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**The Schumpeter Corporation Paradox: Corporations as the Communal Investment**

Mark Warren*

Joseph Schumpeter, in his 1942 book *Capitalism, Socialism and Democracy*, recognised that the insatiable capitalist process was increasingly relying on corporations as the form of business organisation that maximises profits. However, this advance of capitalism, the corporation, was creating a communal vehicle that was diminishing the individual rights and relationships that supposedly distinguish capitalism from socialism. The author labels this the Schumpeter corporation paradox.

This paper considers the modern manifestation of the Schumpeter corporation paradox but places this phenomenon in both its historical and legal context. In terms of history, the early corporations were recognised as closely tied to the state, holding sizable economic and political power that often extended to foreign lands. In terms of law, corporations have always derived their power from the legal rights afforded by the state. In this respect, this paper reminds readers of the historical significance of the corporate form and that the modern manifestations of corporate power are neither unique to our time nor necessarily an indication of capitalist excess. Rather, as highlighted by Schumpeter, the capitalist corporation may still unwittingly serve as a conduit towards social objectives and communal investment that (directly or indirectly) determines the wealth of the population.

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* PhD Candidate (Doctor of Juridical Science) at Central European University, Vienna, Austria.
Email: warren_mark@phd.ceu.edu.
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"*The capitalist process, by substituting a mere parcel of shares for the walls of and the machines in a factory, takes the life out of the idea of property. It loosens the grip that once was so strong – the grip in the sense of the legal right and the actual ability to do as one pleases with one's own; the grip also in the sense that the holder of the title loses the will to fight, economically, physically, politically, for "his" factory and his control over it, to die if necessary on its steps. And this evaporation of what we may term the material substance of property – its visible and touchable reality – affects not only the attitude of holders but also that of the workmen and of the public in general. Dematerialized, defunctionalized and absentee ownership does not impress and call forth moral allegiance as the vital form of property did. Eventually there will be* nobody *left who really cares to stand for it – nobody within and nobody without the precincts of the big concerns.*"

Joseph A. Schumpeter[1]

## 1. Introduction

Joseph Schumpeter, in his 1942 book *Capitalism, Socialism and Democracy* ("*CSD*"), observed that economies operating under capitalism were heading in one direction: towards consolidation. The corporation had become the form of business organisation best placed to maximise profits, as the capitalist process demands. That process leads to corporations undertaking an ever-larger share of commercial activities in the economy and becoming larger institutions. The nature of the corporation, where shareholders own stock and managers run the business, however, detaches economic actors from the tangible nature of property. An investor no longer co-owns a factory building, but rather a claim to a *pro rata* share of whatever profits that their corporation may choose to distribute to its shareholders. There is a recognition of individual property rights that exists when trading in individual assets and contracts. That evaporates once everyone is instead concerned with ownership of a fraction of a dematerialised agglomeration. As capitalism further advances in society, the rise of the corporation turns economic output into a collective endeavour. This is the Schumpeter corporation paradox. The corporation serves capitalism but brings society closer to socialism.

Popular discussion is currently questioning whether the purpose of the corporation is to prioritise shareholders or stakeholders and whether the corporation has a responsibility to help counter environmental and other problems in society. The "ESG" movement has developed in recent years, arguing for corporations and business projects to be selected or rejected for investment due to their (purported) adherence to environmental, social and/or governance principles. There are also accusations raised that corporations have become "too big" or "too powerful". This paper argues that the current discourse overlooks Schumpeter's observations in *CSD* and misconstrues the role of the corporation. The corporation should be viewed in light of its historical purpose and relationship with the state. The growth in the size and role of the corporation in society is also an inevitable outcome of employing the corporate form within a capitalist society. Attention is unduly focused on the wealth-generating impact of corporations on select individuals. Rather, as Schumpeter highlighted, the corporation is a communal institution. Altogether, the answer is not to coerce corporations to ignore their capitalist instincts and employ their discretion towards indeterminate, political

[1] Joseph Alois Schumpeter, *Capitalism, Socialism and Democracy* (3rd [1950] / Harper Perennial Modern Thought [2008], HarperCollins 1942) 142.

policies. It is for society to determine the appropriate boundaries of the corporation. The political process of each society, whether democratic or otherwise, has a means to define public policy – including the regulation of corporate activity within that society. Thereafter, it is then for the state to enforce those boundaries of the profit-maximising corporation within its national borders.

Section 2 of this paper outlines Schumpeter's perception of the role of the corporation in the economy in *CSD* and the inevitable form of the corporation within Schumpeter's framework. Section 3 demonstrates the historical role of the corporation in society and its relationship to the state. Section 4 highlights how modern corporations continue to have a relationship to the state and are dematerialising into representing a single communal investment. Section 5 considers the contemporary promotion of stakeholderism and its compatibility with the role of the corporation. Section 6 outlines an alternative paradigm for viewing the corporation: as a manifestation of state power. Section 7 addresses the likely shortcomings of deferring to the state and the political process to regulate corporations. Section 8 concludes.

## 2. Schumpeter and the Corporation

Schumpeter argues in *CSD* that capitalism cannot survive. This is not because *CSD* is a socialist screed. To the contrary, Schumpeter spends the first part of his book dismantling Marxism and its likelihood of offering "woefully wrong" answers to the questions of the day.[2] Although Schumpeter wrote *CSD* with the threat of the Soviet Union in mind, that does not limit Schumpeter's articulation of how socialism may manifest itself. Rather, Schumpeter sees capitalism as being an eventual victim of its own success. The capitalist process replaced the personal partnership with the impersonal corporation. Capitalism can be expected to continue towards ever greater agglomerations of capital until the public faces a modest final step. Once mega-corporations are representing the collective labour efforts and capital investment of most of the population, it is simple to transition to a central government authority that coordinates society at large.[3] There is no need for a revolution. Capitalism "shapes things and souls for socialism".[4] This is one of many paradoxes of the capitalist process highlighted by Schumpeter in *CSD*. His most famous is the process of "creative destruction": economic progress relies upon incumbent methods, products and markets being persistently driven to obsolescence and supplanted by more productive innovations and more efficient practices.[5] However, this paper focuses on Schumpeter's perception of what the corporation represents and the paradox that the corporate form raises.

Schumpeter recognises that the capitalist process has selected the corporation as its *modus operandi* for economic advancement, which is at the expense of "the small producer and trader".[6] The businessperson as the owner-manager had an added motivation as a person "who knew ownership and its responsibilities".[7] The businessperson as the manager within

[2] ibid 48.
[3] ibid XV. C.f. any "central planning" would still need to rely on prices in the market to coordinate supply and demand; see FA Hayek, 'The Use of Knowledge in Society' (1945) 35 The American Economic Review 519.
[4] Schumpeter (n 1) 220.
[5] ibid VII.
[6] ibid 140.
[7] ibid 156.

the corporation has devolved into "the psychology of the salaried employee working in a bureaucratic organization".[8] Therefore, to Schumpeter, the corporation "socializes the bourgeois mind" away from individual capitalist ambition towards collective economic administration.[9]

Schumpeter observes that the corporation also overturns the orthodoxy of labour. A worker controls their labour and may contract to provide certain services in return for payment. However, the labour contract within the corporation is different. Coase has highlighted how labour is retained under the employment contract and allocated within the firm by the central authority of the "entrepreneur-co-ordinator".[10] A worker signs away control over their labour and "agrees to obey the directions of an entrepreneur *within certain limits*".[11] Schumpeter labels this as the corporation having "already … abolished free contracting in the labor market".[12] Both the worker and the firm opt for this arrangement in place of repeated individual contracting in the marketplace between prospective buyer and willing seller. No matter its benefits for the capitalist process, however, this employment contract represents a "stereotyped, unindividual, impersonal and bureaucratized contract" that has led to corporations amassing "impersonal masses of workmen".[13]

As highlighted in the quote that preludes this paper, Schumpeter does not see the corporation as the harbinger of individualistic capitalism overwhelming society. Schumpeter is keenly aware that, in the corporation, "[i]ndustrial property and management have become depersonalised".[14] The corporation represents individual property and personhood having been subsumed into large, intangible and depersonalised pools of capital that are due to be carved up and distributed among the shareholder population. Berle and Means, the forefathers of analysing the nature of the modern corporation, highlighted that the corporation separates the ownership and control features that were traditionally fused in property rights.[15] Similar to Schumpeter, they feared that "the corporate profit stream" that the shareholder receives "in reality no longer is private property".[16] While the shareholder theoretically retains ownership of a fraction of a given corporation's business and a claim to any dividends declared by the corporation, in reality, without control, the shareholder "has surrendered a set of definite rights for a set of indefinite expectations".[17] This outcome is epitomised by the class of "small stockholders" that Schumpeter complains "often do not care much about" and "hardly ever bother" with the corporation whose stock they possess.[18] The population shares in the

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[8] ibid.

[9] ibid. Berle and Means were sympathetic to the management of the corporation becoming "a purely neutral technocracy, balancing a variety of claims by various groups in the community and assigning to each a portion of the income stream"; see Adolf A Berle and Gardiner C Means, *The Modern Corporation and Private Property* (1st edn, The MacMillan Company 1932) bk IV ch IV.

[10] RH Coase, 'The Nature of the Firm' (1937) 4 Economica 386. Coase's work has been supplemented by the "theory of the firm" field of economics.

[11] ibid 391. C.f. Armen A Alchian and Harold Demsetz, 'Production, Information Costs, and Economic Organization' (1972) 62 The American Economic Review 777, 784; Oliver Hart, 'An Economist's Perspective on the Theory of the Firm' (1989) 89 Columbia Law Review 1757, 1771.

[12] Schumpeter (n 1) 142.

[13] ibid 141.

[14] ibid 219.

[15] Berle and Means (n 9) 118.

[16] ibid 247.

[17] ibid 277.

[18] Schumpeter (n 1) 141.

communal spoils of the economy but is largely disinterested and disempowered as to from where those spoils emanate.[19]

The trajectory of the corporation within Schumpeter's framework is, therefore, apparent. Capitalism remains the governing principle of developed economies for the same economically rational and efficient reasons that have persisted for centuries. The corporation increases its role in the economy. More economic activity shifts from the sole trader and the partnership to within the corporate wrapper. Corporations become ever greater in size, whether due to offering lower prices through efficient production and economies of scale; the successes of creative destruction; the merger of competitors through co-operative acquisitions or hostile takeovers; and/or state aid and other state interference in the market. These corporations represent a greater proportion of the aggregate economic output of a society: they own more assets; they employ more workers. Investment in private enterprise increasingly constitutes purchasing corporate stocks. These corporations, therefore, also represent a greater proportion of the capital invested by society. Yet most of the population lose touch with their capital and how it is employed. Those decisions are left to the discretion of the directors and managers that run these corporations. These communal pools of society's capital become ever more important to the direction of the economy and wider society. The decisions of corporations play a greater role in determining the state of society.

## 3. The Historical Manifestation of the Corporation

Law and economics have been grappling with the question of what is a firm for several decades.[20] Economists such as Coase, Williamson, Alchian and Demsetz observed firms from the bottom up, bonding individuals together in a common entity.[21] Others, such as Jensen and Meckling, concentrated on the principal-agent problems that arise from the separation of ownership and management in the corporation compared to the owner-managed business.[22] Jensen and Meckling presented the firm as simply "the nexus of a set of contracting relationships among individuals".[23] However, Grossman, Hart and Moore recognised the shortcomings of that approach: contracts are "incomplete".[24] Contracts do not and cannot legislate for every potential eventuality. These gaps in contractual rights are governed by ownership of the "residual rights of control".[25]

[19] See also Berle and Means (n 9) 66–67.
[20] See Hart (n 11).
[21] Coase (n 10); Alchian and Demsetz (n 11); Oliver E Williamson, 'The Economics of Organization: The Transaction Cost Approach' (1981) 87 American Journal of Sociology 548.
[22] Michael C Jensen and William H Meckling, 'Theory of the Firm: Managerial Behavior, Agency Costs and Ownership Structure' (1976) 3 Journal of Financial Economics 305. See also Henry G Manne, 'Our Two Corporation Systems: Law and Economics' (1967) 53 Virginia Law Review 259.
[23] Jensen and Meckling (n 22) 311.
[24] Oliver Hart and John Moore, 'Incomplete Contracts and Renegotiation' (1988) 56 Econometrica 755.
[25] Sanford J Grossman and Oliver D Hart, 'The Costs and Benefits of Ownership: A Theory of Vertical and Lateral Integration' (1986) 94 Journal of Political Economy 691; Oliver Hart and John Moore, 'Property Rights and the Nature of the Firm' (1990) 98 Journal of Political Economy 1119. See also Philippe Aghion and Richard Holden, 'Incomplete Contracts and the Theory of the Firm: What Have We Learned over the Past 25 Years?' (2011) 25 The Journal of Economic Perspectives 181.

However, lawyers such as Hansmann, Kraakman and Dari-Mattiacci have shown where economic theory underestimates the importance of the law to the firm.[26] This should not be a surprise when economists concentrate on an abstract concept – the firm – that obfuscates the rigid boundaries that come from a legal entity such as a corporation. Separating the assets, liabilities, rights and obligations of the corporation from its shareholders, managers and employees requires more than a series of contracts.[27] The corporation, therefore, needs more than a private law system in order to exist. Here is where the law, and the property rights that it can bestow on the corporation as a legal person, comes to the fore.[28] The law, as promulgated and enforced by the state, binds an entire population to recognise where the natural person ends and the legal person begins – and divide their assets and liabilities accordingly.[29] Consequently, the corporation only ever represents what the state permits it to represent in a given society.

*Evolution towards the Corporate Form*

The centrality of the state to the existence of the corporation is most apparent in the treatment of the corporate form prior to the 19th century. Corporate personality was a visible exception to the status quo. It would require a specific grant from the state, such as a bespoke statute (charter), to provide for the existence of a corporation. Bodies established to perform a public or quasi-state function could be recognised as a corporeal body that was distinct from (and could outlive) its governing members. Roman law recognised bodies such as municipalities, charitable organisations and public works projects.[30] This continued in Europe in the Middle Ages, including with universities and religious institutions.[31] The earliest examples of corporate bodies in the United States would similarly have a religious, charitable or public purpose.[32]

Separately from the machinations of the state, the exigencies of commerce led to arrangements that facilitated investment towards larger projects that required more capital than any individual could (or would be willing to) invest. The general partnership is typically too precarious for long-term, complex business enterprises.[33] It is terminable at the will of any partner and barely able to shield the firm from the claims of its partners' creditors. The

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[26] See Henry Hansmann and Reinier Kraakman, 'The Essential Role of Organizational Law' (2000) 110 The Yale Law Journal 387; Henry Hansmann, Reinier Kraakman and Richard Squire, 'Law and the Rise of the Firm' (2006) 119 Harvard Law Review 1333; Giuseppe Dari-Mattiacci, 'The Theory of Business Organizations' (5 December 2018) <https://papers.ssrn.com/abstract=3296232> accessed 5 August 2023. See also Edward M Iacobucci and George G Triantis, 'Economic and Legal Boundaries of Firms' (2007) 93 Virginia Law Review 515.
[27] Dari-Mattiacci (n 26) 12–13; Hansmann, Kraakman and Squire (n 26) 1340–1343.
[28] Iacobucci and Triantis (n 26) 518, 569; Hansmann and Kraakman (n 26) 406.
[29] Hansmann and Kraakman (n 26) 392–393. This feature of the corporation is typically described as "affirmative asset partitioning" or "entity shielding".
[30] Barbara Abatino, Giuseppe Dari-Mattiacci and Enrico C Perotti, 'Depersonalization of Business in Ancient Rome' (2011) 31 Oxford Journal of Legal Studies 365, 368.
[31] Timur Kuran, 'The Absence of the Corporation in Islamic Law: Origins and Persistence' (2005) 53 The American Journal of Comparative Law 785, 802; Giuseppe Dari-Mattiacci and others, 'The Emergence of the Corporate Form' (2017) 33 The Journal of Law, Economics, and Organization 193, 204; Carlo Taviani, *The Making of the Modern Corporation: The Casa Di San Giorgio and Its Legacy (1446-1720)* (Routledge 2022) 183.
[32] Margaret M Blair, 'Locking in Capital: What Corporate Law Achieved for Business Organizers in the Nineteenth Century' (2003) 51 UCLA Law Review 387, 423.
[33] ibid 413; Dari-Mattiacci and others (n 31) 201.

common exception is the family firm, as familial ties naturally sustain a long-term partnership.[34] Nonetheless, additional capital for larger business organisations ordinarily requires outside investors and pooling of their capital. Here is where limited partnerships developed to allow the firm and its counterparties to distinguish between those partners that managed the partnership (general partners with full liability) and those who only invested capital (limited partners with limited liability).[35] These practices would eventually develop into the private corporation. In the absence of a charter from the state, others fashioned their own form of corporation: the unchartered joint-stock company. For example in France, the limited partnership with tradable shares (*socièté en commandite par actions*) was formally recognised in the 1807 commercial code (*Code de Commerce*) and came to be utilised to form a joint-stock company when founders failed to receive state authorisation to form a corporation (*socièté anonyme*). This practice ceased once a law change in 1856 diluted the conveniences offered by the *socièté en commandite par actions*.[36]

The limited partnerships formed to finance merchant shipping voyages would develop these principles of limited liability and capital lock-in for passive investors.[37] The funds from investors would be pooled together to finance the voyage. The investors left management of the voyage – and the prospect of an eventual profit from their investment – to the stewardship of the ship captain and their team. The investors would then have to wait for the ship to return, sell its cargo and distribute any profits to the investors *pro rata* to their respective share of the contributed capital. This separation of management from investment justified limited liability for investors. In the intervening period between investment and liquidation, investors could generate funds by instead trading their fractional ownership of the voyage's profits. The limited partnership (*socièté en commandite*) in France was originally provided in the 1673 *Code de Commerce* and was used in port cities for shipping voyages.[38] Such practices persisted into the early 18th century, including in shipping ports in Britain and the US.[39]

The Bank of Saint George (*Casa di San Giorgio*) in Genoa, Italy was created in the 15th century to employ these maritime practices towards the management of the Genoese government debt.[40] The Commune of Genoa could consolidate its debts in a distinct body. Investors could invest in fractional ownership of the returns from financing the Commune's debts.[41] The eventual securities market that developed in corporate stocks and shares are a relatively modern development. Securities trading was originally a market intended for trading in government bonds, whether directly or through such conduits as the *Casa di San*

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[34] See Timothy W Guinnane and Susana Martinez-Rodriguez, 'Choice of Enterprise Form: Spain, 1886-1936' (2018) 34 Journal of Law, Economics, and Organization 1; Cihan Artunc and Timothy W Guinnane, 'Partnership as Experimentation' (2019) 35 Journal of Law, Economics, and Organization 455, 483; Charles E Freedeman, *Joint-Stock Enterprise in France, 1807-1867: From Privileged Company to Modern Corporation* (1st edn, The University of North Carolina Press 1979) 34.

[35] See also Abatino, Dari-Mattiacci and Perotti (n 30). Roman practice recognised the slave and the assets (or business) endowed to the slave from the slave's master (*peculium*) as distinct from the assets of the slave's master and a de facto means of legal personality.

[36] Freedeman (n 34).

[37] Hansmann, Kraakman and Squire (n 26) 1372–1373; Stuart Banner, *Anglo-American Securities Regulation: Cultural and Political Roots, 1690-1860* (Cambridge University Press 2002) 128.

[38] Freedeman (n 34) 7–8.

[39] Banner (n 37) 128.

[40] Taviani (n 31) 24.

[41] ibid 37–38.

*Giorgio*. This institution seemingly served as a model for other states in their management of the public debt during the 17th, 18th and 19th centuries, including the South Sea Company in England,[42] the Mississippi Company in France,[43] the Bank of England[44] and the first Bank of the United States.[45] These later corporations were organised in a form that we perceive today as a private business, including having a corpus of private shareholders as their ultimate owners. The societal shift towards increasingly taxing the landed and productive in society to fund interest owed to the rentier bond investor was contentious in both 18th century England and America.[46] However, the incorporation of these corporations came about to serve the state's interests. Their continued existence was regulated by their company charter, which would require periodic renewal and could always be subject to revision by the state. The state maintained an interest in such corporations serving their public purpose.

*The Early Corporations*

The Dutch East India Company (*Vereenigde Oost-Indische Compagnie*) ("VOC") and the English East India Company ("EIC") are recognised as the first modern corporations. The VOC was chartered in 1602 with its capital committed for ten years. Its charter was amended in 1612 to make its capital permanent, which is commonly recognised as constituting the VOC as the first corporation. The EIC was chartered in 1600, but only made its capital permanent in 1657.[47] These trading companies combined the limited liability practices of shipping voyages with the quasi-state function of bodies such as the *Casa di San Giorgio*. These ostensibly private corporations again served to further public interests, in this case management of conquered and colonised territories and trading routes.[48] The trading companies were sustained by the state awarding monopoly rights to administer the country's activities in a given territory. Whereas no investors in a single voyage would have an economic incentive to engage in long-term investment along trading routes, these monopolies had such an incentive.[49] This began when the VOC opted to lock-in its investor's capital beyond the duration of a single voyage.[50]

It is apparent that during the 17th, 18th and the 19th centuries, a few corporations held tremendous power over the national economy and domestic society in England, some other European countries and eventually also the US. When Adam Smith criticised the corporation in *The Wealth of Nations*, he was concerned with the trading companies and their monopoly powers.[51] Smith complained that the inflated monopoly prices charged by the EIC (and other trading companies) effectively constituted a tax on the English people.[52] This is apparent upon examining the reality of the South Sea Company in England and its eponymous "South

[42] Banner (n 37) 42–45.
[43] Taviani (n 31) 193–200; Banner (n 37) 42–43.
[44] Taviani (n 31) 181–187; Banner (n 37) 64.
[45] Taviani (n 31) 189–190; Banner (n 37) 136–140.
[46] See Banner (n 37) 63–64, 157.
[47] See Dari-Mattiacci and others (n 31) 196–198.
[48] The VOC was also seen as a bulwark against the king of Spain in the event of a Spanish invasion of (the United Provinces of) the Netherlands; see Taviani (n 31) 172–173.
[49] Dari-Mattiacci and others (n 31) 206.
[50] ibid 207.
[51] See Adam Smith, *An Inquiry Into the Nature and Causes of the Wealth of Nations* (Wordsworth Classics [2012], Wordsworth 1776) bk 1 ch 10 pt 2.
[52] ibid bk 5 pt 3 art I.

Sea Bubble" of 1720. The South Sea Company was granted privileges: a monopoly for trading with Spanish colonies in South America, which proved to be worthless. But it was also intended as a vehicle to consolidate government debt.[53] It was in the British Government's interest for the South Sea Company to attract investor capital that could be redeployed to subscribe for government debt. Consequently, the Bubble Act was passed in 1720 to eliminate the unchartered joint-stock companies that were competing with the Company for investor capital.[54] The value of this trading company to current and prospective shareholders was completely predicated on the state's willingness to maintain certain privileges.

The English economy was also subject to the machinations of the Bank of England in regulating the extension of credit. Most importantly, this included the willingness of the Bank to intervene and rescue the banking system whenever crisis occurred. The collapse of Overend Gurney in 1866 is partly blamed on the Bank's willingness to let its competitor in the bill-discounting business go to the wall.[55] The Bank of France (*Banque de France*) similarly had the power to determine the fate of any troubled French bank during the 19th century.[56] However, the Bank of England intervened when there was enough political weight requiring that the Bank deviate from self-interest or self-preservation. Parliament was prepared to periodically suspend the requirement for gold convertibility of Bank banknotes to facilitate Bank pragmatism.[57] London also averted panic following the collapse of Barings bank in 1890 thanks to a guarantee of Barings' liabilities coordinated by the Chancellor of the Exchequer and the governor of the Bank.[58] Schumpeter highlights in *CSD* the fiction of perceiving the Bank of England as a private corporation: it was really "little more than a treasury department".[59] The Bank would not be formally nationalised until 1946.[60]

The corporation in this period was, therefore, a dominant force in society. However, the nature of its activities and the scale of its dominance were both determined by the state. War, trade policy and money are fundamental functions of the state. Despite masquerading as a private investment vehicle, the corporation remained closely tied to the powers of the state.[61] Accordingly, when the governance of India fell within the formal jurisdiction of the British Government in 1858, this move did not represent a sudden expropriation of the EIC. British politics had been debating the relationship between the state, the EIC and India for a century.[62] The EIC's maligned handling of the Indian uprising in 1857 tilted the political equation from corporate administration to state governance.[63] Similarly, following the nationalisation of the VOC in 1796, the quasi-state corporation persisted in the Netherlands in

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[53] Banner (n 37) 42; Charles P Kindleberger, *Manias, Panics, and Crashes: A History of Financial Crises* (1st edn, Basic Books 1978) 85.
[54] Banner (n 37) 76–77; Kindleberger (n 53) 42, 97. The proceedings brought against such unchartered companies under the Bubble Act likely inadvertently burst the bubble instead; see ibid 47, 66.
[55] Timothy L Alborn, *Conceiving Companies: Joint-Stock Politics in Victorian England* (Routledge 1998) 124, 156.
[56] Kindleberger (n 53) 165–167, 176–178; Freedeman (n 34) 74–75.
[57] Alborn (n 55) 57.
[58] ibid 155–157; Kindleberger (n 53) 153–155.
[59] Schumpeter (n 1) 230.
[60] Bank of England Act 1946.
[61] Albert Schrauwers, *Merchant Kings: Corporate Governmentality in the Dutch Colonial Empire, 1815-1870* (e-book edn, Berghahn Books 2021) 13.
[62] Alborn (n 55) 21–24.
[63] ibid 48–49.

the 19th century. Corporations such as the Netherlands Trading Society (*Nederlandsche Handel-Maatschappij*) and the Dutch East Indies Trade Bank (*Nederlandsch-Indische Handelsbank*) maintained colonial trade in the Dutch East Indies.[64] The Dutch also formed a national state apparatus for administering poor relief through corporations, such as the Society of Benevolence (*Maatschappij van Weldadigheid*).[65] The charters for those corporations were granted by the Ministry of Finance on behalf of the Dutch monarch.[66] The king's appointees or a social network of Dutch aristocracy dominated corporate boards and coordinated activities within this web of corporations in furtherance of state policy.[67]

*Public Utility or Private Enterprise*

By the time that John Stuart Mill discussed the corporation in his *Principles of Political Economy*, he recognised that the corporation was represented by a broad range of joint-stock companies, unlike in Smith's day.[68] Nonetheless, the growth of the joint-stock company in the 18th and 19th centuries failed to remove the role of the state in the existence and function of the corporation. Until the advent of general incorporation laws, the state remained the adjudicator as to what businesses merited corporate status. Corporations were initially focused on those industries that most required a large amount of capital to be raised, such as banks, insurers, railroads, utilities and manufacturers.[69] The *Conseil d'Etat* was primarily responsible for determining authorisation of corporate charters in France and sought to limit the corporation (*sociètè anonyme*) to those business that offered a "public utility" until 1867.[70] A committee of the French legislature (the Chamber of Deputies or *Chambre des députés*) would similarly remark in 1838 that the purpose of the *sociètè anonyme* was "above all suited to large enterprises of public utility … [where] it would be difficult to find a man rich enough to offer a serious pecuniary liability and bold enough to undertake it".[71] These industries were removed from the apparent quasi-state functions of the early corporations. However, once incorporated, the corporations had to remain politically sensitive to the state. There remained the risk of a political backlash to any corporate policy, given the importance of these businesses to a large section of society.[72]

One of the most pertinent examples is banks. The maturity transformation function of banks – borrowing short-term (by letting depositors withdraw money on demand) while lending long-term – leads to periodic bouts of instability.[73] Banks require a lender of last resort – typically the government or a central bank – to intervene when banks face a liquidity crunch: when banks have financial assets but lack cash.[74] The Scottish joint-stock banks of the late 18th century were originally an outlier – praised by Adam Smith for their collective

[64] Schrauwers (n 61) 289, 335–338.
[65] ibid 89–90, 93–94, 398–399.
[66] ibid 32-33. 348.
[67] ibid 32–33, 41, 293, 334–335, 362–363, 370–373.
[68] John Stuart Mill, *The Principles of Political Economy with Some of Their Applications to Social Philosophy (Books I-II)* ([1965], University of Toronto Press 1848) ch IX §2.
[69] Banner (n 37) 129–131, 191–193; Alborn (n 55) 79–82; Freedeman (n 34) 24–34.
[70] Freedeman (n 34) 35–37.
[71] ibid 61.
[72] Alborn (n 55) 4; David Millon, 'Theories of the Corporation' (1990) 1990 Duke Law Journal 201, 207; Freedeman (n 34) 21–22.
[73] Douglas W Diamond and Philip H Dybvig, 'Bank Runs, Deposit Insurance, and Liquidity' (1983) 91 Journal of Political Economy 401. See also Kindleberger (n 53) 19–20.
[74] Kindleberger (n 53) ch 9.

self-sufficiency.[75] English provincial joint-stock banks in the 1830s initially emphasised the collective nature of banking to encourage customers to leave their money with the bank: customers would issue bills of exchange to the bank (being debtors), hold banknotes issued by the bank (being creditors) and hold bank shares (being shareholders).[76] However, this pact broke down, particularly once English banks shifted from a banknote system to a deposit system in the 1870s.[77] Scottish banks fell victim to the same incentives as the English banks during the course of the 19th century, embracing deposit banking and extending credit outside of the Scottish economy.[78] With the state standing behind the banking system, this inevitably required the state to govern the nature of the banking corporation. This included concern as to who owned shares in the banks and the relationship between the bankers and their public shareholders. The *Conseil d'Etat* in France rejected granting a charter for a proposed investment bank in 1825, the *Société Commanditaire de l'Industrie*, partly due to its proposed size and the presence of foreigners among its founders.[79] The Joint Stock Bank Act 1844 in England came in response to the joint-stock bank "mania" of the 1830s and a desire to constrain the role of shareholders in directing bank management.[80]

In addition, the ability of banks to create money in the economy plays a key role in providing credit to businesses.[81] Unsurprisingly, the government historically maintained an active interest in where this money was being supplied. In France, this role of the state in credit allocation was more apparent. The state's control over the authorisation of new *sociètès anonymes* was utilised in 1852 to form investment banks that could steer the direction of French economic development: the *Crédit Foncier de France* and the *Société Générale de Crédit Mobilier* to finance the agricultural sector and the railways respectively.[82]

Similarly, the plans of private entrepreneurs for development of the railway system were subject to state acquiescence. Construction by railway companies was dependent on the state to overcome holdouts by calcitrant landowners and claim the necessary private land across the country.[83] In France, the government and the legislature first had to be satisfied in the 1830s and 1840s as to the form that construction and its financing should take place before state policy was then enforced when authorising (or not) proposed railway *sociètès anonymes*.[84] The parliamentary process and pre-conditions attached to chartering of English railway joint-stock companies were likewise onerous and took months or years to satisfy.[85] The Dutch were dissatisfied with their early travails with the English model and "private" railway enterprises in the 1830s.[86] The coordinating force of investment banks in the French model would take hold in the 1860s, beginning with the General Society for Trade and

[75] Alborn (n 55) 88–91.
[76] ibid 89, 104.
[77] ibid 116–118.
[78] ibid 133.
[79] Freedeman (n 34) 32–33.
[80] Alborn (n 55) 108–114.
[81] Michael McLeay, Amar Radia and Ryland Thomas, 'Money Creation in the Modern Economy' (Bank of England 2014) 2014 Q1 <https://www.bankofengland.co.uk/-/media/boe/files/quarterly-bulletin/2014/money-creation-in-the-modern-economy.pdf?la=en>.
[82] Freedeman (n 34) 84–85; Schrauwers (n 61) 306–307.
[83] E.g. in England, see Alborn (n 55) 81. E.g. in France, see Freedeman (n 34) 67.
[84] Freedeman (n 34) 66–70.
[85] Alborn (n 55) 188.
[86] Schrauwers (n 61) 354–355.

Industry (*Algemeene Maatschappij voor Handel en Nijverheid*) and followed by the Society for Exploitation of the State Railways (*Maatschappij tot Exploitatie van Staatsspoorwegen*).[87]

As the railways assumed greater importance in the industrialisation of the economy, its customers and employees made railways a politically sensitive topic that could not be left to private enterprise and market forces. In England, the Railway Regulation Act 1840, which introduced the Railway Department of the Board of Trade, and the Railway Act 1844, which set minimum service requirements for railways, highlighted the state quickly assuming a supervisory role over the nation's railways.[88] Although a given railway company could be allowed to fail, the importance of the railways made the industry as a whole too big to fail. This saw the British Government prepared to save English railway joint-stock companies from an impending wall of maturing debt in 1866. In response, English railway companies were permitted from 1867 to issue their own equivalent to government Consols (perpetual bonds), perpetual mortgage debt.[89] Similarly, most bonds issued by railway corporations in France had a government guarantee for payment of interest (though not principal).[90]

*The Proliferation of Stocks and Shares*

Besides the role of the state, a further prerequisite to the corporation is the presence of a market for trading shares.[91] Share capital is permanent. A shareholder can typically only recover their capital by selling their stock to somebody else in the secondary market.[92] The initial investors in the corporation (i.e. the primary market), therefore, are only willing to invest because of the presence of a secondary market. This has left the corporation in a symbiotic relationship with the financial world from the outset.

There were always those willing to create investment (or speculative) products from securities such as corporate stocks and shares. London "stock-jobbers" in 1694 were already trading options ("refuses" and "puts") and futures ("time bargains"), including financially-settled trades that involved no transfer of the underlying stock.[93] The US copied these trading techniques in the early days of their stock trading in the 1790s.[94] Trading in Paris in the 1780s similarly included buying on margin and trading futures.[95] These investment products also offered investors greater liquidity in the stock market. This, in turn, aided issuing corporations to find willing subscribers for their stock. Yet the "stock-jobber" on Exchange Alley in London or *Rue de Quincampoix* in Paris was initially considered a rogue. They created new means for speculation that detached stock ownership from the theoretical objective: long-term investment in a worthwhile business project. This same profession would eventually come to be the venerable "investment banker" on Wall Street in New York.

[87] ibid 331–335.
[88] Alborn (n 55) 184.
[89] ibid 215.
[90] Freedeman (n 34) 83.
[91] Dari-Mattiacci and others (n 31) 208.
[92] Berle and Means (n 9) 282.
[93] Banner (n 37) 28–29.
[94] ibid 142–143.
[95] Freedeman (n 34) 9.

These investment bankers became keen to distinguish themselves from the rogues in the stock markets, creating bodies such as the Investment Bankers Association in 1912.[96]

The use of the corporate form expanded in the late 19th century and into the 20th century. The corporation was no longer a special case due to the availability of general incorporation laws.[97] The nature of the industries represented by corporations were less concentrated in areas of state interest and democratic concern. By the 1930s, Berle and Means noted that the average American "come[s] in contact with [corporations] almost constantly", whether as shareholder, employee or customer.[98] Here is the basis for Schumpeter's observations in *CSD* on the growing dominance of the corporate form over the partnership form. This occurred alongside the maturation and mainstreaming of the stock markets. These changes encouraged the perception of the modern corporation as a vehicle for private enterprise rather than a function of the state.[99]

## 4. The Modern Corporation and the Communal Investment

Berle and Means recognised in 1932 that corporations hold "a concentration of economic power which can compete on equal terms with the modern state".[100] They have proved to be correct. The multinational corporation transcends national borders in search of convenient legal (and tax) treatment. Certain technology companies hoard vast amounts of personal data that are carried across global social networks and advertising platforms. The world's largest corporations generate revenue that exceeds the budget revenue of most nations.[101] Many banks have assets that exceed the annual economic output (GDP) of their host country.[102] A bank bailout can, therefore, trigger a "sovereign-bank doom loop" that potentially bankrupts a country.[103] Meanwhile, leaders of the world's largest corporations now have access to the halls of power in a manner that can match presidents and prime ministers.[104]

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[96] Jonathan R Macey and Geoffrey P Miller, 'Origin of the Blue Sky Laws' (1991) 70 Texas Law Review 347, 370, 395.
[97] E.g. general incorporation laws were passed in England (1856), France (1867), Spain (1869), Prussian-led Germany (1870), Belgium (1873) and Italy (1883); see Freedeman (n 34) 144.
[98] Berle and Means (n 9) 24–25.
[99] Millon (n 78) 216.
[100] Berle and Means (n 9) 357.
[101] Global Justice Now, '69 of the Richest 100 Entities on the Planet Are Corporations, Not Governments, Figures Show' (17 October 2018) <https://www.globaljustice.org.uk/news/69-richest-100-entities-planet-are-corporations-not-governments-figures-show/> accessed 11 August 2023.
[102] E.g. UBS, following its merger with Credit Suisse this year, represents about 230% of Switzerland's GDP; see FitchRatings, 'Credit Suisse Rescue Supported by Switzerland's Fiscal Space' (*Fitch Wire*, 27 March 2023) <https://www.fitchratings.com/research/sovereigns/credit-suisse-rescue-supported-by-switzerlands-fiscal-space-27-03-2023> accessed 11 August 2023.
[103] See the Committee on the Global Financial System, 'The Impact of Sovereign Credit Risk on Bank Funding Conditions' (Bank for International Settlements 2011) <https://www.bis.org/publ/cgfs43.pdf>.
[104] See e.g. KPMG, 'The CEO as Chief Geopolitical Officer' (2019) 6 <https://assets.kpmg.com/content/dam/kpmg/xx/pdf/2018/03/the-ceo-as-chief-geopolitical-officer.pdf>. See also e.g. Seema Mody, 'Apple's Tim Cook Calls India "Huge Opportunity" after Tech Meeting at White House with Prime Minister Modi' *CNBC* (23 June 2023) <https://www.cnbc.com/2023/06/23/apples-tim-cook-and-tech-execs-meet-indian-prime-minister-modi-.html> accessed 11 August 2023.
CEOs also consider running for the highest political offices. For example, Jamie Dimon, CEO of JPMorgan Chase, has entertained running for US President; see Hugh Son, 'Jamie Dimon, America's Top Banker, Has "No Plans" to Run for Office' *CNBC* (5 June 2023) <https://www.cnbc.com/2023/06/05/jpmorgan-chase-ceo-jamie-dimon-no-plans-to-run-for-office.html> accessed 11 August 2023.

With that size, today there are concerns that corporations control too much of the economy and have an oversized impact on society.[105] There are grounds for such concerns. Six publicly-listed corporations in the world currently have a market valuation above $1 trillion.[106] About 24% of the S&P 500 index of the 500 leading US-listed corporations is represented by just five of these corporations.[107] There are accusations that corporate pricing power has driven the post-COVID 19 surge in inflation in Europe and the US.[108] There has been an attempted shift in antitrust enforcement against some of these corporations, due to fears that antitrust policy has allowed corporations to become too large in recent decades.[109]

The image of the private corporation forged in the early 20th century has obscured the role of the state in underpinning the corporation (other than in the case of state-owned corporations). Some corporations are perceived as more significant than others, but each remains conceptually detached from the functions of the state. Socialism is then the only means for the state to intervene in the functioning of the corporation. Mixed-economy capitalism in developed countries limits the state to public services, general regulation and taxation, while otherwise leaving business enterprise to the private sector. Through this lens, corporate power is portrayed as a novel concern with which the modern economy and government regulation must now grapple. But such concerns both validate and overlook Schumpeter's prognosis in *CSD*. They also overlook the continuing communal nature of the modern corporation.

*A Bundle of Projects*

The concept of the corporation has also been fragmented due to the evolution of the limited liability company. The public corporation faces additional burdens due to its shares being intended to be listed on the stock market for public trading. The private limited liability company is intended for its shares to be closely held and only occasionally (and privately) transferred. The limited liability company, therefore, has much of the trappings of the traditional corporation but can be incorporated after only a few legal formalities.[110] The prevalence of the corporate form for modern commerce is due to small and medium

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[105] See e.g. 'Is Big Business Really Getting Too Big?' [2023] *The Economist* <https://www.economist.com/business/2023/07/12/is-big-business-really-getting-too-big> accessed 29 August 2023.
[106] Apple ($2.8tn), Microsoft ($2.4tn), Saudi Aramco ($2.2tn), Alphabet ($1.6tn), Amazon ($1.4tn) and Nvidia ($1tn), as of August 2023. See Derek Saul, 'Nvidia Hits $1 Trillion Market Value' [2023] *Forbes* <https://www.forbes.com/sites/dereksaul/2023/05/30/nvidia-hits-1-trillion-market-value/> accessed 14 August 2023.
[107] Apple (7.7%), Microsoft (6.8%), Alphabet (3.6%), Amazon (3.1%) and Nvidia (2.8%), as of August 2023. See Vanguard, 'VOO - Vanguard S&P 500 ETF' <https://investor.vanguard.com/investment-products/etfs/profile/voo> accessed 14 August 2023.
[108] See e.g. 'Are Greedy Corporations Causing Inflation?' [2023] *The Economist* <https://www.economist.com/finance-and-economics/2023/04/30/are-greedy-corporations-causing-inflation> accessed 14 August 2023.
[109] See Federal Trade Commission, 'Memo from Chair Lina M. Khan to Commission Staff and Commissioners Regarding the Vision and Priorities for the FTC' <https://www.ftc.gov/system/files/documents/public_statements/1596664/agency_priorities_memo_from_chair_lina_m_khan_9-22-21.pdf> accessed 14 August 2023. See also Lina M Khan, 'Amazon's Antitrust Paradox' (2016) 126 Yale Law Journal 710; Lina M Khan, 'The Ideological Roots of America's Market Power Problem' (2017) 127 Yale Law Journal Forum 960.
[110] Manne (n 22) 277.

enterprises assuming the form of the limited liability company.[111] The availability of the limited liability company has also spawned the "wholly-owned subsidiary" and the "special purpose vehicle" (SPV).

Just as the economists are wont to do, popular discourse refers to a firm or a brand when it elicits warnings of corporate size and power. However, there is no longer a single corporation under scrutiny in such circumstances. These individual limited liability companies are compiled as building blocks towards a network of affiliated companies, the corporate group. It is headed by a parent corporation listed on the stock market (or held in private hands), but accompanied by a web of subsidiary limited liability companies. The limited liability inherent in each individual limited liability company can be exploited. These subsidiaries carve up the assets and liabilities of the firm between the boundaries imposed by law between each constituent company of the corporate group. This can ringfence liabilities away from valuable assets. This can also transfer assets with the execution of a stock transfer form rather than a cumbersome asset conveyance or assignment of contractual rights.[112] The corporate group is also frequently a multinational firm, with business activities operating in many countries and subsidiaries incorporated in different countries. Falling barriers to trade amid the globalisation era and technological advances in the age of the internet have facilitated the growth of the corporation.[113] The impact of technology is merely a Coasian outcome of lower transaction costs in intra-firm coordination leading to the growth of the size of firms, corporations included.[114]

The outcome is that investing in the stock of a publicly-traded corporation is now typically an investment in a collection of businesses. Such a corporation divides its financial reporting between business segments and possesses a portfolio of brands, business lines and equity investments. This corporation is not usually presented as a conglomerate, however. Rather, the corporation incrementally extends its brand into new products, makes bolt-on acquisitions and invests in start-up projects that fly under-the-radar of most people. Such publicly-traded corporations are no longer centred on a specific line of business but an ever-expanding cross-section of the economy. For example, Amazon is no longer merely an online retailer, but also represents a range of businesses as it describes itself as "seek[ing] to be Earth's most customer-centric company".[115] Apple similarly has reached beyond consumer electronic devices and software to extend itself into consumer finance. Apple now offers

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[111] See Timothy Guinnane and others, 'Putting the Corporation in Its Place' (2007) 8 Enterprise & Society 687; Guinnane and Martinez-Rodriguez (n 34).

[112] See Kenneth Ayotte and Henry Hansmann, 'Legal Entities as Transferable Bundles of Contracts' (2013) 111 Michigan Law Review 715; Douglas G Baird and Anthony J Casey, 'No Exit? Withdrawal Rights and the Law of Corporate Reorganizations' (2013) 113 Columbia Law Review 1; Richard A Posner, 'The Rights of Creditors of Affiliated Corporations' (1976) 43 The University of Chicago Law Review 499, 510–513. Cf. Richard Squire, 'Strategic Liability in the Corporate Group' (2011) 78 University of Chicago Law Review 605.

[113] 'Is Big Business Really Getting Too Big?' (n 125).

[114] Coase (n 10) 397.

[115] Amazon, 'Form 10-K - Amazon.Com, Inc. (2022 Annual Report)' 3 <https://s2.q4cdn.com/299287126/files/doc_financials/2023/ar/Amazon-2022-Annual-Report.pdf> accessed 14 August 2023.

These other businesses include electronic devices (Kindle, Fire, Alexa, Ring), retail products (Amazon Basics), supermarkets (Whole Foods Market), cloud computing storage (Amazon Web Services), satellite-based internet service (Kuiper), TV streaming (Amazon Prime), film / TV production (Amazon Studios, MGM Studios), online streaming (Twitch), pharmacies (Amazon Pharmacy) and primary health care (One Medical).

savings accounts, credit cards and "buy now, pay later" payment services.[116] General Electric made a similar foray into financial services in the 1990s and found itself disposing of most of its GE Capital arm after the "Great Financial Crisis" in 2007-2009.[117] GE Capital was among the initial non-bank financial companies designated as a "systematically important financial institution" by the Financial Stability Oversight Council in 2013 following the financial reforms in the Dodd-Frank Wall Street Reform and Consumer Protection Act 2010.[118] This is emblematic of the enormity of General Electric's presence in the financial sector by 2007, something that would have once been unimaginable.

This bundle of projects falls under the overall stewardship of the directors and officers of the parent corporation. Financial statements are reported on a consolidated basis that treat the corporate group as though it is one entity. It is only upon legal jeopardy that the legal boundaries within the corporate group are erected in the minds of the investor. The firm may be incentivised to develop an elaborate corporate group to obscure risks that can be hidden (at least from some of its investors and creditors) in the crevices of its legal structure. Lehman Brothers offers a telling example of the legal limitations of an economy wishing to be built on only recognising the corporate group. Lehman was the investment bank that was the harbinger for the depths of the Great Financial Crisis. At the time of demise, Lehman was awash in intra-firm transactions that traded and lent assets between group companies to facilitate its financial engineering. These only proved problematic once Lehman filed for bankruptcy in September 2008. Separate bankruptcy proceedings took place in the US for its parent, Lehman Brothers Holdings Inc., and its broker-dealer entity, Lehman Brothers Inc.;[119] in England for its main European subsidiary, Lehman Brothers International (Europe);[120] and in further jurisdictions. Among the litany of legal disputes that arose was who was entitled to the assets of the "Lehman group". Lehman creditors miscalculated their counterparty risk, measuring credit default risk against the Lehman name rather than the specific Lehman group company. Assets no longer simply belonged to a firm but had to belong to a given group company and be liquidated to repay the creditors of that group company. The allocation of an asset to one group company would come at the expense of another group company (and its set of creditors). Conflicts of law arose between how the US courts and the English courts

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[116] Apple, 'Form 10-K - Apple Inc. (2022 Annual Report)' 2, 20 <https://d18rn0p25nwr6d.cloudfront.net/CIK-0000320193/b4266e40-1de6-4a34-9dfb-8632b8bd57e0.pdf> accessed 14 August 2023.
Although the credit cards and savings accounts have been provided through banking partners, such as Goldman Sachs, Apple will bear the financial risk for its buy now, pay later service. See Tim Bradshaw and others, 'Apple Sidelines Goldman Sachs and Goes In-House for Lending Service' *Financial Times* (9 June 2022) <https://www.ft.com/content/fc4eeb5c-479a-4daf-9f8b-808ee937530f> accessed 14 August 2023.

[117] GE Capital represented 37% of GE's earnings in 1990-1999 and 41% in 2000-2015; see General Electric, 'Form 10-K - General Electric Company (2015 Annual Report)' 2 <https://www.ge.com/sites/default/files/GE_AR15.pdf>.
GE announced in 2015 that it would sell around $200 billion of GE Capital's assets by the end of 2016; see General Electric, 'GE Capital Nears $100 Billion in Asset Sales As GE Transforms' (*GE News*, 5 October 2015) <https://www.ge.com/news/reports/ge-transforms-ge-capital-nears-100-billion-asset-sales> accessed 14 August 2023; General Electric, 'GE 2015 Annual Report' 5.

[118] This designation was rescinded in 2016 following divestitures as part of the wind-down of GE Capital. See U.S. Department of the Treasury, 'Designations' (*Policy Issues*) <https://home.treasury.gov/policy-issues/financial-markets-financial-institutions-and-fiscal-service/fsoc/designations> accessed 14 August 2023.

[119] *In re Lehman Brothers Holdings Inc, et al* United States Bankruptcy Court, Southern District of New York Case No. 08-13555 (JMP); *In re Lehman Brothers Inc* United States Bankruptcy Court, Southern District of New York Case No. 08-01420 (SCC) SIPA.

[120] *In the Matter of Lehman Brothers International (Europe) (In Administration)* High Court of Justice, England and Wales Case No. 7942 of 2008.

perceived the same contractual arrangement.[121] Hence the global Lehman group was not superior to the requirements of company law, bankruptcy law and property law in the jurisdiction of incorporation of each Lehman group company. The assets and liabilities of the corporate group were pulled back into the legal reality that the state determines the rules governing each individual company incorporated within its jurisdiction.

*The Rise of Fund Investing*

The communal investment nature of the modern corporation is not, however, limited to a choice between each corporate stock available. The financial world recognised the benefits of "portfolio diversification" and investment in the "market portfolio" through the work of Markowitz and Sharpe in the 1950s and 1960s.[122] This strategy has been adopted by the average retail investor. There is the actively-managed mutual fund, where the (purportedly expert) fund manager pools together their clients' money and invests in the manager's predicted highest-yielding investments. There is also the exchange traded fund ("ETF"), where investors can passively invest to track the financial performance of their desired "market index" of stocks, bonds or other financial assets through a single stock. The average investor can now purchase an ETF that represents the S&P 500 in one stock: about 500 of the leading US-listed corporations, held in proportion to their percentage of the aggregate market capitalisation of the S&P 500 companies. Similar "index funds" now pervade the investment world. The ETF owner does not vote on management of the underlying corporations. Each merely collects their dividends and determines when to sell their ETF stock back on the secondary market for a capital gain or loss. Publicly-listed corporations then have a material proportion of their shareholders passive and apathetic to their activities. There is no exit or voice for corporate executives to countenance, and shareholder loyalty is not to the corporation but to their market portfolio.[123]

There is a growing prevalence of investors having common shareholdings across entire industries that comes from such portfolio diversification strategies. Four asset managers – Blackrock, Vanguard, State Street and Fidelity – control about 20-25% of US market capitalisation.[124] The presence of communal investment potentially alters the incentives faced by corporate executives. If rival corporations coordinate rather than compete, some of these corporations may fail to maximise their own profits but diversified shareholders stand to maximise their aggregate returns across their investment portfolio.[125] Schumpeter similarly envisioned in *CSD* that various industries provided by private corporations could conceivably see a gain from central rationalisation in lieu of overlapping

[121] *Belmont Park Investments Pty Ltd v BNY Corporate Trustee Services Ltd* (2011) [2011] UKSC 38 (UK Supreme Court); *In re Lehman Bros Holdings Inc, et al* [2010] United States Bankruptcy Court, Southern District of New York Case No. 08-13555 (JMP), Adversary No. 09-01242 (JMP), 422 BR 407.
[122] See Harry Markowitz, 'Portfolio Selection' (1952) 7 The Journal of Finance 77; William F Sharpe, 'Capital Asset Prices: A Theory of Market Equilibrium under Conditions of Risk' (1964) 19 The Journal of Finance 425.
[123] Cf. Albert O Hirschman, *Exit, Voice and Loyalty: Responses to Decline in Firms, Organisations and States* (Harvard University Press 1970).
[124] 'John Coates on *The Problem of Twelve: When a Few Financial Institutions Control Everything*' <https://macromusings.libsyn.com/john-coates-on-the-problem-of-twelve-when-a-few-financial-institutions-control-everything> accessed 27 September 2023.
[125] José Azar, Martin C Schmalz and Isabel Tecu, 'Anticompetitive Effects of Common Ownership' (2018) 73 The Journal of Finance 1513, 1521; Anna Tzanaki, 'Varieties and Mechanisms of Common Ownership: A Calibration Exercise for Competition Policy' (2022) 18 Journal of Competition Law & Economics 168, 186.

competitors.[126] However, the contemporary theory of "common ownership" encounters ostensibly independent, competing corporations. Common ownership remains an unsubstantiated theory.[127] Yet if it proves to be a valid theory, it may upend the principle that a corporation seeks to maximise its profits.[128] Whereas Schumpeter was concerned that the corporation eviscerated the boundary between tangible assets and intangible rights, this is an example of how the mutual fund and the ETF are eviscerating the boundary between a shareholder's investment in the corporation and a society's communal investment in much of the productive economy.

*The Communal Dividend*

While the rich get richer, labelling corporations as a communal investment may ring hollow. However, it would be false to assert that most of the public (in developed economies) has no stake in the stock market and the returns of today's mega-corporations. Slightly over 50% of US households own individual stocks.[129] About 38% of US stocks are owned by US households.[130] Statistics in many other developed economies are similar to the US.[131]

Institutional investors hold about 41% of global stock market capitalisation.[132] However, ownership by institutional investors should not be misconstrued as representing that most of the population are being excluded from the financial returns from present-day corporations. Firstly, institutional ownership masks the role of ETFs and mutual funds in shepherding financial investment. About 28% of US shareholders are actually a mutual fund or ETF.[133] However, while the stocks are held by the investment vehicle, the (net) returns pass through to the private investor. About 89% of those mutual fund assets are held on behalf of US households.[134] About 8% of US households own ETFs.[135] Secondly, everyone with entitlement to a private pension scheme is similarly essentially invested in a mutual fund, as pension fund managers select stocks (and bonds) for investment of pension contributions.

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[126] Schumpeter refers to the industries of banking; insurance; railways and trucking; mining; electricity production, transmission and distribution; iron and steel production; building and building materials – and potentially even nationalising land; see Schumpeter (n 1) 230–231.

[127] Organisation for Economic Co-operation and Development, 'Common Ownership by Institutional Investors and Its Impact on Competition: Background Note by the Secretariat' (Organisation for Economic Co-operation and Development 2017) DAF/COMP(2017)10 50–52 <https://one.oecd.org/document/DAF/COMP(2017)10/en/pdf> accessed 4 March 2023. See also Douglas Ginsburg, 'Why Common Ownership Is Not an Antitrust Problem' (*The Harvard Law School Forum on Corporate Governance*, 4 December 2018) <https://corpgov.law.harvard.edu/2018/12/04/why-common-ownership-is-not-an-antitrust-problem/> accessed 4 March 2023.

[128] Tzanaki (n 151) 212–213. See also Organisation for Economic Co-operation and Development, 'Common Ownership by Institutional Investors and Its Impact on Competition' (n 153).

[129] 52.6% of US households (65 million households) own stocks, as of 2019; see SIFMA, 'SIFMA Insights: Who Owns Stocks in America, Updating Numbers and Reinforcing Key Points' (2021) 10 <https://www.sifma.org/resources/research/who-owns-stocks-in-america-an-update/> accessed 14 August 2023.

[130] 37.7% of US shareholders are US households, as of 2019; see ibid 9.

[131] For statistics on distribution of stock market holdings internationally, as of 2017, see Adriana De La Cruz, Alejandra Medina and Yung Tang, 'Owners of the World's Listed Companies' (Organisation for Economic Co-operation and Development 2019) <https://www.oecd.org/corporate/ca/Owners-of-the-Worlds-Listed-Companies.pdf> accessed 14 August 2023.

[132] As of 2017; see De La Cruz, Medina and Tang (n 157) 10–11.

[133] US shareholders consist 21.8% of mutual funds and 6.4% of ETFs (therefore, 28.2% in total), as of 2019; see SIFMA (n 155) 9.

[134] US households own 89.2% of mutual fund assets, as of 2019; see ibid 7.

[135] As of 2019; see ibid 8.

Thirdly, those same pension schemes are among the investors in hedge funds, private equity and venture capital. Through pension fund investments in private equity, the population is even exposed to the returns of many large corporations that are not publicly-traded. Fourthly, many banks invest their funds into corporate lending and corporate bonds. The interest accruing on deposit and saving accounts can attribute some of its origins to debt payments received from corporations. Fifthly, public entities, such as governmental bodies, sovereign wealth funds, public pension funds, and state-owned enterprises, are also among the largest investors. The public sector holds about 14% of global stock market capitalisation.[136]

Much of today's financial system, therefore, runs on money invested by the public. The questions are merely whether it takes place directly or indirectly and whether the public does so consciously or unconsciously. The consolidating forces of the corporation anticipated in *CSD* are visible in the modern portfolio investing. The corporation more so than ever represents a form of communal investment on behalf of the population. The layers of intermediaries in that investment process only emphasise the conclusion that corporate investment is ceasing to be about the likely returns of specific enterprises. Members of the population lack any voting power over the management of those corporations. They are oblivious to the specific source of those returns and the size of their stake in the communal pie. Simply, each receives their communal dividend from the work of society's corporations.

## 5. Stakeholderism and Corporate Purpose

Discussions about the appropriate purpose of the corporation are again in vogue.[137] As societies suffer through a climate emergency, economic challenges and severe wealth inequality, attention turns to how corporations should help society rather than enrich their benefactors. "ESG" investment – (purportedly) prioritising investment in projects that demonstrate good "environmental, social and governance" principles – is not only a policy for philanthropic investors. It has become an expectation that corporations, banks and institutional investors will address their conformity with ESG principles.[138] (Although there has been a recent chilling effect in response to anti-ESG sentiment from sections of the public and some politicians.[139]) However, this narrative is based on some false premises as to the place of the corporation in society and the responsibility of the state in addressing these concerns.

Friedman outlined his doctrine in 1962 that "there is one and only one social responsibility of business – to use its resources and engage in activities designed to increase

[136] As of 2017; see De La Cruz, Medina and Tang (n 157).

[137] See e.g. Deloitte, 'Purpose Strategy: Leading with Purpose' (2020) <https://www2.deloitte.com/us/en/pages/operations/articles/value-of-corporate-purpose.html> accessed 14 August 2023; Arne Gast and others, 'Purpose: Shifting from Why to How' (*McKinsey Quarterly*, 22 April 2020) <https://www.mckinsey.com/capabilities/people-and-organizational-performance/our-insights/purpose-shifting-from-why-to-how#/> accessed 14 August 2023.

[138] See e.g. Evan Tylenda and others, 'The Corporate Commotion - a Rising Presence of ESG in Earnings Calls' (Goldman Sachs 2020) <https://www.gspublishing.com/content/research/en/reports/2020/10/13/4124b5d5-48d1-4db5-a8cc-bd7f9be8e265.html> accessed 14 August 2023.

[139] See e.g. Mark Maurer, 'Companies Quiet Diversity and Sustainability Talk Amid Culture War Boycotts' *Wall Street Journal* (12 June 2023) <https://www.wsj.com/articles/executives-quiet-their-sustainability-talk-on-earnings-calls-amid-growing-culture-war-3a358c1f> accessed 14 August 2023. See also BlackRock, 'Energy Investing: Setting the Record Straight' (*BlackRock*) <https://www.blackrock.com/corporate/newsroom/setting-the-record-straight/energy-investing> accessed 18 June 2023.

its profits".[140] Berle and Means similarly gave support in 1932 for the shareholder expecting that the corporation "should be made to earn the maximum profit compatible with a reasonable degree of risk".[141] Although far from unanimously accepted in society, the corporate world has largely espoused this doctrine ever since Friedman. Shareholders may complain that corporate executives have frequently prioritised enriching themselves over maximising shareholder returns.[142] Equally, long-term minded shareholders may complain that corporations prioritise short-term share price movements over long-term profitability. A corporation that conducts itself in a manner that prioritises its sustainable, long-term profitability can treat its stakeholders better without being driven by the implications for its ESG ratings.[143] Simply, improving workers' conditions or the environmental sustainability of business operations is not necessarily inconsistent with the Friedman doctrine. Being a critic of exploitative aspects of corporate culture does not require making the leap towards demoting long-term corporate returns beneath acquiescence with wider stakeholder interests.

Nonetheless, those calling for a shift towards balancing the interests of the corporation's stakeholders generally portray the Friedman doctrine as short-sighted. The Business Roundtable, represented by 181 of the US's leading CEOs, embraced this sentiment with their 2019 statement. This amended their definition of the purpose of a corporation to refer to "a fundamental commitment to all of our stakeholders".[144] Larry Fink, CEO of Blackrock, one of the world's "Big Three" asset managers, similarly emphasised in his 2019 annual letter to CEOs that corporate purpose "is not the sole pursuit of profits".[145] The economics profession is, likewise, offering rationales to support the contention that corporations should deviate from profit maximisation.[146] The incompatibility between Friedman and stakeholderism arises once a corporation is adopting policies for the sake of the "common good" at the expense of its own long-term corporate benefit.

An important caveat to the Friedman doctrine, however, is that the corporation maximise its profits "so long as it stays within the rules of the game, which is to say, engages in open and free competition, without deception or fraud".[147] Therefore, the Friedman doctrine is not a clarion call against corporations sacrificing corporate profits for socially-beneficial objectives. Rather, Friedman is arguing that it is for the state to determine where

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[140] Milton Friedman, *Capitalism and Freedom* (40th Anniversary [2002], University of Chicago Press 1962) 133. See also Milton Friedman, 'A Friedman Doctrine - The Social Responsibility Of Business Is to Increase Its Profits' *The New York Times* (13 September 1970) <https://www.nytimes.com/1970/09/13/archives/a-friedman-doctrine-the-social-responsibility-of-business-is-to.html> accessed 12 January 2022.
[141] Berle and Means (n 9) 121. See also Millon (n 78) 221–224.
[142] See e.g. Michael C Jensen, 'Agency Costs of Free Cash Flow, Corporate Finance, and Takeovers' (1986) 76 The American Economic Review 323; Rafael La Porta and others, 'Investor Protection and Corporate Valuation' (2002) 57 The Journal of Finance 1147.
[143] Alex Edmans, 'The End of ESG' (2023) 52 Financial Management 3.
[144] Business Roundtable, 'Business Roundtable Redefines the Purpose of a Corporation to Promote "An Economy That Serves All Americans"' (*Corporate Governance*, 19 August 2019) <https://www.businessroundtable.org/business-roundtable-redefines-the-purpose-of-a-corporation-to-promote-an-economy-that-serves-all-americans> accessed 18 June 2023; Business Roundtable, 'Our Commitment' <https://opportunity.businessroundtable.org/ourcommitment/> accessed 18 June 2023.
[145] BlackRock, 'Larry Fink's 2019 Letter to CEOs' (*BlackRock*, 2019) <https://www.blackrock.com/corporate/investor-relations/2019-larry-fink-ceo-letter> accessed 18 June 2023.
[146] See e.g. Oliver Hart and Luigi Zingales, 'Companies Should Maximize Shareholder Welfare Not Market Value' (2017) 2 Journal of Law, Finance, and Accounting 247.
[147] Friedman, *Capitalism and Freedom* (n 168) 133.

the corporation must defer its interests to what is deemed to be a socially-beneficial policy.[148] Typically those determinations are made through the policy platforms and politician representatives elected through the democratic process. Stakeholderism activists are overriding society's governance institutions to impose personal preferences that they are potentially mistaking for the societal good.[149] It is the responsibility of the corporation and corporate executives to maximise returns within those boundaries drawn by the state. It otherwise amounts to the tail wagging the dog. Corporations (represented by their directors and officers) would be determining how society should be governed. This would be in lieu of the political process and the role of corporations ordained by the state. In this light, the Friedman doctrine is far better than stakeholderism at grasping the role of the state vis-à-vis the corporation (described in Section 3 above).

Furthermore, the corporation can be destabilised without that clear profit-seeking goal. If corporate executives are awarded discretion to derogate from their mandate some of the time for some other reason than the long-term benefit of the corporation, then where does that derogation stop and a breach of fiduciary duty begin? Ambiguity otherwise inevitably increases the risk that corporate executives use stakeholderism as an excuse for business underperformance.[150] The exception to the profit-maximising norm, the not-for-profit corporation, is explicitly incorporated with that not-for-profit mandate. There are no half-pregnant corporations. Thus, unsurprisingly, the actions of the corporations represented at the Business Roundtable have not followed their words.[151]

## 6. The State Power Paradigm

There are policy debates to be had regarding the wisdom of any proposed legal reform of the rights, responsibilities and regulations attached to the corporation. For instance, it is generally inadvisable for a society to adopt a measure that harms society more than it benefits society. However, the merits of a proposal are beside the point here. The state retains the power to make that determination, for better or worse. The point of emphasis here is the centrality of the state to the workings of the corporation. What the state can and cannot do with that power is subject only to the constitutional constraints and political realities of that society. Look beyond the public façade and the contemporary framing of the corporation. What one can see is a legal construct that relies upon the omnipresence of the state to validate every transaction entered into by the corporation.

There are advocates for the notion that international systems of governance can be devised that offer a "global politics". These systems can offer policy accountability at that

[148] Friedman, 'The Social Responsibility Of Business Is to Increase Its Profits' (n 168): 'What it amounts to is an assertion that those who favor the taxes and expenditures in question have failed to persuade a majority of their fellow citizens to be of like mind and that they are seeking to attain by undemocratic procedures what they cannot attain by democratic procedures.'
[149] Edmans (n 171) 7–8.
[150] See Sanjai Bhagat, 'An Inconvenient Truth About ESG Investing' [2022] *Harvard Business Review* <https://hbr.org/2022/03/an-inconvenient-truth-about-esg-investing> accessed 18 June 2023.
[151] See Lucian Bebchuk and Roberto Tallarita, 'Was the Business Roundtable Statement on Corporate Purpose Mostly for Show? – (1) Evidence from Lack of Board Approval' (*The Harvard Law School Forum on Corporate Governance*, 12 August 2020) <https://corpgov.law.harvard.edu/2020/08/12/was-the-business-roundtable-statement-on-corporate-purpose-mostly-for-show-1-evidence-from-lack-of-board-approval/> accessed 14 August 2023.

supranational level, rather than at the national level through the nation-state.[152] These systems should open participation in democratic processes beyond the confines of the *demos* defined by the nation-state.[153] Such post-nation-state formulations, however, collide into the Hobbesian reality of from where the power emanates to enforce law and justice.[154] That same reality strikes when one attempts to detach the corporation from the nation-state.

Some human constructs are capable of emerging naturally from human interaction and sustaining themselves without state direction. Societies find a medium of exchange that circumvents the inconvenience of barter when transacting with each other: money.[155] Although the state now issues and regulates money, the dollarisation of numerous countries around the world today illustrates the limitation on the state's ability to compel its residents to transact in its state-issued currency. Developed economies today typically do not even transact in state-issued money but rather its bank-created replica.[156] One may argue that there is the same natural occurrence of property rights and contract once counterparties are no longer bound by the egalitarianism of kinship or close community.[157] The same natural emergence cannot be said for the corporation. The Ottoman Empire, in contrast to western Europe, was constrained for centuries from creating large-scale, long-term businesses. This was in part due to the absence of the corporate form.[158] Islamic law only recognised natural persons and the Ottoman Empire was only willing to reform to introduce its first joint-stock company in the mid-19th century. Significant domestic company formation only followed a law of corporations passed in 1908.[159] It took the initiative of the state and its legal toolkit to bring about the corporation in the Middle East.[160]

The privilege of legal personality afforded to the corporation can only travel as far as the state permits. As corporations first sought to transact across national borders, this raised the question of their legal status in foreign lands. Historically, it could not always be taken as given that corporations may operate internationally and their corporate status would be recognised wherever they transact. Where a state has not afforded corporate status to a foreign firm, it is within its powers to ignore a privilege afforded by a foreign state and pierce the corporate veil. Some European countries only committed recognise each other's corporations during the 1850s and 1860s. This emerged through bilateral trade agreements agreed between the states.[161] An international system of mutual recognition of foreign

[152] See e.g. Joshua Cohen and Charles F Sabel, 'Global Democracy?' (2004) 37 New York University Journal of International Law and Politics 763.
[153] See e.g. Nancy Fraser, *Scales of Justice: Reimagining Political Space in a Globalizing World* (Columbia University Press 2008).
[154] [Leviathan]. See Thomas Nagel, 'The Problem of Global Justice' (2005) 33 Philosophy & Public Affairs 113. See also Cohen and Sabel (n 180) 770–771.
[155] See e.g. Yuval Noaḥ Harari, *Sapiens: A Brief History of Humankind* (Vintage Books 2015) ch 10.
[156] E.g. as of July 2023, in the US, the physical currency in circulation was about $2,340 billion, reserve balances (i.e. currency deposited by banks with the US Federal Reserve as bank reserves) were about $3,180 billion and demand deposits at banks and other liquid deposits (i.e. M1 money supply excluding currency) were about $16,108 billion; see Board of Governors of the Federal Reserve System, 'Money Stock Measures - H.6 Release' (22 August 2023) <https://www.federalreserve.gov/releases/h6/20230822/> accessed 25 September 2023.
[157] See e.g. Harari (n 183) 195.
[158] Kuran (n 31) 816.
[159] ibid 787–788.
[160] See e.g. ibid 831–834.
[161] Freedeman (n 34) 133–134.

corporations now exists and is taken for granted. It remains predicated on each state having decided to recognise the legal personality of foreign corporations within its own borders.

Furthermore, corporations continue to be used as tools of the state and advancing state policy. Corporations continue to encounter the state as their gatekeeper to interactions with both their own society and foreign societies. Concepts such as “national interest” and “national security” are today utilised when some of these instances arise. For example, the *Schrems II* case highlighted how US corporations were being compelled to share users' private communications and metadata with the US intelligence services.[162] The National Security Law passed in China in 2018 places “responsibility and duty” (and legal liability) on both citizens and corporations “to safeguard national security”.[163]

In addition, despite being in an age of free circulation of capital globally, each state retains jurisdiction over the fate of the proceeds of its corporations. The state where the corporation is incorporated may levy withholding tax on its dividend payments. Accordingly, to the extent that some of the financial returns of corporations are flowing overseas to foreign shareholders, states can extract taxes from those non-citizens and non-residents through their jurisdiction over a corporation. For example, non-US residents that buy shares in a US corporation face the default position of a 30% withholding tax rate on their dividends. For any discount, such foreign shareholders rely on their home country having agreed a favourable tax treaty with the US – and they must present a W-8BEN form to their broker, which can be shared with the US tax authorities.

With this reality of state power in mind, it is generally disingenuous for representatives of state institutions to hold up their hands and retort that they are powerless to regulate the corporation in a given way. The state creates and enforces the laws that govern conduct within its territory. The state determines the scope of the legal privileges afforded to those individuals that have chosen to associate with each other within its territory in the form of a corporation rather than a partnership. The constant within the corporation is that it navigates these legal requirements and the challenges of operating a business while directed towards a clear goal: generating profits as successfully and durably as possible (i.e. profit maximisation over the long-term). There are certainly directors and managers that fail to live up to their corporate mandate. Yet the failure of society to restrain corporate conduct towards a perceived social goal is not a corporate failure but a political failure. It is failures in the operations of the state that account for the failure to regulate corporations in a manner that is in the best interests of society. Engagements between corporations and society are mediated by the state. Engagements between corporations and the foreign lands in which they do business are a matter of inter-state relations. The only constraints on the state's power over the corporation are those same constraints that fall on all other aspects of the state's power over its governance of its society. Passing the buck to corporate executives to demand that they circumvent the shortcomings of the political system is, therefore, problematic. The instant gratification that may come from remedying a discrete policy goal in this manner opens up a plethora of other questions for the political process and democracy in that society.

[162] *Case C-311/18 Data Protection Commissioner v Facebook Ireland Ltd, Maximillian Schrems* [2020] Court of Justice (Grand Chamber) Case C-311/18, ECLI:EU:C:2020:559 ECLI [61–65].
[163] National Security Law of the People's Republic of China 2015 arts 11, 13.

## 7. The Limitations of the State

Reframing the corporation through a state power paradigm is intended to focus attention on the role of state institutions and the political process in regulating corporate activity. However, it does not imply that corporations will necessarily be better regulated to align with the needs or desires of society. (There is also a distinction between what the population ostensibly *desires* and what the population *needs* to best serve public utility.)

There are three objections to relying on the state to regulate corporations that this paper will specifically address: (1) incompatibility with the constitution; (2) corporate capture of the political process and (3) regulatory arbitrage through globalisation.

*Constitutions*

There will be frictions in the political process that can impede policy preferences being enacted into law. The separation of powers and the presence of constitutional supremacy in many countries means that the courts can act as such an obstacle. A popular policy from the "political" organs of the state (the legislature and the executive) may be invalidated as "unconstitutional" by the judiciary. Constitutional amendment is typically too steep a hurdle for any policy proposal to overcome.

The *Citizens United* decision by the US Supreme Court is such an example.[164] Federal statute regulated the role of corporations in the political process: a prohibition on corporate expenditure on political donations and "electioneering communication". This was ultimately nullified as unconstitutional. The US public may dislike such an outcome from constitutional supremacy, but they have subscribed to being governed pursuant to that principle. Therefore, even when passing unpopular judgments, the state is ostensibly implementing what the people "desire" through the medium of the US Supreme Court.

There are states built upon different foundations than constitutional supremacy. The UK adheres to a principle of parliamentary sovereignty. The Netherlands has a codified constitution (the *Grondwet*) yet prohibits the constitutional review of statute. There are certainly philosophical and political questions that can be raised regarding the legitimacy of the constitution usurping a statute that a majority of the society considers to be a reasonable policy. But that is a question of the adequacy of the political process in a given state to meet the needs of society. There is coherence in a society overthrowing an inadequate constitutional framework. But while usurping the constitutional framework and its ordained political process for a popular policy is problematic. The exception may facilitate benevolent policy this time, but malevolent policy next time.

*Corporate Capture*

A call for the state to be the organ through which to regulate conduct by corporations can be criticised for presupposing that state actors will act in the public interest. In particular, capture by corporations is a concern.[165] Corporations can lobby legislators and regulators to

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[164] *Citizens United v Federal Election Commission* [2010] US Supreme Court No. 08–205, 558 US 310.

[165] See e.g. Tibor Tajti, 'Regulatory- and Other Forms of Capture in Law' in Đorđe Gardašević, Viktor Gotovac and Siniša Zrinščak (eds), *Pravo i Društvo - Liber Amicorum Josip Kregar* (Zagreb University Law School

ignore the public interest and implement or discard policies depending on whether they are favourable or unfavourable to certain corporations. For example, fault for the US "mini-banking crisis" of March 2023 is being partly attributed to banking supervisory requirements being relaxed in 2018 under the Economic Growth, Regulatory Relief, and Consumer Protection Act.[166] Those reforms came in response to lobbying from US "mid-sized" banks.[167]

However, arguing in favour of stakeholderism to compensate for state capture is guilty of a "nirvana fallacy".[168] It employs cognitive dissonance when anticipating corporate behaviour. The same corporations that are anticipated to capture state processes for self-interest are expected to implement practices that respect stakeholderism. This is despite such practices not being legally binding and benefitting third parties at the expense of corporate interests. To the contrary, a society riven by corporate capture is not likely to be a society amenable to placing stakeholder interests above corporate (or executive) welfare. Some corporations may buck that trend at the direction of their management. But there is an asymmetry to the incentives facing returns-minded investors and social-minded investors. This can lead to an "amoral drift" in corporations towards profit maximisation.[169] Would enough of their shareholders be ESG-minded investors and accept reduced returns for its societal good? Would a depressed share price merely make the benevolent corporation a target to be taken private to return to its profit-maximising ways? Therefore, corporate capture is not an obstacle to emphasising the responsibility of the state to regulate corporations. The reason is not that capture will not happen. Rather, as pessimistic as this may be, one should anticipate that corporations will seek to trump individual interests within any political system and any model for corporate governance (including in Schumpeter's socialist destination state).

*Globalisation*

The contemporary multinational corporate group typically employs regulatory arbitrage on a global scale. It can decide in which country to incorporate a given subsidiary and/or operate its business operations. It can decide under which law to govern (many of) its transactions. Altogether, this can shield the corporate group from certain liabilities. The most pressing liability is tax. It is apparent that some corporate groups employ legal devices to shift profits to no/low-tax jurisdictions. Despite transacting in a given state, corporations can inform the applicable tax authorities that their profits actually accrued offshore.[170] Concepts such as the

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2022) <https://www.researchgate.net/publication/365126487_Regulatory-_and_Other_Forms_of_Capture_in_Law>.

[166] Board of Governors of the Federal Reserve System, 'Review of the Federal Reserve's Supervision and Regulation of Silicon Valley Bank' (2023) 81–91. See Economic Growth, Regulatory Relief, and Consumer Protection Act 2018.

[167] Karl Evers-Hillstrom, 'Silicon Valley, Signature Banks Lobbied Hard to Loosen Bank Rules' [2023] *The Hill* <https://thehill.com/policy/technology/3898389-silicon-valley-signature-banks-lobbied-hard-to-loosen-banking-rules/> accessed 26 September 2023.

[168] See Harold Demsetz, 'Information and Efficiency: Another Viewpoint' (1969) 12 Journal of Law & Economics 1.

[169] Hart and Zingales (n 174) 255–258.

[170] See Antony Ting, 'iTax - Apple's International Tax Structure and the Double Non-Taxation Issue' (2014) 2014 British Tax Review 40, 42–54. For an illustrative overview of how the "double Irish and Dutch sandwich" tax structure works, see New York Times, '"Double Irish With a Dutch Sandwich"' *New York Times* (28 April 2012) <https://archive.nytimes.com/www.nytimes.com/interactive/2012/04/28/business/Double-Irish-With-A-Dutch-Sandwich.html?ref=business> accessed 26 September 2023.

"double Irish and Dutch sandwich" acquired public notoriety in the 2010s.[171] Legislators have publicly stated that such assertions by corporations are "deeply convincing" but been left calling for international tax law reform to resolve the problem.[172]

Conversely, the multinational corporate group can conveniently shift its identity from global to national. By placing emphasis on the jurisdiction in which its parent is incorporated, the corporation can call for help from its "home" state against foreign attacks. In turn, for all of its qualms about the conduct of its corporations, a state may intervene to attempt to shield its corporations from an unfavourable policy being proposed or implemented in other countries. In these instances it should now be apparent that the exploitation of globalisation by the corporation has its limitations once state power is being exercised. Corporate power has become meaningless and the corporation is asking another state to come to its rescue.

This dynamic has been at play in how the US Government has responded to EU regulatory policies in the digital technology sector, such as the General Data Protection Regulation ("GDPR")[173], the Digital Markets Act ("DMA")[174] and the Digital Services Act ("DSA").[175] US administrations – from both the Republican Party and the Democratic Party – have perceived such regulation of the tech sector to be a form of EU protectionism.[176] This is because these reforms hinder the profitability of tech companies, which are typically US-headquartered corporate groups. The applicability or enforceability of the GDPR, the DMA or the DSA to multinational corporations is not the question. The EU through its 27 Member States has the means to attach to any assets that a recalcitrant corporation has within its legal jurisdiction. Rather, it is a question of the geopolitical power dynamics between the EU and the US (or any other country). Can the EU expect to impose its tech sector regulations on "foreign" corporations without some form of retaliation by foreign states that outweighs the benefits of those regulations? This is an outcome that "stronger states" (in geopolitical terms) are strong enough to implement without fear of foreign retaliation. In some cases, this can go as far as imposing legal reform on "weaker states" to ensure their compatibility with a stronger state. That is what the export of "regulatory models" by certain states, such as the so-

[171] See e.g. Vanessa Houlder, 'Google Tax: The 6-Year Audit That Ended in a Political Storm' *Financial Times* (29 January 2016) <https://www.ft.com/content/f1c5ca30-c677-11e5-b3b1-7b2481276e45> accessed 26 September 2023.
[172] Public Accounts Committee, UK House of Commons, 'Tax Avoidance-Google' (UK House of Commons 2013) <https://publications.parliament.uk/pa/cm201314/cmselect/cmpubacc/112/11204.htm> accessed 26 September 2023.
[173] Regulation (EU) 2016/679 of the European Parliament and of the Council of 27 April 2016 on the protection of natural persons with regard to the processing of personal data and on the free movement of such data, and repealing Directive 95/46/EC 2016.
[174] Regulation (EU) 2022/1925 of the European Parliament and of the Council of 14 September 2022 on contestable and fair markets in the digital sector and amending Directives (EU) 2019/1937 and (EU) 2020/1828 (Digital Markets Act) 2022.
[175] Regulation (EU) 2022/2065 of the European Parliament and of the Council of 19 October 2022 on a Single Market For Digital Services and amending Directive 2000/31/EC (Digital Services Act) 2022.
[176] Wilbur Ross, 'EU Data Privacy Laws Are Likely to Create Barriers to Trade' *Financial Times* (30 May 2018) <https://www.ft.com/content/9d261f44-6255-11e8-bdd1-cc0534df682c> accessed 26 September 2023; U.S. Chamber of Commerce and Gina Raimondo, 'U.S.-EU Partnerships: Transatlantic Goals and Priorities' (*OnDemand / Government Policy*, 8 December 2021) <https://www.uschamber.com/on-demand/government-policy/us-eu-partnerships-the-biden-administrations-transatlantic-goals-and-priorities> accessed 26 September 2023.

called “Brussels Effect”,[177] can represent. As is evident with the EU, state power can be extended by such collective action between nation states.

The other side of this dynamic is that a weaker state may be politically constrained from enforcing its desired policy against corporations operating within its territory. There is the threat of political or economic (or even military) retaliation from stronger states that are protecting “their” corporations from an adverse law or regulation in weaker states. The Opium Wars of 1839-1842 and 1856-1860 between Britain and China are a historic example. Superficially in the name of upholding international free trade, Britain was preventing China enforcing a domestic prohibition on opium that would harm opium exports by British merchants (including the EIC).[178] By the 21st century, Britain would be on the receiving end. In 2006, Britain discontinued an investigation into alleged bribery at BAE Systems to “safeguard national and international security”.[179] That decision was reported by the press to have been driven by concerns from the British Government regarding the economic, intelligence sharing and diplomatic response of the Kingdom of Saudi Arabia to such an investigation into its arms deals with BAE Systems.[180] Britain found its enforcement of domestic criminal law overwhelmed by the realities of its now-diminished geopolitical power. (It would be the US to prosecute BAE Systems in 2010 instead.[181]) It may seem arcane to view the modern corporate landscape through the historical geopolitical lens of colonialism, treaty ports, trade embargoes and extraterritoriality. Nonetheless, relations between multinational corporations and the states in which they operate remain inextricably intertwined with inter-state relations.

*International Taxation*

With this in mind, it should be clear that the existing international tax law system does not exist despite the helpless protests of developed countries but rather with the acquiescence of these countries.[182] The collective economic power of developed countries means that these states are too powerful to be forced to accept a status quo imposed by low-tax jurisdictions. Many of these territories are merely islands of a few thousand inhabitants. Many exist under some form of constitutional relationship with the US, the UK or other developed countries.[183] The behaviour of the US and the EU in recent years towards low-tax jurisdictions demonstrates what can be achieved with political will.

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[177] See Anu Bradford, *The Brussels Effect: How the European Union Rules the World* (Oxford University Press 2020).
[178] Jeffrey D Sachs, ‘Twentieth-Century Political Economy: A Brief History of Global Capitalism’ (1999) 15 Oxford Review of Economic Policy 90, 91. See also Toby Seddon, *Rethinking Drug Laws: Theory, History, Politics* (Oxford University Press 2023) 85–89.
[179] Tim Jarrett and Claire Mills, ‘Bribery Allegations and BAE Systems’ (House of Commons Library 2010) Standard Note: SN/BT/5367 <https://researchbriefings.files.parliament.uk/documents/SN05367/SN05367.pdf> accessed 25 September 2023.
[180] David Leigh and Rob Evans, ‘Blair Called for BAE Inquiry to Be Halted’ *The Guardian* (22 December 2007) <https://www.theguardian.com/baefiles/story/0,,2231496,00.html> accessed 25 September 2023.
[181] Office of Public Affairs, U.S. Department of Justice, ‘BAE Systems PLC Pleads Guilty and Ordered to Pay $400 Million Criminal Fine’ (*Press Release*, 1 March 2010) <https://www.justice.gov/opa/pr/bae-systems-plc-pleads-guilty-and-ordered-pay-400-million-criminal-fine> accessed 25 September 2023.
[182] Ting (n 199) 56–59, 71.
[183] E.g. American Samoa, Guam and the US Virgin Islands are US territories; the Marshall Islands and Palau are associated with the US; Anguilla, the British Virgin Islands and the Turks and Caicos Islands are British Overseas Territories; and Aruba and Curaçao are part of the Kingdom of the Netherlands.

Initially, information sharing to combat tax evasion was extracted from states, including those that pride themselves on offering banking secrecy and confidentiality of corporate affairs. The US led through its Foreign Account Tax Compliance Act ("FATCA") in 2010.[184] The US required disclosure by foreign financial institutions of the status of financial accounts held by US taxpayers. The US exploited the role of the US dollar as the global reserve currency and the consequential centrality of US correspondent banks to the global financial system. The US could not compel foreign institutions to comply with FATCA but it could compel US institutions to apply 30% withholding tax to any payments made to non-compliant foreign institutions. An international system, the Common Reporting Standard (CRS), was agreed in 2014 through the Organisation for Economic Co-operation and Development ("OECD").[185]

Reform of corporation tax rates has followed. The EU created a list of no/low-tax jurisdictions in 2017 that are deemed "non-cooperative" for having "failed" or "refused" to "fulfil their commitments to comply with tax good governance criteria".[186] Those commitments relate to "tax transparency", "fair taxation" and "measures against base erosion and profit sharing". The EU reserves the right to apply "defensive measures" in response.[187]

Finally, 137 countries (through the OECD) agreed in 2021 to apply a global effective minimum corporation tax rate of 15% as part of the "Global Anti-Base Erosion Rules" (GloBE). To the extent that a corporate group is paying below this global minimum on its profits, another jurisdiction (typically where the parent corporation is incorporated) may levy a "top-up tax".[188] Therefore, without overriding the sovereignty of low-tax jurisdictions to determine their own corporation tax rates, other states have blunted an incentive for multinational corporations to shift their profits to low-tax jurisdictions. Who is the nation unpicking that deal? The US. American corporations stand to be paying more corporation tax to other countries around the world.[189] The international tax system, therefore, demonstrates both the limitations and the potency of state power in governing the boundaries of the corporation and its conduct.

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[184] For a summary, see Internal Revenue Service, 'Summary of Key FATCA Provisions' (21 September 2023) <https://www.irs.gov/businesses/corporations/summary-of-key-fatca-provisions> accessed 26 September 2023.
[185] See Organisation for Economic Co-operation and Development, 'Common Reporting Standard (CRS)' (*Automatic Exchange Portal*) <https://www.oecd.org/tax/automatic-exchange/common-reporting-standard/> accessed 26 September 2023.
[186] The countries on the EU list of non-cooperative jurisdictions for tax purposes (the Annex I "blacklist") as of September 2023 (in the Council decision adopted on 14 February 2023) are: American Samoa, Anguilla, the Bahamas, the British Virgin Islands, Costa Rica, Fiji, Guam, the Marshall Islands, Palau, Panama, Russia, Samoa, Trinidad and Tobago, the Turks and Caicos Islands, the US Virgin Islands, Vanuatu. EU Member States are not capable of being deemed non-cooperative jurisdictions.
[187] Council of the European Union, 'EU List of Non-Cooperative Jurisdictions for Tax Purposes' (*Consilium*, 17 July 2023) <https://www.consilium.europa.eu/en/policies/eu-list-of-non-cooperative-jurisdictions/> accessed 25 September 2023.
[188] See Organisation for Economic Co-operation and Development, 'The Pillar Two Rules in a Nutshell' <https://www.oecd.org/tax/beps/pillar-two-model-rules-in-a-nutshell.pdf> accessed 26 September 2023.
[189] See e.g. Julie Zauzmer Weil, 'Biden Won a Global Tax Rate. Now Americans Wonder If It Was a Good Deal.' *Washington Post* (5 July 2023) <https://www.washingtonpost.com/business/2023/07/03/global-minimum-tax-american-businesses/> accessed 26 September 2023.

## 8. Conclusion

There are three lessons to be taken from this paper. Firstly, the role of the corporation in the economy and wider society is underpinned by the state maintaining the corporate veil between the persons, assets and contracts that form a corporation and that corporation's counterparties. The corporation is itself a legal fiction. Power comes with the agglomeration of capital represented by the corporation. Certain conveniences arise for corporations from the state's willingness to impute legal personhood onto what is no more than an association of persons. With these benefits also comes the responsibilities that the state may impose on the corporation. The corporation is defined by what attributes the state is willing to accept. It falls within the power of the state to determine the role of the corporation in society.

Perceived defects in the state power paradigm are likely to actually be symptoms of limitations of state power or an ineffective political process. Unfortunately, societies are not destined to be governed by state institutions that act in their best interest. Stakeholderism cannot consistently and coherently overcome these limitations. If the state cannot compel the corporation, and if the corporation can lobby one state to defend its interests against other states, how can voluntary commitments be regarded as an effective bind on the corporation? Corporate philanthropy is, at best, a palliative. Relying on the benevolence of corporate actors is not a remedy for the inadequacies in applying state power and the failures in the political process.

Secondly, the presence of large corporations dominating the economy and society is not a new phenomenon. The earliest corporations wielded the state's powers over war, trade policy and money. The joint-stock companies that later emerged represented important industries to society and depended on a mutually-beneficial relationship between the state and the corporation. Schumpeter presciently observed in *CSD* that the corporations of his day would inevitably grow ever larger. Today's mega-corporations, however, only raise questions that are a difference in degree, not a difference in kind, from the corporations of the past. These questions are not enough to recalibrate the compass that navigates how the corporation is expected to be governed: to maximise its long-term returns for the benefit of its pool of investors.

Thirdly, the publicly-traded corporation now represents a part of a communal investment. Profits are not reserved for a select few investors. Nor can an investor identify to where their investment has gone and from where their returns derive. The corporation is itself a pool of corporations known as the corporate group. This is the conduit for modern corporations becoming ever larger and holding a firmer grasp on the economy. The publicly-traded corporation has also seen itself increasingly reduced to dematerialised, defunctionalised and absentee ownership. The mutual fund and the ETF have converted the largest corporations into a communal pool of passive investments. Everyone is left theoretically owning a fraction of practically every corporation. Their intangible substance generates the financial returns that are drip-fed to the population at large. What remains disconcerting to critics is a question regarding the equitable distribution of those proceeds amongst the population.

To the critics of the existing global capitalist order, there is no need for socialism in the legislature, nor stakeholderism in the boardroom. The corporation is already here.