

1973

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## Recommended Citation

Blumberg, Phillip, "Corporate Social Responsibility Panel: The Constituencies of the Corporation and the Role of the Institutional Investor" (1973). *Faculty Articles and Papers*. 154.

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Citation: 28 Bus. Law. 177 1972-1973



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# Corporate Social Responsibility Panel: The Constituencies of the Corporation and the Role of the Institutional Investor

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ELI GOLDSTON\*\*, Boston, Massachusetts; and  
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**PROFESSOR PHILLIP I. BLUMBERG:** We are discussing this afternoon the constituencies of the corporation, and I have been asked to speak on "New Directions for Employees."

Discussion of the so-called constituencies of the corporation rests on the assumption that there is more to the corporate world than the relation of the corporation and its Board of Directors and management to its shareholders. It assumes that there are other groups whose lives and fortunes are vitally affected by corporate operations, whose interests must be considered in corporation decision, and further, who may have a legitimate claim to participate in the corporate decision-making process.

Thus, as long ago as 1919, Mackenzie King stated that the corporation must serve the objectives not only of its shareholders, but also of its employees and the community.<sup>1</sup> In 1929 Owen D. Young, then President of General Electric was similarly expressing the view that the Board was to act as a trustee not solely for shareholders, but also for employees, consumers, and the general public.<sup>2</sup> These views became part of the philosophy of managerialism. This is the philosophy that the function of the Board is not, as the law has traditionally stated, to dedicate itself with single minded loyalty to the advancement of the interests of the shareholders, but instead to mediate among the legitimate claims of the various corporate constituencies, of whom shareholders constitute only one group.<sup>3</sup> Of the so-called constituencies, it is

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1. See, G. GOYDER, *THE FUTURE OF PRIVATE ENTERPRISE* 20 (1951); L.C.B. GOWER, *PRINCIPLES OF MODERN COMPANY LAW* 56, n. 29 (2d ed. 1957).

2. See, W. CARY, *CASES AND MATERIALS ON CORPORATIONS* 239 (4th ed. unab. 1969) [quoting SEARS, *THE NEW PLACE OF THE STOCKHOLDER* 209 (1929)].

3. See, E. STEIN, *HARMONIZATION OF EUROPEAN COMPANY LAWS* 81-82 (1971); M. FOGARTY, *COMPANY AND CORPORATION ONE LAW?* 8-10 (1965); Hetherington, *Fact and Legal Theory: Shareholders, Managers, and Corporate Responsibility*, 21 *STAN. L. REV.* 248, 277-78 (1969); Eisenberg, *The Legal Roles of Shareholders and Management in Modern Corporate Decisionmaking*, 57 *CALIF. L. REV.* 1, 21 (1970).

the employees upon whom the corporation has the most profound impact.<sup>4</sup>

This presentation reviews the changing role of employees in their relation to the large public corporation. This embraces at least four separate areas:

- (a) Increased participation in corporate decision-making, particularly through representation on the Board of Directors.
- (b) Participation in the ownership of the enterprise through employee acquisition of stock.
- (c) Employee concern with job security and resistance to takeovers and mergers; and
- (d) Changing attitudes with respect to the traditional concepts of the employee's duties of loyalty and obedience to his employer.

### I. Forces for Change in the Role of Employees

There are major forces at work creating pressures for change in the objectives and structure of the large public corporation. These forces create the background against which possible change in the role of employees must be evaluated.

*A. The Changing Society.* The outstanding characteristic of our time is that we live in a world of change and in a world of social and environmental crisis. Change in values, change in social institutions, change at an accelerating rate is a major factor that is at work not only in the United States but in the world. With such changes in social attitudes and values, the large public corporation is coming under increasingly critical review.

*B. The Changing Corporation.* The large corporation is changing along with the society. It has acquired immense economic power. The 500 largest industrial corporations do approximately  $\frac{2}{3}$  of the business and earn approximately  $\frac{3}{4}$  of the net profits after tax of all industrial corporations. In some years, the percentage of total industrial profits earned by corporations listed on the New York Stock Exchange has reached 90%.<sup>5</sup> Further, it has emerged as a dominant political and social institution of our society. Accordingly, concern with the problems of the nation is inevitably accompanied by inquiries as to the role of business in their creation and also in their solution.

*C. Changing Corporate Objectives.* Corporate social responsibility has led corporations into new areas and activities. There is increasing concern with the very objective of the corporation. How does one reconcile service

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4. See, L.C.B. GOWER, MODERN COMPANY LAW 10-11 (3rd ed. 1969) ("Insofar as there is any true association in the modern public company it is between management and workers rather than between the shareholders inter se or between them and management. But the fact that the workers form an integral part of the company is ignored by the law . . . the orthodox legal view is unreal in that it ignores the undoubted fact that the employees are members of the company for which they work to a far greater extent than are the shareholders whom the law persists in regarding as its proprietors.")

5. FORTUNE, May 1972, at 188; N.Y. STOCK EXCHANGE, 1972 FACT BOOK 30 (1969: 90.7%, preliminary data), 1970 FACT BOOK 28 (1959: 90.0%).

to society with the drive for profit? Is the goal of the corporation primarily the search for profit or is there a great deal more to it?

*D. Lack of Accountability.* As a result of the separation of ownership and control flowing from the widespread distribution of shares, management of the large public corporation has for practical purposes in most cases become a self-perpetuating group. Management typically lacks accountability.

*E. Lack of Legitimacy.* The corporation affects wide segments of society. "Private" has become "public." Social and economic groups affected by the corporation have no role in its direction. Even if the Board were not self-perpetuating and stockholders possessed the power of election in realistic terms, the question of the legitimacy of a Board of Directors representing solely shareholder interests would continue to be challenged by reform groups, demanding that the social and economic groups affected by the corporation participate in the corporate decision-making process.

*F. Changing Relations with Government.* Relations with government are changing. Business for the first time is welcoming governmental intervention to provide shelter from the searing impact of public demand for change in business conduct, particularly in the environmental field.

*G. Increasing Impact of European Experiences.* Finally, with the growth of the multi-national corporation, American business is experiencing in other parts of the world different forms of industrial organization and of allocation of economic power. These broadened horizons will inevitably be reflected in changed American attitudes.

All these factors create forces for change in the structure of the large American public corporation in general and in the role of employees in particular.

## II. Employee Representation on the Board of Directors

The proposal for employee representation on the Board of Directors is entirely academic in the United States in contrast to its increasing acceptance in Europe.

*A. An Academic Proposal in the United States.* Employee representation on the Board has been the subject of a series of so-called "public interest" proxy proposals,<sup>6</sup> but it has attracted little support in the United States and is still a concern of purely intellectual interest.

Although state corporation law has in the past permitted the election of directors by employees (as well as by creditors) where the charter or by-laws

6. See, e.g., GENERAL MOTORS CORP., NOTICE OF ANNUAL MEETING AND PROXY STATEMENT, Apr. 5, 1971, at 34-37; FORD MOTOR CO., NOTICE OF ANNUAL MEETING AND PROXY STATEMENT, Apr. 7, 1972, at 20-21; JEWEL COMPANIES, INC., NOTICE OF ANNUAL MEETING AND PROXY STATEMENT, May 15, 1972 at 10-11; AMERICAN TEL. & TEL. CO., NOTICE OF MEETING AND PROXY STATEMENT, Apr. 19, 1972, at 13-15. Each of the foregoing proposals included representatives of other groups as well as employees in the proposal to broaden the composition of the Board.

7. See, MASS. GEN. LAWS, c. 156, § 23 (1932), N.J. REV. STAT. § 14.9-1 to -3 (1957) (repealed) (employees); E. DODD & R. BAKER, 1 CASES ON BUSINESS ASSOCIATIONS-CORPORATIONS 196, n.21 (1940); cf. H. BALLANTINE, CORPORATIONS 498 (rev. ed. 1946) (listing statutes providing for election by creditors).

of the corporation so provide,<sup>7</sup> employee representation on the Board is relatively unknown in American corporate life.

At the present time, there is widespread acceptance of the desirability of strengthening the Board of Directors by broadening its perspectives through the addition of members who can introduce fresh "inputs" into the Board decision-making process. Thus, the American corporate scene is changing with long-neglected groups—particularly blacks and women—supplying persons who are being elected to the Boards of major corporations. At present, approximately 70 major American corporations, as well as both the New York and American Stock Exchanges, have added black directors; approximately 20 major corporations have added women directors.<sup>8</sup> It is noteworthy that notwithstanding these developments which herald a new pattern for the composition of the Board, there has been no inclusion of employee directors and no serious demands for the addition of the employee point of view to the Board.

On the surface, this appears odd, particularly in view of the obvious fact that corporate decision-making has a greater impact on employees than on these other groups. Why then is there such little public interest in employee representation on the Board?

The explanation rests on the distinction between broadening the perspectives of the Board and of "special-interest" representation. The black and women directors add a fresh point of view. They are clearly not elected as representatives of a constituency to whom they report and are accountable. At the same time, they also represent an attempt to give symbolic recognition to the aspiration of long-deprived groups for fuller participation in the society as well as to symbolize the dedication of the Board to non-discriminatory principles in the operation of the enterprise.

It is possible to view the addition of employee members of the Board in a similar limited role of broadening the Board's perspectives. Indeed, as we will see, that is precisely the role of employee directors on the Boards of British nationalized industries. However, with general acceptance of collective bargaining and recognition of the legitimacy of unions, the pressure for symbolic recognition is unnecessary. Further, union representation itself provides aggressive presentation of the employee point of view. Board membership is not required for such purposes.

The concept of employee representation rests on the quite different concept of "special-interest" representation, the participation by worker representatives in corporate decision-making at the Board level. This is a proposal to strengthen worker or union power. It is an effort to achieve increased benefits, or economic justice, for workers.

Further, the proposal for worker representation reflects a desire for indus-

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8. See, BUS. & SOC'Y, Sept. 26, 1972, at 4; N.Y. Times, Jan. 24, 1972, at 59, col. 2; Wall St. J., Oct. 5, 1972 at 1, col. 6; June 7, 1972, at 2, col. 2; Vanderwicken, *Change Invades the Boardroom*, FORTUNE, May, 1972, at 156; TIME, Oct. 16, 1972, at 85.

trial democracy or social justice, as well as economic justice, for employees. It is part of an effort to achieve greater employee individual fulfillment and job satisfaction through employee participation in decision-making on all levels. Board representation is only an aspect of the larger movement for greater employee participation.<sup>9</sup>

It is a proposal that rests almost entirely on the German experience where industry has prospered, notwithstanding two decades of employee representation on the Board and the increasing acceptance in Europe generally of the principle of employee representation. It also reflects the successful Yugoslav experience with worker self-management, a society where workers in the plant play a major role in the decision-making process and in participation in the profits of the enterprise.

The proposal attracts support from non-labor reformers who see it, among other things, as a method of restoring accountability and legitimacy to the Board of Directors and of transforming the large corporation from a "private" to a "public" institution.

The crucial aspect about the proposals for employee representation on the American Board of Directors is that they do not reflect any serious objective of the American trade union movement nor of workers generally. The proposals are being advanced without grass roots support. The cold fact of the matter is that, notwithstanding the ferment in this area abroad, American unions and workers are simply uninterested in the proposal for Board representation. Further as Professor Robert Dahl points out, "workers and trade unions may be the greatest barriers at present to any profound reconstruction of economic enterprise in this country."<sup>10</sup> Until such attitudes change, consideration of the advantages and problems involved in such a proposal should be regarded as an educational exercise, not without interest and not without possible usefulness, but completely separated from political realities.

In at least one instance, however, an American trade union has expressed some interest in worker representation on the Board. Pilots of United Air Lines sought Board representation at the 1972 annual meeting. The stated objective for such representation was to improve channels of communication, rather than participation in decision-making. The pilots' proposal received 5% of the vote. It is perhaps not without significance that the only example of a union effort for Board representation involved a union of elite personnel, earning in some cases more than \$50,000 per year. It is hard to view such a development as involving the aspirations of the deprived masses. Further,

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9. See, PAUL BLUMBERG, *INDUSTRIAL DEMOCRACY* (1968); H. CLEGG, *A NEW APPROACH TO INDUSTRIAL DEMOCRACY* (1960); H. CLEGG, *INDUSTRIAL DEMOCRACY AND NATIONALIZATION* (1951); F. EMERY & E. THORSRUD, *FORM AND CONTENT IN INDUSTRIAL DEMOCRACY* (1969); P. VAN GORKUM, *INDUSTRIAL DEMOCRACY IN THE NETHERLANDS: A SEMINAR* (1969); I. ADIZES, *INDUSTRIAL DEMOCRACY: YUGOSLAV STYLE* (1971); IRISH MANAGEMENT INSTITUTE, *INDUSTRIAL DEMOCRACY—A SYMPOSIUM* (1969).

10. Dahl, *Power to the Workers?* N.Y. REV. OF BOOKS, Nov. 19, 1970 at 20, 22.

the proposal received no support from the national Airline Pilots Association.<sup>11</sup>

*B. Foreign Experience with Employee Representation and Worker Self-Management.*<sup>12</sup> Support for employee representation on the Board, or the more sweeping reform of employee ownership and management of industry, arises from the extensive European experience.

*1. German Co-determination.* The major support for the concept of "special interest" directors arises from the German experience with "co-determination," or employee directors on the Supervisory Board (Aufsichtsrat), the upper board in the two-tier German board structure. This upper board elects the members of the Managing Board (Vorstand) and supervises and inspects, but does not manage. The Managing Board is the executive arm of the corporation combining both the direction of day-to-day operations and policymaking. In steel, coal and iron firms with 1000 employees or more, with full co-determination, employee representatives comprise one-half of the Supervisory Board and hold a veto power over the designation of the Labor Director on the Managing Board. In other industries, with partial co-determination, employee representation is restricted to one-third of the Supervisory Board.<sup>13</sup>

The German model of partial co-determination—the dual board with one-third labor representation on the upper board—has been adopted in the proposed statute for a European Company (*Societas Europaea*) in the European Economic Community.<sup>14</sup> The French Law of June 18, 1966, similarly requires the representation of two non-voting labor directors on the boards of public corporations (*sociétés anonymes*).<sup>15</sup>

11. See, UAL, INC., NOTICE OF MEETING AND PROXY STATEMENT, Mar. 24, 1972, at 2-3, 13-14; Wall St. J., Dec. 13, 1971, at 25, col. 5, Apr. 28, 1972, at 34, col. 1.

12. The discussion of the European experience follows the author's Book Review, 50 TEX. L. REV. 598, 610-13 (1972).

13. Law of May 21, 1951, [1951] BGBI. 347; Law of Oct. 14, 1952, [1952] 1 BGBI. 681; Law of Aug. 7, 1956, [1956] BGBI. 707, as amended, Law of July 15, 1957, [1957] 1 BGBI. 714. For a general review of the German experience, see, C. DEHOUGHTON, ed., THE COMPANY—LAW, STRUCTURE, AND REFORM IN ELEVEN COUNTRIES 213-21 (1970); M. FOGARTY, *supra* note 3; A. SHUCHMAN, CO-DETERMINATION: LABOR'S MIDDLE WAY IN GERMANY (1957); H. SPIRO, THE POLITICS OF CODETERMINATION (1958); Frame, *Worker Participation with Particular Reference to Codetermination in the Federal Republic of Germany*, 5 VICT. U. L. REV. 417 (1970); Vagts, *Reforming the "Modern" Corporation: Perspectives from the German*, 80 HARV. L. REV. 23 (1966).

14. COMM'N OF THE EUROPEAN COMMUNITIES, PROPOSED STATUTE FOR THE EUROPEAN COMPANY, Art. 137 (1), Supp. to Bull. 8-1970 of the European Communities. See, Sanders, *The European Company on Its Way*, 8 COMM. MKT. L. REV. 29 (1971); Storm, *A New Impulse Towards a European Company*, 26 THE BUSINESS LAWYER 1443 (1971).

15. The works council (*comité d'entreprise*) of a *société anonyme* may appoint two of its members who are to be present in a non-voting advisory capacity at all meetings of the *conseil d'administration* (in corporations using the single board system) or the *conseil de surveillance* or upper board (in corporations using the dual-board system). Law No. 66-427 of June 18, 1966. See, CCH COMM. MKT. REP., EUROPEAN STOCK CORPORATION 177 (P. Sanders ed. 1969).



The results of the German experience are mixed. In steel, iron, and coal, where labor representation includes one-half of the Supervisory Board as well as a veto power over the designation of the Labor Director on the Managing Board, full co-determination seems to have provided labor with an effective share of power, has apparently contributed to reduced labor strife, and generally has worked satisfactorily. In other industries, where labor representation is restricted to one-third membership on the Supervisory Board, or partial co-determination, labor representation generally has been regarded as not particularly meaningful. Power in fact has not been shared. Often, labor representation has not been taken seriously and has served as a source of sinecures for old faithful trade union officials, with management control essentially unimpaired.<sup>16</sup>

2. *Yugoslav Worker Self-Management.* The Yugoslav experience with worker-owned industry has attracted world-wide attention. As a unique blend of socially-owned enterprise operated both for profit under market conditions and for the benefit (after payment of capital charges) of the workers employed in the enterprise, the Yugoslav model is most interesting. Control is in the hands of the plant workers and the local communes, with the League of Communists playing a significant role behind the scenes. The shift of the locus of power from the federal government to the plant and the local community reflects the strong centrifugal forces in Yugoslavia that make decentralization politically desirable, in light of the divisive influences separating the Serbs, Croats, Slovenes, Macedonians, Montenegrins, and other ethnic groups in the nation. The development has been associated with problems of capital formation and a high level of inflation, which apparently reflect, at least in part, worker pressure for short-term profit maximization. Paradoxically, concern with short-term objectives may be greater in worker self-managed Yugoslav industry than in the United States where management has been increasingly inclined to be concerned with the long-term view.<sup>17</sup>

Whatever the intellectual interest in this experiment, it is hardly a realistic alternative. Even Professor Dahl, one of its leading American proponents, concedes the unlikelihood of American labor support for the program. He visualizes its possible adoption in the United States as a result of middle class pressure.<sup>18</sup> It may be noted that at the present time there is not the slightest indication of any support for this visionary conclusion.

3. *Sweden.* Sweden is moving in the direction of employee representation on the Board. A number of companies, including Volvo, have experimented

16. See, FOGARTY, *supra* note 3, at 120-21, 126-28 (1965); D. GRANICK, THE EUROPEAN EXECUTIVE 220 (1962).

17. For a general review of the Yugoslav experience, see, I. ADIZES, *supra* note 9; M. BROEKMAYER, YUGOSLAV WORKERS' SELF-MANAGEMENT (1970); DEHOGHTON, *supra* note 13, at 320-36; J. KOLAJA, WORKERS' COUNCILS: THE YUGOSLAV EXPERIENCE (1966); G. MACESICH, YUGOSLAVIA: THE THEORY AND PRACTICE OF DEVELOPMENT PLANNING (1964); S. PEJOVICH, THE MARKET-PLANNED ECONOMY OF YUGOSLAVIA (1966); J. VANEK, THE PARTICIPATORY ECONOMY (1971).

18. R. DAHL, AFTER THE REVOLUTION 134-36 (1970).

with the voluntary designation of employee directors as part of a campaign to deal with job dissatisfaction.<sup>19</sup> The 1971 Conference of the Confederation of Swedish Trade Unions has demanded the designation of 2 employee representatives on all boards.<sup>20</sup> Swedish Premier Olaf Palme is pressing for the mandatory appointment of employee and government directors to the boards of all companies with more than 100 employees.<sup>21</sup>

4. *Conflicting European Trade Union Attitudes.* An illuminating aspect of the European experience is the mixed nature of trade union reaction to proposals for employee representation on the Board.

The English unions in the past traditionally opposed such representation. As C. A. R. Crosland puts it, English union attitudes have displayed "not merely apathy but a barely concealed hostility."<sup>22</sup> They regarded Board representation as involving a confusion in roles and impairing their ability to challenge management. The union has been perceived as "the opposition" and therefore by definition would not participate in the exercise of Board power.

In recent years, British union attitudes have tended to change. Before the Donovan Commission, some union representatives argued for voluntary representation on the Boards of Directors of companies. A minority of the Commission agreed, but the *Commission Report* regarded such a movement as unwise and premature.<sup>23</sup>

In sharp contrast, the German unions have regarded Board membership as an objective of high priority. It has replaced socialism as the objective of the trade union movement.<sup>24</sup> At the present time, German unions are pressing for the extension of full co-determination or one-half representation on the Boards of all German corporations, rather than solely in iron, coal, and steel.<sup>25</sup>

The Confederation of Swedish Trade Unions has taken a middle ground. It has endorsed mandatory employee representation on the Board while emphasizing that the Confederation would maintain its independence of action.<sup>26</sup>

5. *Latin America.* In his recent review of Latin American enterprise, Professor Bayitch reports the establishment of co-determination in national-

19. 18 BUS. INT'L 175 (May 28, 1971).

20. See, Liddon, *Industrial Democracy in Sweden*, FREE LABOR WORLD, Nov. 1971, at 14; 11 BUS. EUROPE 310 (Sept. 24, 1971).

21. N.Y. Times, Nov. 12, 1972, § 1, at 28, col. 1.

22. C.A.R. CROSLAND, *THE CONSERVATIVE ENEMY* 218 (1962); See, *THE FUTURE OF PUBLIC OWNERSHIP* 21 (Fabian Society Tract No. 344, 1963); W. PUCKEY, *THE BOARD ROOM* 96-97 (1969) ("I have yet to hear a senior [English] union official give wholehearted support to worker representation in boards in the private sector").

23. See, L.C.B. GOWER, *supra* note 4, at 63 n. 53, W. FRIEDMANN & J. GARNER, *GOVERNMENT ENTERPRISE* 39 (1970).

24. See, SPIRO, *supra* note 13, at 5, 35-36, 39-41 (1958).

25. See, Friedrich, *German Co-Determination: Parity Is the Goal*, COLUM. J. WORLD BUS., Jan.-Feb. 1970, at 49. DE HOUGHTON, *supra* note 13, at 220-21, 361-68, 370; Winkhaus, *Co-Determination of Employees in West Germany Companies*, 27 THE BUSINESS LAWYER 879, 882 (1972).

26. See, note 20 *supra*; Geijer, *Industrial Democracy in the Seventies*, FREE LABOR WORLD, Apr. 1971, at 15.

ized industries in 4 countries. After observing that nationalization represented a reaction to foreign ownership rather than a movement for social reform, he notes that there has been provision for substantial employee representation on the Boards of nationalized Latin American industries, including electric utilities in Argentina, tin in Bolivia, copper in Chile, and oil and railways in Mexico. The Peruvian industrial reform law also provides for employee membership on the Board.<sup>27</sup>

*C. Problems Presented by Reform Proposals Generally.* The proposals for employee representation on the Board presents serious problems.

1. *Limitations on the Applicability of the European Experience.* There is a complete lack of United States experience. All we can do is speculate how solutions attempted in cultures abroad might function at home. It is evident that experiments in industrial organization abroad may provide some insight and understanding in appraising possible change in American industrial organization to deal with the known problems of the existing order. This does not mean, however, that European models may be expected to function in the same manner in the vastly different climate in the United States. The European experience reflects German solutions to German needs and Yugoslav solutions to Yugoslav needs. To lift these solutions from their political, economic, historical and cultural setting and transport them to the United States is of dubious validity. As Professor Carl Friedrich has noted, co-determination is "deeply imbedded in German past experience and traditions."<sup>28</sup> There are no parallels in the United States.

2. *Conflict of Interest.* To whom would the employee director owe primary loyalty? Under traditional corporation law, the director owes undivided loyalty to the corporation and to the shareholders; further, such loyalty runs to all shareholders and not merely to those who elected him.<sup>29</sup> Would not the "special interest" director designated to represent the interests of the group responsible for his designation be confronted with a fundamental conflict of interest?

British nationalized industries have sought to avoid this problem by requiring primary loyalty to the corporation. Labor directors added to the Boards of nationalized firms have been required to resign all formal affilia-

27. See, Bàyitch, *Empresa in Latin American Law: Recent Developments*, 4 LAWYER OF THE AMERICAS 399, 429-33 (1972); N.Y. Times, Oct. 5, 1972, at 16, col. 1; Wall St. J., Aug. 4, 1972, at 6, col. 4.

28. C. J. Friedrich, Introduction, in SPIRO, *supra* note 13, at viii (1958). Fogarty similarly demonstrates how co-determination reflects more than 100 years of German experience. See, M. FOGARTY, *supra* note 3, at 60-153 (1965).

29. E.g., Parke v. Daily News Ltd., [1962] Ch. 927, 963; Dodge v. Ford Motor Co., 204 Mich. 459, 170 N.W. 668 (1919). ("A business corporation is organized and carried on primarily for the profit of the stockholders. The powers of the directors are to be employed for that end.") See, H. HENN, LAW OF CORPORATIONS 475 (2d ed. 1970); L.C.B. GOWER, PRINCIPLES OF MODERN COMPANY LAW 474-76 (2d ed. 1957). But see, L.C.B. GOWER, *supra* note 4, at 523-24 (Twelve years later, Prof. Gower regarded the traditional view as "increasingly anachronistic" and concluded: "Further developments in the law in this respect seem inevitable—and overdue").

tion with the trade union movement. The labor directors come to the Board as persons with a trade union perspective, but not as representatives of the trade union movement. The same pattern has occurred in Norway.<sup>30</sup>

If, however, the employee director comes not simply as a person with a labor perspective, but as a "representative," the problem of conflict seems inevitable so long as there is no corresponding change in the objectives of the enterprise.

This would be the result if isolated employee "representatives" were added to the Boards of American Corporations as presently constituted. On the other hand, if the concept of "special interest" representation were accompanied by a broadening of the objectives of the corporation and the advancement of shareholder interests were no longer the primary goal, the premise of undivided loyalty to shareholders would disappear. The question would then arise whether the loyalty of the employee director to the workers or union which designated him was inconsistent with the new objectives set for the enterprise.

Thus, it would appear that in the end, "special interest" representation accompanied by restatement of the goals of the corporation would require the fashioning of new fiduciary standards for directors to reflect the changed composition of the Board and the revised objectives of the corporation. Such standards would almost inevitably involve the realization that except in most unusual circumstances, "special interest" representatives would place loyalty to the group which designated them and which they represent above all other loyalties: whether to the enterprise as a whole, the community, or the nation.

The Board would then function essentially as a political institution. There is a serious question whether such a Board could effectively function in the face of the pressures on the individual Board members to advance the interests of the groups which they represent. Thus, in France, the tri-partite structure of nationalized corporations with government, employee, and consumer directors has been strongly criticized as resulting "in a constant tug-of-war between the different representatives and interests instead of providing a balanced administration in the public interest."<sup>31</sup>

3. *Effectiveness of the Employee Director.* Without regard to the troubling question of loyalties, the imposition of a minority number of employee directors upon an unwilling Board may accomplish little. The hostility of the majority of the Board may remove much of the significance of the development. If decisions are made in caucus prior to the Board meeting which is then reduced to an empty formality, if there is an inadequate flow of information, if there is limited cooperation from management, the employee di-

30. See, W. FRIEDMANN & J. GARNER, *supra* note 23, at 39 (1970); A. STURMTHAL, *WORKERS COUNCILS* 56-57 (1964); W. ROBSON, *NATIONALIZED INDUSTRY AND PUBLIC OWNERSHIP* 217 (1960); M. FOGARTY, *A COMPANIES ACT 1970?*, at 75 (P.E.P. No. 500, Oct. 1967); F. EMERY & E. THORSRUD, *supra* note 9, at 13 (Norway).

31. See, W. FRIEDMANN & J. GARNER, *supra* note 23, at 113, 315; Jacoby, *Who Should Be on the Board?*, *CENTER MAGAZINE*, Jan./Feb. 1972, at 73, 74.

rector will not be able to function effectively, as illustrated by the German experience with partial co-determination. Minority representation has built-in limitations.

4. *Wisdom of the Proposal.* A fundamental objection may be made to the wisdom of the proposal. What is the objective? Is it to advance the interests of the employees of the firm? Is it to advance the interests of employees generally in the society? Is it to advance the "public interest"?

It is clear that employee Board representation may be desired in order to introduce a measure of countervailing power in the highest levels of the corporation that will strengthen the position of employees in the firm versus the management. As noted previously, many trade unions, particularly in England, have not always been convinced that this is in fact the case, and have concluded, at least in the past, that union power would be compromised and weakened by representation on the Board. In contrast, the German unions have firmly embraced the principle. Employee representation regarded in this light merely becomes a new chapter in labor relations, although on a grand scale. The values involved relate to the relative positions of labor and management in the society, and the social desirability of further strengthening union power as well as the question of the appropriateness of achieving such an objective through the device of restructuring the corporate organization rather than in some other manner, such as the collective bargaining process.

If, however, employee representation on the Board is regarded as a method of advancing the interest of workers as a whole, not merely those employed by the corporation, the German and the Yugoslav experience would both appear to demonstrate that it is unlikely that any such objective will be achieved. Worker power on the Board is reflected in improved conditions for workers in the corporation. It does not appear to be concerned with the aspirations and problems of workers elsewhere in the country.

If this is the case, it is even more doubtful to expect that employee representation will advance the interest of the public as a whole. After all, it is "special interest" not "public interest" representation which is being proposed.

There is a further consideration. Employee representation transfers to the Board level the struggle between the competing interests. It is far from clear that it is desirable to have labor negotiations conducted in the Board room. In view of the significant impact that the ultimate terms of the labor bargain have on the society as a whole, there are major advantages in having the conflict conducted in the traditional arena where public scrutiny is possible and where public attitudes may influence the result.

To the extent that the proposal for employee representation is intended as a method of increasing union power, it may also fairly be asked whether such representation is required to enable the major unions to deal in equal terms with the major industries, whether such representation would advance the interests of any group other than the workers directly affected, and whether

employee directors are any more likely than other directors to be concerned with the impact of the corporation's operations on the consumer, on the community, on the environment, or indeed, on other workers generally.

5. *The Significance of the Proposal.* The discussion of employee representation on the Board requires at least passing reference to the fundamental question of whether the Board of Directors does in fact determine corporate policy or whether the non-management or "outside" directors are relatively impotent prisoners of senior management or the chief executive officer. To the extent that "outside" directors are part-time and under-compensated, lack staff support, and are not truly independent of the management which has designated them in the first place, there are increasing doubts as to the realities of Board power, except perhaps in rare times of crisis. The ultimate question accordingly is whether employee representation, although independent, could have a significance that would transcend the existing limitations on the exercise of corporate sovereignty by the Board.

### III. Employee Stock Ownership

Employee stock ownership as a method of increasing employee participation in the control of the corporation and assuring a role in the decision-making process has made relatively little progress either in the United States or in Europe.

A. *Indirect Ownership through Employee Benefit Funds.* A major problem in the development of a sufficiently large employee equity stake in the enterprise to create a significant employee influence in management or participation in profits has been the difficulty of accumulating the substantial capital required. The employee trust fund, investing in the purchase of shares of the employer corporation, provides a possible alternative to accomplish this result.

The influence on management will depend on the procedure for voting the shares held by the trust. In the typical case, where the shares are voted by trustees appointed (and often subject to removal) by the Board of Directors, the employee trust fund—far from increasing the relative power of employees—becomes a device for further strengthening the entrenched position of management through the creation of captive votes.

Where an enlightened management wisely declines the opportunity to vote a large bloc of trust-held shares for itself and provides for "pass-through" voting by the employee-beneficiaries, a framework has been created under which employees as a group conceivably play a significant role as indirect shareholders.<sup>32</sup>

32. See, Eisenberg, *Megasubsidiaries: The Effect of Corporate Structure on Corporate Control*, 84 HARV. L. REV. 1577, 1597-98 (1971); Hone, *Pass Through Voting: An Analysis*, 17 PROFIT SHARING, Oct. 1969, at 22 (Hone lists 101 such corporations). The New York Stock Exchange requires as a condition of listing that corporations with approximately one per cent or more of their voting shares held by the corporation's pension or similar fund establish procedures for pass-through voting.

An outstanding instance is Sears, Roebuck & Company, where 20.4% of the outstanding shares (or more than \$3.6 billion market value) were held by the Sears Savings and Profit Sharing Pension Fund for the benefit of 222,866 participants as of December 31, 1971 and voted on a "pass-through" basis by vested participants under a procedure that assured a secret ballot.<sup>33</sup> This procedure theoretically permits effective control of the corporation by the participants. However, there is no indication that employees have attempted to exercise such control or, indeed, desire to do so. Further, the participants with an average interest of approximately \$17,000 each in the trust fund no doubt regard their indirect interest in the corporation as an investment rather than as a form of industrial democracy. The participant as investor has supplanted the participant as employee.

*B. The Kelso Plans.* Mr. Louis Kelso has advocated plans under which undercapitalized firms would raise needed capital utilizing pre-tax dollars through tax-deductible contributions to qualified pension or profit sharing trust funds (or through bank loans to such funds in anticipation of such contributions), which in turn would be re-invested in the purchase of company shares. The participating corporation receives back not only its contribution, but realizes a tax saving as well, which at a 50% rate would provide the corporation with twice the amount available if it had simply retained the earnings in the first place. The corporation shares are ultimately distributed to the employees. Thus, a measure of employee ownership is achieved. Presumably over a long enough period, the bulk of outstanding shares would be employee-owned. Although the Kelso Plan has attracted increasing attention, it involves serious potential dilution for existing shareholders, and obviously has appeal only to capital-hungry firms unable to raise funds through any other route. A variation of the Kelso Plan has been proposed by Governor Ferré in Puerto Rico.<sup>34</sup>

Whatever the usefulness of the Kelso Plans as methods of raising capital, they will not hold out serious promise for significant social change unless employees regard the shares not as an investment, but as enfranchisement

33. SEARS, ROEBUCK & CO., NOTICE OF ANNUAL MEETING AND PROXY STATEMENT, Apr. 20, 1972, at 1, 4; Letter to Fund members dated Apr. 23, 1971 from Austin T. Coleman, Chairman of the Board of Trustees of the Sears Savings and Profit Sharing Pension Fund. Contrast Federated Department Stores which has successfully resisted demands for the institution of a pass-through voting system with respect to its 3,137,249 shares (or 7.2% of the outstanding shares) held by its Retirement, Income and Thrift Incentive Plan. FEDERATED DEPARTMENT STORES, INC., REPORT OF THE ANNUAL MEETING OF SHAREHOLDERS, June 1, 1971, at 2; L. & J. GILBERT, THIRTY-SECOND ANNUAL REPORT OF SHAREHOLDER ACTIVITIES AT CORPORATION MEETINGS 251-259 (1971).

34. L. KELSO & P. HETTER, TWO-FACTOR THEORY: THE ECONOMICS OF REALITY (1967); Kelso, *The Invisible Violence of Corporate Finance*, INVESTOR RELATIONS 1972 (Proceedings of 2d Annual National Conference of National Investor Relations Institute, Nov. 1, 1971), at 133; Kelso & Hetter, *Man without Property*, BUS. & SOC'Y REV., Summer 1972, at 14; see, Henderson, *Radical Capitalism*, BUSINESS TODAY, Autumn 1970 at 10; BUS. WEEK, Nov. 20, 1971, at 86; N.Y. Times, Jan. 16, 1972, § 1, at 29, col. 1.

leading to employee participation in the direction of the enterprise. The Sears, Roebuck experience does not indicate that this is likely.

Further, the stake of each individual employee in the corporation through such stock ownership must be significant enough to produce such a meaningful change in his fundamental attitudes. As Robert Heilbroner has noted, a relatively trivial equity stake in the corporation has only a tangential relationship to the achievement of significant participation in decision-making.<sup>35</sup>

*C. Isolated United States Experience.* There is some limited experience in the United States with employee-owned concerns. Recently, the Chicago & Northwestern Railway was sold to a newly organized corporation owned by 1,000 of the railroad's 13,500 employees, including senior executives, who invested approximately \$3,600,000. This appears, however, to represent more an ingenious method for the parent, Northwest Industries, Inc., to divest itself of its railroad operations and \$338,804,000 of railroad debt. It hardly constitutes a grass-roots effort by employees to achieve a new society. Thus, the three-man Board of Directors of the employee-owned enterprise consists of two senior executives and an outside director, who also are trustees of a trust, which will hold the sole right to vote for directors and certain other matters for a ten-year period.<sup>36</sup>

Other isolated examples of firms in which employees have a significant equity interest include Levi Strauss & Co., Lincoln Electric (Cleveland, Ohio), American Cast Iron Pipe Company (Birmingham, Ala.), and Merimack Hat Company (Amesbury, Massachusetts) now in dissolution. There are no signs that these examples represent any significant trends or any meaningful employee participation in management.

#### *D. The European Experience.*

*1. France.* Approximately 5 years ago, Premier Charles De Gaulle undertook to introduce "popular capitalism" into France by partial distribution of "surplus profits," after dividends and adjustments, to employees in the form of shares of stock of the corporation, with the ultimate objective of substantially broadening employee ownership of corporate enterprise. Equity participation within the firm was to be a new middle way between socialism and capitalism.

Under the decree of August 17, 1967, employees of all French companies with more than 100 employees became entitled to a statutory right of profit sharing.

35. Conversation with R. Heilbroner, *On Power and the Corporation*, BUS. & SOC'Y REV., Summer 1972, at 10, 12. See, N. ROSS, THE DEMOCRATIC FIRM 3-4 (Fabian Research Series 242, 1964) ("The employee-shareholder remains predominantly a wage or salary earner and in any fundamental conflict of interest within the firm, is unlikely to be deflected from the pursuit of his primary interest. . . . Employee-shareholding is, in fact, a rather neat way of dodging the fundamental issue of employee rights in modern industrial society.")

36. CHICAGO & NORTH WEST TRANSPORTATION CO., OFFERING CIRCULAR, May 5, 1972, at 10, 20, 35-36, 47; Wall St. J., Oct. 6, 1970, at 2, col. 1, June 2, 1972, at 2, col. 2; N.Y. Times, Nov. 22, 1970, § 3, at 2, col. 4; BUS. WEEK, Dec. 9, 1972, at 48.



The program involved the following elements:

(a) The profit-sharing allocation for the benefit of employees was retained by the employer and was available for reinvestment.

(b) The securities allocated to employees were frozen for a five year period and not available for distribution nor transfer by employees, except in the event of death.

(c) As a result of tax incentives, the cost to the employer was negligible so long as its new investment in plant and equipment exceeded the profit-sharing allocation for the previous year. This result was achieved by giving the employer a tax deduction for new investment equal to twice the allocation for the previous year.

Estimates of the impact of the plan vary with the rate of return of the enterprise and the relation of labor cost to total value added. Fogarty provides examples of the operation of the program which appeared in *Le Monde*. These indicated profit allocations of up to 5.7% of total remuneration.<sup>37</sup>

The profit-sharing allocation could be evidenced not only by shares of the enterprise, but also either by debt or by investment certificates reflecting investment in other corporations.

In December 1970, under the program, Renault, the state-owned automobile corporation, distributed to 45,600 employees a total of 542,000 shares with a market value of \$9.8 million, or an average of more than \$200 per employee. This represented 4.5% of the outstanding shares. The distribution was made according to seniority and rank to white and blue collar employees with 5 years of service.<sup>38</sup>

This program, sponsored by left-wing Gaullists, such as Louis Vallon, met bitter opposition from both the right and left wings of French politics, who viewed it as dangerous radicalism on the one hand, or as an inadequate palliative, distracting workers from a major reconstruction of the social and economic order, on the other. The program has lost support and been rejected as unsuccessful.

2. *English proposals.* There has been discussion in England of the desirability of restricting stockholders to a fixed return. "Excess" earnings would be reallocated for the benefit of employees, either directly or through capitalization, with the shares evidencing the capitalized earnings distributed to employees who would ultimately come to control the enterprise. Still another suggestion has been a program for allocation of a portion of earnings as a mandatory sinking fund to redeem non-employee owned shares over

37. See, DEHOUGHTON, *supra* note 13, at 80, 107-16; Law No. 67-673 of August 17, 1967 implemented by Decree No. 67-112 of Dec. 19, 1967; FOGARTY, *supra* note 30, at 112-15; 2 CCH COMM. MKT. REP. ¶6567; FOGARTY, *supra* note 3, at 112 (correction sheet); Marty-Lavauzelle, *Labor Law Developments in France*, 27 THE BUSINESS LAWYER 857, 857-58 (1972).

38. Wall St. J., Dec. 14, 1970, at 7, col. 2.

the long term, as an alternative method of ultimately achieving full employee ownership.<sup>39</sup>

There is no indication that these proposals have attracted significant support.

3. *German proposals.* The German trade unions have urged a profit-sharing program that contrasts sharply with the French statutory reform and the English proposals which have sought to achieve ultimate transfer of ownership of the firm to employees. The German unions in the past have proposed that a portion of earnings be transferred to investment trusts, in which all employees, including those in other industries and in public service, would participate. Thus, workers would participate in a diversified trust portfolio rather than in shares of their employer.<sup>40</sup> This German proposal rested on ideological considerations. The German unions deemed it undesirable for workers to identify too closely with their own enterprise lest they be tempted to advance their parochial plant interests at the expense of the working class, or community, as a whole. In the current election, the Social Democratic party is pressing for a program to give workers an ownership stake in German companies.<sup>41</sup>

E. *Peru.* Following the revolution in Peru four years ago, the new military government instituted an industrial reform law under which workers receive 10% of profits before taxes in cash and 15% in shares to be distributed until employees control one-half of industrial companies. Initially, there is one employee board member, with provision for increase as employee stock ownership increased. Businessmen anticipate loss of control over their businesses in 5 to 10 years. Related statutes were also enacted with respect to fishing, mining and telecommunications companies.<sup>42</sup>

F. *World-wide Voluntary Experiments in Employee Ownership.* There have been occasional experiments in various countries to establish some form of industrial democracy where private firms have been dedicated by their owners to employee ownership. Thus, Mr. George Goyder has provided a detailed description of the system established in 1896 for the Carl Zeiss Works in Germany. We have already noted parallel developments in the United States. The common aspect of such developments, notwithstanding their innovative character, is that they are no more than isolated experiences usually reflecting personal or family philanthropy rather than any social movement of significant strength.<sup>43</sup>

39. See, G. GOYDER, *supra* note 1, at 93-96, 98, 108-20 (1951); G. GOYDER, THE RESPONSIBLE COMPANY 81-82, 104-05 (1961) FOGARTY, *supra* note 30, at 99-100; L.C.B. GOWER, *supra* note 4, at 62.

40. See, M. FOGARTY, COMPANIES BEYOND JENKINS 55 (P.E.P. No. 486, Feb. 1965), FOGARTY, *supra* note 3, at 182-83.

41. See, BUS. WEEK, Oct. 7, 1972, at 42; Friedrich, *German Co-Determination: Party Is the Goal*, COLUM. J. WORLD BUS., Jan.-Feb. 1970, at 49.

42. See, Bayitch, *supra* note 27, at 424-25, 429, 432; N.Y. Times, Oct. 5, 1972, at 16, col. 1; Wall St. J., Aug. 4, 1972, at 6, col. 4.

43. G. GOYDER, *supra* note 1, at Appendix B; Ulman, *Bringing Robert Owen Up to Date*, Wall St. J., June 23, 1972, at 11, col. 3.

G. *Summary.* Nothing in the experience to date with employee ownership through accumulation of shares indicates that this alternative will be a major factor in the reallocation of corporate power or in increased participation by employees in corporate affairs.

#### IV. Employee Concern with Job Security; Resistance to Take-Overs and Mergers

Notwithstanding the acceleration of merger and takeover activity in the United States, there has been little pressure for statutory protection of affected employees. On isolated occasions, there has been employee resistance to the take-over. Thus, an attempted raid on Endicott Johnson was defeated with the assistance of employees, who purchased shares to help defend the local management. This is a rare instance of corporate "loyalty" on the part of employees, attributable, no doubt, in large measure to the extent of identification of the firm with the local area and a xenophobic reaction to outsiders.<sup>44</sup>

In Europe, however, there has been statutory protection under which consultation with employees is required for mergers, relocation, and shutdowns. Thus, both the German Works Council Act, 1972<sup>45</sup> and the Netherlands Employees Council Act, 1971,<sup>46</sup> require consultations with the works council on such matters, with elaborate procedures for mediation in the event of disagreement. This is employee participation in decision-making on the high strategic level.

The English have no comparable requirement. However, concern with reduction in the number of employees following takeovers led English unions to join with the management of Watneys in an unsuccessful effort to resist the recent takeover by Grand Metropolitan Hotels as well as to oppose other takeovers.<sup>47</sup> This was a form of "corporate loyalty" comparable to the Endicott Johnson experience. Similarly, the English have become increasingly concerned with "asset stripping: or the takeover of firms, with the intent to reduce the scale of operations and the number of employees and to achieve recovery of the bulk of the purchase price through the sale of the redundant assets. This practice has become increasingly controversial, because of the adverse impact on employees."<sup>48</sup>

44. See, Mahoney, *What Happened at Endicott Johnson after the Band Stopped Playing*, FORTUNE, Sept. 1962, at 126.

45. CCH, GERMAN WORK COUNCILS ACT 1972, §§ 111-13.

46. See, Van de Ven, *Corporate Developments in the Netherlands*, 27 THE BUSINESS LAWYER 873, 874-75 (1972).

47. See, letter to shareholders dated May 1972 of Watney Mann Trade Union Defence Council ("For how much longer can the practice of buying and selling the future of loyal workforces, and the dissolution of famous Company names be allowed to blemish the social and industrial fabric of this country"?); London Financial Times May 31, 1972, Aug. 4, 1972, Sept. 19, 1972. I am grateful to Eli Goldston, Esq. for calling these materials and those cited in note 43 *infra* to my attention.

48. London Sunday Times, June 11, 1972 at 59; The Guardian, June 9, 1972; London Financial Times, Oct. 24, 1972; THE LISTENER, June 15, 1972, at 789-90.

### V. New Developments with respect to the Employee's Duty of Loyalty and Obedience

With general acceptance of the concept of corporate social responsibility and with the major public corporation assuming a role of increasing significance in social problem solving, there is increasing expression of a new, and still controversial, view that the corporation should be regarded as a social institution to achieve social objectives, rather than as an economic institution to be operated for economic objectives for the benefit of shareholders. This new view of the corporation has a dramatic impact upon traditional concepts of the duties of loyalty and obedience of the employee to his employer, firmly recognized in the law of agency.

The conflict is illustrated by the increasing number of recent developments relating to the right of the employee of the large public corporation to take action adverse to the interests of his employer, reflecting his personal view as to the proper social responsibility of his corporate employer.

In view of the limited time available today and the fact that I have elsewhere discussed this interesting development at considerable length in a recent article,<sup>49</sup> I shall do no more than sketch hastily some instances that have sharply posed these questions.

(1) Mr. Ralph Nader has established a Clearing House for Professional Responsibility and has urged employees to disclose information about their employers' practices that they consider harmful to public or consumer interests. Mr. Nader terms this "whistle-blowing" and calls for employee disclosure whenever in the employee's judgment "responsibility to society transcends responsibility to his organization."<sup>50</sup>

(2) Another example involves Eastern Air Lines. The airline's procedure required pilots after take-off to jettison in the atmosphere a small amount of excess fuel. A senior pilot had unsuccessfully sought to have the procedure changed to permit draining on the ground and thereby avoid atmospheric pollution. He thereon violated the regulation and had the fuel drained while on the ground. Eastern discharged him, pointing out that "each of its 3,700 pilots cannot make his own rules." After considerable publicity and union pressure, the pilot was reinstated.<sup>51</sup>

(3) A third example is the attempt of a small number of black employees calling themselves the Polaroid Revolutionary Workers Movement to force Polaroid to cease doing business in South Africa by "confrontation" tech-

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49. Blumberg, *Corporate Responsibility and the Employee's Duty of Loyalty and Obedience: A Preliminary Inquiry*, 24 OKLA. L. REV. 279 (1971) reprinted in *CORPORATE COUNSEL'S ANNUAL*—1972, at 3 (1972).

50. See, R. NADER, P. PETAKS, & K. BLACKWELL, *WHISTLE BLOWING* (1972); N.Y. Times, Jan. 15, 1971, at 43, col. 2, Jan. 27, 1971, at 32, col. 3, Mar. 21, 1971, § 6, at 16, col. 5; Branch, *Courage Without Esteem: Profiles in Whistle Blowing*, WASHINGTON MONTHLY, May 1971, at 23.

51. TIME, Nov. 2, 1970, at 40; Boston Globe, Nov. 8, 1970, at 2, col. 3.

niques including boycott of Polaroid products and picketing, disruptions and demonstrations. Polaroid responded on a number of levels, including the use of an advisory committee of employees who visited South Africa. Eventually, Polaroid suspended one of the leaders of the movement without pay "for her persistent activities in fomenting public disapproval" of the firm and for being "involved in a deliberate campaign calculated to damage the "well being" of the company."<sup>52</sup>

(4) A final example is the Ohio steel worker who was suspended for five days for refusing to obey a foreman's order to dump oil and other wastes into the Cuyahoga River. After a threat of a wildcat strike by the United Steel Workers local, the employee was reinstated.<sup>53</sup>

These acts reflect a new view of responsibility on the part of employees: a view that the employee's duty as a citizen transcends his duty as employee, a view that the employee should act primarily for the good of the country—*i.e.* the public interest—rather than for the good of the employer. They also may involve a different concept, a view that employees should play a part in the corporate decision-making process, particularly in issues of public concern involving questions of corporate social responsibility.

These manifestations provide an insight into forces making for a changing relationship of the employee to the corporation that, in my opinion, may well prove to be more significant in the United States than the academic proposals for employee representation on the Board and employee ownership of stock.

## VI. Prospects for Acceptance of Reform

There is no indication at the present time that radical change in the American corporate structure to include employees representation in the senior councils of the corporation is apt to become a serious possibility in the near future. Until the proposal for employee representation is adopted and vigorously pursued by American trade unions, it is purely a theoretical suggestion. Further, there is the inescapable fact that American trade unions do not represent American employees as a whole. Out of a total labor force of 83,000,000,<sup>54</sup> only 20,000,000 are union members.<sup>55</sup>

Nevertheless, there are powerful factors at work at fundamental levels which in time could make the possibility of employee representation, in particular, a challenging reality. Accordingly, the possibility of such a development cannot be dismissed.

*A. Changing Attitudes of Employees.* It is clear that the fundamental rela-

52. Boston Globe Oct. 18, 1970, at 64, col. 2, Nov. 1, 1970, at B-31, col. 3, Nov. 25, 1970 at 7, Feb. 11, 1971, at 3, col. 1; N.Y. Times, Jan. 13, 1971, at 9, col. 1, at 23, Feb. 21, 1971, at 17, col. 1; BUS. WEEK, Nov. 14, 1970, at 32; NEWSWEEK, Jan. 25, 1971.

53. N.Y. Times, July 26, 1971, at 50, col. 7.

54. DEP'T OF COMMERCE, STATISTICAL ABSTRACT OF THE UNITED STATES 210 (1971).

55. *Id.* at 234.

tion of the employee to the employer is undergoing change. The attitudes of employees toward work are a matter of increasing concern. Job alienation, increased absenteeism, increased labor turn-over, declining productivity, resistance to dull and repetitive work assignments, weak morale, hostility toward the production line, are familiar features of the current scene and have made business aware of the importance of increasing job satisfaction. Lordstown is today a part of the vocabulary.<sup>56</sup>

Human fulfillment through participation in decision-making has been recognized as one of the most effective methods of dealing with the problem of worker alienation. Enfranchisement and involvement in job organization, work allocation and production have become established techniques for labor participation.<sup>57</sup> The pressures that make for such participation at the grass-roots level may conceivably over the long pull make for representation on the Board level as well.

Added to this underlying dissatisfaction with work is the growing phenomenon of employee dissent. The emergence of "underground" employee newspapers, highly critical of employer policies,<sup>58</sup> leafletting on company premises,<sup>59</sup> and boycotts by employees protesting company attitudes,<sup>60</sup> the phenomenon of "whistle blowing" or unauthorized disclosure of company conduct deemed socially undesirable by the employee in question<sup>61</sup>—all illustrate the current ferment. Employer-employee relationships are obviously being affected by the profound and accelerating change in society itself. The magnitude in the degree of change of values, of attitudes, of so-called consciousness may conceivably create a social and political climate in which employee representation on the Board—entirely visionary at the present time—could become a realistic possibility in the future.

The foregoing factors will undoubtedly strengthen a movement toward greater job participation and employer-employee interaction at the grass roots level. Such a movement may well mean greater employee participation in the decision-making process on the lower levels of management. This may in turn lead ultimately to pressure for employee representation on Board level. However, a number of students of worker participation have concluded that Board representation may be distinctly less useful and less important in

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56. BUS. WEEK, Sept. 9, 1972, at 79, 108 (Special Issue on Productivity); Mar. 4, 1972, at 69; Wall St. J., Aug. 21, 1972, at 1, col. 6, Sept. 12, 1972, at 12, col. 3.

57. See, note 9 *supra*.

58. BUS. WEEK, Oct. 9, 1971, at 86; BUS. & Soc'y, Sept. 5, 1972, at 2; Wall St. J., Nov. 3, 1971, at 16, col. 2.

59. CORPORATE INFORMATION CENTER, CORPORATE EXAMINER 5 (Sept. 1972). (2,000 anti-U.S. Savings Bonds leaflets distributed as an anti-war demonstration at Bell Laboratories, Holmdel, N.J.)

60. N.Y. Times, Feb. 21, 1971, at 17, col. 1 (Polaroid Chemist, leader of Polaroid Revolutionary Workers Movement, dismissed for organizing a boycott of Polaroid products to protest its business in South Africa).

61. See, note 50 *supra*.

achieving the values that flow from worker participation than opportunities on the plant level.<sup>62</sup>

Further, these elements may emerge as a part of the political scene if there is any development of a populist political movement. Political challenge to the large corporation will almost inevitably include, among other things, proposals for the introduction of employees into the senior decision-making processes of the corporation.<sup>63</sup>

*B. Federal Incorporation.* The development of interest in federal incorporation of major corporations<sup>64</sup> may create the stage for consideration of employee representation on the Board. The increasing abdication by the various states of control over the internal conduct of corporate affairs and increased concern with the role of the large corporation in society make enactment of a federal incorporation statute within the next 15 years a realistic possibility.<sup>65</sup>

The open question is the substantive content of any such statute. That is quite another question, and one for which we have little glimpse as to what may be expected. It is clear, however, that consideration of such a fundamental departure as a federal incorporation statute would inevitably involve a basic review of possible areas of corporate reform. Consideration of employee representation on the Board would find a priority place on any such agenda.

*C. Impact of the European Experience.* A third fundamental factor is the strength of the movement for employee directors outside of the United States. The world is increasingly becoming smaller and the experiences of other nations increasingly significant at home. The widespread European acceptance of employee representation on the Board will unmistakably have impact on American business attitudes.

In addition, the multi-national experience of many large American corporations has profound implications. Firsthand experience with the reality of employee representation can only increase understanding of the proposal and reduce resistance to it. Business that operates its foreign subsidiaries successfully notwithstanding employees on the foreign subsidiaries' boards can-

62. See, PAUL BLUMBERG, *supra* note 9, at 2-3; F. EMERY & E. THORSRUD, *supra* note 9, at 10.

63. See, J. NEWFIELD & J. GREENFIELD, *A POPULIST MANIFESTO* 173 (1972).

64. See, Schwartz, *Federal Chartering of Corporations: An Introduction*, 61 GEO. L. J. 71 (1972); Note, *Federal Chartering of Corporations: A Proposal*, 61 GEO. L. J. 89 (1972); Note, *Federal Chartering of Corporations: Constitutional Challenges*, 61 GEO. L. J. 123 (1972) Nader, *The Case for Federal Incorporation* Address, Conference on Corporate Accountability, Oct. 30, 1971; Flynn, *Corporate Democracy—Who Needs It?* Address, Conference on Corporate Accountability, Oct. 30, 1971; N.Y. Times, Jan. 24, 1971, § 3, at 1, col. 3.

65. Cf. Senator Hart (Michigan) who favors federal incorporation informed a Georgetown Law Center seminar in February 1972 that "my most optimistic guess is that we might get six votes right now in the whole Senate." (Statement from Office of Sen. Hart for release Feb. 3, 1972.)

not readily contend that such representation produces unworkable results.

Recognition of the dual board structure and employee representation will clearly receive further impetus in the event the Common Market adopts the European Company Draft Statute which incorporates these concepts.

Further, the British entry into the Common Market will encourage British consideration of the principles of partial co-determination and of the dual board embodied in the European Company Draft Statute. This will accelerate the educational process by which American business becomes more familiar with the concept of employee representation. British law and institutions exert considerable influence on American thought. If partial co-determination crosses the Channel to Great Britain, the chances of its jumping the Atlantic are considerably increased.<sup>66</sup>

Finally, the objective of the extension of full co-determination, or 1/2 membership on the Supervisory Board, to German industry generally has been firmly embraced by the German trade union movement and by the Social Democratic Party. If accepted in Germany, the reverberations will clearly have a wide range of influence.

## VII. Conclusion

Employee representation is presently no more than a topic for academic discussion in the United States. Nevertheless, there are deep-seated underlying forces that could conceivably make proposals of this nature a matter of realistic concern in the future.<sup>67</sup>

**MR. GEORGE D. GIBSON:** Our next speaker, with three Harvard degrees, might well be expected to prove a perceptive traditionalist. On the contrary, he is distinguished for his originality and innovation.

**MR. ELI GOLDSTON:** As an erstwhile lawyer, I would remind you that you can take the boy out of the law, but you can't take the law out of the boy. So to the extent that a lawyer becomes a businessman, when he looks at his function he carries with him some of the lawyer's traditional concern for logic and legitimacy in the things he does. He looks for reason and he looks for morality because he wants to feel that what he is doing carries with it a sense of rationality, and a sense of continuity of a moral tradition. As a consequence, as more lawyers run more businesses, and as more business school graduates run more businesses, the function of the lawyer in relationship to the larger corporation is going to change a little because he is going to find that—as I am going to turn to a bit later—"maximization" is no longer an adequate economic description of a professionalized business management.

At the same time, the business manager can't run around just trying to be loved by everybody—perhaps by doing as Professor Phillip Blumberg sug-

66. See, Vagts, *The European System*, 27 THE BUSINESS LAWYER 165, 168 (Special Issue, Feb. 1972).

67. See, Shonfield, *Business in the Twenty-First Century*, DAEDALUS, Winter 1969, at 202-3.



gests—having employees on your Board of Directors, women, some blacks, some homosexuals—just to make everybody happy!

Making everybody happy simply is not the essential function of an economic organization in our business society.

You know, there is an old Israeli story about an elderly gentleman who was taking his grandson to town on a very hot day in the summer when it was about ninety degrees in the shade and there wasn't any shade. They had a donkey and the grandfather put the weary little boy on the donkey. As they went down the dusty road they came to a corner, and a fellow was there who said, "Little boy, this is awful! Your poor, tired, old gray-haired and bearded grandfather is walking in the dusty road and you are riding on the donkey!"

So the grandfather said, "You get off. I'll get on. Keep him happy."

They went on down the road a little bit and another fellow sitting along the roadside said, "Old man, you are riding on that donkey, and your little grandson is trudging in the dust. He's only a little fellow and the dust is getting into his nostrils. The poor kid will drop dead!"

So the grandfather reached over and scooped up the little boy and put him on the donkey with him and they went around the next corner. There they ran into a chap from the Israeli branch of the Society Against Cruelty to Animals, and this fellow said, "You two human beings riding on that poor donkey! It is ninety degrees in the shade. A human being can barely struggle along the dusty road and you two guys are riding on one little donkey!"

The grandfather said to the little boy, "Let's get off." Then he noticed a tree on the side of the road, a little sapling, and he cut it down. He said to the little boy, "Look, I am done with criticism!" So they made a kind of a pole and they tied the donkey's two front feet together and his back feet together, and they put the pole between them, and the little boy took one end of the sapling, and the grandfather took the other end, and down the dusty road they went, carrying the donkey hanging from the sapling.

Soon they came to a little bit of a river and tried to ford it. The tired little boy stumbled, and the donkey fell into the little river, feet tied together. The donkey couldn't help himself and he drowned.

One might say that this story proves the difficulty of achieving consensus—or, as they say in Israel, if you try to please everybody, you are going to lose your ass!

That, I think, is the fundamental thing for counsel to remember when you advise the businessman that he has to be kind to labor and be nice to the women and help out the homosexuals and just do nice things for everybody. Primarily the function of your businessman client is to bring some profit down to the bottom line so that the business can survive. To the extent that there is criticism of business concentration on the bottom line, it is really very irritating sometimes for a businessman when he considers the source.

Our gas company in Boston has a better record on improving Negro employment than any university in the State of Massachusetts, with the single

exception of the Harvard Yard Police, and yet every week or so we get letters from various professors and student groups around New England, wanting to know what we are doing about this, and what we are doing about that. It is important for us, I think, as businessmen, to respond to our critics, because, until people realize how complex these things are, they tend to find the wrong devil and exorcizing the wrong devil doesn't solve the problem.

We had some young fellows who came to see us a bit ago about Harvard's ownership of Gulf Oil stock. Some black students at Harvard got mad at Gulf because Gulf is allegedly doing some things in Angola the students dislike. They wanted Harvard to sell its Gulf stock.

Now the theory that Harvard adopted turned out to be not only foolish but expensive. They adopted the theory that John Simon at Yale, another erstwhile lawyer and a present law professor, has suggested—that the duty of a university is to handle its portfolio as an ethical investor. He recently wrote a book called *The Ethical Investor*.

So Harvard said, "Look, how could we possibly sell Gulf? It is a complicated question. Nobody is sure about it. After all, our investment people think it is a good investment and we ought to hang onto it."

Then they spent about several thousand dollars repairing damages and hiring police and having the Commencement attended by earnest young men with big signs about selling Gulf and all of the rest. Meanwhile Gulf stock dropped about twenty per cent in the market. And meanwhile, the Mellon family, who control Gulf, registered a secondary to sell many more shares than Harvard owns. Life isn't very simple and the ethical action isn't so clear in these things.

Some students came in to see me about this time and they said, "Look, you are a Harvard graduate, and we think you can be of great help. We think Harvard should sell its Gulf stock because the Gulf Company is acting immorally in Angola."

My reply was, "I don't think that you have to make that judgment. For all I know Gulf probably is pretty moral in Angola. But I think that a university has no business owning anything that is going to get it into controversy. The function of a university isn't to get into complex controversies with ardent professors and ill-informed students. Its function is to provide an education, and the reason it should sell Gulf is a political matter. It should have gotten the hell out, but it should get out quietly."

"Don't sell Gulf because of Angola. If the university doesn't own any other oil stocks, go out and buy a few, and then sell Gulf and the six other stocks because you have come to the conclusion that you are better off putting the money into equities of retail distribution stores, so that you depart, but you depart gracefully."

But the students had read the book by Professor Simon of Yale Law School, and they said, "This isn't right. We have got to approach it morally

and we want you to bring the moral issue out. Your company has re-housed at one time a seventh of the black population of Boston. We think that your company is the kind of thing that Harvard should own, and we want to carry this controversy one step further. We are not only going to demand that they sell Gulf; we are going to demand that they reinvest the proceeds in your stock."

Well, since our stock at that time was sliding a bit in the market, I had to give that a long, hard thought.

But I figured that my function really was to educate the young men, and so I said, "That's great, because Harvard will not only make a moral investment, they will probably lose money on it, and that will really delight you fellows. But first of all, we have got to let Harvard know about our strip mining operations." And the poor kids leaped out of their chairs. "Strip mining!"

There were those who thought strip mining was better and those who thought it was worse than doing business in Angola, and those who thought both were equally bad, and those who were just confused. They finally stumbled out having, I think learned a lesson.

It is a lesson that I think counsel also needs to learn on these complicated subjects—which is that the businessman has a central concern for the bottom line, but he has also a great many other concerns, and in most areas he has done much better than he gets credit for.

The single largest polluter in almost every city in the United States is the city itself. The single city that pollutes more water in the United States than any other entity in the United States is headed by Mayor Lindsey, and his Commissioner of Pollution, Kretchmer, who wants to succeed him. That would be a real recycling operation!

So you have to say to yourself that you live in a complicated world and the function of the lawyer is to make distinctions clear and to achieve trade-offs. Therefore, when you try to figure out how laws are going to get something done in this complicated society, you have to understand how the society works.

One of the difficulties is the thing that Professor Blumberg mentioned in passing—the notion that management has, or even thinks it has, an exclusive duty to produce maximum profits for the shareholders. That is called "maximizing." When those of you with gray hair like mine studied economics, that was what it was all about—maximizing! And it is all wrong, because businessmen don't maximize.

Now there is an alternative theory, espoused by Professor Galbraith, which is that the management primarily take care of themselves. His argument is that members of management own practically nothing of the company, so their chief goal in life is to climb up some ladder of executive succession and enrich themselves by large amounts of bonuses and salaries and so forth. Since they can get larger salaries if they have a larger company, they really

don't pay much attention to the earnings and to the maximizing—they largely concern themselves with growth, because the bigger the company, the better off they are.

Professor Galbraith isn't entirely wrong. Penn-Central didn't happen because somebody focused with concentrated concern on maximizing return on equity. But the central thrust of business, I think, most economists today would describe as "satisficing." "Satisficing" is something in between maximization and the business world as seen by Professor Galbraith. It describes a political function, and it relates to what Professor Blumberg was talking about in having a Board of Directors with different viewpoints on it.

We don't decide to elect a Committee as President of the United States and have a black and an old person and a young one and a this and a that. We say, "Let's elect ourselves a real shrewd political animal, and in one guy, with fifty-seven political antennae, we will have a representative of everybody."

That is what the theory of "satisficing" is: that business management regards itself as having a primary duty of managing to get something done. And if you are going to manage to get something done, you are not maximizing and trying to make the last buck on every transaction. But if you don't want to spend what little money you have left paying lawyers to defend you from take-over bids, the way our system works, you have got to make a reasonable amount on the equity. So, as a consequence, you "satisfice."

You pay labor what you have to, and now and then you take a strike. You pay the executives what you have to, and once in a while you overpay your brother-in-law!

You pay your suppliers what you have to, to keep them alive and healthy, but you don't overpay them unless you work for Chrysler and own part of the supplier!

So, you end up with a very complicated society that on both analytical and personal grounds has all sorts of complicated cross currents, and that is "satisficing." But central to the "satisficing" is producing enough money on the equity so that the stock will sell at a decent enough price that you will be able to stay in the job.

Once you get this concept of business, you can then deal more intelligently with these questions of social responsibility. I say to myself, how can I, as a business manager, know what I ought to do? Or, you, as either in-house or out-house counsel to a business manager (that is a sort of a contradiction in terms, you know, because it is the in-house who is more privy to the company's secrets)—what do you say to the manager who wants to know what he ought to do?

Of course, there is a very easy answer, "Obey the law!" And the manager says to counsel, "Well, all right, I will obey the law. What's the law?"

"Well", you say, "that is a very complicated question."

That gives you a start on the notion of the brackets within which I think

we work. There is a floor, and the floor is the law, but not as written in the books. After all, practically everybody who has had any trouble with water pollution is being chased after with some law passed in 1885 or something like that. That law has been there a long time, so it is not a question of the law in the books—it is a question of the requirements of the law as society expects them to be enforced. That is a floor of minimum social responsibility.

There is also a ceiling, and the ceiling is set by what I was talking about before—competitive problems. The law requires me to pay my employees what they negotiate out in a labor negotiation, but suppose I love them and want to give them another ten dollars. That is fine if I have a monopoly or a patent or something. But if I am in a bitterly competitive manufacturing operation, I can't pay them more than a penny or two above what the competition pays. And the competition is probably paying the minimum wage, and so I am paying the minimum wage.

On the other hand, there is a lot of leeway generally in most businesses between the ceiling that is set by competition and the floor that is set by legal expectations. I think it is a duty of counsel to remind businessmen that if they can throw money away in all sorts of other directions, if they can keep the eighty-seven year old founding father on the board of directors at a cost of fifteen thousand dollars a year, if they can every once in a while buy insurance from their brother-in-law, then they can afford to raise their contribution to the United Fund and the rest.

Within this range, narrow as it is, you are talking about immense amounts of money.

The average American corporation pays out one per cent of its pre-tax income to charity. I don't think there is any lawyer in the room who wouldn't take on a contingent basis the defense of the company that pays four per cent of its pre-tax income to charity, provided they were earning a reasonably good income. After all, you can deduct up to five per cent.

And if all we did was increase from one per cent to four per cent the pre-tax contributions to charity of American corporations, you would have created a half dozen more Ford Foundations, with all the immense impact that would have on American society.

So, when you come down to what are the relationships of business and law to the social expectations of society, I think that you advise your client, that he has two choices:

If he wants to have some space to sail his boat between the river and the bridge, he can lower his floor, the river, or he can raise his ceiling, the bridge. He can devote himself to trying to lower the river—"let's see if we can't repeal Social Security; that will give us some space to move around!" Or he can try to raise the bridge. He can say, "God, I would love to do it, but the competition won't." Why doesn't he then support a law to require them all to do it?

Being in the coal mining business, I have been through that any number

of times. Every time we talk about doing something about sulphur emissions, there is some coal magnate who says, "My grandma drank that sulphur every spring and she lived to be ninety-seven. I think a man needs a certain amount of sulphur."

Every time we have a big argument about increasing the safety requirements of underground mining machinery, somebody at the meeting always says, "Do you think, while we are at it, we could repeal the last laws?"

What you can do, then, is to persuade your clients that they have an area within which they can operate. You can also persuade them that sensible legislation can raise the river for everyone. And this will maintain the space up to the bridge, because the amount of space competition permits you to do more starts at the new higher level.

That is the guts, I think, of what a businessman today, who worries himself—as a lawyer must also do—about these problems of being logical, and being moral, and surviving. In a changing society, with rising expectations of conduct, you simply have to see that as you raise the level of your conduct, the competition raises theirs, and you are still left enough margin to have some space above minimum legal requirements.

**MR. GEORGE D. GIBSON:** Now for our third topic—the relationship between the corporation and society—which has been assigned to me.

If we still had faith in so-called "progress," business would have everything going for it. But we do not. The one-way street of science, says Jacques Monod, is a

"... path that the Nineteenth Century devotees of progress by science believed would infallibly culminate in a prodigious blossoming of humanity, while nowadays we see opening before us an abyss of shadows."<sup>68</sup>

This is nothing less than a Copernican revolution. It brings to an end all the beatitudes of the last three centuries. No longer can we equate gross national product with happiness. Indeed an increase in production is viewed with suspicion, for fear of its effect on environment, for fear of its effect on humanity itself. As Charles Reich at Yale says:

"... the present transformation goes beyond anything in modern history. Beside it, a mere revolution, such as the French or the Russian, seems inconsequential—a shift in the base of power."<sup>69</sup>

The corporation, as the active vehicle of industry and capital, is naturally identified with the industrial system. Doubts and complaints are therefore directed against it. As Professor Staughton Lynd said:

68. "... trajet que le progressisme scientifique du XIX<sup>e</sup> siècle voyait déboucher infailliblement sur un épanouissement prodigieux de l'humanité; alors que nous voyons aujourd'hui se creuser devant nous un gouffre de ténèbres." JACQUES MONOD, *LE HASARD ET LE NECESSITE* 186 (1970).

69. C. REICH, *THE GREENING OF AMERICA*, 350 (1970).

"Our inevitable enemy in the coming years is the corporation."<sup>70</sup>

Or, as found by Hugh C. Hoffman,

"If, by word and deed, business cannot dispel public mistrust, further government intervention is certain."<sup>71</sup>

Now this cosmic change is far more profound and fundamental than the murder of one segment of society or the appropriation of property from one group for another group. It involves nothing less than the transmutation of our fundamental values and aspirations. As Professor George Cabot Lodge says:

"You are indeed on the leading edge of a gigantic transformation in Western civilization, a transformation which has been long in its building and which is calling into question ideas and assumptions which were born in the 16th Century when the West began its passage out of mediaevalism."<sup>72</sup>

It is impossible to change fundamental values and aspirations without requiring corresponding changes in the purposes of corporate organization, since it is the *chargé d'affaires* of society on the industrial scene.

The most forward thinkers of the last generation concluded that corporate powers are held in trust. Today it may be more accurate to say that corporate powers are held in sufferance. The powers of an aroused and vigilant society, and of its all-powerful spokesman government, cannot be defied or resisted. As society wills, these powers may threaten, as in Campaign GM, or restrain, as by tax or antitrust, or sustain, as by tariffs or subvention, or obliterate, as under the Public Utility Holding Company Act.

In short, toleration of the corporation as a competitive agency for achieving an allocation of resources consistent with the most deeply held convictions of society depends on identification of corporate activity with those convictions.

Where, then, shall we look? In what direction shall corporate management peer? It is axiomatic that corporate management must identify the various constituencies it must serve, to which it is responsive. In addition to stockholders, we are told about employees and suppliers of capital, those who supply the materials of industry, those who purchase the products of industry, those who are middle men in either process, minority groups, women (now statistically, and perhaps vocally, a majority), environmentalists, neighbors, news media, government and the general public. Particular industries will need to assess the immediacy of their relationship to particular

70. Blumberg, *Introduction to the Politicalization of the Corporation*, 26 THE RECORD, ASS'N BAR OF N.Y. 372 (1971).

71. BUS. WEEK, June 17, 1972, at 103.

72. Final Lecture in AMP 62, December 1971.

ones of such groups, estimate their demand, calculate the probable channel through which their power will be applied, foreshadow its impact and adopt a proper responsive posture. This adaptation will necessarily evolve as points of view become evident. No one can conceivably lay down in advance a blue print for survival.

But as we grope for some unifying generalization, we may well remember the axiom of contemporary thinking laid down by Barry Commoner that:

"Everything is connected to everything else."<sup>73</sup>

Still more poignantly, he said:

". . . nothing can survive on the planet unless it is a cooperative part of a larger, global whole."<sup>74</sup>

This leads directly to my first conclusion or suggestion, and that is that it is not enough for corporate policy to look to multiple constituencies. It must look to the totality of interrelated interests. This means first the people whom its activities involve. The corporation must provide a forum for their participation in decision and in action. Only thus can it provide a creative role, and reward with a sense of personal achievement. It must at the same time make it possible to contribute to the partnership of man with nature by which alone our fragile biosphere can be preserved and the human species maintained. This is not a matter of managerial nobility. It is a necessity for managerial survival and indeed for corporate survival.

Such grandeur cannot be approached by cultivation of myths or improvement of forms, howsoever desirable they may individually appear to be. Shareholder democracy is one of these myths. It is inconceivable that the massive body of uninformed stockholders could be a fructifying influence on corporate policy. An illusion of pure form, I would suggest, is the notion of Federal incorporation. Public powers to regulate, reshape and redirect are equally effective regardless of the domiciliary scene. A change in the corporate domicile does not make those powers either more or less effective. Election of directors from different corporate constituencies from different sources of society has become very fashionable. And it is meritorious, to the extent that differing points of view can influence management to larger decisions. But it must be remembered that directors who try to help management manage are guilty of a serious mistake, as TWA has recently demonstrated.<sup>75</sup>

This brings us to my second conclusion, that the responsibility for exercising this basic leadership, this type of basic judgment, must rest directly on the shoulders of top management. This means the top executives and

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73. THE CLOSING CIRCLE 33 (1971).

74. *Id.* at 299.

75. *Resignation of Goldberg from the TWA Board of Directors*, NEWSWEEK, Oct. 30, 1972, at 47.



also their top lawyers. It is a solemn responsibility. Its discharge may well involve a relinquishment of some traditional powers. But without it the enterprise may end. Unless management can succeed in this reorientation, government will intervene. Of that there can be no doubt. Of the merits of such a result there can be a good deal. The economic failure to be redressed is the unlimited privilege accorded to technocracy and the inattention to human needs. As the Commission on Marijuana and Drug Abuse reported:

"Many Americans, due to the nature of their jobs in an automated economic system, find little personal satisfaction in their work. . ."<sup>76</sup>

But machines, like the Sabbath, were made for man, rather than man for the machine.

So now, what star shall we follow across this uncharted sea? There is no fixed beacon. The good may well be reappraised from day to day and then only by painful groping. But for an example we may turn to what may well be called the most spectacular success story in American history.

That, I suggest, is supplied by the history of the Supreme Court. Some of you may doubt that it has been such an unqualified success. But consider with me the facts for a moment. Adopting the 18th Century dogma of separation of powers, the Constitution of the United States establishes 3 separate departments of government, the legislative, the executive and the judicial. Purists are wont to smile at the illogicality of the English, for there the head of the judicial system presides over the House of Lords, which until recently was a co-equal legislative house. But I suggest to you that the Chief Justice of the United States is at the same time our preeminent legislative authority.

The great leap was taken in *Marbury v. Madison* (1803). There it was held that legislative acts explicitly in conflict with clear Constitutional provisions should be denied effect. This was the beginning of an endless adventure. The leap was bold enough when the Constitution was viewed as a static document to be interpreted like a contract. But it took on different dimensions with the concept of an evolving Constitution. That means, of course, that the Constitution is now no more than a process of thought which has meaning only as the Justices may declare, even though with that degree of imprecision which often accompanies inspiration. (We all remember the Delphic Oracle.) At one time the Court may say that the National Industrial Recovery Act is unconstitutional because of inadequate relation to interstate commerce.<sup>77</sup> At another time the Court may say that the Agricultural Adjustment Act is constitutional even as applied to a farmer using his produce on the farm where it was raised.<sup>78</sup> At one time the Court may say that separate but equal school facilities are constitutional<sup>79</sup>; yet at an-

76. Wall St. J., April 4, 1972, at 20.

77. *Schechter Corp. v. United States*, 295 U.S. 495 (1935).

78. *Wickard v. Filburn*, 317 U.S. 111 (1942).

79. *Plessy v. Ferguson*, 163 U.S. 537 (1896).

other time, the Court may hold that legislative action to that effect is unconstitutional.<sup>80</sup>

There can be no doubt that when the Court changes its mind at this level of sovereignty and strikes down a legislative act previously sustained, it is exercising a super-legislative power. Indeed the selection of Justices is not wholly unlike the ritualistic elevation of a king, with the ceremony and dignity so richly described in *The Golden Bough*. From that moment on they speak with a new voice that embodies the tone of juristic history, but effectively exercises the power of sovereignty. The Court is, in short, the ultimate embodiment of sovereignty in America, so far as it can be localized.

Throughout its history the Court has been surrounded by controversy. There have been times when the challenges were very grave, when the controversy was severe. The *Dred Scott* case was the overture to the Civil War. The protectionist decisions of the early Thirties led to the celebrated Court-packing effort of Franklin Roosevelt. But in each case the Court survived because of the veneration in which it was held by the American people.

The relevant question, for our present purposes, is, how has the Court been able to maintain its power of survival? It can be nothing other than its success in identifying and articulating the fundamental aspirations of the American dream. That which is every man's friend will not be put to naught. We can see the agonies of appraisal when the Justices are forced to grapple with new issues that introduce the future. The opinions in *Sierra Club*<sup>81</sup> are a poignant example, as also those in the death sentence decision.<sup>82</sup> The survival of the Court rests on the belief that it governs the American people better than any other authority can be trusted to do. The tumult of presidential selections is no reassurance of rationality. The fragmentation of Congress makes its decisions difficult to predict and of uncertain stability. But, despite objections from one group or another to every decision on major matters, the Court possesses the abiding confidence of the American people that it is struggling, without fear or favor, to find and realize the public good.

The parallel for corporate leaders is now clear. Their offices and their institutions will survive only if the public is convinced that they are contributing more to the public good, over the long term and in the most essential appraisal, than will result from any alternative. The American corporation must so harmonize its goals and methods with emerging public values that it regains the basic confidence of the American people as the best assurance of their economic wellbeing. There is nothing wrong with making a profit. In fact it is socially necessary to make a profit, since otherwise no capital could be generated and no technology developed. But the profit must be made in a method that commands admiration and reliance.

This is not to say that corporate management is expected, or even per-

80. *Brown v. Board of Education*, 347 U.S. 483 (1954).

81. *Sierra Club v. Morton*, 405 U.S. 727 (1972).

82. *Furman v. Georgia*, 408 U.S. 238 (1972).

mitted, to roam across the country like Don Quixote attacking what it may deem to be public evils without regard to their relationship to the corporate purpose. Indeed this would subject the interests of stockholders to the utmost hazard. Rather the pursuit of excellence by corporate management must be within the confines of the corporate purpose. As Voltaire said, at the conclusion of one of his most brilliant sceptical essays, our conclusion must be "*cultiviez votre jardin*" or "cultivate your own garden."

In this manner the fundamental objective of corporate management becomes not profit maximization, but profit optimization. While the challenge is immediate and mortal, no other instrument of American enterprise has shown equal powers of innovation. When aroused to this new task we may feel confident that they will prevail. As the movement from status to contract has been completed, so also the movement from contract to consensus will be completed.

But the hour is late and the obsolescence of knowledge escalates momentarily. Since the top executive must constantly be looking beneath the surface and "His duty is nowhere decreed,"<sup>83</sup> he can only remember "the delicacy and vulnerability of all the living species," among which "he, too, is a part of this single web."<sup>84</sup>

Can we then at last attempt any suggestions for the discharge of this prophetic task? Perhaps one might start provisionally along these lines:

1. The philosophy of the business is more important than its technique, so top management should focus on the former and harmonize the latter.

2. Developing creeds are more important than departing creeds, so top management must be in continuous communication with the most sensitive and innovative elements of society. That is not to say they must make friends with everyone, but they must be aware of everyone.

3. For this purpose it may be helpful to have the guidance of a full time observer of the desires and beliefs of the young, the academic, the literary and others who suggest oncoming standards of value.

4. Top management should have closer communication with the middle ranks of management to impart a point of view, to receive a feedback from their own experience and to unify the corporate *esprit de corps*.

5. Top management should create, or see that there is created, an exposition of the corporate conscience in the journals of opinion, not for the purpose of persuading whatever management thinks is best, but for the purpose of refining management thought until it is the best and then demonstrating its conceptual validity so that makers of opinion and decision, commentators, editors, lawyers and judges, may have

83. LE HASARD ET LA NECESSITE 195 (1970).

84. BARBARA WARD & RENE DUBOS, ONLY ONE EARTH 114 (1972).

available a sound basis of analysis to offset the continuous stream of anti-corporate opinion that now dominates the innovative press.

6. Ride with a loose rein, in obedience to the tolerant precept of an English solicitor that:

"On the whole, you probably get the best results if, within reason, you recognize and accept the independence and initiative of individuals and groups."

In sum, the powers of corporate management, like those of the Supreme Court, are immense, though never granted explicitly. They have grown by assertion, but are maintained only by public trust. Corporate leadership rests on economics, but looks above economics, rests on law, but looks beyond law. It is a spiritual experience that will require humility and imagination, perhaps also, in Fred Kahn's phrase, "apocalyptic vision."

**PROFESSOR PHILLIP I. BLUMBERG:** I have an inquiry as to the role of collective bargaining in employee participation in corporate decision making: will trade unions try to bargain over what have been traditional areas of management prerogatives?

My presentation has been primarily concerned with the relationship of employees to the internal structure of the company: representation on its board and ownership of its shares.

If I had a message, it was that in my opinion, the proposals for changes of this nature would have viability and strength only to the extent that they were adopted by trade unions and by workers themselves as fundamental objectives. This question thus points up the fact that collective bargaining in the United States outside of the corporate structure has been the traditional arena for the advancement of worker objectives and the achievement of what one might call economic justice.

I have no doubt that the trade unions will attempt to bargain over what in the past has been regarded as traditional prerogatives of management. I also have no doubt that trade unions will endeavor to represent in the future groups, including junior executives, who previously have been regarded as beyond the pale of trade union representation. In the United States, the life of the relationship between the employee and the major corporation has been represented by the collective bargaining process. The suggestions as to change in the structure of the Board to advance employee objectives, must be regarded as visionary until such time as they are adopted as major union objectives. Further, we must remember that there are eighty-three million employed Americans and that trade unions today represent no more than twenty million of them.

**MR. ELI GOLDSTON:** I have received this question: "Within the gap you defined between the requirements of law and the need for sufficient profit to keep management safe from effective challenge, do you have any guidelines

for management in either seeking out opportunities for socially responsible behavior or in responding to pressure groups?"

I might suggest something that we do within our own company: Years ago when I first came to the company, I was brought a slip of paper to O.K. It seems that in Philadelphia we had given \$4500. I think it was to the United Fund and it needed my O.K. The funny thing is that you get all sorts of people that can spend a half a million dollars, and can keep seven fellows who earn twenty thousand dollars a year on the payroll, but who are no longer needed, but if you want to give fifty bucks to some charity, it has to come to the head office.

So I signed and I said, "Tell me, why do we give \$4500?"

"Well, that's what we gave last year."

So I said, "All right." But that night at home I got to thinking. Why did we give \$4500 the year before? We had closed down half of the facility, and did that mean we really should have given half as much because we had half as many employees in Philadelphia? Or because we had thrown a lot of people out of work should we give more?

At dinner that evening I bumped into a chap who was Dean of the Florence Heller School of Philanthropy. So we hired a couple of his crack graduate students to look over what we were doing.

And this is a tip you might give some of your clients. They really ought to audit what they are doing on charity. It is unbelievable.

We didn't know what we were doing. Some of the things that we were doing were absolutely insane. We were giving \$2,500 to a church at one of our installations. When I found that out, I asked, "Why do we do it?"

The manager said, "If you don't want to do it, we won't do it." I said, "No, why do we do it?" And he said, "Well, we were doing it when I came here." I said, "When did you come here?"

"Fifteen years ago."

We never did find out why we started it, but we gave them \$7,500 as a three-year terminal gift and got rid of the annual payment.

But as a consequence of that, we decided to think through our charitable giving, and what we then did was we made up a charitable budget. We say that we are going to take about one per cent of our pre-tax income and we are going to spend it where we make it.

That is quite a novelty because most corporations spend it at headquarters, where the chief executive can be the Chairman of this year's Red Cross drive and that kind of thing if the company gives enough money.

So you start out and say to yourself, "I am going to put it back where I got it." Then you find that you can't get the people to spend it. As the Chief Executive, you have spent your entire life training them to be thrifty and to chisel around and increase the return on equity. Now you say, "You have \$7,000 to give away," and he says, "I can get away with \$500 easily!"

Then what happens is that he sends some money back to headquarters.

When you get the money back at headquarters, as we do, we take our principal officers, our so-called senior vice presidents, and give them each a kind of power of appointment over \$2,500 per year for the company to give to anything that is tax deductible and not religious. This is an immense time saver, you see, because I used to have a fellow who would come in and say, "Don't you think that the company ought to give something to the new drive at East Hampton Community College?"

I would say, "Where in the hell is East Hampton?" And he would say, "In Montana." I'd say, "We don't have anything to do in Montana." And he would say "Yes, but my daughter's going there."

Then it would develop that if he were less happy because his daughter isn't so happy, the corporate efficiency would decline and all of that kind of thing.

You eliminate all that nonsense. You say, "Take \$2,500 bucks out of the company. Do what you damn please with it, subject to three conditions:

"One, it is tax deductible.

"Two, it isn't religious.

"And three, it won't embarrass the company."

I suggest to you that what you do is to start out with the goal: "I've got to give one per cent away." Then you try to give it back where it came from, and you end up with a kitty that is left. With that kitty, first of all, you buy the executives off your back with a sort of a power of appointment, and then you take what is left and you plunk it into two or three very imaginative things. You will set some examples and you will also get your people excited. If you just simply say to your secretary, "Everybody that shows up that you can't get rid of, give them \$500 and get rid of them," you end up just sort of sprinkling it over the atmosphere like a bit of rain on a hot summer day and it all disappears.

What I am suggesting to you is that you go about it thoughtfully, and it is counsel's function to encourage thoughtfulness.

**MR. GEORGE D. GIBSON:** I have a simple question:

"If profit is not to be the only measure of corporate management, what other objective measures do you suggest?"

Let me comment on each clause:

One is, if profit is to be the only measure of corporate management, that is, the success of corporate management, the corporation is a candidate for early governmental take-over.

Secondly, the concluding phrase, "What other objective measures do you suggest?"

"Objective measures" is a synonym for a statistical measurement or yardstick. The burden of my remarks was that the problem is not susceptible of such a simplistic answer. It must depend upon a sensitive executive appraisal of the changing needs and enduring aspirations of the society the corporation serves.

Notwithstanding the sensitivity of our appraisal, it will do little good unless the corporation has a profit at the bottom line, as Eli says.

Presupposing a profit, and one that endures despite the contemporary social accounting standards, nevertheless the corporation must, within the parameters of its corporate purpose, supply a service better than can be done by other means and reward the society that makes its profit possible. The reason why corporate management should be compensated is its responsibility in making from day to day that very difficult and changing appraisal.

