The Case of Corporate Philanthropy, European Corporate Governance Institute (ECGI) - Finance Working Paper No. 603/2019 (2019), https://ssrn.com/abstract=3298951.

[58] *See* Licht, *supra* note 45, at 657-658, citing, in particular, Shalom H. Schwartz, *Universals in the Content and Structure of Values: Theoretical Advances and Empirical Tests in 20 Countries,* in 25 ADVANCES IN EXPERIMENTAL SOCIAL PSYCHOLOGY 1 (Mark P. Zanna ed. 1992).

[59] Renée B. Adams, Amir N. Licht & Lilach Sagiv, *Shareholders and Stakeholders: How Do Directors Decide?*, 32 STRATEGIC MGMT. J. 1331 (2011).

[60] Amir N. Licht & Renée B. Adams, Shareholders and Stakeholders around the World: The Role of Values, Culture, and Law in Directors' Decisions, working paper (2019), https://ssrn.com/abstract=3407873.

Direct legal regulation of directors' conduct in shareholder-stakeholder dilemmas thus could face formidable difficulties.

III. STAKEHOLDER IMPARTIALITY

A. The Classical Doctrine

Consider a simple scenario: In preparation for meeting his maker, one settles a trust, instructing the trustee to care for the financial needs of his loved ones at her absolute discretion. The survivors include a widow and a number of orphans of different ages. The widow is ageing and is looking at existing and foreseeable medical expenses, whereas the orphans are quite healthy now and will likely enjoy a longer life than the trustee can imagine. Assume for simplicity that the estate consists only of cash and that only securities are to be purchased (thus excluding real property, etc.). In addition, it is undisputed that the trustee operates with the punctilio of an honor the most sensitive and that she is perfectly prudent and fully skilled for the task. What should be the makeup of the trust's investment portfolio in terms of the ratio between stocks and bonds? With regard to equities, should the trustee invest in high-tech start-up companies? Respectively, should she prefer government bonds over corporate bonds?

The trustee in this setting faces an irreconcilable conflict between the interests of the two classes of beneficiaries that stem from their different life expectancies. This, in turn, calls for different investment strategies for fulfilling the financial needs of each generation. The widow's needs militate for liquid, low-risk, fixed-income securities. The children can better tolerate market fluctuations so would rather have high-volatility, high-yield investments. *Any* decision by the trustee could adversely affect one or both of the beneficiary classes. It could thus be challenged upon standard fiduciary law analysis - and the trustee could be called to account - on the basis of breaching the no-conflict rule by way of dual fiduciary or duty-duty conflict, or for failing to act in subjective good faith, or for acting in light of an ulterior motive. Fiduciary law's standard response - to disable the trustee - is no answer, as the problem does not lie with the trustee but rather with the beneficiaries. Splitting the estate in two is no cure either: similar tensions will immediately emerge between the commerce-oriented child who would benefit most from a capital infusion and the artsy, dreamy one who needs a stable source of income for living expenses.

This generic dilemma became prominent in late-eighteenth-century England.[61] A typical settlement would authorize the trustee to manage the estate for the benefit of a life-tenant (the widow) and the remainderman or the residuary (the orphans). Oftentimes, the distinction between the life beneficiary and the remainderman overlapped with different financial (equitable) interests in the estate - to income and to capital, respectively. But this seemingly clear distinction caused as many problems as it purported to solve. For example, what should be the rule if capital assets require current expenses for maintenance? Should dividends from shares be treated as income or as capital? Early nineteenth century cases have established technical rules of apportionment in light of the financial circumstances of the era.[62] Those rules have since been revised or abolished, in line with developments in finance.[63]

Of greater importance here is the substantive conceptual framework for the comparative treatment of beneficiary classes. Originally, the trustee's obligation to

---

[61] The following draws on the compelling account in CHANTAL STEBBINGS, THE PRIVATE TRUSTEE IN VICTORIAN ENGLAND 65-97 (2002).

[62] *See*, e.g., Howe v. Earl of Dartmouth (1802) 32 ER 56, (1802) 7 Ves Jun 137; Earl of Chesterfield's Trusts (1883) 24 Ch D 643; Allhusen v. Whittell [1861-1873] All ER 149, (1867) LR 4 Eq 295.

[63] In the United Kingdom, for instance, the rules in *Earl of Dartmouth*, *Earl of Chesterfield's Trusts*, and *Allhusen* were abolished by the Trusts (Capital and Income) Act 2013.

treat beneficiaries impartially and fairly as part of her duty of loyalty was understood to imply equal treatment. According to Chantal Stebbings, this was "in accordance with the maxim 'Equality is Equity' and with the very foundation of Equitable jurisprudence in concepts of fairness and even-handedness."[64] This is feasible when the beneficiaries are on equal footing.[65] This laudable principle is incompatible, however, with handling differential interests of differently-situated beneficiaries. Moreover, in the social circumstances of Victorian England, in which many trustees were relatives or close friends of the settlor or beneficiaries, it proved difficult to resist pressures to adjust trust administration to the needs of particular beneficiaries - sometimes, with solid justification. The technical rules of apportionment further triggered litigation over equality issues and motivated settlors to opt out of these rules.[66] Due to a confluence of these and additional factors, by the early twentieth century, equality was abandoned as the substantive content meaning of the trustee's duty of impartiality.[67]

Today, the duty of impartiality (or even-handedness, or fairness) "regulates trustee/beneficiary conflicts when the trust terms create a conflict that abridges the sole interest rule."[68] It is recognized and implemented largely similarly in all the major common law jurisdictions. Its application has spread during the late twentieth century beyond private trusts - most notably, to administration of pension funds. This

---

[64] STEBBINGS, *supra* note 61, at 67.

[65] *See*, e.g., Hutchinson v. Morritt (1839) 160 ER 818, 3 Y & C Ex. 547 ("[I]t is the duty of trustees … to divide the profit so made rateably amongst the cestui que trusts.")

[66] STEBBINGS, *supra* note 61, at 70-71.

[67] STEBBINGS, *supra* note 61, at 79.

[68] John H. Langbein, *Questioning the Trust Law Duty of Loyalty: Sole Interest or Best Interest?*, 114 YALE L.J. 929, 939 (2005).

obligation is further implemented with respect to executors in corporate insolvency. The following provides a brief survey of its contemporary content meaning.

Succinctly, the duty of impartiality imposes on the fiduciary an obligation to consider the interests of her beneficiaries. Not more than that, but not less either. "[U]nder a discretionary trust," noted the court in *Kain v. Hutton*, "there is no right to distributions but only a right to be considered."[69] In *Cowan v. Scargill*, probably the most famous case in the modern era, Megarry VC stated that it is "the duty of trustees to exercise their powers in the best interests of the present and future beneficiaries of the trust, holding the scales impartially between different classes of beneficiaries."[70] In *Nestle v. National Westminster Bank*, Hoffmann J clarified:

> [T]he trustee must act fairly in making investment decisions which may have different consequences for different classes of beneficiaries. There are two reasons why I prefer this formulation to the traditional image of holding the scales equally between tenant for life and remainderman. The first is that the image of the scales suggests a weighing of known quantities whereas investment decisions are concerned with predictions of the future. … The second reason is that the image of the scales suggests a more mechanistic process than I believe the law requires. The trustees have in my judgment a wide discretion. … It would be an inhuman law which required trustees to adhere to some mechanical rule for preserving the real value of the capital when the tenant for life was the testator's widow who had fallen upon hard times and the remainderman was young and well off.[71]

Nestle was approved on appeal, where Staughton LJ and Leggatt LJ said, respectively:

> At times it will not be easy to decide what is an equitable balance. If the life-tenant is living in penury and the remainderman already has ample wealth, common sense suggests that a trustee should be able to take that into account, not necessarily by seeking the highest possible income at the expense of capital but by inclining in that direction. …
>
> The very process of attempting to achieve a balance, or (if that be old-fashioned) fairness, as between the interests of life-tenants and those of a

[69] Kain v. Hutton [2007] NZCA 199, [243].

[70] Cowan v. Scargill [1985] Ch 270, 286-287.

[71] Nestle v. National Westminster Bank plc [2000] WTLR 795 (Ch), (1988) 10 Tru LI 112. This decision has been cited with agreement several times. *See*, e.g., X v. A, B, C [2000] EWHC Ch 121; Forester Maurice Labrouche v. Frey [2016] EWHC 268 (Ch).

> remainderman inevitably means that each can complain of being less well served than he or she ought to have been.[72]

The courts have emphasized that impartial administration of the trust does not entail equal treatment. In *Edge v. Pension Ombudsman*, the Court of Appeal rejected an attempt to find fault in pension fund trustees who failed to give equal weight to the interests of all groups of savers.[73] In *Forbes Trustee Services Ltd v. Jackson*, the court noted that "[s]ome inequalities in treatment are inevitable, but [trustees] must not pursue a course of action which clearly favours one class of members over another."[74] The law in Australia, New Zealand, and Canada is virtually similar;[75] so is trust law and federal ERISA law in the United States, where the trustee is required to have "due regard" to the interests of the different beneficiary classes.[76] For example, *Siskind v. Sperry Retirement Program* held that "[i]t was reasonable for the plan fiduciary to approve an amendment that would provide increased benefits to those employees whose jobs were at greater risk of elimination, [because] employees

---

[72] Nestle v. National Westminster Bank [1992] EWCA Civ 12.

[73] Edge v. Pension Ombudsman [1999] EWCA Civ 2013.

[74] Forbes Trustee Services Ltd v. Jackson [2004] EWHC 2448 (Ch).

[75] *See*, e.g., respectively, for Australia: Commonwealth Bank Officers Superannuation Corporation Pty Ltd v. Beck [2016] NSWCA 218; Manglicmot v. Commonwealth Bank Officers Superannuation Corporation [2010] NSWSC 363; for New Zealand: Enright v. Enright [2019] NZHC 1124; Re Mulligan (Deceased) [1998] 1 NZLR 481 (HC); for Canada: Neville v. Wynne, 2006 BCCA 460; Anova Inc. Employee Retirement Pension Plan (Administrator of) v. Manufacturers Life Insurance Co. (1994) 121 DLR (4th) 162 (ON SC).

[76] *See*, with regard to private trusts, Restatement (Third) of Trusts, § 78-79; Uniform Trust Code § 803 (2005); Uniform Principal and Income Act § 103 (2000); Varity Corp. v. Howe, 516 U.S. 489 (1996). With regard to ERISA, *see*, e.g., Siskind v. Sperry Retirement Program, 47 F.3d 498 (2d Cir. 1995); Morse v. Stanley, 732 F.2d 1139 (2d Cir. 1984). With regard to trust indentures of debt facilities, *see* Steven L. Schwarcz, *Fiduciaries with Conflicting Obligations*, 94 MINN. L. REV. 1867 (2010).

at overstaffed plants and employees at ‘lean’ plants are not similarly situated.”[77] As noted, company liquidators and administrators are subject to a similar duty as well.[78]

Cases holding fiduciaries to account for breaching the duty of impartiality are rare. Still, the trustee’s exceptionally ample discretion in discharging her duty to act in the best interests of the body of beneficiaries as a whole does not mean unbridled discretion, let alone immunity from liability. For example, in *Mulligan,* the trustees were held liable for indulging the wishes of the widow by investing solely in high-interest fixed-income assets that did not provide any capital appreciation.[79] Before its judgment was reversed on appeal, the primary court in *Wendt v. Orr* held an executor accountable for monies he paid out in breach of the duty of impartially to potential claimants and for related costs and ordered for his removal.[80] In *re Smith*, the trustee was removed from office for heeding the objections of the remainderman to purchasing higher-yielding investments that would have benefitted the life-tenant.[81] In *Boe v. Alexander,* a pension fund trustee was found to have breached his duty to balance the interests of all the beneficiaries.[82]

B. The Proposed Approach

It is the thesis of this paper that the duty of impartiality holds substantial promise as a doctrinal framework for addressing the interests of stakeholder constituencies in business firms. In this view, directors and other corporate fiduciaries with strategic responsibilities will be obliged to treat the company’s

---

[77] *Siskind, id.,* at 506.

[78] *See* In re Contract Corporation (Gooch’s Case) (1871) LR 7 Ch App 207; IND Energy Inc v. Langdon [2014] WASC 364; ASIC v. Edge [2007] VSC 170; Bovis Lend Lease v. Wily [2003] NSWSC 467.

[79] *Mulligan, supra* note 75.

[80] *See* Wendt v. Orr [2004] WASC 28; reversed in Orr v. Wendt [2005] WASCA 199.

[81] *See* Re Smith, (1971) 16 DLR (3d) 130 (ON SC), affirmed (1971) 18 DLR (3d) 405 (ON CA).

[82] Boe v. Alexander (1987) 15 BCLR (2d) 106 (C.A.).

stakeholders impartially when they make business judgments in the best interest of the company as a whole - an obligation that will be discharged by considering the interests of the company's various stakeholders. This obligation of stakeholder impartiality will form part of directors' duty of loyalty and will be discharged with skill and care that are reasonably required in the circumstances.

The proposed duty draws on the traditional duty of trustees only as a source of inspiration for its conceptual framework. This is because trustees' duty of impartiality in discretionary trusts cannot be applied directly in a corporate setting. While trust beneficiaries are direct objects of trustee duties, it is the company (as a whole) that is the object/beneficiary of directors' duties.[83] Shareholders are only secondary notional beneficiaries, whose interest as a general constituency proxies for the company's interest in legal systems that endorse shareholder primacy. (Delaware and other U.S. laws are an exception, with their dual corporation-and-shareholders-oriented duty of loyalty under *Guth.*[84])

The duty of impartiality of liquidators may be viewed as a mid-way version, closer to the proposed duty of regular directors than the trustee's duty, because the liquidator's duty of loyalty, including impartiality, is formally oriented to both creditors and shareholders without ignoring the company's legal personality.[85] On this notional continuum, between regular trustees and liquidators, one could locate trustees of pension funds. The latter owe direct loyalty to the beneficiaries, but different beneficiary classes comprise large and changing numbers of individual beneficiaries akin to shareholders, bondholder, and employees. Common to all three

[83] *Compare* JJ Harrison (Properties) Ltd v. Harrison [2001] EWCA Civ 146, [25].

[84] *See supra* text around note 17.

[85] It is also directed to the court. *See Gooch's Case*, *supra* note 78; *see*, generally, In re Pantmaenog Timber Co Ltd [2003] UKHL 49.

types of fiduciary duties - of trustees, liquidators, and directors (as proposed) - is the discretion that these fiduciaries are required to exercise in good faith in the interest of a body of ultimate beneficiaries as a whole. At the same time, only directors exercise *business* judgment - with a view to taking up risky projects with uncertain payoffs - while trustees' and liquidators' mission and judgment are custodial in nature - with a predominant task of preserving the estate to reasonably ensure payout distribution.

Substantively, stakeholder impartiality would require directors to give proper consideration ("due regard" in U.S. usage) to stakeholders' interests. The duty's contribution to extant obligations - e.g., under section 172 of the U.K. Companies Act - lies in providing content and structure. First, this model explicates the obligation as requiring deliberation only, and thus, by construction, not requiring to take other kinds of action - e.g., to ameliorate certain adverse effects (while not forbidding it either). Second, this model clarifies that the duty is process-oriented rather than outcome-oriented. Specifically, it rejects an obligation to strive for, let alone achieve, any kind of equality among the different stakeholder constituencies, or, put otherwise, it does not call for balancing stakeholders' interests. Together, these features ensure that the proposed model is workable - that directors and courts can implement it "with clarity and force", as Berle and Brudney have insisted.[86]

By eschewing regulation of substantive equality of outcome, the proposed stakeholder impartiality does not encroach on directors' business judgment, thus preserving a sphere that is free of post hoc legal intervention. At the same time, while the proposed duty admittedly has lean content, it is anything but hollow. As a primarily process-oriented duty, it calls on directors to discharge it by conducting a structured and well-documented deliberation that is reasonable in the circumstances,

[86] *See supra* text to note 45 *et seq*.

in line with jurisprudence on the business judgment rule[87] and with a similar duty of trustees to exercise an informed discretion in a proper procedure.[88]

Procedures that focus on giving due regard to participants are nonetheless not devoid of content and should not be regarded as mere "box-checking". They can yield desirable outcomes despite, and perhaps thanks to their lean substantive content. Several mechanism may engender such effects. From the decision-makers' perspective, a formal requirement to consider someone in a discussion ensures that his or her issue is indeed discussed at any level of detail rather than neglected, either knowingly or subconsciously. Such a requirement also helps in raising awkward issues for discussion by team members who might otherwise prefer to avoid friction with their fellows. More basically, conducting discussions in an orderly and transparent fashion likely changes the very mode of analysis from intuitive to high-level deliberation thanks to dual-process mechanisms.[89] From the stakeholders' perspective, a duty to consider ensures that they would be given "their day in the board". Ample research on procedural justice by Tom Tyler and others has shown that such procedural features could engender positive outcomes, including acceptance of and collaboration with adverse decisions.[90]

---

[87] *See*, e.g., In re Walt Disney Co. Derivative Litigation, 907 A.2d 693, 750 (Del. Ch. 2005).

[88] *See* Abacus Trust Company (Isle of Man) v. Barr [2003] EWHC 114 (Ch), [16] and references therein.

[89] *See*, e.g., Gerard P. Hodgkinson & Eugene Sadler-Smith, *The Dynamics of Intuition and Analysis in Managerial and Organizational Decision Making*, 31 ACAD. MGMT. PERSP. 473 (2018); Jonathan St. B. T. Evans, *Dual-Processing Accounts of Reasoning, Judgment, and Social Cognition*, 59 ANN. REV. PSYCH. 255 (2008).

[90] *Compare* E. ALLAN LIND & TOM TYLER, THE SOCIAL PSYCHOLOGY OF PROCEDURAL JUSTICE (1988); *see* also Harris Sondak & Tom Tyler, *How Does Procedural Justice Shape the Desirability of Markets?*, 28 J. ECON. PSYCH. 79 (2007); Rebecca Hollander-Blumoff & Tom R. Tyler, *Procedural Justice in Negotiation: Procedural Fairness, Outcome Acceptance, and Integrative Potential*, 33 L. & SOC. INQUIRY 473 (2008).

Stakeholder impartiality as a legal doctrine need not overlap with stakeholder-oriented strategic management. According to Edward Freeman's capacious definition, a stakeholder could be "any group or individual who can affect or is affected by the achievement of the organization's objectives."[91] This is a positive axiomatic definition; it entails neither particular normative implications (which stakeholders deserve what), nor any instrumental implications (what would happen if some stakeholders got something).[92] The latter aspects would be determined separately, using different methodologies.

Recent jurisprudence in Australia and New Zealand demonstrates this point with regard to executors' duty of impartiality. In light of legislation that gives certain persons not mentioned in a will a right to nonetheless claim benefits from the estate within a limited period of time, the question arose whether the executor owes a duty of impartiality to such potential claimants. The courts have split on this question, and a full discussion, albeit instructive, is beyond the present scope.[93] The key point is that such potential claimants clearly fall within Freeman's definition of stakeholders, as they affect the administration of the estate. Nevertheless, a court may decline to recognize them as such as a matter of law and thus deny them the coverage of the duty of impartiality. A fully analogous analysis would be in place with regard to corporate stakeholder impartiality.

To ensure that stakeholder impartiality is not merely whitewash for hard-nosed shareholder primacy (for those who are concerned about this possibility), non-

---

[91] R. EDWARD FREEMAN, STRATEGIC MANAGEMENT: A STAKEHOLDER APPROACH 46 (1984).

[92] A large literature elaborates on these issues. For introductions *see*, e.g., Thomas Donaldson & Lee E. Preston, *The Stakeholder Theory of the Corporation: Concepts, Evidence, and Implications*, 20 ACAD. MGMT. REV. 65 (1995); Eric W. Orts & Alan Strudler, *Putting a Stake in Stakeholder Theory*, 88 J. BUS. ETHICS 605 (2009).

[93] For comprehensive analyses reaching opposite conclusions *see Wendt v. Orr*, *supra* note 80; *Orr v. Wendt*, *supra* note 80 and references therein.

shareholder stakeholders must be able to enforce their right to impartial treatment.[94] While beneficiaries of trusts and estates can bring a personal claim against the trustee, in companies only shareholders can bring a derivative claim - a point that *Gheewalla* has forcefully underscored.[95] Past experience indeed has shown that this is not a fanciful concern. In *Parke v. Daily News* the court applied *Hutton* to condemn paying employees beyond their legal entitlement.[96] Section 309 of the U.K. Companies Act 1985 was then amended to require the directors to have regard to the interests of the company's employees in general, as well as the interests of its shareholders. That section (now repealed) further provided that "the duty imposed by this section on the directors is owed by them to the company (and the company alone) and is enforceable in the same way as any other fiduciary duty owed to a company by its directors" - that is, excepting the company or a liquidator, by shareholders in a derivative action. Len Sealy famously quipped that "[Section 309] is either one of the most incompetent or one of the most cynical pieces of drafting on record."[97]

In order to prevent repetition of such a farce, members of stakeholder constituencies should have personal standing, or a direct cause of action, against the directors with regard to the latter's compliance with the duty of impartiality. Granted, such an arrangement would exceed the conventional array of rights and duties among and between the company, its directors and officers, and the shareholders. In tandem, relatively little will suffice to show proper discharge of this obligation - basically, evidence that the directors have indeed given their mind to the relevant stakeholders.

---

[94] Recall the critique by Naniwadekar and Varottil, *supra* test to note 43.

[95] *See Gheewalla*, *supra* note 10, and text to note 20 *et seq*.

[96] *Parke*, *supra* note 7.

[97] L.S. Sealy, *Directors' "Wider" Responsibilities - Problems Conceptual, Practical and Procedural* 13 MONASH U. L. REV. 164, 177 (1987).

There will be no need to mention any actual or potential substantive effect, as this is not called for by the duty, although it would be allowed to do so. One must not dismiss such evidence - typically, records of board meetings and related documents - as useless bureaucratic hassle, since the duty is process-oriented by design.

Stakeholder impartiality could prove particularly useful in legal systems that endorse a pluralistic approach to the objectives of the corporation, Canada being a prime example. Recall how the *BCE* court openly acknowledged that "there is no principle …"[98] *BCE* was decided in a legal framework of oppression/unfair prejudice, that in Canada includes the creditors. This is an outcome-oriented doctrine that aims to protect some minimum legitimate expectations; it connotes substantive fairness, not procedural fairness. It is not surprising therefore that the Court found itself in want of means for providing consistent guidance on the doctrine's content. To clarify: the rule in *BCE* is not meaningless or hollow; it is just not particularly workable, if at all. In contrast, if *BCE* were to be read as implying stakeholder impartiality, it is submitted that both market participants and the courts would be better able to comply with its ruling and promote the legal policy it reflects. A similar analysis would apply to section 166 of India's Companies Act, which formally designates the interest of all stakeholder constituencies as objectives of Indian companies.

Stakeholder impartiality could prove useful also in shareholderistic systems. For example, implementing this approach in the U.K. would provide boards of companies that are subject to the new reporting regulations mentioned in the Introduction a clear framework for establishing compliance with their duties under Section 172. Perhaps surprisingly, this approach might be applied in Delaware, too. Recall that in *Trados* and *ODN*, the courts denied preferred stockholders the

---

[98] *See supra* text to note 35.

protection of directors' duty of loyalty because common stockholders were deemed more deserving of this protection as residual claimants.[99] These decisions marginalized the residual equity feature of preferred stock. If stakeholder impartiality had been implemented in those cases the result might have remained the same, but the legal analysis would have been more loyal to the reality of the financial interests involved.[100]

IV. CONCLUSION

About twenty years ago, Henry Butler and Fred McChesney complained that "[f]or centuries legal, political, social, and economic commentators have debated corporate social responsibility *ad nauseam*."[101] Nauseating as it may be to some, the debate over shareholders and stakeholders as the focal objective of the corporation appears as lively as ever, even though the positions voiced in it now have a long lineage indeed. This essay does not attempt to resolve this debate, among other things, because the present author believes it cannot be resolved.[102] The goal of this essay is more modest yet still ambitious - to push the discourse forward by advancing a doctrinal framework for considering the interests of various stakeholders in those legal systems that already do or may in the future require directors to do so - e.g., in the United Kingdom and, in a very difference modus, in Canada - but also in legal system that currently focus on shareholder interests - e.g., in Delaware. Stakeholder

---

[99] *See supra* note 22.

[100] For proposals to implement impartiality analysis with regard to preferred stock, *see* LICHT, *supra* note 9; Shachar Nir, One Duty to All: The Fiduciary Duty of Impartiality and Stockholders' Conflict of Interest, working paper (2019), https://ssrn.com/abstract=3456340.

[101] Henry N. Butler & Fred S. McChesney, *Why They Give at the Office: Shareholder Welfare and Corporate Philanthropy in the Contractual Theory of the Corporation*, 84 CORNELL L. REV. 1195, 1195 (1999).

[102] *See supra* text to note 58 *et seq.*

impartiality, as proposed in this essay, is at the same time novel in corporate law yet classical in fiduciary law. Courts who wanted to experiment with it thus would be able to draw on a solid body of jurisprudence that would facilitate its implementation. It is hoped that some indeed will.

about ECGI

The European Corporate Governance Institute has been established to improve *corporate governance through fostering independent scientific research and related activities.*

The ECGI will produce and disseminate high quality research while remaining close to the concerns and interests of corporate, financial and public policy makers. It will draw on the expertise of scholars from numerous countries and bring together a critical mass of expertise and interest to bear on this important subject.

The views expressed in this working paper are those of the authors, not those of the ECGI or its members.

ECGI Working Paper Series in Law

www.ecgi.org\wp

Electronic Access to the Working Paper Series

The full set of ECGI working papers can be accessed through the Institute's Web-site (www.ecgi.org/wp) or SSRN:

Finance Paper Series	http://www.ssrn.com/link/ECGI-Fin.html
Law Paper Series	http://www.ssrn.com/link/ECGI-Law.html