CORPORATE GOVERNANCE AFTER THE FINANCIAL CRISIS, P.M. VASUDEV & SUSAN WATSON, EDS. (NORTHAMPTON, MA: EDWARD ELGAR, 2012)

There is a wide body of writing of varying levels of sophistication, specialization, and academic heft chronicling and analyzing the financial crisis that struck the world economy in 2008. The full significance of those events remains unknown; the effects linger. *Corporate Governance after the Financial Crisis*[1] broadly considers the corporate governance[2] environment in the context of those turbulent times. The book is a collection of papers presented at a symposium, *Corporate Governance in the Post, Post World*, which was hosted by the New Zealand Governance Centre at the University of Auckland in 2010.[3]

An excellent introduction by the editors outlines the general themes of the book, which is divided into four parts: shareholder/stakeholder interests in directorial decisions, private corporate law remedies and their efficacy as governance drivers, corporate governance and globalization, and a discussion of contemporary corporate ethics and responsibility. The distinguished scholars present their topics from unique angles, with due consideration given to jurisprudence, legal and economic history, and exploration of how a business structure — the corporation — is and should be governed when there is a macro-economic collapse of the sort recently experienced. To what degree do the constitutional workings of the corporate entity play a causal role? Can they be adjusted through regulation or otherwise to reduce negative results?

The major themes, particularly the friction between stakeholder and shareholder interests, will be quite familiar to those with a background in corporate law and practice. One is reminded of the opposing approaches to substantive legal issues characterized by Duncan Kennedy (as "individualism" and "altruism") in his 1976 essay "Form and Substance in Private Law Adjudication."[4] Individualist rhetorical approaches tend to favour solutions that have clear, clean, and formal rules that are highly susceptible to efficient administration; altruistic approaches tend to favour "equitable" standards, community, and the well-being of all through sacrifice. The "invisible hand" contrasts with "arrangement"; "exchange" contrasts with "sharing." Considerations of how best to achieve the goals of corporate governance (which, of course, are themselves subject to debate and subjective preference) are informed to some degree by a recognition of apparent contraries: "stakeholder" versus "shareholder," "affected party" versus "proprietary party," "policy-implementing" versus "market-supporting," "public responsibility" versus "private ordering," "command and

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1. PM Vasudev & Susan Watson, eds, *Corporate Governance after the Financial Crisis* (Northampton, MA: Edward Elgar, 2012).
2. In her paper "Codes of ethics and corporate governance — a study of New Zealand listed companies," in Vasudev & Watson, *ibid*, 271 at 278, Trish Keeper adopts the Organisation for Economic Co-operation and Developments (OECD) definition of corporate governance: "[It] involves a set of relationships between a company's management, its board, its shareholders and other stakeholders. Corporate governance also provides the structure through which the objectives of the company are set, and the means of attaining those objectives and monitoring performance are determined."
3. PM Vasudev & Susan Watson, "Acknowledgments" in Vasudev & Watson, *ibid*, x.
4. Duncan Kennedy, "Form and Substance in Private Law Adjudication" (1976) 89:8 Harv L Rev 1685. Kennedy states: "I argue that there are two opposed rhetorical modes for dealing with substantive issues, which I will call individualism and altruism. There are also two opposed modes for dealing with questions of the form in which legal solutions to the substantive problems should be cast. One formal mode favors the use of clearly defined, highly administrable, general rules; the other supports the use of equitable standards producing ad hoc decisions with relatively little precedential value" (*ibid* at 1685).

control" versus "sustainable commerce," "long term value" versus "quarter to quarter share price," "shareholder primacy theorists" versus "stakeholder/progressive theorists," and so forth. This is a tension that can be observed continuously by those of us who work as lawyers to corporations that value strong corporate governance and ethical conduct.

It is a dialectic that recurs throughout *Corporate Governance after the Financial Crisis*: the "persistent theme in corporate governance … that corporations perform best when left alone"[5] contrasted with regulation, which, the editors observe in the "Introduction," does not offer "neat solutions" in cases where the market does not motivate desired corporate behaviours.[6] Vasudev and Watson assert that change seemed imminent at the time that the global financial crisis peaked in force: "The tenets that underpinned our economic systems were called into question, and faith in the invisible hand of the market wavered."[7] However, while "change" became a common incantation, problems endured: "[R]egulatory responses that addressed symptoms of the Crisis [did not touch] the underlying malaise."[8] The American *Dodd-Frank Act*,[9] for example, included measures aimed at addressing deficiencies in corporate governance through, among other things, what is grouped as "shareholder empowerment" measures. Ultimately, the book queries whether or not a business environment that placed greater importance on corporate governance would have prevented the financial events of 2008-2009, or at least reduced the severity of their impact.

The first section of the book, entitled "The 'Great Debate,'" considers differing schools of thought within corporate law concerning director duties. Should directors make decisions to promote shareholder benefit alone, or should they take into account the interests of other parties who are affected by those decisions, including employees, consumers, environmental advocates, and society at large? Is shareholder primacy — where the purpose of the corporation is to maximize shareholder wealth above all other purposes — the proper paradigm? Or do other stakeholders have a say, and if so, to what degree and through what mechanism? This is not a settled issue. Rather, it is a question of proclivity that is never firmly set. There is a push and pull between the narrower and wider focus, often imperceptibly, and often driven by societal mores and the state of the economy at a given time. Specific events can precipitate a shift in the balance. In her paper, "New thinking on 'shareholder primacy,'" Lynn A. Stout states that by the 1990s the paradigm firmly (and nearly conclusively) reflected the shareholder primacy view that the goal of corporate governance is to maximize shareholder wealth.[10] She argues, however, that this view has "reached its zenith, and is poised for decline."[11] In Stout's view, despite opinions to the contrary, United States corporate law does not truly evidence a shareholder primacy model. Shareholders themselves have acted in the market in a way that exhibits a preference for "rules that weakened shareholder authority,"[12] and she states that the model itself "might be

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5 PM Vasudev & Susan Watson, "Introduction" in Vasudev & Watson, *supra* note 1, 19.
6 *Ibid* at 20.
7 *Ibid* at 1.
8 *Ibid* .
9 *Dodd–Frank Wall Street Reform and Consumer Protection Act*, Pub L No 111-203, 124 Stat 1376 (2010) [*Dodd–Frank Act*].
10 Lynn A Stout, "New thinking on 'shareholder primacy'" in Vasudev & Watson, *supra* note 1, 25. Stout notes: "Shareholder primacy became widely viewed as the only intellectually respectable theory of corporate purpose" (*ibid* at 26).
11 *Ibid*.
12 *Ibid* at 27.

incoherent" and lacking in logical consistency.[13] Thus, she concludes, shareholder primacy is no longer the dominant mode of thought in corporate governance.

Peter Watts responds directly to Stout. He argues that while there is no legal requirement or fetter placed on corporations to emphasize or downplay profit maximization, profit maximization itself does not equate with shareholder primacy.[14] The real issue, in his view, is whether corporate stakeholders who are not shareholders should have their interests considered in the decision-making process. Citing the New Zealand example, Watts concludes that any attempt to "juridify"[15] these non-shareholder interests, regardless of the level of influence (weak or strong) that shareholders wield over corporate directors, must be avoided. Environmental and labour laws (to cite two examples) are the more efficient means to protect those interests. He notes that "[t]he fact that shareholders might be less powerful in practice, or indeed even impotent (as to which I am skeptical), provides no mandate whatever for conferring rights on stakeholders. The powerlessness of shareholders, should it exist, creates no vacuum that can legitimately be filled by other stakeholders."[16]

Susan Watson's paper considers board power in the United Kingdom, which originates in articles of association rather than statutory enactment. Her paper explores the origin and separation of ownership and control and methods of raising capital (and shielding investors) historically, considering the deed of settlement form, the foundations of the joint stock company, and the ascent of incorporation by registration statutes. Watson concludes that "[w]ith control comes power."[17] That is the reality of the modern corporation and it does not matter whether that power comes from a statute or from the articles of association, it resides in the board.

David Millon's paper, "Enlightened shareholder value, social responsibility and the redefinition of corporate purpose without law," addresses a common point of discussion in many modern corporations.[18] Millon points out that US law mandates neither shareholder primacy nor social responsibility considerations.[19] He argues that long-term considerations, in and of themselves, force corporations to consider the interests of affected stakeholders as a necessary adjunct to the profit motivations of shareholders. For instance, he notes: "[T]he idea that corporations should pursue shareholder wealth with a long-run orientation that seeks sustainable growth and profits based on responsible attention to the full range of relevant stakeholder interests … contrasts with a short-term focus on current share price even when that objective entails immediate or longer-term negative effects on non-shareholders."[20] The former is, in a sense, a recasting of what shareholder wealth actually means. Millon characterizes this as a "third way," an alternative to shareholder primacy and "pluralist"

13 *Ibid* at 28.
14 Peter Watts, "Shareholder primacy in corporate law — a response to Professor Stout," in Vasudev & Watson, *ibid*, 42. Watts notes, "the law makes no assumption that profit-maximization at all costs is what shareholders want" (*ibid* at 43).
15 *Ibid* at 45.
16 *Ibid*.
17 Susan Watson, "Derivation of powers of boards of directors in UK companies" in Vasudev & Watson, *ibid*, 47 at 63.
18 In Vasudev & Watson, *ibid*, 68.
19 For instance, he notes, "US law, in other words, is surprisingly agnostic on the important question of management's primary duty" (*ibid* at 68).
20 *Ibid*.

views of corporate social responsibility that "elevates non-shareholders to the same plane as shareholders."[21] Using case studies, his thesis is that market pressures have the power to move US multinationals away from shareholder primacy, in large part based on risk management emphases. This approach actively considers stakeholder interests with a view to favouring sustainable long-term profits, which serves to build shareholder value while creating "better outcomes for affected constituencies."[22] This does not mean that there is not a role for law, but a space for management to act within its authority to foster long-term success — even if profits are not maximized in the short term — will lead to non-shareholder interests inevitably being considered in building sustainability. Risk management's essential concerns, such as liability, brand value, and reputation, are powerful underlying corporate concerns that necessitate the consideration of non-shareholder interests.

Other papers in the first section of the book include Leonard I. Rotman's "Re-evaluating the basis of corporate governance in the post, post-Enron era," which argues against the "end of history" position taken by certain scholars in 2001, who concluded that the debate between shareholder and stakeholder visions of the corporation was over, and that shareholder primacy was victorious.[23] In fact, Rotman reasons that progressive corporate governance approaches have greater visibility now than they have in some time.[24] Vasudev reviews the results of a survey of New Zealand listed companies to assess the degree to which individual corporate policies reflect the stakeholder principle.[25] The country's corporate legislation allows "entitled persons" to avail themselves of certain corporate law remedies (for example, oppression) and allows companies to designate employees and other stakeholders as "entitled."[26] This is consistent with legal theories that emphasize rights and remedies over "interests."[27] The first part of the book concludes with Aviv Pichhadze's detailed thoughts on the role of institutional investors in corporate governance, particularly their power to influence corporate action.[28]

The second section of the book is entitled "Private Remedy in Corporate Law and its Limits" and contains only one paper. Franklin A. Gevurtz examines the efficacy of private remedies in corporate law to affect corporate decision-making and behaviour, specifically using the *In re Citigroup Inc. Shareholder Derivative Litigation* as a case study.[29] Can courts and legislatures apply corporate law to mitigate the devastating effects of a financial crisis? To what degree is corporate law and its enactors and enforcers (the legislature and the courts

21 *Ibid* at 69.
22 *Ibid* at 70.
23 In Vasudev & Watson, *ibid*, 101.
24 Also see Rotman's interesting discussion of the jurisprudence related to corporate entity theory, with case studies of *Dodge v Ford Motor Co*, 170 NW 668 (Mich Sup Ct 1919) and *Revlon v MacAndrews*, 506 A 2d 173 (Del Sup Ct 1986). Rotman's paper concludes with the strong thesis that shareholder primacy has been "clearly and thoroughly discredited in favor of the entity theory" (Rotman, *ibid* at 115) and that stakeholder interests outside of shareholder interests are highly relevant in determining the best corporate interest.
25 "Corporate Stakeholders in New Zealand — the present, and possibilities for the future" in Vasudev & Watson, *ibid*, 120.
26 *Ibid* at 121.
27 *Ibid* at 122. Stakeholder remedies are discussed at length by Vasudev, with Canada cited as an example of an early-adopter of a system that allows non-shareholder groups (see list in *Canada Business Corporations Act*, RSC 1985, c C-44) as potential remedial actors.
28 "Institutional investors as blockholders" in Vasudev & Watson, *ibid*, 145.
29 "The role of corporate law in preventing a financial crisis — reflections on *In re Citigroup Inc Shareholder Derivative Litigation*," in Vasudev & Watson, *ibid*, 163; *In re Citigroup Inc Shareholder Derivative Litigation*, 964 A 2d 106 (Del Ch 2009) [*Citigroup*].

respectively) "institutionally capable"[30] of reducing the possibility of a financial crisis? What can the law do to address excessive risk taking? Gevurtz identifies legal tools such as regulation, capitalization regulations for financial institutions, adjusting the "asymmetry" that sometimes exists between executive pay and results,[31] imposition of liability for taking unreasonable risks, and management selection. The *Citigroup* case saw shareholders bringing a derivative action against current and former directors and officers of a sizeable financial institution for breach of fiduciary duty because they did not provide proper management of risk, particularly with respect to the subprime mortgage instruments. As one who is exposed to the risk management practices of American-based companies on a daily basis, I found Gevurtz's discussion of Delaware as the jurisdiction of choice for incorporation particularly interesting.

The effect of globalization on corporate governance thinking is dealt with in Part 3, with papers on Taiwanese and Malaysian developments.[32] It is interesting to note, particularly in Taiwan, that the impacts of legislation (and the regulatory approach generally) are circumscribed somewhat by high corporate concentration and family ownership levels. In Taiwan, the concept of independent directors on corporate boards was introduced in 2002 to improve public company governance. This regulatory environment, and the importance of individual family connection and relationships in that country, led to nearly half of the listed companies in Taiwan having at least one independent director by 2011. The author concludes, however, that Taiwan is still in a transition period, in which "new legal measures grind against pre-existing local conditions."[33] Malaysia has also been paying close attention to company law reform, and Aishah Bidin gives the reader some useful historical context. Much of the discussion addresses "corporate rehabilitation"[34] in insolvency-type situations, with comparisons made to Australia, Singapore, and the UK. The Malaysian government is characterized as employing legal tools proactively to effect change with businesses that have not necessarily taken a leadership role.

A section on business ethics and corporate responsibility concludes the book. To say the least, it is not unusual in the corporate world to hear discussions about corporate social responsibility. "Public regulatory encouragement to the adoption of private ordering systems to achieve environmental protection through sustainable commerce"[35] is a stimulating paper about sustainable commerce, which the authors define as "products and practices that minimize environmental impacts and optimize commercial value while realizing both public and private environmental benchmarks."[36] The authors conclude that regulation is required, and it is unrealistic to expect corporations to automatically self-correct. However, sustainable commerce goals (including environmental conservation) can in fact be served through non-regulatory means: the incentive to avoid costly regulatory penalties, civil liability, and the

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30 Gevurtz, *ibid* at 163.

31 He calls it the "'heads-I-win, tails-who-cares' approach" (*ibid* at 173).

32 Yu-Hsin Lin, "How public regulation changes corporate governance practice — corporate board reform in Taiwan" in Vasudev & Watson, *ibid*, 211; Aishah Bidin, "Corporate law reform and corporate governance in Malaysia — responses to globalization" in Vasudev & Watson, *ibid*, 229.

33 Lin, *ibid* at 225.

34 Biden, *supra* note 32 at 229.

35 Peter A Appel & T Rick Irvin, "Public regulatory encouragement to the adoption of private ordering systems to achieve environmental protection through sustainable commerce" in Vasudev & Watson, *ibid*, 251.

36 *Ibid* at 251.

financial cost of waste (he cites 3M Corporation's "Pollution Prevention Pay" program), along with the fiscal value of innovation, are contributors to this shift in thinking. In other words, earnings before interest and taxes (EBIT) can improve through the implementation of environmentally sound practices. However, many corporations do not consider sustainable commerce strategically. Corporations that take a progressive approach will sometimes see "progressive agendas curtailed by the business judgment rule … [which] more often than not insulates corporations that have rejected sustainable commerce measures rather than companies that have pursued these measures too aggressively."[37]

The final article is Trish Keeper's "Codes of ethics and corporate governance — a study of New Zealand listed companies."[38] Keeper examines the historical background of today's emphasis on codes of conduct, which she states began in the mid-1970s, the corporate governance debate itself going as far back as the 1720 "South Sea Bubble."[39] While she notes that "codes of ethics are now generally accepted, if not required, as part of a company's corporate governance processes,"[40] opponents have viewed business ethical pronouncements as "little more than a form of risk management"[41] rather than as a "social contract between corporations and their stakeholders."[42] This area of debate complements the "rules versus standards," and "individualism versus altruism" theme. Keeper notes that one can view corporate ethics from a legal perspective which "emphasizes rules and requires monitoring and penalties to enforce these rules" or take an ethical approach, which "views ethics as a set of principles to guide choices, with the aim of achieving responsible conduct."[43] Values are a prime mover, and corporate culture is the underlying consideration in achieving a corporate practice that reflects the values promoted in codes of conduct and statements of ethics. Keeper states: "An ethical approach views ethics as permeating every part of an organization's business practice and is based on individual and communal values."[44] One would theorize that a real permeation per se will create precedential value from ethical decisions, obviating the need for a predominantly compliance-driven mode of practice.

Some of the papers in *Corporate Governance after the Financial Crisis* will not directly resonate with the reader who is primarily interested in a Canadian perspective. Additionally, the diversity of the selection and their origins as papers presented at a symposium leads to some repetition in content between papers. However, the quality of the scholarship, and the clarity and thoughtfulness of each author's work, make this book a positive addition to the canon. For those readers who are interested in extra-jurisdictional approaches to corporate issues, and the principles of corporate comparative law, this book has plenty to offer. Overall,

37 *Supra* note 35 at 259.
38 *Supra* note 2.
39 *Ibid* at 277.
40 *Ibid* at 276.
41 *Ibid* at 275.
42 *Ibid*. Milton Friedman is quoted in this paper as saying, "[t]here is one and only one social responsibility of business – to use its resources and engage in activities designed to increase its profits so long as it stays within the rules of the game, which is to say, engages in free and open competition, without deception and fraud" (*ibid*).
43 *Ibid* at 279. The ethical approach to corporate governance gets away from a "tick-box or legalistic mentality towards compliance" (*ibid*).
44 *Ibid*.

this is an inviting collection of well-researched papers, full of references for further reading and research. The book examines issues that illuminate basic tensions in governance that exist everywhere that the corporate structure is used as a vehicle to generate wealth through enterprise.

Steven N. Mandziuk, Q.C.
General Counsel, Finning (Canada)
Edmonton, Alberta