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FOR WHOM ARE CORPORATE MANAGERS TRUSTEES?

AN individual who carries on business for himself necessarily enters into business relations with a large number of persons who become either his customers or his creditors. Under a legal system based on private ownership and freedom of contract, he has no duty to conduct his business to any extent for the benefit of such persons; he conducts it solely for his own private gain and owes to those with whom he deals only the duty of carrying out such bargains as he may make with them.

If the owner employs an agent or agents to assist him in carrying on business, the situation is only slightly changed. The enterprise is still conducted for the sole benefit of the owner; the customers and creditors have contract rights against him and not normally against the agent even when the agent is the person who actually transacts business with them. The agent himself shares in the receipts of the enterprise only to the extent provided by his agreement. He, however, on his part owes something more than a contract duty toward his principal. He is a fiduciary who must loyally serve his principal's interests.

Substitute several owners for one and the picture is scarcely altered, except that insofar as the owners take part in the conduct of the enterprise, there is a fiduciary relation between owner and owner, as well as between employee and owner. Incorporate the enterprise, making the owners stockholders and some of them or persons selected by them directors, and — if we adopt the widely

prevalent theory that the corporate entity is a fiction[1] — our picture is substantially unchanged. The business is still a private enterprise existing for the profit of its owners, who are now the stockholders. Its customers and creditors have contract rights, nominally against the corporation but in reality against the stockholders, whose liability is limited to the assets used in the business.[2] The directors and other agents are fiduciaries carrying on the business in the sole interest of the stockholders. These latter have indeed lost much of their *de jure* and, if the enterprise is a large one, perhaps nearly all of their *de facto* control so that they may appear to be more like *cestuis que trust* than like partners. Nevertheless they are not strictly *cestuis que trust,* for it is the association of which they are members and not an individual acting as trustee for them that comes into contract relations with customers and creditors.

Stress the theory of the corporate entity and the picture is altered slightly, but more in form than in substance. The corporation as a distinct legal person is now conceived of as carrying on the business and making the contracts, and the directors and other agents are fiduciaries for it. The sole function of the corporation is, however, conceived to be the making of profit for its stockholder-members,[3] so that they are the ultimate beneficiaries of the business and of the activities of the persons by whom it is carried on.

Subject to this, from a practical standpoint, relatively minor controversy as to the emphasis to be placed upon the corporate entity,[4] it is undoubtedly the traditional view that a corporation

[1] There has been a voluminous amount of legal writing of late years on the corporate personality. Among legal expressions of the view that the corporation is in essence merely an aggregate of its members, see Hohfeld, *The Individual Liability of Stockholders and the Conflict of Laws* (1909) 9 COL. L. REV. 492, (1910) 10 *id.* 283, 520; Radin, *The Endless Problem of Corporate Personality* (1932) 32 *id.* 643. Compare also the tendency today to "disregard the corporate fiction" in a wide variety of situations.

[2] For an analysis of the legal duties of corporations as legal duties of their stockholders, see Hohfeld, *supra* note 1.

[3] For a vigorous assertion of this view, see Dodge v. Ford Motor Co., 204 Mich. 459, 170 N. W. 668 (1919).

[4] The amount of emphasis which should be given to the corporate entity concept is unimportant for our present purpose if we assume that the sole function of the entity is to make profits for the stockholders. If the latter proposition be disputed, the entity concept may then, as indicated below, become important.

is an association of stockholders formed for their private gain and to be managed by its board of directors solely with that end in view. Directors and managers of modern large corporations are granted all sorts of novel powers by present-day corporation statutes and charters, and are free from any substantial supervision by stockholders by reason of the difficulty which the modern stockholder has in discovering what is going on and taking effective measures even if he has discovered it. The fact that managers so empowered not infrequently act as though maximum stockholder profit was not the sole object of managerial activities has led some students of corporate problems, particularly Mr. A. A. Berle, to advocate an increased emphasis on the doctrine that managerial powers are held in trust for stockholders as sole beneficiaries of the corporate enterprise.[5]

The present writer is thoroughly in sympathy with Mr. Berle's efforts to establish a legal control which will more effectually prevent corporate managers from diverting profit into their own pockets from those of stockholders, and agrees with many of the specific rules which the latter deduces from his trusteeship principle.[6] He nevertheless believes that it is undesirable, even with

[5] See Berle, *Corporate Powers as Powers in Trust* (1931) 44 HARV. L. REV. 1049.

[6] That directors are fiduciaries for their corporations is indisputable. That many of their powers, such as the power of declaring or passing dividends and the power of issuing new stock, may affect the individual interests of the stockholders rather than the corporate enterprise as a whole is obvious and has led to a growing tendency to treat directors as fiduciaries for stockholders as well as for the corporate entity. Thus, a stockholder may under some circumstances compel the declaration of a dividend even though the corporate entity would not be injured by the failure to declare. Dodge v. Ford Motor Co., *supra* note 3; *In re* Brantman, 244 Fed. 101 (C. C. A. 2d, 1917). A stockholder may also enjoin the issue of new stock by directors where the purpose of the issue is to change the control of the enterprise, even though the issue may not injure the corporation and even though the stockholder may not under the circumstances have any contractual preëmptive right to have the stock issued to him. Elliott v. Baker, 194 Mass. 518, 80 N. E. 450 (1907); Luther v. C. J. Luther Co., 118 Wis. 112, 94 N. W. 69 (1903); see Dunlay v. Avenue M. Garage & R. R., 253 N. Y. 274, 279, 170 N. E. 917, 919 (1930).

It may be questioned, however, whether some of the problems which Mr. Berle treats as fiduciary problems — *e.g.*, that relating to dividends on non-cumulative preferred stock — are not questions of contract rather than of fiduciary law. *Cf.* Wabash Ry. v. Barclay, 280 U. S. 197 (1930). A further controversy as to the fiduciary duties of management when management is vested not in directors but in a particular group of stockholders is beyond the scope of the present article. See BERLE, STUDIES IN THE LAW OF CORPORATION FINANCE (1928) c. 3. But *cf.* Wood, *The Status of Management Stockholders* (1928) 38 YALE L. J. 57.

the laudable purpose of giving stockholders much-needed protection against self-seeking managers, to give increased emphasis at the present time to the view that business corporations exist for the sole purpose of making profits for their stockholders. He believes that public opinion, which ultimately makes law, has made and is today making substantial strides in the direction of a view of the business corporation as an economic institution which has a social service as well as a profit-making function, that this view has already had some effect upon legal theory, and that it is likely to have a greatly increased effect upon the latter in the near future.

Several hundred years ago, when business enterprises were small affairs involving the activities of men rather than the employment of capital, our law took the position that business [7] is a public profession rather than a purely private matter, and that the business man, far from being free to obtain all the profits which his skill in bargaining might secure for him, owes a legal duty to give adequate service at reasonable rates. Although a growing belief in liberty of contract and in the efficacy of free competition to prevent extortion led to abandonment of this theory for business as a whole, the theory survived as the rule applicable to the carrier and the innkeeper. In recent years we have seen this carrier law expanded to include a variety of businesses classed as public utilities. Under modern conditions the conduct of such businesses normally involves the use of a substantial amount of property. This fact, together with the accidental circumstance that a passage from Lord Hale was quoted in one of the briefs in the leading case of *Munn v. Illinois*,[8] has led to a change in the conventional legal phraseology. Instead of

[7] It has been asserted that the medieval like the modern law drew a distinction between those businesses which were public and those which were private. See 1 WYMAN, PUBLIC SERVICE CORPORATIONS (1911) 5. It is reasonably clear, however, that this view involves reading modern conceptions into the early cases and that what those cases really indicate is that all business publicly carried on was regarded as public in character. See Adler, *Business Jurisprudence* (1914) 28 HARV. L. REV. 135. "The notion of a distinct category of business 'affected with a public interest,' employing property 'devoted to a public use,' rests upon historical error." Brandeis, J., dissenting, in New State Ice Co. v. Liebmann, 52 Sup. Ct. 371, 383 (1932).

[8] See Hamilton, *Affectation With Public Interest* (1930) 39 YALE L. J. 1089, 1095.

talking, as the early judges talked, in terms of the duty of one engaged in business activities toward the public who are his customers, it has become the practice since *Munn v. Illinois* [9] to talk of the public duty of one who has devoted his property to public use, the conception being that property employed in certain kinds of business is devoted to public use while property employed in other kinds of business remains strictly private.

This approach to the problem has been justly criticized as attempting to draw an unreasonably clean-cut distinction between businesses which do not differ substantially, and as furnishing no intelligible criterion by which to distinguish those businesses which are private property from those which are property devoted to public use.[10] The phrase does, however, have the merit of emphasizing the fact that business is permitted and encouraged by the law primarily because it is of service to the community rather than because it is a source of profit to its owners. Accordingly, where it appears that unlimited private profit is incompatible with adequate service, the claim of those engaged therein that the business belongs to them in an unqualified sense and can be pursued in such manner as they choose need not be accepted by the legislature. Despite certain recent conservative decisions such as *Tyson v. Banton*,[11] it may well be that the law is approaching a point of view which will regard all business as affected with a public interest. If certain businesses then continue to be allowed unregulated profits, it will be as a matter of legislative policy because the lawmakers regard the competitive conditions under which such businesses are carried on as making regulation of profits unnecessary, and not because the owners of such enterprises have any constitutional right to have their property treated as private in the sense in which property held merely for personal use is private.

At any rate, there is no doubt that property employed in a business now classed as a public utility is private property only in a qualified sense. Such a utility as an interstate railroad must

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[9] 94 U. S. 113 (1877).

[10] See Hamilton, *supra* note 8; Brandeis, J., in New State Ice Co. v. Liebmann, 52 Sup. Ct. 371, 383 (1932).

[11] 273 U. S. 418 (1927); *cf.* New State Ice Co. v. Liebmann, 52 Sup. Ct. 371 (1932).

render adequate service, expand its facilities when called upon by public authority, charge only reasonable rates, and treat all customers alike even though profitable new business might be secured by making concessions to certain patrons.[12] In addition to such regulations of its rates and services, an interstate railroad is powerless to issue new securities even to its existing stockholders without the consent of an administrative board which is charged with the duty of considering primarily the bearing of such security issue upon the welfare of the traveling or shipping public rather than the desirability of the issue from the standpoint of the stockholders as owners.[13] Furthermore, the relations between such a railroad and its employees are no longer solely a matter of private bargaining but have of recent years been regulated, first by the Adamson Act,[14] a thinly disguised measure for increasing wages, and more recently by an act creating a labor board with power to determine wages in case of a dispute, although without any weapon save an appeal to public opinion for the enforcement of its determinations.[15] Whether these labor regulations be regarded as designed to protect the public against possible interruptions of service due to strikes, or as derived from a partial recognition of the validity of the claims of labor as an integral part of the enterprise to a fair share of the receipts — fairness to be dependent on criteria which, however vague, are not wholly a matter of bargaining strength — it is plain that these regulations, like those previously referred to, involve important limitations on the right of stockholders and managers acting in their interests to treat the enterprise as the private property of the former.

The law applicable to interstate railroads has, moreover, recently broken away from the idea that each business enterprise is a wholly distinct entity owing no obligations to aid in the success of the industry as a whole. The Transportation Act of 1920 as construed by the United States Supreme Court in the *New England Divisions Case* [16] treats the railroads of the country as parts

[12] See 41 STAT. 474, 483 (1920), 49 U. S. C. §§ 1, 6 (1926).

[13] See 41 STAT. 494 (1920), 49 U. S. C. § 20a (1926).

[14] 39 STAT. 721 (1916), 45 U. S. C. § 65 (1926). Held constitutional in Wilson v. New, 243 U. S. 332 (1917).

[15] 41 STAT. 469 (1920), 45 U. S. C. §§ 131–34 (1926).

[16] 261 U. S. 184 (1923). *Cf.* Dayton-Goose Creek Ry. v. United States, 263

of a single system to such an extent as to justify the Interstate Commerce Commission in dividing the joint rates charged by connecting carriers between those carriers in such a way as to increase the resources of the weaker roads by giving them a disproportionately large share of the total.

Although this single system concept has thus far been confined to interstate railroads, the limitations on unqualified pursuit of private profit imposed by the more advanced states on other so-called public utilities such as gas, electric, and telephone companies, are substantially similar to those imposed by federal law upon interstate railroads.[17] Outside the public utility field there is in the present state of the law little or no attempt to curtail private property in the interest of the customer, it being generally assumed that competition furnishes him adequate protection.[18] On the other hand, the inequality of bargaining power between employer and employee — an inequality which the recent rise of the large corporation has greatly accentuated — has resulted in a considerable amount of legislation designed to protect the health and safety, and even to a slight extent the financial rewards, of the employee.[19]

Recent economic events suggest that the day may not be far distant when public opinion will demand a much greater degree of protection to the worker. There is a widespread and growing feeling that industry owes to its employees not merely the negative duties of refraining from overworking or injuring them, but the affirmative duty of providing them so far as possible with economic security. Concentration of control of industry in a relatively few hands [20] has encouraged the belief in the practica-

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U. S. 456 (1924); Fifteen Per Cent Case, 178 I. C. C. 539 (1931). (For modification of the order in that case, see U. S. Daily, Dec. 8, 1931, at 2275.)

[17] See, *e.g.*, N. Y. PUB. SERV. COM. LAW (1910) c. 480.

[18] The United States Supreme Court, as indicated above, takes the position that charges to the consumer can not constitutionally be regulated unless the business is one which in the Court's opinion may properly be regarded as a public utility.

[19] Reasonable health and safety measures such as limitations of hours of service are accepted as proper exercises of the police power. Bunting v. Oregon, 243 U. S. 426 (1917). Minimum wage laws are deemed invalid. Adkins v. Children's Hospital, 261 U. S. 525 (1923). More limited wage regulations such as those compelling payment in cash have been upheld. Knoxville Iron Co. v. Harbison, 183 U. S. 13 (1901).

[20] The extent to which control of American industry is thus concentrated has

bility of methods of economic planning by which such security can be achieved in much greater degree than at present. This belief is no longer confined to radical opponents of the capitalistic system; it has come to be shared by many conservatives who believe that capitalism is worth saving but that it can not permanently survive under modern conditions unless it treats the economic security of the worker as one of its obligations and is intelligently directed so as to attain that object.[21]

It is true that, as many advocates of industrial planning have pointed out, high wages and economic security for workers tend in the main to increase the profits of stockholders, inasmuch as they tend to increase consumption of the things which business corporations produce.[22] It can not, however, be successfully maintained that the sort of industrial planning which may be found desirable to protect the employee is necessarily under all circumstances in line with the interest of the stockholders of each individual corporation. If contemporary discussion of the need for a planned economic order ultimately results in a more stabilized system of production and employment, we may safely predict that this will involve some further modifications of the maximum-profit-for-the-stockholders-of-the-individual-company formula.

It may, however, be forcibly urged that all these and other past, present, and possible future limitations on the pursuit of stockholder profit in no way alter the theory that the sole function of directors and other corporate managers is to seek to obtain the maximum amount of profits for the stockholders as owners of the enterprise. Ownership of a modern railroad may today be hedged about with restrictions which make such ownership considerably less absolute than was the ownership of a cotton mill at the time when economic and legal theories of *laissez faire* were most completely accepted. Ownership in the cotton industry tomorrow may be even more restricted in some ways than is

recently been investigated. See LAIDLER, CONCENTRATION OF CONTROL IN AMERICAN INDUSTRY (1931).

[21] See, *e.g.*, DONHAM, BUSINESS ADRIFT (1931) *passim*; THE SWOPE PLAN (Frederick editor, 1931); Address of Daniel Willard, President of Baltimore & Ohio R. R. in AMERICA FACES THE FUTURE (Beard editor, 1932) 29; Butler, *Unemployment*, *id.* at 141.

[22] *E.g.*, DONHAM, BUSINESS ADRIFT 129–37; THE SWOPE PLAN 20.

ownership in the railroad field today. Regulations imposed in the interest of employees, consumers, or others may increasingly limit the methods which managers of incorporated business enterprises may employ in seeking profits for their stockholders without in any way affecting the proposition that the sole function of such managers is to work for the best interests of the stockholders as their employers or beneficiaries.

If, however, as much recent writing suggests, we are undergoing a substantial change in our public opinion with regard to the obligations of business to the community, it is natural to expect that this change of opinion will have some effect upon the attitude of those who manage business. If, therefore, the managers of modern businesses were also its owners, the development of a public opinion to the effect that business has responsibilities to its employees and its customers would, quite apart from any legal compulsion, tend to affect the conduct of the better type of business man. The principal object of legal compulsion might then be to keep those who failed to catch the new spirit up to the standards which their more enlightened competitors would desire to adopt voluntarily. Business might then become a profession of public service, not primarily because the law had made it such but because a public opinion shared in by business men themselves had brought about a professional attitude.[23]

Our present economic system, under which our more important business enterprises are owned by investors who take no part in carrying them on — absentee owners who in many cases have not even seen the property from which they derive their profits — alters the situation materially. That stockholders who have no contact with business other than to derive dividends from it should become imbued with a professional spirit of public service is hardly thinkable. If incorporated business is to become professionalized, it is to the managers, not to the owners, that we must look for the accomplishment of this result.

If we may believe what some of our business leaders and students of business tell us, there is in fact a growing feeling not only that business has responsibilities to the community but that our corporate managers who control business should voluntarily and without waiting for legal compulsion manage it in such a way as

[23] *Cf.* BRANDEIS, BUSINESS — A PROFESSION (1925).

to fulfill those responsibilities. Thus, even before the present depression had set many business men thinking about the place of business in society, one of our leading business executives, Mr. Owen D. Young, had expressed himself as follows as to his conception of what a business executive's attitude should be:

"If there is one thing a lawyer [24] is taught it is knowledge of trusteeship and the sacredness of that position. Very soon he saw rising a notion that managers were no longer attorneys for stockholders; they were becoming trustees of an institution.

If you will pardon me for being personal, it makes a great difference in my attitude toward my job as an executive officer of the General Electric Company whether I am a trustee of the institution or an attorney for the investor. If I am a trustee, who are the beneficiaries of the trust? To whom do I owe my obligations?

My conception of it is this: That there are three groups of people who have an interest in that institution. One is the group of fifty-odd thousand people who have put their capital in the company, namely, its stockholders. Another is a group of well toward one hundred thousand people who are putting their labor and their lives into the business of the company. The third group is of customers and the general public.

Customers have a right to demand that a concern so large shall not only do its business honestly and properly, but, further, that it shall meet its public obligations and perform its public duties — in a word, vast as it is, that it should be a good citizen.

Now, I conceive my trust first to be to see to it that the capital which is put into this concern is safe, honestly and wisely used, and paid a fair rate of return. Otherwise we cannot get capital. The worker will have no tools.

Second, that the people who put their labor and lives into this concern get fair wages, continuity of employment, and a recognition of their right to their jobs where they have educated themselves to highly skilled and specialized work.

Third, that the customers get a product which is as represented and that the price is such as is consistent with the obligations to the people who put their capital and labor in.

Last, that the public has a concern functioning in the public interest and performing its duties as a great and good citizen should.

I think what is right in business is influenced very largely by the

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[24] Mr. Young practised law for many years before he became a business executive.

growing sense of trusteeship which I have described. One no longer feels the obligation to take from labor for the benefit of capital, nor to take from the public for the benefit of both, but rather to administer wisely and fairly in the interest of all." [25]

More recently Mr. Young's colleague, President Swope of the General Electric Company, has put forward his plan for the stabilization of industry which is based on the idea that "organized industry should take the lead, recognizing its responsibility to its employees, to the public, and to its stockholders — rather than that democratic society should act through its government." [26] That industry as at present organized can take this lead only through the agency of the directors and corporate executives who manage it is obvious and is tacitly assumed by Mr. Swope. As Professor Beard has put it in commenting on the Swope plan, "Mr. Swope spoke as a man of affairs, as president of the General Electric Company. No academic taint condemned his utterance in advance; no suspicion of undue enthusiasm clouded his product. As priest-kings could lay down the law without question in primitive society, so a captain of industry in the United States could propose a new thing without encountering the scoffs of the wise or the jeers of the practical." [27] In his recent study of the situation which confronts American business today, Dean Donham of the Harvard Graduate School of Business Administration has stated the problem as follows: "How can we as business men, within the areas for which we are responsible, best meet the needs of the American people, most nearly approximate supplying their wants, maintain profits, handle problems of unemployment, face the Russian challenge, and at the same time aid Europe and contribute most to or disturb least the cause of international peace?" [28]

Answering this question he says, "The only way to defend capitalism is through leadership which accepts social responsibility and meets the sound needs of the great majority of our

[25] Address of Owen D. Young, January, 1929, quoted in SEARS, THE NEW PLACE OF THE STOCKHOLDER (1929) 209. *Cf.* WORMSER, FRANKENSTEIN, INCORPORATED (1931) c. 8.

[26] THE SWOPE PLAN 22.

[27] AMERICA FACES THE FUTURE 186.

[28] DONHAM, BUSINESS ADRIFT 38.

people. Such leadership will seek to form constructive plans framed not in the interest of capital or capitalism but in the interest of the American people as a whole. . . . The responsibility of capital for leadership is overwhelming. To a large extent in this industrial civilization of ours the potential leadership of the country is concentrated in industry." [29] Dean Donham does not explicitly state that leadership of industry is in the hands of those who do not own it but he is too well-informed an observer of modern business not to be thoroughly aware that such is the case. Assumption of social responsibility by industrial leadership necessarily means assumption of such responsibility by corporate managers.

The view that those who manage our business corporations should concern themselves with the interests of employees, consumers, and the general public, as well as of the stockholders, is thus advanced today by persons whose position in the business world is such as to give them great power of influencing both business opinion and public opinion generally. Little or no attempt seems to have been made, however, to consider how far such an attitude on the part of corporate managers is compatible with the legal duties which they owe the stockholder-owners as the elected representatives of the latter.

No doubt it is to a large extent true that an attempt by business managers to take into consideration the welfare of employees and consumers (and under modern industrial conditions the two classes are largely the same) will in the long run increase the profits of stockholders. As Dean Donham and others have demonstrated, it is the lack of a feeling of security on the part of those who are dependent on employment for their livelihood which is largely responsible for the present under-consumption which has so disastrous an effect upon business profits. If the social responsibility of business means merely a more enlightened view as to the ultimate advantage of the stockholder-owners, then obviously corporate managers may accept such social responsibility without any departure from the traditional view that their function is to seek to obtain the maximum amount of profits for their stockholders.

And yet one need not be unduly credulous to feel that there is

[29] *Id.* at 105–06.

more to this talk of social responsibility on the part of corporation managers than merely a more intelligent appreciation of what tends to the ultimate benefit of their stockholders. Modern large-scale industry has given to the managers of our principal corporations enormous power over the welfare of wage earners and consumers, particularly the former. Power over the lives of others tends to create on the part of those most worthy to exercise it a sense of responsibility. The managers, who along with the subordinate employees are part of the group which is contributing to the success of the enterprise by day-to-day efforts, may easily come to feel as strong a community of interest with their fellow workers as with a group of investors whose only connection with the enterprise is that they or their predecessors in title invested money in it, perhaps in the rather remote past.[30] Moreover, the concept that the managers are merely, in Mr. Young's phrase, "attorneys for the investors" leads to the conclusion that if other classes who are affected by the corporation's activities need protection, that protection must be entrusted to other hands than those of the managers. Desire to retain their present powers accordingly encourages the latter to adopt and disseminate the view that they are guardians of all the interests which the corporation affects and not merely servants of its absentee owners.

Any clash between this point of view and the orthodox theory that the managers are elected by stockholder-owners to serve their interests exclusively has thus far been chiefly potential rather than actual. Judicial willingness — which has increased of late — to allow corporate directors a wide range of discretion as to what policies will best promote the interests of the stockholders, together with managerial disinclination to indulge a sense of social responsibility to a point where it is likely to injure the stockholders, has thus far prevented the issue from being frequently raised in clear-cut fashion in litigation.[31]

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[30] Some of our most successful industrial corporations have for years obtained all the additional capital which they needed out of surplus profits without any further issue of securities. See, *e.g.*, The General Electric Co., MOODY'S MANUAL OF INVESTMENTS, INDUSTRIAL SECURITIES (1931) 971, indicating that the only outstanding bonds of that corporation were issued in 1902 and that no stock has been issued since 1920 except as a stock dividend or split-up.

[31] It was raised in the case of Dodge v. Ford Motor Co., *supra* note 3, in which Mr. Ford's expressions of an intention to share profits with the public through a

Nevertheless there are indications that even today corporation managers not infrequently use corporate funds in ways which suggest a social responsibility rather than an exclusively profit-making viewpoint. Take, for example, the matter of gifts by business corporations to local charities. The orthodox legal attitude toward such gifts is well stated in the following language of Lord Bowen: "Charity has no business to sit at boards of directors *quâ* charity. There is, however, a kind of charitable dealing which is for the interest of those who practise it, and to that extent and in that garb (I admit not a very philanthropic garb) charity may sit at the board, but for no other purpose." [32] Other courts have expressed substantially the same view, which is generally regarded as representing the law on the subject.[33] There is, however, another viewpoint which is undoubtedly becoming widely prevalent with laymen if not with lawyers. Most local charities are designed to carry on relief work which, if not thus carried on, might be undertaken as a public enterprise supported by taxa-

reduction in prices were relied upon as justifying a decree compelling the declaration of a dividend out of the large surplus of the company. Neither the language of the opinion nor the relief granted necessarily involves an unqualified acceptance of the maximum-profit-for-stockholders formula. The opinion states that "a business corporation is organized and carried on primarily for the profit of the stockholders" and that directors cannot lawfully "conduct the affairs of a corporation for the merely incidental benefit of shareholders and for the primary purpose of benefiting others." 204 Mich. at 507, 170 N. W. at 684. Despite testimony of Mr. Ford that he planned to expand the enterprise in the interest of consumers rather than of stockholders, the court was careful so to limit its decree as not to interfere seriously with the expansion program. Its avowed reason for so doing was that expansion might be made profitable despite Mr. Ford's expressed indifference to profit. One may suspect that it was also motivated, consciously or unconsciously, by a reluctance to prevent the growth of a socially important enterprise.

[32] Hutton v. West Cork Ry., 23 Ch. D. 654, 673 (1883). "The law does not say that 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." *Ibid.*

[33] The present tendency is to take a liberal view of what gifts may reasonably be thought by the directors to be for the financial benefit of the corporation. *Cf.* Evans v. Brunner, Mond & Co., 90 L. J. Ch. 294 (1920); Armstrong Cork Co. v. H. A. Meldrum Co., 285 Fed. 58 (W. D. N. Y. 1922). Many of the recent cases on corporate gifts involve the deductibility of the gift from income under the federal income tax act as an "ordinary and necessary expense incurred in carrying on trade or business." Here also the modern cases take a liberal view of what may be to the business advantage of the company. *Cf.* Corning Glass Works v. Lucas, 37 F.(2d) 798 (App. D. C. 1929); American Rolling Mill Co. v. Commissioner of Int. Rev., 41 F.(2d) 314 (C. C. A. 6th, 1930); Forbes Lithograph Mfg. Co. v. White, 42 F.(2d) 287 (D. Mass. 1930).

tion. As recent efforts to relieve unemployment indicate, one community may rely wholly on charitable contributions for what another community may undertake with public funds. Where taxation is the method used, corporate, like individual wealth, contributes. There is a widespread feeling that it should also contribute where the voluntary method is employed. Lists of contributors to such charitable enterprises as community chests and unemployment relief funds indicate that donations by corporations, even by those whose employees are unlikely to share in any great part in the funds, are becoming frequent.[34] Conceivably, a stockholder advantage may result thereby through the creation of good will, but the suggestion that charitable gifts increase the good will of a corporation as a business enterprise assumes that the public no longer whole-heartedly believes in the principle that corporations have no right to be charitable. The view that directors may within limits properly use corporate funds to support charities which are important to the welfare of the community in which the corporation does business probably comes much nearer representing the attitude of public opinion and the present corporate practice than does the traditional language of courts and lawyers. Nor are there wanting signs of the adoption of a more liberal attitude by legislatures [35] and judges.[36]

Such a view is difficult to justify if we insist on thinking of the business corporation as merely an aggregate of stockholders with

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[34] For example, the New York Telephone Company is said to have spent $233,000 for charity during the past three years, including $130,000 for unemployment relief. The New York Public Service Commission has recently ruled that such contributions must be charged against surplus and not to operating expenses. See (1932) 70 NEW REPUBLIC 219.

[35] *Cf.* Tex. Acts 1917, c. 15, §§ 1, 3; construed in James McCord Co. v. Citizens' Hotel Co., 287 S. W. 906 (Tex. Civ. App. 1926); N. Y. Laws 1931, Supp. c. 24, § 33.

[36] "Again, we see no reason why if a railroad company desires to foster, encourage and contribute to a charitable enterprise, or to one designed for the public weal and welfare, it may not do so. Maitland, in 'Collected Essays,' says: 'If the law allows men to form permanently organized groups, those groups will be, for common opinion, right-and-duty bearing units; and if the lawgiver will not openly treat them as such he will misrepresent, or, as the French say, he will "denature" the facts: in other words, he will make a mess and call it law.' We see no reason why a railroad corporation may not, to a reasonable extent, donate funds or services to aid in good works." *Per* Letton, J., in State *ex rel.* Sorensen v. Chicago, B. & Q. R. R., 112 Neb. 248, 255–56, 199 N. W. 534, 537 (1924).

directors and officers chosen by them as their trustees or agents. It is not for a trustee to be public-spirited with his beneficiary's property. But we are not bound to treat the corporation as a mere aggregate of stockholders. The traditional view of our law is that a corporation is a distinct legal entity. Unfortunately, its entity character has been thought of as something conferred upon it by the state which, by a mysterious rite called incorporation, magically produces "*e pluribus unum.*" The present vogue of legal realism breeds dissatisfaction with such legal mysteries and leads to insistence on viewing the corporation as it really is. So viewing it we may, as many do, insist that it is a mere aggregate of stockholders; but there is another way of regarding it which has distinguished adherents. According to this concept any organized group, particularly if its organization is of a permanent character, is a factual unit, "a body which from no fiction of law but from the very nature of things differs from the individuals of whom it is constituted." [37]

If the unity of the corporate body is real, then there is reality and not simply legal fiction in the proposition that the managers of the unit are fiduciaries for it and not merely for its individual members, that they are, in Mr. Young's phrase, trustees for an institution rather than attorneys for the stockholders. As previously stated, this entity approach will not substantially affect our results if we insist that the sole function for the entity is to seek maximum stockholder profit. But need we so assume?

We have seen that the law has already reached the point, particularly in the public utility field, where it compels business enterprises to recognize to some extent the interests of other persons besides their owners. We have seen further that the same trend of public opinion which may in some cases compel such recognition may in other cases encourage and approve it without compelling it. A sense of social responsibility toward employees, consumers, and the general public may thus come to be regarded as the appropriate attitude to be adopted by those who are engaged in business, with the result that those who own their own busi-

[37] DICEY, LAW AND PUBLIC OPINION IN ENGLAND (3d ed. 1920) 165. *Cf.* Laski, *The Personality of Associations* (1916) 29 HARV. L. REV. 404. See also United Mine Workers v. Coronado Coal Co., 259 U. S. 344 (1922); Taff Vale Ry. v. Amalgamated Soc. of Ry. Servants, [1901] A. C. 426.

nesses and are free to do what they like may increasingly adopt such an attitude. Business ethics may thus tend to become in some degree those of a profession rather than of a trade.

Such a development of business ethics which goes beyond the requirements of law and beyond the dictates of enlightened self-interest is impossible in these days when most business is incorporated unless it can touch incorporated business enterprises as well as those conducted by individual owners. As a practical matter, this can happen only if the managers of such corporations have some degree of legal freedom to act upon such an attitude without waiting for the unanimous consent of the stockholders. That the duty of the managers is to employ the funds of the corporate institution which they manage solely for the purposes of their institution is indisputable. That that purpose, both factually and legally, is maximum stockholder profit has commonly been assumed by lawyers. That such is factually the purpose of the stockholders in creating the association may be granted. Nevertheless, the association, once it becomes a going concern, takes its place in a business world with certain ethical standards which appear to be developing in the direction of increased social responsibility. If we think of it as an institution which differs in the nature of things from the individuals who compose it, we may then readily conceive of it as a person, which, like other persons engaged in business, is affected not only by the laws which regulate business but by the attitude of public and business opinion as to the social obligations of business. If business is tending to become a profession, then a corporate person engaged in business is a professional even though its stockholders, who take no active part in the conduct of the business, may not be. Those through whom it acts may therefore employ its funds in a manner appropriate to a person practising a profession and imbued with a sense of social responsibility without thereby being guilty of a breach of trust.

It may well be that any substantial assumption of social responsibility by incorporated business through voluntary action on the part of its managers can not reasonably be expected. Experience may indicate that corporate managers are so closely identified with profit-seeking capital that we must look to other agencies to safeguard the other interests involved, or that the competition of the

socially irresponsible makes it impracticable for the more public-spirited managers to act as they would like to do, or that to expect managers to conduct an institution for the combined benefit of classes whose interests are largely conflicting is to impose upon them an impossible task and to endow them with dangerous powers. The question with which this article is concerned is not whether the voluntary acceptance of social responsibility by corporate managers is workable, but whether experiments in that direction run counter to fundamental principles of the law of business corporations.

The view that they do so rests upon two assumptions: that business is private property, and that the directors of an incorporated business are fiduciaries (directly if we disregard the corporate fiction, indirectly in any case) for the stockholder-owners. The first assumption is being rapidly undermined, so rapidly that decisions like those in *Tyson v. Banton* [38] and *Adkins v. Children's Hospital* [39] can hardly long survive. Business — which is the economic organization of society — is private property only in a qualified sense, and society may properly demand that it be carried on in such a way as to safeguard the interests of those who deal with it either as employees or consumers even if the proprietary rights of its owners are thereby curtailed.

The legal recognition that there are other interests than those of the stockholders to be protected does not, as we have seen, necessarily give corporate managers the right to consider those interests, as it is possible to regard the managers as representatives of the stockholding interest only. Such a view means in practice that there are no human beings who are in a position where they can lawfully accept for incorporated business those social responsibilities which public opinion is coming to expect, and that these responsibilities must be imposed on corporations by legal compulsion. This makes the situation of incorporated business so anomalous that we are justified in demanding clear proof that it is a correct statement of the legal situation.

Clear proof is not forthcoming. Despite many attempts to dissolve the corporation into an aggregate of stockholders, our legal tradition is rather in favor of treating it as an institution directed

[38] 273 U. S. 418 (1927). [39] 261 U. S. 525 (1923).

by persons who are primarily fiduciaries for the institution rather than for its members. That lawyers have commonly assumed that the managers must conduct the institution with single-minded devotion to stockholder profit is true; but the assumption is based upon a particular view of the nature of the institution which we call a business corporation, which concept is in turn based upon a particular view of the nature of business as a purely private enterprise. If we recognize that the attitude of law and public opinion toward business is changing, we may then properly modify our ideas as to the nature of such a business institution as the corporation and hence as to the considerations which may properly influence the conduct of those who direct its activities.

E. Merrick Dodd, Jr.

HARVARD LAW SCHOOL.