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Collaboration Theory and Corporate Tax Avoidance

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I. Introduction

Taxation is one of the hottest legal topics today. When President Donald J. Trump signed the Tax Cuts and Jobs Act (TCJA)[1] into law on December 22, 2017, it represented the most sweeping tax reform in generations.[2] In the area of tax law, no issue is more important than the proper rate of corporate taxation in the United States.[3] The TCJA reduced the corporate tax rate

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1. Tax Cuts and Jobs Act of 2017, Pub. L. No 115-97, 131 Stat. 2054 (codified as amended in scattered sections of 26 U.S.C.).

2. *See* Julia Horowitz, *34 Things You Need to Know About the Incoming Tax Law*, CNNMONEY (Dec. 26, 2017, 9:59 AM), http://money.cnn.com/2017/12/20/news/economy/republican-tax-reform-everything-you-need-to-know/index.html (last visited Feb. 18, 2019) ("[The Tax Cuts and Jobs Act] is the first significant reform of the U.S. tax code since 1986.") (on file with the Washington and Lee Law Review); Jim Tankersley, *Washington's Fight Over Taxes Is Only Beginning*, N.Y. TIMES (Feb. 23, 2018), https://www.nytimes.com/2018/02/23/business/washingtons-fight-over-taxes-is-only-beginning.html (last visited Feb. 18, 2019) ("An old Washington axiom is that Congress passes a major tax overhaul once every 30 years. By that logic, the sweeping 2017 tax law, which was raced through Congress by Republicans before it was signed in late December by President Trump, was right on time.") (on file with the Washington and Lee Law Review); Deirdre Walsh et al., *White House, GOP Celebrate Passing Sweeping Tax Bill*, CNNPOLITICS (Dec. 20, 2017), https://edition.cnn.com/2017/12/20/politics/house-senate-trump-taxbill/index.html (last visited Feb. 18, 2019) ("Republican lawmakers joined President Donald Trump . . . to celebrate their largest legislative achievement of 2017, in a public ceremony spotlighting the most sweeping overhaul of the US tax system in more than 30 years.") (on file with the Washington and Lee Law Review).

3. *See* Shaun Terrill, *Corrections and Substantive Fixes Needed with Respect to Employee Benefit Changes Made by the 2017 Tax Act*, BLOOMBERG BNA: FED. TAX BLOG (Feb. 16, 2018), https://www.bna.com/corrections-substantive-fixes-b57982088882/ (last visited Feb. 18, 2019) ("On December 22, President Trump signed into law . . . the first major overhaul of the U.S. tax system in 30 years.") (on file with the Washington and Lee Law Review).

from 35% to 21%.[4] While some business-related deductions and credits were reduced or eliminated, the tax cut represents a major windfall for corporate America.[5] Some estimate that the savings to corporations and cost to tax payers will be around $1 trillion.[6] One of the major reasons that politicians advanced for changing the law was that the corporate tax rate was driving corporations to relocate overseas and to engage in various tax avoidance strategies to reduce their tax burdens.[7] Whether the TCJA will reduce this

4. *See* Amanda Becker & David Morgan, *What's in the Final Republican Tax Bill*, REUTERS (Dec. 19, 2017), https://www.reuters.com/article/us-usa-tax-provisions-factbox/whats-in-the-final-republican-tax-bill-idUSKBN1ED27K (last visited Feb. 18, 2019) (reporting that the final version of the bill that was signed into law as the Tax Cuts and Jobs Act "[c]uts corporate income tax rate permanently to 21 percent from 35 percent, as of Jan. 1, 2018") (on file with the Washington and Lee Law Review); Tara Golshan, *4 Winners and 4 Losers from the Republican Tax Bill*, VOX (Dec. 22, 2017), https://www.vox.com/2017/12/20/16790040/gop-tax-bill-winners (last visited Feb. 18, 2019) ("This bill permanently cuts the corporate tax rate from 35 percent to 21 percent to bring it closer to that of countries like Canada, which has a 15 percent corporate tax rate, or Ireland, which has a 12.5 percent rate.") (on file with the Washington and Lee Law Review); Sabrina Siddiqui, Ben Jacobs & Lauren Gambino, *Senate Approves Most Drastic Changes to US Tax Code in 30 Years*, GUARDIAN (Dec. 20, 2017), https://www.theguardian.com/us-news/2017/dec/19/donald-trump-tax-bill-plan-house-approves-senate (last visited Feb. 18, 2019) ("The bill lowers the top individual tax rate from 39.6% to 37% and slashes the corporate tax rate to 21%, a dramatic fall from its current rate of 35%.") (on file with the Washington and Lee Law Review).

5. *See* David Harding, Michael Mankins & Karen Harris, *What U.S. CEOs Should Do with the Money from Corporate Tax Cuts*, HARV. BUS. REV. (Feb. 1, 2018), https://hbr.org/2018/02/what-u-s-ceos-should-do-with-the-money-from-corporate-tax-cuts (last visited Feb. 18, 2019) ("The new U.S. tax law is likely to increase after-tax cash flows for U.S.-based companies by anywhere from 10% to 20%, depending on their current tax position. . . . The size of this windfall is remarkable . . . .") (on file with the Washington and Lee Law Review); Brian Peccarelli, *Too Early to Call the Winners and Losers of Major Corporate Tax Cut*, HILL (Dec. 16, 2017), http://thehill.com/opinion/finance/365239-too-early-to-call-the-winners-and-losers-of-major-corporate-tax-cut (last visited Feb. 18, 2019) ("[The Tax Cuts and Jobs Act] is . . . the one piece of the tax reform legislation that the left and right agree would produce benefits for its intended audience: big businesses.") (on file with the Washington and Lee Law Review).

6. *See* Peccarelli, *supra* note 5 ("It's hard to overemphasize the significance of the Republican proposal to cut the corporate tax rate to 21 percent. At an estimated cost of $1 trillion, it's the headline and most expensive measure in the entire tax reform package.").

7. *See* Akane Otani, Richard Rubin & Theo Francis, *Boom in Share Buybacks Renews Question of Who Wins From Tax Cuts*, WALL ST. J. (Mar. 1, 2018), https://www.wsj.com/articles/boom-in-share-buybacks-renews-question-of-who-wins-from-tax-cuts-1519900200 (last visited Feb. 18, 2019) ("The long-run

problem remains unclear. With that said, it is unlikely that tax avoidance can ever be completely eliminated.[8]

The permissibility of corporate tax avoidance is a central issue in tax law. As of June 7, 2017, seventy-six countries and jurisdictions signed or formally expressed their intention to sign the Multilateral Convention to Implement Tax Treaty Related Measures to Prevent Base Erosion and Profit Shifting (Convention), a multilateral agreement that is designed to reduce corporate tax avoidance practices by multinational businesses by closing gaps in existing international tax law.[9] The Convention is the product of the OECD/G20 Base Erosion and Profit Shifting Project,[10] which involves collaboration by the thirty-four members of the Organization for Economic Cooperation and Development (OECD), all G20 members, and more than forty developing countries.[11] Notably, the United States is not a signatory.[12]

Although the Trump Administration has shown a recurrent hostility to binding itself to international agreements, the United States' unwillingness to sign the Convention is surprising

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economic case for the corporate tax cut was that the rate reduction and incentives for business investment would give companies more reasons to invest in the U.S., because projects that didn't make financial sense would become profitable.") (on file with the Washington and Lee Law Review).

8. *See* David Gamage, *How Should Governments Promote Distributive Justice?: A Framework for Analyzing the Optimal Choice of Tax Instruments*, 68 TAX L. REV. 1, 2 (2014) ("No one seriously suggests that tax avoidance and evasion could be completely eliminated in real world contexts. Indeed, historical experience with fundamental tax reform suggests that high-income taxpayers will eventually find numerous ways to circumvent any plausible real world forms of taxation.").

9. *See Multilateral Convention to Implement Tax Treaty Related Measures to Prevent BEPS*, ORG. FOR ECON. CO-OPERATION & DEV., http://www.oecd.org/tax/treaties/multilateral-convention-to-implement-tax-treaty-related-measures-to-prevent-beps.htm (last visited Feb. 18, 2019) (providing an overview of the agreement) (on file with the Washington and Lee Law Review).

10. *See id.* (explaining that the treaty "offers concrete solutions . . . by transposing results from the OECD/G20 BEPS Project into bilateral tax treaties worldwide").

11. *See id.* (providing a list of signatories and parties to the agreement).

12. *See id.* (showing the absence of the United States from the list of signatories or jurisdictions expressing their intent to sign).

considering the seriousness of the issue. The OECD estimates that tax avoidance practices by multinational firms may lead to up to $240 billion of lost tax revenue globally, which is the equivalent of 10% of global corporate tax revenues.[13] In the United States, the Congressional Research Service estimates tax revenue losses of $100 billion due to tax avoidance.[14] A recent study suggests that that 73% of Fortune 500 companies use tax havens.[15] The study notes, "American multinational companies collectively reported forty-three percent of their foreign earnings in five small tax haven countries: Bermuda, Ireland, Luxembourg, the Netherlands, and Switzerland."[16] In short, the impact of tax avoidance is substantial, important, and pressing.

Notably, tax avoidance should not be confused with tax evasion. While tax evasion is the illegal nonpayment or underpayment of taxes, corporate tax avoidance is the structuring of business transactions to reduce a firm's tax obligations in a manner that technically complies with the law but violates the spirit of the law.[17] As a result, avoidance is distinguishable from evasion by the legality of the action.[18] For purposes of this Article, corporate tax avoidance should also be differentiated from tax minimization. Corporate tax minimization involves arranging a firm's affairs in a way envisioned by the legislative body to reduce the firm's tax burden.[19] The Supreme Court of the United States and other judicial bodies have regularly held that this type of

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13. *See* OECD, POLICY BRIEF: TAXING MULTINATIONAL ENTERPRISES, BASE EROSION AND PROFITS SHIFTING (BEPS) 1 (Oct. 2015), http://www.oecd.org/policy-briefs/PB-Base-Erosion-Profit-Shifting-(BEPS-III)-Oct-2015.pdf (discussing the global impact of base erosion and profit shifting).

14. *See* JANE GRAVELLE, CONG. RESEARCH SERV., R40623, TAX HAVENS: INTERNATIONAL TAX AVOIDANCE AND EVASION 1 (2015), https://www.fas.org/sgp/crs/misc/R40623.pdf (explaining the impact of corporate profit shifting).

15. *See* RICHARD PHILLIPS ET AL., OFFSHORE SHELL GAMES 2016: THE USE OF OFFSHORE TAX HAVENS BY FORTUNE 500 COMPANIES 1 (2016), http://ctj.org/pdf/offshoreshellgames2016.pdf (explaining that at least 367 of Fortune 500 companies "operate one or more subsidiaries in tax haven countries").

16. *Id.* at 2 (citing a 2008 Congressional Research Service Report).

17. *See infra* Part II.A (defining tax evasion).

18. *See infra* Part II.A (explaining the difference between tax avoidance and tax evasion).

19. *See infra* Part II.A (discussing tax minimization).

behavior is legally permissible.[20] Because tax minimization complies with both the letter and the spirit of the law, one would have a hard time arguing that corporations should be blamed for this behavior. If any entity should be faulted for tax minimization, the legislative body establishing the tax regime should receive the blame. Obviously, bright lines do not exist between tax evasion and tax avoidance, and between tax avoidance and tax minimization. These concepts often blur into each other.

While corporate tax evasion is prohibited because of the illegality of the behavior, the question of whether corporate tax avoidance is permissible is a much more difficult one. Some corporate managers and tax advisors claim that aggressive tax avoidance is mandated based upon the fiduciary duties owed within the corporation.[21] Explicitly or implicitly, they rely on the holding in the seminal case, *Dodge v. Ford Motor Co.*,[22] in which the Supreme Court of Michigan held that "[a] business corporation is organized and carried on primarily for the profit of the

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20. *See* Gregory v. Helvering, 293 U.S. 465, 469 (1935) ("The legal right of a taxpayer to decrease the amount of what otherwise would be his taxes, or altogether avoid them, by means which the law permits, cannot be doubted."); Helvering v. Gregory, 69 F.2d 809, 810 (2d Cir. 1934), *aff'd*, 293 U.S. 465 (1935) ("Any one may so arrange his affairs that his taxes shall be as low as possible; he is not bound to choose that pattern which will best pay the Treasury; there is not even a patriotic duty to increase one's taxes."); *see also* Jerome B. Libin, *Congress Should Address Tax Avoidance Head-On: The Internal Revenue Code Needs a GAAR*, 30 VA. TAX REV. 339, 352 (2010) ("Tax minimization is part of our taxpayer culture. Tax minimization within the boundaries of the law has been approved, if not encouraged, by the Supreme Court."); Allen D. Madison, *The Legal Framework for Tax Compliance*, 70 TAX LAW. 497, 521–22 (2017) ("[T]axpayers are entitled to make choices in their lives—taking into account the government's communications of its expectations for reporting—that minimize their taxes.").

21. *See* Jasmine M. Fisher, Note, *Fairer Shores: Tax Havens, Tax Avoidance, and Corporate Social Responsibility*, 94 B.U. L. REV. 337, 348–49 (2014) ("Some corporate leaders and analysts perceive tax avoidance as unproblematic, pointing to lawmakers' failures to make such practices illegal as an indication of its acceptability. . . . Corporate leaders may even view tax avoidance as obligatory; as part of their fiduciary duties to shareholders."); Alexander J. Morgenstern, Note, *Corporate Tax Avoidance: Addressing the Merits of Preventing Multinational Corporations from Engaging in the Practice and Repatriating Overseas Profits*, 16 J. INT'L BUS. & L. 333, 334 (2017) ("Many corporate executives justify corporate participation in tax avoidance as being 'capitalistic' or encompassed in their fiduciary duties owed to shareholders.").

22. 170 N.W. 668 (Mich. 1919).

stockholders. The powers of the directors are to be employed for that end."[23] This holding can be derived from the fiduciary duties that management owes to the corporation and its shareholders, especially the duty of loyalty and the duty of good faith.[24] As discussed in my recent article with Professor Karie Davis-Nozemack, *Corporate Tax Avoidance and Honoring the Fiduciary Duties Owed to the Corporation and Its Stockholders*, although the holding in *Dodge* remains true in general, the *Dodge* mandate fails to require tax avoidance in any specific instance because of the discretion that is granted to corporate managers under the business judgment rule.[25] As a result, a vacuum is created regarding when engaging in tax avoidance is required, permissible, or prohibited.[26] One potentially can look to the fields of corporate social responsibility, business ethics, and economics to fill this vacuum,[27] but the issue lingers whether corporate tax avoidance is legally required, permissible, or prohibited.

This Article argues that aggressive corporate tax avoidance is legally impermissible based upon the essential nature of the corporate form. The history of the debate over the essential nature of the corporation is substantial.[28] This debate has been reinvigorated by the Supreme Court's recent opinions, *Citizens United v. Federal Election Commission*[29] and *Burwell v. Hobby Lobby Stores, Inc.*,[30] which explore the scope of corporate rights.[31]

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23. *Id.* at 684.

24. *See infra* Part III.B (explaining how the *Dodge* mandate can be derived from the fiduciary duties that corporate managers owe the corporation and its stockholders).

25. *See* Eric C. Chaffee & Karie Davis-Nozemack, *Corporate Tax Avoidance and Honoring the Fiduciary Duties Owed to the Corporation and Its Stockholders*, 58 B.C. L. REV. 1425, 1429–30 (2017) (discussing the scope of the *Dodge* mandate that corporations be run primarily for profit).

26. *See id.* at 1470 ("[A]lthough the *Dodge* mandate remains true in general, it provides little guidance in specific matters, including tax avoidance.").

27. *See id.* at 1473–80 (discussing the role that the fields of corporate social responsibility, business ethics, and economics can play in determining whether corporations should engage in tax avoidance).

28. *See infra* Part IV (discussing the three prevailing theories of the corporation that have developed over the past few centuries: artificial entity theory, real entity theory, and aggregate theory).

29. 558 U.S. 310 (2010).

30. 573 U.S. 682 (2014).

31. *See generally, e.g.*, Reuven S. Avi-Yonah, Citizens United *and the*

The debate has yielded three prevailing theories of the corporation. First, the artificial entity theory, which is also referred to as concession theory, suggests that corporations are artificial entities that owe their existence completely to the government.[32] Second, the real entity theory, which is also referred to as the natural entity theory, suggests that each corporation has an existence and identity that is separate and apart from the individuals who organize, operate, and own it.[33] Third, the aggregate theory, which is also known as the nexus of contracts theory, suggests that a corporation is a collection of individuals joined together through the intersection of various obligations.[34]

Corporate Form, 2010 WIS. L. REV. 999; Margaret M. Blair, *Corporate Personhood and the Corporate Persona*, 2013 U. ILL. L. REV. 785; Margaret M. Blair & Elizabeth Pollman, *The Derivative Nature of Corporate Constitutional Rights*, 56 WM. & MARY L. REV. 1673 (2015); Teneille R. Brown, *In-corp-o-real: A Psychological Critique of Corporate Personhood and* Citizens United, 12 FLA. ST. U. BUS. REV. 1 (2013); Ronald J. Colombo, *The Corporation as a Tocquevillian Association*, 85 TEMP. L. REV. 1 (2012); Reza Dibadj, *(Mis)conceptions of the Corporation*, 29 GA. ST. U. L. REV. 731 (2013); Malcolm J. Harkins III, *The Uneasy Relationship of* Hobby Lobby*,* Conestoga Wood*, the Affordable Care Act, and the Corporate Person: How a Historical Myth Continues to Bedevil the Legal System*, 7 ST. LOUIS U. J. HEALTH L. & POL'Y 201 (2014); Virginia Harper Ho, *Theories of Corporate Groups: Corporate Identity Reconceived*, 42 SETON HALL L. REV. 879 (2012); Jason Iuliano, *Do Corporations Have Religious Beliefs?*, 90 IND. L.J. 47 (2015); Jonathan A. Marcantel, *The Corporation as a "Real" Constitutional Person*, 11 U.C. DAVIS BUS. L.J. 221 (2011); Roger M. Michalski, *Rights Come with Responsibilities: Personal Jurisdiction in the Age of Corporate Personhood*, 50 SAN DIEGO L. REV. 125 (2013); Joseph F. Morrissey, *A Contractarian Critique of* Citizens United, 15 U. PA. J. CONST. L. 765 (2013); Stefan J. Padfield, *The Silent Role of Corporate Theory in the Supreme Court's Campaign Finance Cases*, 15 U. PA. J. CONST. L. 831 (2013) [hereinafter Padfield, *The Silent Role of Corporate Theory*]; Stefan J. Padfield, *Rehabilitating Concession Theory*, 66 OKLA. L. REV. 327 (2014) [hereinafter Padfield, *Rehabilitating Concession Theory*]; Martin Petrin, *Reconceptualizing the Theory of the Firm—From Nature to Function*, 118 PENN. ST. L. REV. 1 (2013); Elizabeth Pollman, *A Corporate Right to Privacy*, 99 MINN. L. REV. 27 (2014); Elizabeth Pollman, *Reconceiving Corporate Personhood*, 2011 UTAH L. REV. 1629 [hereinafter Pollman, *Reconceiving Corporate Personhood*]; Susanna Kim Ripken, *Corporate First Amendment Rights After* Citizens United: *An Analysis of the Popular Movement to End the Constitutional Personhood of Corporations*, 14 U. PA. J. BUS. L. 209 (2011).

32. *See infra* Part IV.A (explaining the artificial entity theory of the corporation).

33. *See infra* Part IV.B (explaining the real entity theory of the corporation).

34. *See infra* Part IV.C (explaining the aggregate theory of the corporation).

While each of the prevailing essentialist theories of the corporation is compelling because they describe some aspect of the corporate form, each fails to provide a robust definition of what is a corporation. The artificial entity theory, for instance, focuses on the role of the government in creating the corporation, but it largely ignores the role of the individuals organizing, operating, and owning the corporation.[35] The real entity theory focuses on the corporation as a separate entity, but it largely ignores the role of the government in creating the corporation and the individuals organizing, operating, and owning the entity.[36] In addition, the aggregate theory focuses on the individuals organizing, operating, and owning the corporation, but it largely ignores the role of the government in creating the corporation and does little to explain the corporation's separate legal status.[37] Moreover, all of the prevailing theories concentrate on the question of *how* corporations exist without answering *why* corporations exist. Because determining the essential nature of a corporation is a definitional inquiry, an essentialist theory that answers both questions is needed.

In my recent work, I have developed an essentialist theory of the corporation that I refer to as "collaboration theory."[38] Collaboration theory posits that the corporation is a collaboration among the government and the individuals organizing, operating, and owning the corporation. For purposes of my theory, collaboration is defined as a common effort between or among multiple entities to accomplish a task or a project. In regard to for-profit corporations, the common project is economic development and economic gain. This theory is superior to the existing essentialist theories because it explains how corporations

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35. *See infra* Part IV.A (explaining the artificial entity theory of the corporation).

36. *See infra* Part IV.B (explaining the real entity theory of the corporation).

37. *See infra* Part IV.C (explaining the aggregate theory of the corporation).

38. *See generally* Eric C. Chaffee, *Collaboration Theory: A Theory of the Charitable Tax Exempt Nonprofit Corporation*, 49 U.C. DAVIS L. REV. 1719 (2016) [hereinafter Chaffee, *Collaboration Theory*] (introducing and explaining collaboration theory as an essentialist theory of the corporation); Eric C. Chaffee, *The Origins of Corporate Social Responsibility*, 85 U. CIN. L. REV. 353 (2017) [hereinafter Chaffee, *Corporate Social Responsibility*] (applying collaboration theory to the questions of why and when corporations should engage in socially responsible behavior).

exist (i.e. as a collaboration among the government and the individuals organizing, operating, and owning the corporation), and why corporations exist (i.e. for economic development and economic gain). The goals of the government and the individuals do vary a bit in the sense that the government is seeking social economic development and gain, and the individuals organizing, operating, and owning the corporation are seeking personal economic development and gain. However, in most collaborations, goals and interests do not perfectly align, and collaboration theory offers a robust and compelling definition of what is a corporation. This theory has generally been well received.[39]

By understanding the corporation as a collaboration between the government and the individuals organizing, operating, and owning the corporation, the impermissibility of aggressive corporate tax avoidance becomes apparent. Collaborators in business ventures owe each other a duty of good faith,[40] and the contractual nature of the corporation carries with it a duty of a good faith as well.[41] As a result, the notion becomes fanciful that depriving the government of revenue through aggressive corporate tax avoidance strategies is required or even permissible. Tax avoidance is by definition violating the spirit of the law, and it is an affront to the collaboration that forms the foundation of the corporate form because it frustrates one of the government's purposes for entering the collaboration, i.e., gaining revenue.[42]

This Article advances the existing scholarship in three main ways. First, this Article breaks new grounds by being the first piece to examine how essentialist theories of the corporation should inform the permissibility of corporate tax avoidance. Only after one

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39. This work was featured on the *Harvard Law School Forum on Corporate Governance and Financial Regulation*. Eric C. Chaffee, *The Origins of Corporate Social Responsibility*, HARV. L. SCH. F. ON CORP. GOVERNANCE & FIN. REG. (May 28, 2017), https://corpgov.law.harvard.edu/2017/05/28/the-origins-of-corporate-social-responsibility/ (last visited Feb. 18, 2019) (on file with the Washington and Lee Law Review).

40. *See infra* Part VI.A (discussing the duty of good faith that collaborators in business ventures owe each other).

41. *See infra* note 263 (explaining the implied duty of good faith that underlies all contractual relationships).

42. *See infra* Part II.A (providing a definition of tax avoidance).

understands what a corporation is can one understand what obligations a corporation has. Remarkably, no other article has explored how essentialist theories of the corporation apply in the corporate tax avoidance context. Second, this Article breaks new ground because it explores how collaboration theory, a new theory of the corporation that I developed, applies to corporate tax avoidance. Third, this Article answers the question of whether corporations are permitted or required to engage in aggressive tax avoidance strategies. Once it becomes apparent that corporate managers are not mandated by their fiduciary duties to engage in aggressive tax avoidance, a vacuum is created regarding whether corporate managers have any legal obligations regarding such behavior.[43] This Article argues that based upon the essential nature of the corporate form as a collaboration, corporate managers are legally required not to engage in aggressive tax avoidance strategies because they violate the spirit of the law and the duties of good faith that undergird the corporation.

The remainder of this Article is structured as follows. Part II defines tax avoidance, explains why corporations engage in such behavior, and why such behavior is wrong. Part III explores why managers are not required to engage in corporate tax avoidance based upon the fiduciary duties that they owe to the corporation and its stockholders, which demonstrates that there is a lack of understanding of when engaging in tax avoidance is required, permissible, or prohibited. Part IV suggests that the essential nature of the corporation is the place to begin in understanding when tax avoidance is allowable and explores the prevailing theories of the corporation, including artificial entity theory, real entity, and aggregate theory. Part V discusses collaboration theory, a theory that I have developed that better describes the essential nature of the corporation. Part VI applies collaboration theory to corporate tax avoidance and determines that corporate tax avoidance should be avoided because it violates the duties the individuals organizing, owning, and operating the corporation owe to the government as collaborators in the corporate form. Part VII provides brief concluding remarks.

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43. *See infra* Part III.C (explaining that corporate managers have broad discretion in how they go about seeking profit for the entity).

II. Understanding Tax Avoidance

As a starting point, a few brief words ought to be offered about the contours of tax avoidance. This Part explores the definition of that term and its benefits and harms.

A. Defining Tax Avoidance

For purposes of this Article, tax avoidance is defined as structuring business transactions to reduce a firm's tax obligations in a manner that technically complies with the law but violates the spirit or underlying policies of the law.[44] To put that definition in the context of tax compliance behavior, one must understand what I shall term the "spectrum of tax compliance behavior."

At one end of the spectrum exists unreflective compliance in which a taxpayer simply undertakes an activity without reflecting on the tax implications. For example, many individuals purchase homes, obtain educational loans, and undertake work activities without prospectively considering how these activities might impact the amount of taxes that they owe to the government.[45]

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44. *See* Derek E. Anderson, *Turning the Corporate Inversion Transaction Right Side Up: Proposed Legislation in the 108th Congress Aims to Stamp Out Any Economic Vitality of the Corporate Inversion Transaction*, 16 FLA. J. INT'L L. 267, 286 n.71 (2004) ("[N]aked tax avoidance, as openly admitted by various companies is clearly contrary to public policy and the spirit of the IRC."); Assaf Likhovski, *"Training in Citizenship": Tax Compliance and Modernity*, 32 LAW & SOC. INQUIRY 665, 691 (2007) ("Tax avoidance . . . is . . . the attempt to follow the letter of the law ignoring the legislator's intention (or the 'spirit' of the law) . . . ."); Daniel T. Ostas & Axel Hilling, *Global Tax Shelters, the Ethics of Interpretation, and the Need for a Pragmatic Jurisprudence*, 53 AM. BUS. L.J. 745, 749 (2016) ("Tax avoidance refers to not paying a tax or paying a reduced tax based on the assertion of a literal interpretation of tax law that one knows was not intended by the legislature, and if challenged, may not prevail in court.").

45. *See* Kate Leifeld, *Creating Access to Tax Benefits: How Pro Bono Tax Professionals Can Help Low-Income Taxpayers Claim the Earned Income Tax Credit*, 62 ME. L. REV. 543, 556 (2010) ("Taxpayers often do not understand what information the IRS needs or why their documentation is insufficient."); Sagit Leviner, *The Role Tax Preparers Play in Taxpayer Compliance: An Empirical Investigation with Policy Implications*, 60 BUFF. L. REV. 1079, 1087 (2012) ("With the growing complexity of the tax code, many taxpayers do not understand their filing requirements and face significant difficulties completing tax forms by themselves."); Susan Striz, Note, *The Key to Closing the Tax Gap: Understanding*,

Importantly, however, just because an individual or entity undertakes a form of tax compliance behavior in one context does not mean that they will undertake the same type of tax compliance behavior in all contexts. To put it another way, the completely oblivious tax payer is likely a rarity.

Next to unreflective compliance on the spectrum of tax compliance behavior is tax minimization. This type of behavior occurs when a taxpayer reflectively makes tax compliance decisions with the goal of reducing that taxpayer's tax burden within the intended scope of the law; this type of behavior is completely permissible.[46] For example, this type of behavior might occur in a situation in which a taxpayer opts to schedule two surgeries that are not covered by insurance within the same tax year to maximize the taxpayer's health care deduction under § 213 of the Internal Revenue Code.[47] It might also occur in a circumstance in which a taxpayer chooses to do a large amount of charitable giving in a single tax year to maximize their charitable tax deduction under § 170.[48]

After tax minimization comes tax avoidance. As previously mentioned, in the corporate context, tax avoidance is defined as structuring business transactions to reduce a firm's tax obligations in a manner that technically complies with the law but violates the spirit or underlying policies of the law.[49] However, the concept can obviously be extended more broadly than the corporate tax context. It extends to any instance in which a taxpayer attempts to exploit an unintended weakness in the tax code.[50]

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112 W. VA. L. REV. 1053, 1077 (2010) ("Due to the complexity of the tax code, many taxpayers make unintentional errors simply because they do not understand what they are doing.").

46. *See supra* note 20 and accompanying text (reporting that tax minimization is legally acceptable).

47. *See* I.R.C. § 213(a) (2012) ("There shall be allowed as a deduction the expenses paid during the taxable year, not compensated for by insurance or otherwise, for medical care of the taxpayer, his spouse, or a dependent . . . to the extent that such expenses exceed 10 percent of adjusted gross income."). Notably, the 10% was reduced to 7.5% for "any taxable year . . . beginning after December 31, 2016, and ending before January 1, 2019." I.R.C. § 213(f) (2012).

48. *See* I.R.C. § 170 (2012) ("There shall be allowed as a deduction any charitable contribution . . . payment of which is made within the taxable year.").

49. *See supra* note 17 and accompanying text (providing a definition of tax avoidance).

50. *See* Dora Arash, *Crummey Trusts: An Exploitation of the Annual*

Finally, at the opposite end of the spectrum from unreflective compliance is tax evasion. Tax evasion occurs when an individual violates the tax law and includes any sort of behavior that violates the law regardless of whether it is willful or not.[51] Importantly, tax avoidance, as used in this Article, in no way involves illegal conduct.

B. The Benefits and Harms of Tax Avoidance

With the definition of tax avoidance explained, the issue now becomes whether tax avoidance is a good or bad thing. As the introduction to this Article reveals, tax avoidance is certainly popular in corporate America.[52] If tax avoidance is completely bad, this reality would not exist. This subpart explores the benefits and

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Exclusion, 21 PEPP. L. REV. 83, 84 (1993) ("The imposition of taxes generally fosters an intense ambition on the part of those individuals adversely affected by such taxes to seek means of avoidance. Tax practitioners . . . search for and discover loopholes within the tax law that can be utilized for the purpose of tax avoidance."); Simone M. Haug, *The United States Policy of Stringent Anti-Treaty-Shopping Provisions: A Comparative Analysis*, 29 VAND. J. TRANSNAT'L L. 191, 199 n.19 (1996) ("As opposed to tax evasion, which identifies tax reduction by illegal means, tax avoidance is used to describe the reduction of tax liability by legal means. Tax avoidance, however, has pejorative overtones, especially in the context of artificial arrangements, loopholes, anomalies, or other deficiencies of tax law."); T. Modibo Ocran, *Double Taxation Treaties and Transnational Investment: A Comparative Study*, 2 TRANSNAT'L LAW. 131, 138 (1989) ("Tax avoidance . . . occurs where the taxpayer takes advantage of loopholes in the tax laws. . . . [T]ax avoidance does not technically infringe the law, even though it may be equally damaging to the host state and can be morally reprehensible.").

51. *See* James Alm & Jay A. Soled, *W(h)ither the Tax Gap?*, 92 WASH. L. REV. 521, 524–25 (2017) ("[T]he phrase 'tax evasion' refers to illegal and intentional actions taken by taxpayers to circumvent their legally due tax obligations by underreporting incomes, overstating deductions, exemptions, or credits, failing to file appropriate tax returns, and even engaging in barter."); Kayal Munisami, *The Role of Corporate Social Responsibility in Solving the Great Corporate Tax Dodge*, 17 FLA. ST. U. BUS. REV. 55, 55–56 (2018) ("[T]ax evasion . . . is clearly and uniformly illegal across jurisdictions . . . ."); Kyle Richard, *Are All Tax Rulings State Aid? Examining the European Commission's Recent State Aid Decisions*, 18 HOUS. BUS. & TAX L.J. 1, 8 n.20 (2018) ("[T]ax evasion . . . involves the illegal underpayment (or non-payment) of taxes by a taxpayer.").

52. *See supra* notes 13–16 and accompanying text (discussing the widespread use of tax avoidance by large corporations).

harms of tax avoidance, and explains the reasons why the harms outweigh the benefits.

Tax avoidance has six major benefits. First, tax avoidance benefits the corporation itself because if a corporation can lower its tax burden through tax avoidance, then the financial performance of the firm will improve.[53] Second, if the financial performance of the corporation improves through tax avoidance, corporate managers are likely to be rewarded because of the improved financial performance of the firm.[54] Third, if the corporation is doing well, stockholders will likely reap the benefit in the form of increased value of their shares and dividends.[55] Fourth, if the corporation is doing well, creditors, employees, and other stakeholders will also reap the benefit by having greater assurance that debts will be repaid, and they will prosper.[56] Fifth, if the

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53. *See* Joshua D. Blank, *The Timing of Tax Transparency*, 90 S. CAL. L. REV. 449, 497 (2017) ("[A]s U.S. corporations can claim valuable tax losses and other tax benefits that reduce their taxable income and tax liability without reducing their earnings for financial accounting purposes, corporate tax directors often face pressure, from shareholders and non-tax management, to pursue tax avoidance strategies."); Orly Sulami, *Tax Abuse—Lessons from Abroad*, 65 SMU L. REV. 551, 559 (2012) ("Taxpayers often . . . benefit on their financial statements from abusive tax avoidance arrangements.").

54. *See* Reuven S. Avi-Yonah, *Corporate Taxation and Corporate Social Responsibility*, 11 N.Y.U. J.L. & BUS. 1, 24 (2014) ("If tax is considered a cost . . . , it behooves the management to try to minimize this cost, or even turn it into a profit. Thus, the goal of shareholder profit maximization can naturally lead to corporations trying to minimize taxes and thus enhance earnings per share."); Noam Noked, *Can Taxes Mitigate Corporate Governance Inefficiencies?*, 9 WM. & MARY BUS. L. REV. 221, 230 (2017) ("There is evidence which shows that a higher level of incentive compensation is associated with an increased level of tax avoidance, especially among firms with better corporate governance.").

55. *See* Dennis F. Dunne, *The Revlon Duties and the Sale of Companies in Chapter 11*, 52 BUS. LAW. 1333, 1345 (1997) ("In exchange for placing their capital at risk, the stockholders will prosper if the company succeeds."); Kent Greenfield, *Defending Stakeholder Governance*, 58 CASE W. RES. L. REV. 1043, 1054 (2008) ("[S]hareholders benefit only when the firm prospers."); Robert C. Illig, *The Promise of Hedge Fund Governance: How Incentive Compensation Can Enhance Institutional Investor Monitoring*, 60 ALA. L. REV. 41, 49 (2008) ("[I]nstitutional investors have a direct financial interest in the success of the corporations in which they invest. As professional stockholders, institutional investors presumably prosper when their investments appreciate and languish when they disappoint.").

56. *See* Lynn A. Stout, *The Mythical Benefits of Shareholder Control*, 93 VA. L. REV. 789, 804–05 (2007) ("[W]hile shareholders may share in the wealth when the corporation does well and suffer when the firm does poorly, so may employees, creditors, and other stakeholders.").

corporation is performing well, society will benefit from increased economic growth, especially because it is usually the largest corporations that engage in tax avoidance.[57] Sixth, if corporations are doing well, the government will also likely benefit because the electorate will be happy, assuming that tax avoidance leads to a stronger national economy.[58]

The problem is that the harms of tax avoidance offset and eclipse the benefits. Firms that undertake aggressive tax avoidance strategies typically draw additional governmental scrutiny as a result of their behavior,[59] and they are increasingly drawing scorn from the public.[60] Tax avoidance deprives the government of necessary funds to do its job properly,[61] and it allows

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57. *See supra* note 15 and accompanying text (reporting that 73% of Fortune 500 companies reduce their tax burden through the use of tax havens).

58. *Cf.* Christine Fauvelle-Aymar & Mary Stegmaier, *Presidential Popularity Rises and Falls with the Stock Market*, LONDON SCH. OF ECON. U.S. CTR. (Sept. 23, 2013) http://blogs.lse.ac.uk/usappblog/2013/09/23/presidential-popularity-stock-market/ (last visited Feb. 18, 2019) (concluding that presidential approval ratings are higher during times of economic growth) (on file with the Washington and Lee Law Review).

59. *See* Linda M. Beale, *Tax Advice Before the Return: The Case for Raising Standards and Denying Evidentiary Privileges*, 25 VA. TAX REV. 583, 585–86 (2006) ("Recently, abusive tax shelters and customized tax planning have shone a particularly unappealing light on lawyers who single-mindedly pursue their clients' tax-reduction goals . . . . The government's answer to abusive tax transactions has been greater transparency, tougher sanctions, and more vigorous enforcement . . . .").

60. *See* Allison Christians, *Avoidance, Evasion, and Taxpayer Morality*, 44 WASH. U. J.L. & POL'Y 39, 41 (2014) ("[T]he ongoing media coverage of single-digit effective tax rates paid on a global basis by household brand companies like GE, Google, Apple, Starbucks, and Amazon, taught the public about an epidemic of tax avoidance, often characterized as 'aggressive' to move it conceptually closer to the concept of evasion."); Sara Dillon, *Tax Avoidance, Revenue Starvation and the Age of the Multinational Corporation*, 50 INT'L LAW. 275, 276 (2017) ("Tax avoidance by large corporations is well-established, standard practice, and the global public has waited in vain for effective steps to be taken to bring it to an end."); Tracy A. Kaye, *The Offshore Shell Game: U.S. Corporate Tax Avoidance Through Profit Shifting*, 18 CHAP. L. REV. 185, 185 (2014) ("[P]ress coverage is important because public perception matters to legislators on Capitol Hill and the public is becoming increasingly aware of the corporate tax avoidance issue.").

61. *See* Andrew Blair-Stanek, *Intellectual Property Law Solutions to Tax Avoidance*, 62 UCLA L. REV. 2, 54 (2015) ("IP-based tax avoidance imposes enormous economic harm: distorted worldwide investment decisions by multinationals that lower economic output; massive tax revenue losses, with

corporations to shirk paying their fair share of taxes, which angers the public.[62] Even if one views tax avoidance as an implicit tax subsidy because governments sometimes tolerate or ignore it, tax avoidance erodes confidence in the tax system and the democratic process in general because tax avoidance is defined as structuring business transactions to reduce a firm's tax obligations in a manner that technically complies with the law but violates the spirit or underlying policies of the law.[63] In sum, the harms of tax avoidance outweigh its benefits because of the problems it creates.

III. Corporate Fiduciary Duties and the Requirement to Engage in Tax Avoidance (or Lack Thereof)

While tax avoidance does have negative consequences, the benefit to a corporation can be substantial. The issue then becomes whether corporate managers are legally required, permitted, or

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results like higher government deficits, lower spending, and higher taxes on individuals; and the high transaction costs involved in implementing the tax-avoidance strategies.").

62. *See* Leo P. Martinez, *Taxes, Morals, and Legitimacy*, 1994 BYU L. REV. 521, 538 ("The selfishness of tax avoidance is promoted, even admired, despite the fact that reduction of tax liability harms others."); Julie Roin, *Taxation Without Coordination*, 31 J. LEGAL STUD. 61, 75 (2002) ("[Tax avoidance's] sole real-world effect is to decrease government revenues. Those who regard this effect to be harmless fail to appreciate the fact that such lost revenue must be recouped, generally by increasing taxes on other taxpayers or by moving to different taxing mechanisms.").

63. *See* William B. Barker, *The Ideology of Tax Avoidance*, 40 LOY. U. CHI. L.J. 229, 229 (2009) ("Tax avoidance is recognized today by practically all governments as a serious threat to the integrity of tax systems in democratic societies."); Kyle Logue, *Tax Law Uncertainty and the Role of Tax Insurance*, 25 VA. TAX REV. 339, 352 (2005) ("[S]ome tax experts also worry that the highly publicized spread of sophisticated tax avoidance on the part of corporate and wealthy taxpayers undermines the average taxpayer's respect for the system and thus can lead to increased noncompliance at every level."); Stephanie Hunter McMahon, *London Calling: Does the U.K.'s Experience with Individual Taxation Clash with the U.S.'s Expectations?*, 55 ST. LOUIS U. L.J. 159, 214 (2010) ("As studies . . . have shown, the perception of widespread tax avoidance often reduces the compliance of taxpayers who were not previously engaging in tax avoidance because they begin to perceive the system as unfair."); Zoë Prebble & John Prebble, *The Morality of Tax Avoidance*, 43 CREIGHTON L. REV. 693, 726 (2010) ("Both avoidance and evasion risk undermining public confidence in the tax system. This can give rise to a vicious circle: as confidence falls, members of the public become less likely voluntarily to comply with tax laws.").

prohibited to engage in tax avoidance. Many corporate managers will argue that their fiduciary duties to the corporation and its stockholders require them to engage in tax avoidance as a means of achieving profit maximization.[64] They either directly or indirectly derive this requirement from the classic corporate law case, *Dodge v. Ford Motor Co.*,[65] in which the Supreme Court of Michigan held that "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."[66]

Some commentators have argued that the *Dodge* mandate should be rejected and ignored. For example, in *Why We Should Stop Teaching* Dodge v. Ford, Professor Lynn A. Stout argues that the *Dodge* mandate is outdated, is not from a leading court, and is dicta.[67] Moreover, she argues that the *Dodge* mandate is incorrect because charters and articles of incorporation allow those organizing the corporation to focus on more than seeking profit; because most state codes allow corporate managers to focus on more than mere wealth maximization in decision-making for the firm; and because subsequent case law demonstrates a weakening of the *Dodge* mandate.[68] Finally, she argues that economic theory also calls into question whether the *Dodge* mandate yields a "well-functioning corporation."[69] She writes, "most contemporary experts understand that economic theory alone does not permit us to safely assume that corporations are run best when they are run according to the principle of shareholder wealth maximization."[70] As a result, she asserts that the *Dodge* mandate cannot be justified on normative grounds.[71]

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64. *See supra* note 21 and accompanying text (explaining the view by some corporate managers and tax experts that corporations must engage in aggressive tax avoidance).

65. 170 N.W. 668 (Mich. 1919).

66. *Id.* at 684.

67. *See* Lynn A. Stout, *Why We Should Stop Teaching* Dodge v. Ford, 3 VA. L. & BUS. REV. 163, 166–67 (2008) (discussing "why legal experts should hesitate before placing much weight on *Dodge v. Ford*").

68. *See id.* at 169–70.

69. *Id.* at 173.

70. *Id.* at 174.

71. *Id.*

While Professor Stout's article is thoughtfully written and makes many valid points, the relationship of the mandate to tax avoidance is still worth discussing, however, because of the ubiquity of the *Dodge* mandate in classrooms, boardrooms, and courtrooms. As analyzed in my recent article with Professor Karie Davis-Nozemack, *Corporate Tax Avoidance and Honoring the Fiduciary Duties Owed to the Corporation and Its Stockholders*, while the *Dodge* mandate remains true in general because of the fiduciary duties undergirding it, when coupled with the business judgment rule, the *Dodge* mandate fails to require tax avoidance in any specific instance because of the discretion that is granted to corporate managers in undertaking their roles.[72]

A. The Dodge *Mandate*

To begin, a brief overview of the *Dodge* mandate ought to be provided, including a summary of the case from which it derives. In *Dodge v. Ford Motor Co.*, the Supreme Court of Michigan held that for-profit corporations must be run "primarily for the profit of the stockholders."[73] In that case, the Ford Motor Co. became tremendously profitable and was retaining a large amount of money, rather than distributing it to shareholders as dividends.[74] Henry Ford dominated and controlled the board, served as president of the company, and owned 58% of the stock of the corporation.[75] He declared that the company would no longer issue dividends to shareholders and that all future profits would be reinvested in the corporation.[76] Two reasons were cited by the court for this new policy. First, in discussing this policy, Henry Ford was quoted by the Detroit press and by news outlets throughout the United States as declaring, "My ambition . . . is to employ still more men; to spread the benefits of this industrial system to the greatest possible number, to help them build up their lives and their homes. To do this, we are putting the greatest share

72. *See generally* Chaffee & Davis-Nozemack, *supra* note 25.
73. Dodge v. Ford Motor Co., 170 N.W. 668, 684 (Mich. 1919).
74. *See id.* at 670–71.
75. *Id.* at 671.
76. *Id.*

of our profits back into the business."[77] Second, the retained profits were also to be used to build an iron smelting plant to allow the company to produce its own metal parts.[78] As a result of the failure to issue dividends and the new policies underlying them, John F. Dodge and Horace E. Dodge, who were stockholders of the company, brought suit.[79] The lower court ruled in favor of the plaintiffs and held that Ford's actions were impermissible.[80]

The Supreme Court of Michigan affirmed in part and reversed in part.[81] In regard to the humanitarian aspirations of the company, the supreme court affirmed the lower court's holding that they are an impermissible ground for failing to issue dividends.[82] Writing for the majority, Chief Judge Russell C. Ostrander stated, "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."[83] Simply put, a for-profit corporation must be run to make a profit.[84] In regard to the smelting plant, the supreme court reversed the lower court's holding. Chief Judge Ostrander wrote on behalf of the court, "[J]udges are not business experts. It is recognized that plans must often be made for a long future, for expected competition, for a continuing as well as an immediately profitable venture."[85] As a result, because a business purpose existed for the smelting plant, the decision to build such a plant was squarely within the discretion of the individuals running the corporation.[86] In essence, the court was applying the business judgment rule.[87]

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77. *Id.*
78. *Id.*
79. *Id.* at 668.
80. *Id.* at 677.
81. *Id.* at 684.
82. *Id.*
83. *Id.*
84. *Id.*
85. *Id.*
86. *See id.* (applying the business judgment rule in the decision).
87. *Business-Judgment Rule*, BLACK'S LAW DICTIONARY (10th ed. 2014) ("The judicial presumption that in making business decisions not involving direct self-interest or self-dealing, corporate directors act on an informed basis, in good faith, and in the honest belief that their actions are in the corporation's best

Notably, despite the fact that the court in *Dodge v. Ford Motor Co.* stated that for-profit corporations must be run "primarily for the profit of the stockholders," which suggests that other considerations may be taken into account in making decisions for the corporation,[88] some have suggested that the opinion stands for the stronger proposition that corporate management must engage in wealth maximization, i.e., relentless profit seeking.[89] As a result of various limitations, which will be discussed later, the strong version of the *Dodge* mandate that demands unrelenting wealth maximization is likely not defensible.[90] However, at minimum, a robust focus on generating profit is required.

B. The Fiduciary Duties Management Owes to the Corporation and Its Stockholders

Despite the recent criticism regarding the continued relevance of *Dodge v. Ford Co.*, the weaker version of the *Dodge* mandate, i.e., that for-profit corporations must be run "primarily for the profit of the stockholders," does remain true.[91] Even though the *Dodge* mandate is outdated, is not from a leading court, and is dicta,[92] the weaker version of the *Dodge* mandate is derivable from

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interest.").

88. Dodge v. Ford Motor Co., 170 N.W. 668, 684 (Mich. 1919).

89. *See* Stephen M. Bainbridge, *Director Primacy: The Means and Ends of Corporate Governance*, 97 NW. U. L. REV. 547, 575 (2003) ("*Dodge*'s theory of shareholder wealth maximization has been widely accepted by courts over an extended period of time."); Vincent S. J. Buccola, *Beyond Insolvency*, 62 U. KAN. L. REV. 1, 24 (2013) ("The managerial ideal described in *Dodge* and similar cases is that of shareholder-wealth maximization. Not every decided case is consistent with the rule, of course, but it is a fair approximation to say that shareholder-wealth maximization has been the traditional, direct aim of the duty of loyalty."); Keith William Diener, *The Restricted Nature of the Profit Motive: Perspectives from Law, Business, and Economics*, 30 NOTRE DAME J.L. ETHICS & PUB. POL'Y 225, 237 (2016) ("The 1919 Michigan Supreme Court case of *Dodge v. Ford* is often cited as the basis for a legal obligation to maximize shareholder wealth.").

90. *See infra* Part III.C (exploring various limitations placed upon the *Dodge* mandate, including the business judgment rule, constituency statutes, and drafting of bylaws and articles of incorporation).

91. *Dodge*, 170 N.W. at 684.

92. *See* Stout, *supra* note 67 and accompanying text (discussing Professor Lynn A. Stout's criticisms of teaching *Dodge v. Ford Motor Co.*).

the fiduciary duties that corporate managers owe to the corporation and its stockholders.

Although sometimes known by different names, the fiduciary duties management by default owes to the corporation and its stockholders are care, loyalty, good faith, and disclosure.[93] The duty of care requires corporate managers to reasonably inform themselves of material facts prior to making decisions,[94] and it includes the obligation to engage in basic monitoring of the business entity.[95] It does not require that the decision that has

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93. *See* S. Burcu Avci, Cindy A. Schipani & H. Nejat Seyhun, *Ending Executive Manipulations of Incentive Compensation*, 42 J. CORP. L. 277, 314 (2016) ("Although the Delaware courts have stated that there are no other fiduciary duties outside of the recognized duties of care, loyalty, and perhaps good faith, some applications of these duties may include the duty of candor or disclosure."); David L. Ponet & Ethan J. Leib, *Fiduciary Law's Lessons for Deliberative Democracy*, 91 B.U. L. REV. 1249, 1257 (2011) ("The fiduciary duties are routinely described as a duty of loyalty and a duty of care—as well as duties of candor, disclosure, and utmost good faith."); Cynthia A. Williams & John M. Conley, *Is There an Emerging Fiduciary Duty to Consider Human Rights?*, 74 U. CIN. L. REV. 75, 87 (2005) ("Corporate directors have a number of well-established fiduciary duties under state corporate law: the duties of care, loyalty and full disclosure, and the duty to act in good faith.").

94. *See* Jorge E. Leal Garrett & Bryan A. Green, *Considerations for Professional Sports Teams Contemplating Going Public*, 31 N. ILL. U. L. REV. 69, 85 (2010) ("[T]he duty of care imposes an obligation on the directors of the corporation to inform themselves of material information prior to making any decision."); Claire Hill & Brett McDonnell, *Sanitizing Interested Transactions*, 36 DEL. J. CORP. L. 903, 908 (2011) ("The duty of care requires directors to be adequately informed in making all corporate decisions."); Gabriel Rauterberg & Eric Talley, *Contracting Out of the Fiduciary Duty of Loyalty Waivers: An Empirical Analysis of Corporate Opportunity Waivers*, 117 COLUM. L. REV. 1075, 1084 (2017) ("The duty of care mandates that corporate fiduciaries exercise informed business judgment in their stewardship of the company, imposing liability if a fiduciary acts (or fails to act) without first being adequately informed.").

95. *See* Seth Davis, *The False Promise of Fiduciary Government*, 89 NOTRE DAME L. REV. 1145, 1164 (2014) ("Directors . . . owe a duty of care, which requires informed decisionmaking and some modicum of monitoring of the corporation's activities."); Julie Andersen Hill & Douglas K. Moll, *The Duty of Care of Bank Directors and Officers*, 68 ALA. L. REV. 965, 972 (2017) ("[D]irectors and officers are obligated to use care in monitoring the activities of the principal employees and the general affairs of the corporation as a whole."); Lyman P.Q. Johnson & Mark A. Sides, *The Sarbanes-Oxley Act and Fiduciary Duties*, 30 WM. MITCHELL L. REV. 1149, 1198 (2004) ("Directors . . . may be liable for breach of the duty of care if they fail to properly monitor and oversee the business affairs of a

been made be correct or wise, and mere errors in judgment do not constitute a breach of the duty of care.[96] The duty is procedural in nature,[97] and a court will not look at the substance of the decision, unless the decision constitutes corporate waste.[98] Adherence to the duty is judged by a gross negligence standard.[99] Even so,

corporation.").

96. *See* Leonard M. Baynes, *Racial Stereotypes, Broadcast Corporations, and the Business Judgment Rule*, 37 U. RICH. L. REV. 819, 856 (2003) ("Mere errors of judgment and honest mistakes are insufficient as grounds for breach of the duty of care. . . . Traditionally, courts generally do not want to interfere with the corporate executives' discretion."); Robert J. Rhee, *The Tort Foundation of Duty of Care and Business Judgment*, 88 NOTRE DAME L. REV. 1139, 1197 (2013) ("[T]he duty of care is a misnomer to the extent that it suggests liability for economic loss caused by errors in judgment. Corporation law is correct to preclude substantive review of good or bad risk taking . . . .").

97. *See* Onnig H. Dombalagian, *Investment Recommendations and the Essence of Duty*, 60 AM. U. L. REV. 1265, 1323 (2011) ("In the context of corporate law, the duty of care has been rendered largely a procedural rule, rather than a substantive rule, in order to free directors to take calculated risks."); Stephen Ellis, Grant Hayden & Cynthia Rogers, *A Game Changer for the Political Economy of Economic Development Incentives*, 56 ARIZ. L. REV. 953, 976 (2014) ("In the corporate setting, the board of directors is subject to a legal duty of care, which imposes a procedural requirement that it asks the right sorts of questions and considers the right sorts of information when making decisions."); Charles R. Korsmo, *Lost in Translation: Law, Economics, and Subjective Standards of Care in Negligence Law*, 118 PENN ST. L. REV. 285, 336–37 (2013) ("[C]ompliance with the duty of care in corporate law—at least in Delaware—is largely evaluated in procedural terms, i.e., did the board employ a thorough procedure?").

98. *See* Carl T. Bogus, *Excessive Executive Compensation and the Failure of Corporate Democracy*, 41 BUFF. L. REV. 1, 77 (1993) ("[W]hen directors waste corporate assets they violate their duty of substantive due care . . . ."); Brett H. McDonnell, *Committing to Doing Good and Doing Well: Fiduciary Duty in Benefit Corporations*, 20 FORDHAM J. CORP. & FIN. L. 19, 43 (2014) ("The substantive side of the duty of care is embodied in the . . . waste standard: managers may be held liable for actions which are so irrational that they amount to giving away corporate assets."); William O. Fisher, *To Thine* Own *CEO Be True: Tailoring CEO Compensation to Individual Personality and Circumstances*, 2017 COLUM. BUS. L. REV. 599, 666 (2017) ("[D]uty of care prohibits extreme substantive decisions that cannot conceivably benefit the corporation and effectively constitute waste.").

99. *See* Kathleen M. Boozang, *Responsible Corporate Officer Doctrine: When is Falling Down on the Job a Crime?*, 6 ST. LOUIS U. J. HEALTH L. & POL'Y 77, 93 (2012) ("The duty of care requires boards to engage ordinary care in the processes by which they make decisions, and to supervise and monitor the activities of corporate managers; however, liability results only when the fiduciaries' behavior constitutes gross negligence."); Daniel S. Kleinberger, *Delaware Dissolves the Glue of Capitalism: Exonerating from Claims of Incompetence Those Who Manage Other People's Money*, 38 WM. MITCHELL L. REV. 737, 745 (2012) ("Delaware law

determining what constitutes reasonably informing oneself of relevant information is far from a bright-line standard. As a result, states have enacted statutes allowing corporations to include provisions in their articles of incorporation eliminating liability for breaches of the duty of care, if those organizing and owning the corporation decide to do so.[100]

Next, the duty of loyalty requires that corporate managers not engage in self-dealing.[101] This means that corporate managers

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has always been careful about imposing liability on corporate directors. Delaware states its duty of care as the avoidance of 'gross negligence' and uses the business judgment rule to reinforce the protections against personal liability for directors of Delaware corporations."); J. Haskell Murray & Edward I. Hwang, *Purpose with Profit: Governance, Enforcement, Capital-Raising and Capital-Locking in Low-Profit Limited Liability Companies*, 66 U. MIAMI L. REV. 1, 33 (2011) ("Under Delaware law, which often cues the market for corporate law, the directors' conduct is measured against a gross negligence standard in duty of care cases.").

100. *See* Janet E. Kerr, *The Financial Meltdown of 2008 and the Government's Intervention: Much Needed Relief or Major Erosion of American Corporate Law? The Continuing Story of Bank of America, Citigroup, and General Motors*, 85 ST. JOHN'S L. REV. 49, 83 (2011) (explaining that the Delaware General Corporation Law "allows shareholders to adopt a clause in their corporation's articles of incorporation protecting directors from personal liability for monetary damages for breaching the duty of care. Since Delaware enacted section 102(b)(7), all other jurisdictions, with the exception of the District of Columbia, have enacted a similar provision"); Geoffrey P. Miller, *Pleading After* Tellabs, 2009 WIS. L. REV. 507, 531 n.52 ("Section 102(b)(7) of the Delaware General Corporation Law, and its counterparts in other states, now allows companies to exempt directors from liability for money damages for breaches of the duty of care, even if the conduct involves gross negligence."); Amy Deen Westbrook, *Does the Buck Stop Here? Board Responsibility for FCPA Compliance*, 48 U. TOL. L. REV. 493, 506 (2017) ("Director personal liability, however, has been limited by most states, Delaware in particular, . . . [by corporate law statutes] providing that corporations may include in their articles of incorporation clauses that exculpate directors from monetary liability for conduct that is a breach of their duty of care.").

101. *See* Jordan M. Barry & John William Hatfield, *Pills & Partisans: Understanding Takeover Defenses*, 160 U. PA. L. REV. 633, 638 (2012) ("[C]orporate law imposes a duty of loyalty on corporate managers that prohibits them from self-dealing to the detriment of the shareholders."); John A. Pearce II, *The Rights of Shareholders in Authorizing Corporate Philanthropy*, 60 VILL. L. REV. 251, 270 (2015) ("The duty of loyalty requires directors to act on behalf of the corporation and not engage in acts that constitute self-dealing or benefiting improperly from their positions, to the detriment of shareholders."); Russell C. Silberglied, *Litigating Fiduciary Duty Claims in Bankruptcy Court and Beyond: Theory and Practical Considerations in an Evolving Environment*, 10 J. BUS. & TECH. L. 181, 185 (2015) ("The duty of loyalty prohibits a corporate director from

cannot use their positions to advance their own interests at the expense of the corporation and its stockholders.[102] This requires that managers put the interests of the corporations and stockholders that they serve ahead of their own financial and other personal pursuits.[103] Moreover, the duty requires that managers disclose and mitigate conflicts of interests with the corporations and stockholders.[104] It also limits their ability to engage in

engaging in self-dealing . . . .").

102. *See* Iman Anabtawi, *Predatory Management Buyouts*, 49 U.C. DAVIS L. REV. 1285, 1290 (2015) ("Self-dealing offends the very essence of the fiduciary duty of loyalty applicable to corporate managers. According to that duty, managers must place the best interests of the corporation and its shareholders ahead of their personal interests."); Avci, Schipani & Seyhun, *supra* note 93, at 312 ("The duty of loyalty requires that corporate officers and directors act in the best interest of the corporation and prioritize the interests of the corporation over their own self-interests."); Alina S. Ball, *Social Enterprise Governance*, 18 U. PA. J. BUS. L. 919, 957 (2016) ("[T]he duty of loyalty . . . requires the director to place the interest of the corporation above her own personal interest in a transaction or decision.").

103. *See* Lisa M. Fairfax, *Managing Expectations: Does the Directors' Duty to Monitor Promise More Than It Can Deliver?*, 10 U. ST. THOMAS L.J. 416, 419 (2012) ("The duty of loyalty seeks to ensure that in those situations, directors do not place their own interests before the interests of the corporation and its shareholders."); Nizan Geslevich Packin, *It's (Not) All About the Money: Using Behavioral Economics to Improve Regulation of Risk Management in Financial Institutions*, 15 U. PA. J. BUS. L. 419, 444 (2013) ("[D]irectors owe a duty of loyalty to prioritize the interests of the corporation and its shareholders over their own."); Amy Deen Westbrook, *Does Banking Law Have Something to Teach Corporations Law About Directors' Duties?*, 55 WASHBURN L.J. 397, 398 (2016) ("In fulfilling their duty of loyalty, directors must not put their own interests, or even the interests of others, ahead of those of the corporation.").

104. *See* Virginia Harper Ho, *Of Enterprise Principles and Corporate Groups: Does Corporate Law Reach Human Rights?*, 52 COLUM. J. TRANSNAT'L L. 113, 152 (2013) ("[T]he duty of loyalty requires the fiduciary to act in the best interests of the corporation without self-dealing and to disclose the nature of any conflict of interest or opportunity that may confer a financial benefit upon the fiduciary that is unavailable to other shareholders or to the corporation."); Phill Kline, Robert T. Stephan & Reid F. Holbrook, *Protecting Charitable Assets in Hospital Conversions: An Important Role for the Attorney General*, 13 KAN. J.L. & PUB. POL'Y 351, 360 (2004) ("The duty of loyalty requires corporate directors to disclose actual and potential conflicts of interest in business transactions and act in the best interests of the corporation."); Dana M. Muir & Cindy A. Schipani, *Fiduciary Constraints: Correlating Obligation with Liability*, 42 WAKE FOREST L. REV. 697, 717 (2007) ("The duty of loyalty requires that corporate interests supersede personal interests, and when conflicts of interest occur, they must either be avoided or disclosed and approved by disinterested directors.").

transactions with the corporation and limits their ability to take advantage of corporate opportunities.[105]

In addition, the duty of good faith requires that corporate managers deal fairly and honestly with the corporation and its stockholders.[106] Some courts and commentators have conceived of this duty as an independent fiduciary duty,[107] while other courts and commentators have conceived of it as a subsidiary duty to the duty of loyalty.[108] The duty of good faith is often coupled with other

105. *See* Norman D. Bishara & Cindy A. Schipani, *A Corporate Governance Perspective on the Franchisor-Franchisee Relationship*, 19 STAN. J.L. BUS. & FIN. 303, 316 (2014) ("[T]he duty of loyalty is breached when directors divert corporate opportunities, assets, or information away from the corporation for their own personal gain."); Ian David McClure, *Accountability in the Patent Market: A Duty to Monitor Patent Risk from the Boardroom*, 31 SANTA CLARA HIGH TECH. L.J. 217, 231 (2015) ("The duty of loyalty generally arises through a conflict of interest created by a director that diverts corporate assets or usurps opportunities or information from the corporation for personal gain."); Peter Molk, *How Do LLC Owners Contract Around Default Statutory Protections?*, 42 J. CORP. L. 503, 524–25 (2017) ("In addition, to a general bar on self-dealing, the duty of loyalty has expanded to include a prohibition on competing with the firm via one's other activities as well as a prohibition against claiming corporate opportunities for oneself.").

106. *See* Byron F. Egan, *Fiduciary Duties of Corporate Directors and Officers in Texas*, 43 TEX. J. BUS. L. 45, 62–63 (2009) ("The duty of good faith requires that directors act honestly, in the best interest of the corporation, and in a manner that is not knowingly unlawful or contrary to public policy."); Melvin A. Eisenberg, *The Duty of Good Faith in Corporate Law*, 31 DEL. J. CORP. L. 1, 5 (2006) ("The duty of good faith in corporate law is comprised of a general baseline conception . . . of four elements: subjective honesty, or sincerity; nonviolation of generally accepted standards of decency applicable to the conduct of business; nonviolation of generally accepted basic corporate norms; and fidelity to office."); Janet E. Kerr, *Developments in Corporate Governance: The Duty of Good Faith and Its Impact on Director Conduct*, 13 GEO. MASON L. REV. 1037, 1051 (2006) ("[D]irectors may be held personally liable for corporate misbehavior if their conduct evidences improper motive or ill will, a reckless disregard of known risks, a sustained failure to oversee management, or is so egregious that it is unexplainable on any other grounds other than bad faith.").

107. *See* Hillary A. Sale, *Delaware's Good Faith*, 89 CORNELL L. REV. 456, 494 (2004) ("[G]ood faith is a separate duty from those of care and loyalty."); Julian Velasco, *How Many Fiduciary Duties Are There in Corporate Law?*, 83 S. CAL. L. REV. 1231, 1271 (2010) ("[T]he Delaware General Corporation Law provides support for the existence of an independent duty of good faith. Although it does not explicitly create the duty of good faith, neither does it explicitly create a duty of care or loyalty.").

108. *See* Seth Davis, *The False Promise of Fiduciary Government*, 89 NOTRE

fiduciary duties to express a court's disdain for a particular breach, and it is often used as a gap-filler when the other fiduciary duties may not easily apply.[109] This is especially true when the liability for breaching the duty of care has been eliminated in the corporation's articles of incorporation.[110] Because allowing corporations to eliminate the duty of care by placing a provision in their articles of incorporation is a relatively recent innovation in corporate law, the duty of good faith is currently in a state of flux and its coverage is evolving.[111]

Finally, the duty of disclosure requires that corporate managers disclose information that is material to the operation of the corporation.[112] Some view this duty as a subsidiary duty to the

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DAME L. REV. 1145, 1164–65 (2014) ("For a time, Delaware, the leading corporate law jurisdiction, flirted with an independent duty of good faith, ... [b]ut in *Stone v. Ritter* the court folded the duty of good faith into the duty of loyalty . . . ."); Jonathan C. Lipson, *Governance in the Breach: Controlling Creditor Opportunism*, 84 S. CAL. L. REV. 1035, 1074 (2011) ("Today, leading authorities seem to view the debate as having come to rest at the latter point: good faith in the corporate governance context is not a separate class of fiduciary duty, but instead is a subspecies of the duty of loyalty."); Edward B. Rock, *Adapting to the New Shareholder-Centric Reality*, 161 U. PA. L. REV. 1907, 1960 (2013) ("Part of the fiduciary duty of loyalty is the duty to act in good faith.").

109. *See* Sean J. Griffith, *Good Faith Business Judgment: A Theory of Rhetoric in Corporate Law Jurisprudence*, 55 DUKE L.J. 1, 6 (2005) ("[T]he emerging duty of good faith is best understood as a rhetorical device rather than as a substantive standard."); Troy A. Paredes, *Too Much Pay, Too Much Deference: Behavioral Corporate Finance, CEOs, and Corporate Governance*, 32 FLA. ST. U. L. REV. 673, 753–54 n.296 (2005) ("[B]ecause the duty of good faith is malleable, Delaware judges have room to shape the duty of good faith, whereas judges have less flexibility extending the duties of care and loyalty, the contours of which are more fixed by an extensive body of caselaw and recognized corporate law principles.").

110. *See supra* note 100 (explaining that many states have adopted statutes allowing corporations to place provisions in their articles of incorporation eliminating the duty of care).

111. *See* Regina F. Burch, *Director Oversight and Monitoring: The Standard of Care and the Standard of Liability Post-Enron*, 6 WYO. L. REV. 481, 525 (2006) ("The contours of the duty of good faith, as a fiduciary duty not subsumed within the duty of loyalty or the duty of care, are still evolving.").

112. *See* James A. Fanto, *Braking the Merger Momentum: Reforming Corporate Law Governing Mega-Mergers*, 49 BUFF. L. REV. 249, 306–07 n.184 (2001) ("The duty of disclosure obligates directors to provide the stockholders with accurate and complete information material to a transaction or other corporate event that is being presented to them for action."); Jack B. Jacobs, *The Fiduciary Duty of Disclosure After* Dabit, 2 J. BUS. & TECH. L. 391, 395 (2007) ("A classic, although perhaps not complete, definition of the fiduciary duty of disclosure under Delaware law is that corporate directors are required to disclose all material

duties of care and loyalty,[113] but others view it as a separate fiduciary duty.[114] Regardless, significant portions of this duty have been codified within federal and state securities regulation.[115] In

information within their control when they seek stockholder action."); Jennifer O'Hare, *Director Communications and the Uneasy Relationship Between the Fiduciary Duty of Disclosure and the Anti-Fraud Provisions of the Federal Securities Laws*, 70 U. CIN. L. REV. 475, 492 (2002) ("The fiduciary duty of disclosure requires directors of Delaware corporations to fully and fairly disclose all material facts within their control when they make certain communications to their shareholders. Put simply, if a director makes a material misrepresentation to shareholders, he has potentially breached his fiduciary duty of disclosure.").

113. *See* Kenneth R. Davis, *Cash of the Titans: Arbitrating Challenges to Executive Compensation*, 86 TEMP. L. REV. 245, 250 (2014) ("Officers and directors have fiduciary duties of care, loyalty, and good faith to their corporation and its shareholders, though courts often view the duty of good faith as a subset of the duty of loyalty."); Rebecca Hollander-Blumoff, *Social Value Orientation and the Law,* 59 WM. & MARY L. REV. 475, 499 n.141 (2017) ("[T]he Delaware Supreme Court has described the duty of good faith as a subsidiary element or condition of the duty of loyalty."); Mike Koehler, *Foreign Corrupt Practices Act Ripples*, 3 AM. U. BUS. L. REV. 391, 434 (2014) ("A director's fiduciary duties include the duty of care and the duty of loyalty, including its subsidiary component the duty of good faith.").

114. *See* David Rosenberg, *Making Sense of Good Faith in Delaware Corporate Fiduciary Law: A Contractarian Approach*, 29 DEL. J. CORP. L. 491, 513 (2004) ("Viewed as a device for interpreting contracts or other kinds of obligations, the duty of good faith seems not to be a subsidiary or subset of loyalty as the Delaware Court of Chancery would have made it. Rather, the duty to act in good faith is broader . . . ."); Luke Scheuer, *The "Legal" Marijuana Industry's Challenge for Business Entity Law*, 6 WM. & MARY BUS. L. REV. 511, 538 (2015) ("[M]anagers owe their businesses and investors a duty of good faith, which some states include as a separate fiduciary duty and some include as a part of the duty of care or loyalty."); Julian Velasco, *A Defense of the Corporate Law Duty of Care,* 40 J. CORP. L. 647, 680–81 (2015) ("The duty of good faith has alternatively been described as one of triads of fiduciary duty and as a subset of the duty of loyalty . . . .").

115. *See* Donald C. Langevoort, *On Leaving Corporate Executives "Naked, Homeless and Without Wheels": Corporate Fraud, Equitable Remedies, and the Debate Over Entity Versus Individual Liability*, 42 WAKE FOREST L. REV. 627, 631 (2007) ("Although fraud fits easily enough into the duty of candor category at state law, most of the litigation about fraud takes place in federal court under the federal securities laws."); Geoffrey Rapp*, On the Liability of Corporate Directors to Holders of Securities for Illegal Corporate Acts: Can the Tension Between the "Net-Loss" and "No-Duty-to-Disclose" Rules Be Resolved*, 7 FORDHAM J. CORP. & FIN. L. 101, 111 (2001) ("Under federal securities laws, corporate directors have an affirmative duty of disclosure under certain circumstances."); Kellye Y. Testy, *Linking Progressive Corporate Law with Progressive Social Movements*, 76 TUL. L. REV. 1227, 1235 (2002) ("[L]arge public corporations are already under

regard to federal securities regulation, Justice Arthur Goldberg famously wrote in the majority opinion for *SEC v. Capital Gains Research Bureau, Inc.*,[116] "[a] fundamental purpose . . . [of federal securities law] was to substitute a philosophy of full disclosure for the philosophy of *caveat emptor* and thus to achieve a high standard of business ethics in the securities industry."[117] The same is true of state systems of securities law.[118]

The issue now becomes whether the *Dodge* mandate is derivable from these fiduciary duties, which it is. For purposes of deriving the *Dodge* mandate, among the fiduciary duties that management owes to the corporation and its stockholders, the most important is the duty of loyalty.[119] The *Dodge* mandate requires, "[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."[120] The duty of loyalty requires that corporate managers cannot use their positions to advance their own interests at the expense of the interests of the corporation and its stockholders.[121] The interests of a for-profit corporation, although they can be altered in the articles of incorporation, are primarily to make a profit.[122] The interests of

substantial duties of disclosure under the federal securities laws . . . .").

116. 375 U.S. 180 (1963).

117. *Id.* at 186.

118. *See* Therese H. Maynard, *The Uniform Limited Offering Exemption: How "Uniform" is "Uniform?"—An Evaluation and Critique of the ULOE*, 36 EMORY L.J. 357, 363 n.12 (1987) ("State Blue Sky statutes . . . generally insist on full disclosure of all material facts as the basis for their local regulatory scheme. Many states, however, . . . also apply the merit standard of review to examine the fairness of the terms of a proposed offering.").

119. *See supra* notes 101–105 (providing an overview of the duty of loyalty).

120. Dodge v. Ford Motor Co., 170 N.W. 668, 684 (Mich. 1919).

121. *See supra* notes 101–105 and accompanying text (explaining the contours of the duty of loyalty).

122. *See* Caroline Mala Corbin, *Corporate Religious Liberty*, 30 CONST. COMMENT. 277, 293 (2015) ("By definition, for-profit corporations exist to make money; otherwise they would be non-profit."); Carol Goforth, *A Corporation Has No Soul, and Doesn't Go to Church: Relating the Doctrine of Piercing the Veil to* Burwell v. Hobby Lobby, 67 S.C. L. REV. 73, 78 (2015) ("The purpose of a for-profit corporation is to run a business and make a profit . . . ."); Daniel J. Morrissey, *The Riddle of Shareholder Rights and Corporate Social Responsibility*, 80 BROOK. L. REV. 353, 353 (2015) ("Corporations exist primarily to make profit for their shareholders. This has been the black letter rule of law and the reigning orthodoxy of American business for a century."); Christyne J. Vachon, *Playing in*

the shareholders are more complex. Shareholders may buy the stock of a corporation for a myriad of different reasons, including wanting to make a profit; liking the corporation's products; liking the corporation's services; liking the corporation's politics; having personal or professional relationships with the individuals organizing, operating, or owning the corporation; or wanting for some other reason to be affiliated with the firm.[123] This raises the following question: what interests of shareholders does the duty of loyalty protect? To answer this question, one must remember that the corporate form is contractual in nature.[124] By purchasing stock in a corporation, the shareholders are agreeing to be bound together in a common entity that is designed to make a profit.[125] Although shareholders may buy stock for a myriad of different reasons, the one that matters for purposes of determining the

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the Sandbox: Moral Development and the Duty of Care in Collaborations Between For-Profit and Nonprofit Corporate Persons, 33 PACE L. REV. 1045, 1067 (2013) ("[T]he underlying constraint on the for-profit is that law restricts its goal as a cooperative enterprise to . . . profit maximization for the benefit of the corporation and its owners.").

123. *See* Rugger Burke & Samuel P. Bragg, *Sustainability in the Boardroom: Reconsidering Fiduciary Duty Under* Revlon *in the Wake of Public Benefit Corporation Legislation*, 8 VA. L. & BUS. REV. 59, 71 (2014) ("[M]any shareholders invest for reasons other than just the bottom line. For example, many investors take a socially responsible approach by endorsing companies that share their values or do not invest in industries that they find to be inherently negative."); Paul Rose, *Common Agency and the Public Corporation*, 63 VAND. L. REV. 1355, 1373 (2010) ("[S]ome shareholders invest with what may be characterized as mixed motives—they are largely concerned with financial returns, but are also likely, for various reasons, to support certain social causes.").

124. *See* Michael M. Epstein & Nazgole Hashemi, *Crowdfunding in Wonderland: Issuer and Investor Risks in Non-Fraudulent Creative Arts Campaigns Under the Jobs Act*, 6 AM. U. BUS. L. REV. 1, 11 (2016) ("[T]he Contractarian theory of corporate law . . . holds that the relationship between the shareholders and managers of a public corporation is contractual in nature."); Benjamin D. Landry, 18 FORDHAM J. CORP. & FIN. L. 889, 894 (2013) ("The courts and the academic community have, for many years, broadly conceptualized the relationship between the stockholders, the board of directors, and the corporation as contractual in nature."); Ann Lipton, *Manufactured Consent: The Problem of Arbitration Clauses in Corporate Charters and Bylaws*, 104 GEO. L.J. 583, 589 (2016) ("There is a long history of courts referring to a corporation's constitutive documents as contractual in nature.").

125. *See supra* note 122 and accompanying text (discussing the purpose of a for-profit corporation).

contours of the duty of loyalty owed by corporate managers is the interest in making a profit because that is the agreement that they made by investing in a for-profit corporation. This means that the *Dodge* mandate is derivable from the duty of loyalty because the duty of loyalty requires that managers must put aside their other interests for purposes of seeking profit for the corporation and its stockholders.[126]

The duties of care, good faith, and disclosure also support the *Dodge* mandate.[127] Because the duty of care requires managers to reasonably inform themselves of material facts prior to making decisions,[128] and because for-profit corporations exist to make a profit,[129] corporate managers must reasonably inform themselves of profit-making activities and cost-reducing opportunities. Although the duty of care does not require that decisions be correct or wise,[130] it forces corporate managers to focus on profit-making and profit-maximizing in performance of their duties, i.e., it forces corporate managers to focus on the *Dodge* mandate.[131]

The relationship between the duty of good faith and the *Dodge* mandate is more difficult to define for two reasons. First, the duty of good faith is malleable, and its contours are difficult to define.[132] Second, the duty of good faith is evolving in the wake of state legislatures' relatively recent decisions to allow corporations to include provisions in their articles of incorporation eliminating the duty of care, which has led to the duty of good faith regulating some of the conduct that the duty of care used to be employed to

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126. *See supra* notes 101–105, 122 and accompanying text (discussing the duty of loyalty and the purpose of a for-profit corporation).

127. *See supra* notes 98–1040,1106–115, 1182–18 and accompanying text (discussing the duties of care, good faith, and disclosure).

128. *See supra* notes 98–1040 and accompanying text (describing the duty of care).

129. *See supra* note 122 and accompanying text.

130. *See supra* notes 96–98 and accompanying text (reporting that the duty of care does not require that corporate managers make an accurate or intelligent decision).

131. *See* Dodge v. Ford Motor Co., 170 N.W. 668, 684 (Mich. 1919) (stating that corporations should be managed "primarily for the profit of the stockholders").

132. *See supra* notes 106–11 and accompanying text (describing the duty of good faith).

regulate.[133] With that said, the duty of good faith requires that corporate managers deal fairly and honestly with the corporation and its stockholders.[134] Because the relationship among the corporation, its stockholders, and its managers exists for purposes of making a profit,[135] this suggests that the duty of good faith requires that corporate managers adhere to the *Dodge* mandate as a consequence of the agreement struck that beget the corporation and allowed the investors to invest in it.

Lastly, the duty of disclosure also helps to support the *Dodge* mandate as well. Although the duty does not directly require that the corporation primarily seek profit, it does require that corporate managers disclose information that is material to the operation of the corporation, especially when mandated by state and federal securities regulation.[136] As a consequence, this creates transparency in the operation of the corporation that makes it more apparent whether managers are adhering to the *Dodge* mandate.

C. Limitations upon the Dodge Mandate and the Lack of Clear Guidance in Tax Avoidance Matters

While the *Dodge* mandate and the fiduciary duties from which it derives might seem to require corporate managers to unrelentingly attempt to maximize profit, various limitations on the mandate give managers wide latitude in how they undertake their functions.[137] Notably, the mandate itself only requires that "[a] business corporation is organized and carried on primarily for

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133. *See supra* notes 110–11 and accompanying text (explaining that the duty of good faith is evolving because many states allow corporations to draft articles of incorporation in ways that eliminate the duty of care, which creates questions as to whether the duty of good faith might cover some of the behavior that the duty of care previously covered).

134. *See supra* notes 106–11 and accompanying text (describing the duty of good faith).

135. *See supra* note 122 and accompanying text.

136. *See supra* note 112–18 and accompanying text (exploring the duty of disclosure).

137. Dodge v. Ford Motor Co., 170 N.W. 668, 684 (Mich. 1919).

the profit of the stockholders."[138] The word "primarily" suggests that other interests may be considered.[139] These other interests could be included in the articles of incorporation or bylaws. Even if they are not, many jurisdictions have adopted constituency statutes that allow corporate managers to consider a much wider range of interests of other constituencies—such as creditors, employees, customers, and the general public—beyond the interests of stockholders in making profits.[140] In addition, corporate managers can also seek stockholder approval or ratification in the event that they are pursuing courses of action that might be an affront to the *Dodge* mandate.[141]

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138. *Id.*

139. *Id.*

140. *See* ALA. CODE § 10A-2-11.03(c) (2017); ARIZ. REV. STAT. ANN. §§ 10-830(D), 10-2702 (2017); ARK. CODE ANN. § 4-27-1202(c) (2017); COLO. REV. STAT. § 7-106-105(7) (2017); CONN. GEN. STAT. § 33-756(g) (West 2018); FLA. STAT. § 607.0830(3) (2017); GA. CODE ANN. § 14-2-202(b)(5) (West 2018); IDAHO CODE § 30-1702 (2017); 805 ILL. COMP. STAT. 5/8.85 (2017); IND. CODE § 23-1-35-1(d) (2017); IOWA CODE § 491.101B (2017); KY. REV. STAT. ANN. § 271B.12-210(4) (West 2018); ME. STAT. tit. 13-C § 831(6) (2017); MASS. GEN. LAWS ch. 156B, § 65 (2017); MINN. STAT. § 302A.251(5) (2017); MISS. CODE ANN. § 79-4-8.30(f) (2017); MO. ANN. STAT. § 351.347(1) (West 2018); MONT. CODE ANN. § 35-1-815(3) (2017); NEV. REV. STAT. § 78.138(4) (2017); N.H. REV. STAT. ANN. § 293-A:12.02(c) (2017); N.J. STAT. ANN. § 14A:6-1(2) (West 2018); N.M. STAT. ANN. § 53-11-35(D) (West 2018); N.Y. BUS. CORP. LAW § 717(b) (McKinney 2017); N.C. GEN. STAT. § 55-11-03(c) (2017); N.D. CENT. CODE § 10-19.1-50(6) (2017); OHIO REV. CODE ANN. § 1701.59(F) (West 2018); OR. REV. STAT. § 60.357(5) (2017); 15 PA. CONS. STAT. § 1715(a) (2017); 7 R.I. GEN. LAWS ANN. § 7-5.2-8(a) (West 2018); S.C. CODE ANN. § 33-11-103(c) (2017); S.D. CODIFIED LAWS. § 47-33-4 (2017); TENN. CODE ANN. § 48-103-204 (2017); TEX. BUS. ORGS. CODE ANN. § 21.401 (West 2018); UTAH CODE ANN. §§ 16-10a-840(5), 16-10a-1103(3) (West 2018); VT. STAT. ANN. tit. 11A, § 8.30(a)(3) (2017); VA. CODE ANN. § 13.1-718(B) (2017); WASH. REV. CODE § 23B.11.030(3) (2017); WIS. STAT. § 180.0827 (2017); WYO. STAT. ANN. § 17-16-830(g) (2017); *see also* Burke & Bragg, *supra* note 123, at 68 n.34 ("Constituency statutes, also known as stakeholder statutes, permit a board of directors to consider an enumerated list of constituent (i.e., primary stakeholder) interests as well as shareholder interests when making business decisions."). *But see* William H. Clark, Jr. & Elizabeth K. Babson, *How Benefit Corporations Are Redefining the Purpose of Business Corporations*, 38 WM. MITCHELL L. REV. 817, 830–31 (2012) ("Conspicuously absent from the list of states adopting constituency statutes is Delaware, where more than 900,000 business entities have their legal home, including more than fifty percent of all U.S. publicly-traded companies and sixty-three percent of the Fortune 500 companies.").

141. *See* Kelli A. Alces, *Debunking the Corporate Fiduciary Myth*, 35 J. CORP. L. 239, 249 (2009) ("Activity that would otherwise constitute a breach of the duty of loyalty can be cured or ratified by approval from a majority of disinterested directors or a majority of disinterested shareholders."); J. Travis Laster, *The*

However, the most important limitation on the *Dodge* mandate is the business judgment rule, which gives corporate managers broad discretion in making business decisions.[142] The business judgment rule exists because courts do not wish to spend their time second-guessing corporate managers.[143] Judges frequently have limited experience with making business decisions, and managers know their corporations' operations and the environments in which they exist better than a court

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Effect of Stockholder Approval on Enhanced Scrutiny, 40 WM. MITCHELL L. REV. 1443, 1459 (2014) ("If the board makes a business decision on an issue within its authority and submits the matter to the stockholders for a voluntary vote, . . . then the resulting stockholder approval . . . causes the business judgment rule to protect the board's decision . . . ."); D. Theodore Rave, *Politicians as Fiduciaries*, 126 HARV. L. REV. 671, 703 (2013) ("[C]orporate law provides two primary safe harbor options for cleansing the taint of interested director transactions: (1) approval by a majority of the disinterested directors or (2) ratification through a fully informed vote by a majority of the disinterested shareholders.").

142. *See* Paul B. Miller & Andrew S. Gold, *Fiduciary Governance*, 57 WM. & MARY L. REV. 513, 581–82 (2015) ("[D]irectors have substantial freedom to make decisions in the public interest. The business judgment rule means that courts will refuse to second guess directors' substantive business decisions, barring conflicts of interest, corporate waste, or egregious procedural impropriety."); Chad J. Pomeroy, *Well Enough Alone: Liability for Wrongful Foreclosure*, 68 ALA. L. REV. 943, 960 (2017) ("The business judgment rule is, essentially, a presumption of correctitude reflecting the judiciary's hesitance to second-guess the risk-taking decisions of corporate officers and directors."); Lynn A. Stout, *The Toxic Side Effects of Shareholder Primacy*, 161 U. PA. L. REV. 2003, 2013 (2013) ("[T]he business judgment rule gives boards legal discretion at any time to increase employee salaries and benefits, treat suppliers more generously, retain earnings to give creditors a larger 'equity cushion,' or decline to pursue aggressive tax-avoidance strategies.").

143. *See* Barry E. Adler & Marcel Kahan, *The Technology of Creditor Protection*, 161 U. PA. L. REV. 1773, 1782 (2013) ("[U]nder the business judgment rule, a court will not second-guess a board judgment if the board was informed, independent, disinterested, and acted in good faith."); Justin Blount & Patricia Nunley, *Social Enterprise, Corporate Objectives, and the Corporate Governance Narrative*, 52 AM. BUS. L.J. 201, 238 (2015) ("Through the business judgment rule, officers and directors can direct the affairs of the corporation the best they are able, without the fear that courts will second guess the difficult decisions they must make."); David G. Yosifon, *The Social Relations of Consumption: Corporate Law and the Meaning of Consumer Culture*, 2015 BYU L. REV. 1309, 1342 ("Adhering to the "business judgment rule," courts do not second-guess the substance of business decisions that boards make.").

adjudicating a matter.[144] Often, business decisions are complex and do not have a single correct answer, which makes determining whether a decision was providently made difficult.[145] In addition, the business judgment rule allows corporate managers to pursue more aggressive courses of action that help to fuel economic growth.[146]

To take advantage of business judgment rule, all the manager has to do is to articulate any business purpose for the decision.[147]

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144. *See* Rachel J. Anderson, *Reimagining Human Rights Law: Toward Global Regulation of Transnational Corporations*, 88 DENV. U. L. REV. 183, 197 n.104 (2010) ("The business judgment rule is based on the presumption that directors possess more expertise than judges when it comes to making business decisions and so should not be second-guessed by judges as long as appropriate procedures have been followed in the decision-making process."); Lucian A. Bebchuk, *The Case Against Board Veto in Corporate Takeovers*, 69 U. CHI. L. REV. 973, 996 (2002) ("Given courts' limited information, expertise, and resources, the business judgment rule rightly counsels courts against substantive review of the merits of board decisions."); Joseph Mead & Michael Pollack, *Courts, Constituencies, and the Enforcement of Fiduciary Duties in the Nonprofit Sector*, 77 U. PITT. L. REV. 281, 304 (2016) ("The business judgment rule is also based on the premise that directors have more expertise than courts and that investors prefer business decisions in the board room instead of the courtroom.").

145. *See* Davis, *supra* note 113, at 270 ("One rationale for the business judgment rule is that judges may lack the expertise to evaluate complex business decisions."); Spencer Weber Waller, *Corporate Governance and Competition Policy*, 18 GEO. MASON L. REV. 833, 855 (2011) ("The business judgment rule rests largely on the presumption that directors (business professionals)—rather than courts—boast the business acumen required to sufficiently assess the economic risk associated with their often complex decisions.").

146. *See* Aaron Brumbaugh, *The Business Judgement Rule and the Diversified Investor: Encouraging Risk in Financial Institutions*, 17 U.C. DAVIS BUS. L.J. 171, 174 (2017) ("The Business Judgment Rule offers decision makers a safeguard from liability associated with the possible poor outcomes of those risky decisions, which . . . encourages the decision makers to be less averse to risk . . . and aim for the returns that diversified shareholders want."); Alex Devience, Jr., *A Hindsight Review of the Business Judgment Rule in a Takeover Environment: The State of the Business Judgment Rule After the Fall*, 5 DEPAUL BUS. L.J. 113, 135 (1992) ("The business judgment rule is a judicial principle that attempts to balance a corporation's need for honest governance with its need for aggressive managers who may make imprudent judgments in the general management scheme."); David G. Yosifon, *The Law of Corporate Purpose*, 10 BERKELEY BUS. L.J. 181, 223 n.155 (2013) ("The business judgment rule helps support . . . risk-preferring strategy in individual companies, as it absolves corporate boards from fear that aggressive, unorthodox decision-making will be second-guessed if it goes wrong.").

147. *See* Blount & Nunley, *supra* note 143, at 306 ("[T]he business judgment rule . . . insulates directors and officers from liability in carrying on the business of the organization as long as their decisions are made in good faith and

In *Dodge v. Ford*, for example, the Supreme Court of Michigan held that the Ford Motor Company's retention of profits to build an iron smelting plant to allow the company to produce its own metal parts was acceptable because of the business judgment rule.[148]

In tax strategy matters, courts have given corporate managers the benefit of the business judgment presumption to defeat claims of breach of fiduciary duty. *Kamin v. American Express Co.*[149] offers one classic example of a court issuing such a holding.[150] In that case, two minority stockholders of American Express Company brought a derivative suit against the directors of the corporation based upon the board's decision to issue a special dividend, rather than pursuing a course of action that would have a tax benefit.[151] In 1972, American Express had acquired 1,954,418 shares of Donaldson, Lufken and Jenrette, Inc. (DLJ) for investment at a cost of $29.9 million.[152] The market value of company at the time of the court's opinion had declined to $4 million.[153] On July 28, 1975, the board declared that the stockholders of American Express would receive the DLJ shares as a special dividend.[154] The plaintiffs contended that American Express should have sold the

attributable to a rational business purpose."); Julie Andersen Hill & Douglas K. Moll, *The Duty of Care of Bank Directors and Officers*, 68 ALA. L. REV. 965, 978 (2017) ("The business judgment rule is an especially deferential standard of review that insulates directors and officers from liability for a poor decision so long as the decision can be attributed to a rational business purpose."); Westbrook, *supra* note 103, at 399 ("[C]ourts refrain from second-guessing board decisions after the fact unless it is shown that the decision was uninformed, did not serve a rational business purpose, was made by directors with a personal interest in the decision, or was made by directors who were not independent . . . .").

148. *See* Dodge v. Ford Motor Co., 170 N.W. 668, 684 (Mich. 1919) ("[J]udges are not business experts. It is recognized that plans must often be made for a long future, for expected competition, for a continuing as well as an immediately profitable venture.").

149. 86 Misc.2d 809 (N.Y. Sup. Ct. 1976).

150. *Id.* at 813.

151. *Id.* at 810.

152. *Id.* at 811.

153. *Id.*

154. *Id.*

shares at a capital loss of $25 million to offset capital gains on other investments.[155]

The Supreme Court of New York held that the directors' decision was protected by the business judgment presumption because no evidence was presented of fraud, self-dealing, bad faith, or oppressive conduct.[156] Writing for the court, Justice Edward J. Greenfield stated, "[a] complaint which alleges merely that some course of action other than that pursued by the board of directors would have been more advantageous gives rise to no cognizable cause of action."[157] He continued, "[t]he directors' room rather than the courtroom is the appropriate forum for thrashing out purely business questions which will have an impact on profits, market prices, competitive situations, or tax advantages."[158] The court also stated that it did not matter if the directors acted "imprudently" as long as they acted in good faith.[159] Importantly, he did acknowledge, "[a]ll directors have an obligation, using sound business judgment, to maximize income for the benefit of all persons having a stake in the welfare of the corporate entity."[160] However, the court will not interfere in the absence of "a clear case . . . of fraud, oppression, arbitrary action, or breach of trust."[161] In short, the decision to engage in tax avoidance remains within the discretion of the board.[162]

In recent opinions, Delaware courts have continued this tradition of employing the business judgment presumption to give corporate managers broad discretion in determining tax strategy. In *Freedman v. Adams*,[163] the Supreme Court of Delaware affirmed a decision of the Court of Chancery of Delaware and held that tax strategy decisions represent "a classic exercise of business judgment."[164] In that case, Susan Freedman, a stockholder of XTO

155. *Id.*
156. *Id.* at 815.
157. *Id.* at 812.
158. *Id.* at 812–13.
159. *Id.* at 813.
160. Kamin v. American Express Co., 86 Misc.2d 809, 814 (N.Y. Sup. Ct. 1976).
161. *Id.* at 815.
162. *Id.*
163. 58 A.3d 414 (Del. 2013).
164. *Id.* at 417.

Energy Inc., brought a derivative suit that alleged the board of directors had committed waste by adopting an executive bonus plan that failed to make its payments tax deductible under the Internal Revenue Code.[165] She alleged that a plan could have been fashioned that this would have resulted in an approximately $40 million savings for the corporation.[166] The court held that the business judgment presumption protected the board, even if their decision was a bad one, because the board should have flexibility in making tax strategy determinations.[167]

In addition to that case, the Court of Chancery of Delaware also addressed the application of the business judgment presumption to tax strategy decisions in *Seinfeld v. Slager*.[168] In that case, Frank Seinfeld, a stockholder of Republic Services, Inc., brought a derivative suit against members of the board of directors relating to the corporation's compensation decisions.[169] Specifically, he asserted that various compensation to be paid was waste because it was not tax deductible under § 162(m) of the Internal Revenue Code.[170] As characterized by the court, Seinfeld was claiming that "there is an independent duty to minimize taxes, or alternatively that the failure to minimize taxes is *per se* a waste of corporate assets."[171] Although the court was unwilling to state that the decision to pursue or forgo tax savings is never a breach of fiduciary duty, the court held, "a decision to pursue or forgo tax savings is generally a business decision for the board of directors."[172] The court was willing to hold unequivocally that "there is no separate duty to minimize taxes, and a failure to do so is not automatically a waste of corporate assets."[173] As a consequence, corporate managers have broad discretion in how they formulate tax strategies, and while true in general, the *Dodge*

165. *Id.* at 416–17.
166. *Id.*
167. *Id.* at 417.
168. No. 6462–VCG, 2012 WL 2501105 (Del. Ch. June 29, 2012).
169. *Id.* at *1.
170. *Id.*
171. *Id.* at *3.
172. *Id.*
173. *Id.*

mandate provides very little guidance as to what tax strategy should be pursued in any particular situation.

IV. Essentialist Theories of the Corporation

In the search for guidance on the acceptability of tax avoidance, Professor Karie Davis-Nozemack and I have argued elsewhere that at least in part social science theories from fields such as corporate social responsibility, business ethics, and economics should be used to fill the void.[174] Still, while such theories may provide some direction in filling in the gaps, one must wonder whether the law offers any other binding mandates on corporate managers. One place to look is the essential nature of the corporate form itself. Because the corporation is at least in part a legal construct, understanding the nature of the form helps to explain the legal requirements placed upon its managers.[175]

To begin, a few brief words ought to be said about the history of the corporate form as a precursor to exploring the prevailing essentialist theories of the corporation because it will help to explain how these theories developed. Although the ancestors of modern corporations are found in a variety of cultures, one obvious place to start is ancient Rome because the term "corporation" derives from the Latin term "corpus" which means "body of the people."[176] In ancient Rome, the state recognized various entities

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174. *See* Chaffee & Davis-Nozemack, *supra* note 25, at 1473–80 (discussing various social science fields that may be helpful to corporate managers in addressing corporate tax avoidance decision-making).

175. *See* Robert J. Rhee, *A Legal Theory of Shareholder Primacy*, 102 MINN. L. REV. 1951, 1952 (2018) ("[C]orporations are wealth-producing socioeconomic legal constructs that should profit shareholders . . . ."); Omer Tene & Jules Polonetsky, *Taming the Golem: Challenges of Ethical Algorithmic Decision-Making*, 19 N.C. J.L. & TECH. 125, 142–43 (2017) ("Corporations are legal constructs intended to maximize profit and shareholder value."); Felix T. Wu, *The Commercial Difference*, 58 WM. & MARY L. REV. 2005, 2014 (2017) ("[C]orporations are legal constructs to which legal rights or duties can attach, just as they can to individuals.").

176. *See* Lyman Johnson, *Law and Legal Theory in the History of Corporate Responsibility: Corporate Personhood*, 35 SEATTLE U. L. REV. 1135, 1161 n.126 (2012) ("The etymology of the word 'corporation' comes from the Latin 'corpus,' which means 'body,' as in a 'corps' or group of people."); Michael J. Kelly, *"Never Again"? German Chemical Corporation Complicity in the Kurdish Genocide*, 31 BERKELEY J. INT'L L. 348, 350 (2013) ("From the Latin *corpus* for body,

that had a separate identity from the people who composed them, and in addition to being referred to by the term "corpus," these organizations were referred to by other names, including "collegium" and "universitas."[177] These entities had strong ties to the communities in which they existed and were organized for social purposes such as asylums, burial societies, homes for the poor, homes for the aged, hospitals, orphanages, political clubs, and religious societies.[178] These entities even included municipalities and the Roman state itself.[179]

The attributes of the modern corporation developed over time. During the thirteenth century, the Roman Catholic Church played a major role in this development when Sinibaldo Fieschi, who went on to become Pope Innocent IV, developed the concept of *persona ficta*, which entailed the idea of fictitious legal personhood for non-corporeal entities.[180] During the Middle Ages, England began

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corporations have been around since Roman times.").

177. *See* Brian M. McCall, *The Corporation as Imperfect Society*, 36 DEL. J. CORP. L. 509, 517, 529 n.93 (2011) ("In addition to *universitas*, the corporation was also referred to by the words, *corpus* (body) and *collegium* (college)."); Ian D. McClure, *From a Patent Market for Lemons to a Marketplace for Patents: Benchmarking IP in Its Evolution to Asset Class Status*, 18 CHAP. L. REV. 759, 765– 66 (2015) ("In the early sixth century, Roman law recognized various types of municipal-led, political or religious-focused corporations under the names *universitas*, *corpus*, or *collegium*."); Sean M. O'Connor, *Hired to Invent vs. Work Made for Hire: Resolving the Inconsistency Among Rights of Corporate Personhood, Authorship, and Inventorship*, 35 SEATTLE U. L. REV. 1227, 1230 (2012) ("The term and concept 'corporation' derived from the *universitas*, *corpus*, and *collegium* of Roman law.").

178. *See* HAROLD J. BERMAN, LAW AND REVOLUTION: THE FORMATION OF THE WESTERN LEGAL TRADITION 216 (1983) (reporting that in ancient Rome, "many private associations, including organizations for maintaining a religious cult, burial clubs, political clubs, and guilds of craftsmen or traders, were considered to be corporations").

179. *See id.* at 215 (discussing the origins of the corporate form in ancient Roman law); Bruce P. Frohnen, *The One and Many: Individual Rights, Corporate Rights and the Diversity of Groups*, 107 W. VA. L. REV. 789, 807 (2005) ("Corporate entities, including municipalities, trade guilds and burial societies, were known in Roman law from the earliest times.").

180. *See* Nicholas P. Cafardi, *The Availability of Parish Assets for Diocesan Debts: A Canonical Analysis*, 29 SETON HALL LEGIS. J. 361, 362 (2005) ("The Canon law of the Roman Catholic Church was the first legal system in the world to develop the notion of a fictitious legal personality. . . . [T]he term persona ficta . . . [was] actually used for the first time . . . by . . . , Sinibaldo Fieschi in the

allowing the creation of corporations for charitable purposes,[181] and the English government started to recognize perpetual existence for incorporated ecclesiastical, municipal, and charitable entities.[182] During the sixteenth and seventeenth centuries, the English government chartered corporations to develop newly conquered lands and began creating corporations for overseas trading, which popularized private stock ownership of corporations.[183] Throughout this period, the Crown and later Parliament retained exclusive power to grant corporate charters

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mid-thirteenth century."); Erin Sheley, *Perceptual Harm and the Corporate Criminal*, 81 U. CIN. L. REV. 225, 239 (2012) ("Pope Innocent IV is generally credited with the first articulation of the 'legal fiction' view of the corporation for his description of ecclesiastical bodies as both distinct entities as a matter of social fact, yet spiritually *personae fictae*—lacking a body or will and thus not susceptible of excommunication."); Mary Szto, *Limited Liability Morality: Fiduciary Duties in Historical Context*, 23 QUINNIPIAC L. REV. 61, 109 (2004) ("Canon law . . . influenced the development of the corporation . . . . Sinibaldo Fieschi, also known as Sinibaldus Fliscus, is known as the father of modern corporations theory. In the thirteenth century he wrote about 'persona ficta,' which led to the notion of 'legal persons.'").

181. *See* Blair, *supra* note 31, at 789 ("The earliest corporations were not organized for business purposes. Corporate law as we know it today evolved out of laws and practices governing municipalities, churches, and religious institutions in Europe during the Middle Ages."); Leo E. Strine, Jr. & Nicholas Walter, *Originalist or Original: The Difficulties of Reconciling* Citizens United *with Corporate Law History*, 91 NOTRE DAME L. REV. 877, 891 (2016) ("The first corporations chartered in Europe in the Middle Ages were not business corporations. Rather, they were religious, municipal, and benevolent corporations.").

182. *See* ALAN R. PALMITER, CORPORATIONS 7 (6th ed. 2009) (offering a historical overview of corporations).

183. *See* Franklin A. Gevurtz, *The Globalization of Corporate Law: The End of History or a Never-Ending Story*, 86 WASH. L. REV. 475, 481 (2011) ("Today's corporations derive from the English and continental European joint-stock companies formed late in the sixteenth and early in the seventeenth centuries to engage in trade with the Far East."); Jenny S. Martinez, *New Territorialism and Old Territorialism*, 99 CORNELL L. REV. 1387, 1408 (2014) ("European nations . . . outsourced empire to business enterprises. An important predecessor of the modern business corporation was the joint stock company, which flourished with European exploration, trade, and expansion in the seventeenth century."); Pollman, *Reconceiving Corporate Personhood*, *supra* note 31, at 1632 ("By the late sixteenth century, several European countries had begun chartering corporations to develop foreign trade and colonies. Some of these early corporations, such as the East India Company and the Hudson Bay Company, became well-known players in American colonial times.").

and create corporations, which meant corporations could only be formed through the direct action of the government.[184]

During the colonial period and early days of the United States, corporations could still only be created by specific act of the government. In practice, this meant that corporations were bespoke entities brought to life through bills passed by state legislatures and signed by state governors, and any alteration to a corporation's charter had to occur through a similar process.[185] As a result, a relatively small number of corporations existed during this period and most served relatively public functions, such as building and operating canals, bridges, and roads or operating banks or insurance companies, and state legislatures regularly granted corporate charters to noncommercial associations, such as charities, churches, and universities.[186] During the nineteenth

184. *See* Ryan Bubb, *Choosing the Partnership: English Business Organization Law During the Industrial Revolution*, 38 SEATTLE U. L. REV. 337, 340 (2015) ("Until 1844, [in England,] corporations could only be formed by an act of Parliament or a charter granted by the Crown."); Beth Stephens, *The Amorality of Profit: Transnational Corporations and Human Rights*, 20 BERKELEY J. INT'L L. 45, 55 (2002) ("Until well into the nineteenth century, corporations could be formed only by an act of the government—the king or Parliament in England, or the state legislatures in the United States.").

185. *See* Colin P. Marks, *Jiminy Cricket for the Corporation: Understanding the Corporate "Conscience"*, 42 VAL. U. L. REV. 1129, 1131 (2008) ("The earliest forms of the corporation in America came by specific charters from the states in the late eighteenth century, which were carried-over from the colonial days when corporations obtained charters directly from the King of England."); Celia R. Taylor, *The Inadequacy of Fiduciary Duty Doctrine: Why Corporate Managers Have Little to Fear and What Might Be Done About It*, 85 OR. L. REV. 993, 997 (2006) ("This conceptualization of the corporation clearly gave strong regulatory control to states through their exclusive and individualized charter authority. State legislatures, carrying on the work of the colonial assemblies, issued special charters conferring limited rights to corporations."); Christopher J. Wolfe, *"An Artificial Being": John Marshall and Corporate Personhood*, 40 HARV. J.L. & PUB. POL'Y 201, 204 (2017) ("Initially, colonial governments were granted this power by the King's agents; after the colonies broke away and created new state governments, the power to create corporate persons was considered part of the sovereign power of the state governments.").

186. *See* Margaret M. Blair, *A Contractarian Defense of Corporate Philanthropy*, 28 STETSON L. REV. 27, 42 (1998) ("[T]he earliest corporations were formed only upon the grant of a special charter by the crown, or in the early United States, by state charter, and these charters nearly always specified some sort of public purpose."); Stefan J. Padfield, *In Search of a Higher Standard: Rethinking Fiduciary Duties of Directors of Wholly-Owned Subsidiaries*, 10

century, states began to adopt general incorporation statutes, which allowed private individuals to form corporations without seeking an act of the state legislature, as Americans began to embrace competition, markets, and industrialization.[187] The modern corporation quickly came to dominate business in the United States.[188]

As will be explained below, throughout the history of the United States, three prevailing theories of the corporation were developed, i.e., artificial entity theory, real entity theory, and

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FORDHAM J. CORP. & FIN. L. 79, 87 (2004) ("[I]n the colonial United States, the responsibility for granting charters fell to the legislature. These charters were initially granted primarily to further various public works projects and, like in England, were handed out on a case-by-case basis."); Ann M. Scarlett, *Shareholder Derivative Litigation's Historical and Normative Foundations*, 61 BUFF. L. REV. 837, 899–900 (2013) ("In colonial times, corporations were created by royal charters just as they were in England, and only local public service corporations were well represented.").

187. *See* Steven G. Calabresi & Larissa C. Leibowitz, *Monopolies and the Constitution: A History of Crony Capitalism*, 36 HARV. J.L. & PUB. POL'Y 983, 1071 (2013) ("It was not until the development of general incorporation laws, beginning in the mid-nineteenth century, that corporate law in the United States ceased to be a field of special grants of privilege to a few individuals."); Henry Hansmann & Mariana Pargendler, *The Evolution of Shareholder Voting Rights: Separation of Ownership and Consumption*, 123 YALE L.J. 948, 993–94 (2014) ("[G]eneral incorporation laws, which allowed firms to incorporate without the need to obtain special legislative charters and conferred no exclusive privileges, gradually became dominant after the mid-nineteenth century; by the end of the century, they were the typical basis for incorporation . . . ."); Elizabeth Pollman, *Constitutionalizing Corporate Law*, 69 VAND. L. REV. 639, 647 (2016) ("Over the course of the nineteenth century, states moved from a system of exclusively granting charters by discretionary special acts of the legislature to a system in which . . . businesses could seek a corporate charter without specific involvement of the legislature.").

188. *See* Lynn A. Stout, *On the Nature of Corporations*, 2005 U. ILL. L. REV. 253, 256 (2005) ("[T]he corporation has evolved into the dominant business form for pursuing certain kinds of large, long-term economic projects."); Kevin M. Teeven, *Decline of Freedom of Contract Since the Emergence of the Modern Business Corporation*, 37 ST. LOUIS U. L.J. 117, 119 (1992) ("Corporations grew in importance in the 1860s and became the dominant business form in the 1880s and 1890s . . . ."); Harwell Wells, *"Corporation Law Is Dead": Heroic Managerialism, Legal Change, and the Puzzle of Corporation Law at the Height of the American Century*, 15 U. PA. J. BUS. L. 305, 313 (2013) ("[B]y late in the nineteenth century the corporate form was a commonplace frame for business organizations, its adoption made easy by the passage of general incorporation statutes during the century, and giant corporations had become an increasingly common feature of the economic landscape, beginning with the railroads.").

aggregate theory.[189] At one time or another, each of these theories was dominant.[190] However, as will also be explained below, although each of these theories has its attractiveness, none of them fully define what a corporation is. As a result, some have advocated for embracing the indeterminacy of the corporation by embracing all of the theories at once, despite conceptual inconsistencies.[191] Each of the prevailing theories of the corporation will be examined below, and this will set the stage for a discussion of my theory of the corporation—collaboration theory.

A. Artificial Entity Theory

Artificial entity theory, which is also referred to as concession theory, asserts that corporations are artificial entities that owe their existence completely to a concession by the government, i.e., a government grant of specific rights and privileges.[192] The government creates these entities to achieve goals that it does not have time, money, or other resources to achieve.[193] Under this

189. *See infra* Parts IV.A–C (exploring the prevailing essentialist theories of the corporation, i.e., artificial entity theory, real entity theory, and aggregate theory).

190. *See infra* notes 197, 206, 211 and accompanying text.

191. *See infra* Part IV.D (discussing the claim that the best course of action in determining the essential nature of the corporation is to embrace its indeterminacy by embracing all of the prevailing essentialist theories of the corporation, despite the logical inconsistencies created by such an approach).

192. *See* Vincent S.J. Buccola, *Corporate Rights and Organizational Neutrality*, 101 IOWA L. REV. 499, 506–07 (2016) ("'[A]rtificial entity' or 'concession' theory . . . focuses on the sense in which the corporation owes its very existence to the state's largesse."); Harper Ho, *supra* note 31, at 891–92 ("[T]he concession or 'artificial entity' theory . . . sees the corporation as a creation of the state or sovereign that grants its charter . . . ."); David Min, *Corporate Political Activity and Non-Shareholder Agency Costs*, 33 YALE J. REG. 423, 442 n.83 (2016) ("For much of its history, the corporation was understood as an organizational form that was granted by the state and which owed its existence to the state.").

193. *See* Avi-Yonah, *supra* note 54, at 12 ("Under the artificial entity view, the corporation owes its existence to the state and is granted certain privileges in order to be able to fulfill functions that the state would like to achieve."); Nathan Oman, *Corporations and Autonomy Theories of Contract: A Critique of the New* Lex Mercatoria, 83 DENV. U. L. REV. 101, 115 (2005) ("The concession theory claims that the corporation is a creation of the state that exercises delegated

theory, the corporation's rights and obligations are defined by the government that provided for its existence.[194] As a result, the government retains the power to define the scope of corporate activity, regulate corporate behavior, and punish corporations that fall short of the government's mandates.[195]

Artificial entity is the original conception of the corporation. As previously discussed, corporations originally could be created only through an act of the government, and this tradition was carried on from medieval England throughout the early days of the United States.[196] As a consequence, artificial entity theory was dominant during this period.[197] This dominance was so pronounced

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authority to serve the purposes of the government . . . ."); Padfield, *Rehabilitating Concession Theory*, *supra* note 31, at 332 ("[T]he concession theory of the . . . views the corporation as a tremendous capital accumulation device that was only made possible by the state conveying certain privileges to incorporators . . . [to] achieve goals that might otherwise fail for lack of funding.").

194. *See* Atiba R. Ellis, Citizens United *and Tiered Personhood*, 44 J. MARSHALL L. REV. 717, 737 (2011) ("This 'artificial person' or 'concession' theory rested on the view that a corporation effectively exists at the sufferance of the state and, therefore, is not entitled to any rights or protections not granted to it by statute."); Roger M. Michalski, *Rights Come With Responsibilities: Personal Jurisdiction in the Age of Corporate Personhood*, 50 SAN DIEGO L. REV. 125, 136 (2013) ("[C]orporations under the artificial entity framework had no political rights as they were conceived as purely economic entities, created by the state and subject to significant control and regulation."); J. Janewa OseiTutu, *Corporate "Human Rights" to Intellectual Property Protection?*, 55 SANTA CLARA L. REV. 1, 42 (2015) ("[T]he concession theory postulates that corporations are created by the state and have only the rights that are granted to them by the state.").

195. *See* Carliss N. Chatman, *Judgment Without Notice: The Unconstitutionality of Constructive Notice Following* Citizens United, 105 KY. L.J. 49, 58 n.48 (2016) ("The artificial entity theory envisions corporations as state approved entities, which exist at the pleasure of the government, are non-corporeal, and may be subject to more extensive regulation than a natural person due to this privileged position."); John C. Coates IV, Note, *State Takeover Statutes and Corporate Theory: The Revival of an Old Debate*, 64 N.Y.U. L. Rev. 806, 828 (1989) ("Under a pure artificial entity theory, a corporation can be regulated in *any* manner the state desires."); Padfield, *Rehabilitating Concession Theory*, *supra* note 31, at 333 ("Under concession theory, the state retains significant presumptive authority to regulate the corporate entity in exchange for granting this bundle of rights to incorporators.").

196. *See supra* notes 184–85 (discussing how corporations were formed in England, colonial America, and during the early days of the United States).

197. *See* Richard L. Cupp, Jr., *Moving Beyond Animal Rights: A Legal/Contractualist Critique*, 46 SAN DIEGO L. REV. 27, 54 (2009) ("The artificial entity theory dominated the first part of the 1800s."); Jess M. Krannich, *The*

that in *Trustees of Dartmouth College v. Woodward*,[198] the Supreme Court of the United States explicitly adopted artificial entity theory.[199] Writing on behalf of the Court, Chief Justice John Marshall stated:

> A corporation is an artificial being, invisible, intangible, and existing only in contemplation of law. Being the mere creature of law, it possesses only those properties which the charter of its creation confers upon it either expressly or as incidental to its very existence. These are such as are supposed best calculated to effect the object for which it was created. Among the most important are immortality, and, if the expression may be allowed, individuality; properties by which a perpetual succession of many persons are considered as the same, and may act as a single individual. They enable a corporation to manage its own affairs and to hold property without the perplexing intricacies, the hazardous and endless necessity, of perpetual conveyances for the purpose of transmitting it from hand to hand.[200]

Although proponents of artificial entity still exist today, the Court's holding likely represents the point of artificial entity theory's greatest popularity.

With the advent of general incorporation statutes in the early and mid-1800s, the popularity of the artificial entity theory waned as the role of state governments in forming corporations was

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Corporate "Person": A New Analytical Approach to a Flawed Method of Constitutional Interpretation, 37 LOY. U. CHI. L.J. 61, 71 (2005) ("The artificial entity metaphor remained the dominant view of the corporate entity through much of the nineteenth century, and it remains prevalent in corporate theory as well as constitutional law today."); Marcantel, *supra* note 31, at 225 ("[I]t is unequivocal that concessionary theory was a dominant theory in the late eighteenth and early nineteenth centuries.").

198. Trs. of Dartmouth Coll. v. Woodward, 17 U.S. 518 (1819).

199. *See id.* at 636 (explaining the form and function of the corporate entity in the United States).

200. *Id.*

reduced.[201] As a result, many corporate law theorists began to re-conceptualize the corporation as a real entity.[202]

B. Real Entity Theory

Real entity theory, which is also known as natural entity theory, is another prevailing essentialist theory of the corporation. Real entity theory posits that the corporation is an entity separate and apart from the individuals organizing, owning, and operating it.[203] Unlike artificial entity theory, real entity theory suggests that the corporation does not owe its existence to the state, but it is a product of the group identity of the individuals organizing, owning,

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201. *See* Colombo, *supra* note 31, at 11 ("General incorporation statutes sounded the death knell of concession theory—the notion that corporations are creations of the state."); Ripken, *supra* note 31, at 220 ("By the mid-nineteenth century, special chartering gave way to general incorporation statutes. . . . The idea that corporations existed only because of the concession of the state held far less force . . . ."); Gerald J. Russello, *Catholic Social Thought and the Large Multinational Corporation*, 46 J. CATH. LEGAL STUD. 107, 130–31 (2007) ("Changes in law and business practice in the early twentieth century changed the understanding of the corporation from a state-chartered entity towards a view that understood the corporation as a 'natural entity' established by the incorporators and shareholders, with only minimal state involvement.").

202. *See* Nicole Bremner Càsarez, *Corruption, Corrosion, and Corporate Political Speech*, 70 NEB. L. REV. 689, 718–19 (1991) ("Philosophical questions about the nature of corporations had fascinated German and French political thinkers during the nineteenth century. Otto von Gierke, in particular, advanced the idea that groups (and, therefore, corporations) are natural extensions of human society."); Anthony W. Kraus, *Absolute Protection for Intracorporate Personnel Communications Under Defamation Law: A Philosophical Reappraisal of the Nonpublication Doctrine*, 25 U. MEM. L. REV. 155, 171 (1994) ("Attention to the subject of corporate legal status increased greatly in Europe during the second half of the nineteenth century. The fictive view of corporations was rejected by the leading German scholar of the time, Otto von Gierke."); Michalski, *supra* note 31, at 136 ("Beginning in the late nineteenth century, natural entity theory replaced the conception of the corporation as an artificial creation of state law.").

203. *See* Marjorie E. Kornhauser, *Corporate Regulation and the Origins of the Corporate Income Tax*, 66 IND. L.J. 53, 59 (1990) ("[T]he real or natural entity theory of corporations held that the corporation was an entity separate from its members."); Pollman, *Reconceiving Corporate Personhood*, *supra* note 31, at 1641–42 ("Also known as the natural entity or person theory, [the real entity theory] regarded the corporation as a real entity with a separate existence from its shareholders and from the state."); Sloan G. Speck, *The Social Boundaries of Corporate Taxation*, 84 FORDHAM L. REV. 2583, 2591 (2016) ("[T]he 'real entity' theory treats corporations as distinct legal persons with specific rights and obligations not linked to those of their owners.").

and operating the business form.[204] As a result of this collective personality, some proponents of this theory suggest that the corporation possesses human rights that emerge from the separate identity of the group.[205]

Although advocates for real entity theory have existed throughout the history of the United States and even today, real entity theory was the dominant essentialist theory of the corporation throughout the second half of the nineteenth century and much of the twentieth century.[206] As a result of the widespread

204. *See* Mark M. Hager, *Bodies Politic: The Progressive History of Organizational "Real Entity" Theory*, 50 U. PITT. L. REV. 575, 580 (1989) ("The real entity paradigm implied that corporations owe their existence and legitimacy to the distinct and unified purposes and wills of groups."); Teemu Ruskola, *What Is a Corporation? Liberal, Confucian, and Socialist Theories of Enterprise Organization (and State, Family, and Personhood)*, 37 SEATTLE U. L. REV. 639, 659 (2014) (discussing "the views of late nineteenth-century 'real entity' theorists for whom the corporation was effectively a kind of super-person, a metaphysically real entity in its own right, the existence of which preceded law whose main task was merely to declare its social existence"); Kenya J.H. Smith, *Incomplete Sentences:* Hobby Lobby*'s Corporate Religious Rights, the Criminally Culpable Corporate Soul, and the Case for Greater Alignment of Organizational and Individual Sentencing*, 77 LA. L. REV. 75, 92–93 (2016) ("[T]he real entity theory . . . embraces the explanation of corporations as a natural consequence of group dynamics, analogous to a family, religious congregation, or other types of assemblies formed by groups of natural persons.").

205. *See* Marcantel, *supra* note 31, at 222 n.7 ("In the constitutional sense, real entity theory posits that the corporation, as an entity, is entitled to constitutional protection independent of its shareholders."); Dalia Tsuk Mitchell, *Status Bound: The Twentieth Century Evolution of Directors' Liability*, 5 N.Y.U. J.L. & BUS. 63, 84 (2009) ("Natural entity theory described corporations as separate entities, distinct from their individual members and having real existence, with rights and liabilities similar to those of persons (specifically, constitutional rights and criminal and tort liabilities)."); Seema Mohapatra, *Time to Lift the Veil of Inequality in Health-Care Coverage: Using Corporate Law to Defend the Affordable Care Act*, 50 WAKE FOREST L. REV. 137, 162 (2015) ("The real entity theory suggests that as a corporation is separate and apart, the corporation has a 'collective consciousness' that is separate and apart from those who manage its operations. Therefore, it is said that a corporation may then be considered a person under the law and entitled to legal rights that would naturally flow to any person.").

206. *See* Krannich, *supra* note 197, at 85 ("[T]he real entity theory became the most prominent definition of the corporate 'person' in the early twentieth century."); Michael J. Phillips, *Reappraising the Real Entity Theory of the Corporation*, 21 FLA. ST. U. L. REV. 1061, 1068 (1994) ("The . . . real entity theory of the corporation, also known as natural-entity theory, was influential from the

adoption of general incorporation statutes during the 1800s, corporate theorists' focus on the role of the state lessened, and they searched for a new answer to the metaphysical question of what is the essential nature of the corporation.[207] Ultimately, they looked to European corporate legal theorists in their search, and specifically, the work of German legal theorist Otto von Gierke, who suggested that groups of individuals take on a separate "collective spirit" from the individuals that compose them, which he believed applied to corporations as well.[208] American corporate law theorists imported this idea to the United States.[209]

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end of the [nineteenth] century until at least the 1920s."); Susanna Kim Ripken, *Corporations Are People Too: A Multi-Dimensional Approach to the Corporate Personhood Puzzle*, 15 FORDHAM J. CORP. & FIN. L. 97, 112 (2009) ("At the turn of the 20th Century, the real entity, or natural entity theory became the popular way of describing the corporate person.").

207. *See supra* notes 205–02 and accompanying text (discussing the transition from artificial entity theory to real entity theory as the dominant essentialist theory of the corporation).

208. *See* Martin Gelter & Geneviève Helleringer, *Lift Not the Painted Veil! To Whom Are Directors' Duties Really Owed?*, 2015 U. ILL. L. REV. 1069, 1089 n.112 ("In German law, the name of Otto von Gierke is typically associated with the 'entity' theory of the corporation. Gierke understood legal personality as the reflection of social reality and argued that individuals would form fellowships that developed an autonomous existence necessary for their social fulfillment."); Iuliano, *supra* note 31, at 80 ("Otto von Gierke and Frederic Maitland are two of the most notable thinkers who advanced the position that group agents are emergent entities. According to them, a collective consciousness springs forth from the associations of individuals within corporations."); Oman, *supra* note 193, at 116 ("The real theory of the corporation received its most forceful statement in German legal thought. . . . Otto Gierke became the proponent of this approach in the context of corporate law.").

209. *See* Sean J. Griffith, *Corporate Governance in an Era of Compliance*, 57 WM. & MARY L. REV. 2075, 2132 (2016) ("[T]he 'real entity' theory [is] a late nineteenth-century theory exported from Germany to England and the United States as a basis for the legal rights of business organizations."); Ron Harris, *The Transplantation of the Legal Discourse on Corporate Personality Theories: From German Codification to British Political Pluralism and American Big Business*, 63 WASH. & LEE L. REV. 1421, 1422–23 (2006) ("The German-Gierkian real entity theory of the corporation journeyed through several contexts and discourses in Britain and the United States. It inspired numerous articles and books in English, French and German."); Ian B. Lee, *Corporate Law, Profit Maximization and the "Responsible" Shareholder*, 10 STAN. J.L. BUS. & FIN. 31, 40 (2005) ("Under the influence of German theorists who suggested that corporate legal personality translated the corporation's existence as a real entity separate from its shareholders, the corporation came increasingly to be viewed as an institution in its own right, rather than as the shareholders in special form.").

C. Aggregate Theory

The aggregate theory, which is also known as the nexus of contracts theory, is the third prevailing essentialist theory of the corporation. Although this theory initially developed in the nineteenth century,[210] it took until the second half of the twentieth century to become the dominant theory of the corporation, and it remains so today.[211] Under this theory, the corporation consists of individuals organizing, owning, and operating it.[212] Some proponents of this theory extend it to include other parties, such

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210. *See* Cupp, Jr., *supra* note 197, at 55 ("The aggregate entity theory of corporate personhood was . . . invoked beginning in the 1800s, and it reached prominence in the latter half of the century."); Iuliano, *supra* note 31, at 58 ("During the late nineteenth century, corporations were reconceived as objects of private, not government, creation. . . . Corporations had become collective entities that derived their powers from the individuals who comprised them."); Phillips, *supra* note 206, at 1065 ("[D]uring the latter part of the nineteenth century some theorists began to use partnership analogies to describe the corporation, thereby characterizing it as an aggregate formed by private contracting among its human parts.").

211. *See* Brett McDonnell, *ESOPs' Failures: Fiduciary Duties When Managers of Employee-Owned Companies Vote to Entrench Themselves*, 2000 COLUM. BUS. L. REV. 199, 246 ("The dominant view in law and economics scholarship treats corporations as a nexus of contracts."); Meredith R. Miller, *Contracting Out of Process, Contracting Out of Corporate Accountability: An Argument Against Enforcement of Pre-Dispute Limits on Process*, 75 TENN. L. REV. 365, 365–66 (2008) ("In the field of corporate law, the 'nexus of contract' model is the dominant theoretical explanation of the law concerning the management of corporations. Under this view, corporations are nothing more than a network of contracts between voluntary, private actors."); Rachel F. Moran, *Whatever Happened to Racism?*, 79 ST. JOHN'S L. REV. 899, 924–25 (2005) ("Corporate law scholars have themselves questioned images of personhood, but the dominant response has been to characterize corporations as nothing more than a nexus of efficient contracts dedicated to the maximization of shareholder wealth.").

212. *See* Marcantel, *supra* note 31, at 222 n.6 ("Aggregate theory posits that corporations are conduits through which collections of individuals conduct business."); Stefan J. Padfield, *Corporate Social Responsibility & Concession Theory*, 6 WM. & MARY BUS. L. REV. 1, 26–27 (2015) ("The aggregate view rejected the fiction of the corporation as an artificial entity that was promoted by concession theory, and instead focused on the property rights of the underlying shareholders to conceive of the corporation as simply an association of individuals."); Petrin, *supra* note 31, at 34 ("According to the nexus of contracts model, the firm consists of various explicit and implicit contracts between a firm's constituencies . . . .").

as creditors, employees, and customers.[213] Unlike the artificial entity theory and real entity theory, under the aggregate theory, the corporation has no separate existence from the individuals composing it.[214] The rights of the corporation are derived from those individuals.[215]

As the real entity theory gained prominence in the late nineteenth century and early twentieth century, business scholars wanted the opportunity to do deeper economic analysis of the firm. In 1937, Ronald Coase published his seminal article, *The Nature of the Firm*, which served as a foundation for modern analysis of the firm as a nexus of contracts.[216] After a period of dormancy of

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213. *See* Alicia E. Plerhoples, *Representing Social Enterprise*, 20 CLINICAL L. REV. 215, 242 (2013) ("Dominant modern corporate law theory describes a corporation as a 'nexus of contracts'. Under this widely-accepted theory, the corporation is a nexus of a set of contracts among the firm's constituents which include its shareholders, as providers of capital, but also its employees, creditors, suppliers, and board of directors"); Usha Rodrigues, *Entity and Identity*, 60 EMORY L.J. 1257, 1273 (2011) ("The dominant metaphor for the corporation is the 'nexus of contracts': The firm in this view serves a coordinating function among managers, shareholders, suppliers, and consumers."); Adam F. Scales, *Following Form: Corporate Succession and Liability Insurance*, 60 DEPAUL L. REV. 573, 576 (2011) ("Dominant for now is the view that a corporation is a nexus of contracts among labor, capital, and management.").

214. *See* J. Haskell Murray, *An Early Report on Benefit Reports*, 118 W. VA. L. REV. 25, 40–41 (2015) ("The nexus-of-contracts theory . . . view[s] the corporation not as a separate entity, but as an accumulation of private contracts between stakeholders."); Padfield, *The Silent Role of Corporate Theory*, *supra* note 31, at 841 (reporting that the nexus-of-contract theory views the corporation "as a mere aggregation of natural individuals that is a product of private initiative serving a predominantly private function."); Phillips, *supra* note 206, at 1071 ("[T]he nexus-of-contracts theory refuses to recognize a meaningful corporate entity distinct from the components that form the corporation.").

215. *See* Coates, *supra* note 195, at 815 n.50 ("Under the aggregate theory, the extent to which a corporation may be said to have 'rights,' especially constitutional rights, corresponds to the rights of the individuals which make it up."); Iuliano, *supra* note 31, at 60 ("Under the aggregate entity theory, corporations were only capable of possessing rights that could be attributed to a collection of individuals."); Petrin, *supra* note 31, at 9–10 ("The 'aggregate' or 'contractualist' theory asserted that corporations . . . constituted aggregations of natural persons. . . . [B]oth a legal entity's legal rights and duties were often seen . . . as simply those of its shareholders or other individuals that made up the entity.").

216. R.H. Coase, *The Nature of the Firm*, 4 ECONOMICA 386 (1937); *see also* Stephen M. Bainbridge, *The Board of Directors As Nexus of Contracts*, 88 IOWA L. REV. 1, 9 (2002) ("The dominant model of the corporation in legal scholarship is the so-called nexus of contracts theory. This model's origins fairly can be traced to Nobel Prize laureate Ronald Coase's justly famous article, *The Nature of the*

the debate over the essential nature of the corporation, which will be discussed in the next Part, the aggregate theory of the corporation emerged as the dominant theory of the corporation as a result of the interweaving of law and economics that began during the late 1970s and early 1980s because the aggregate theory is well suited to allow economic analysis of the corporate form.[217]

D. Indeterminacy

Some scholars have argued for accepting all of the prevailing essentialist theories of the corporation at the same time and embracing the indeterminacy of the corporation.[218] Each of the prevailing theories of the corporation has its virtues and

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Firm."); Oman, *supra* note 193, at 124 ("The modern nexus of contract theory of the corporation traces its origin to a 1937 article by Ronald Coase."); J. Gregory Sidak, *Mr. Justice Nemo's Social Statics*, 79 TEX. L. REV. 737, 745 (2001) ("Coase's insight that the firm is the nexus of contracts between the owners of various factors of production also has gained widespread acceptance among legal scholars.").

217. *See* Harper Ho, *supra* note 31, at 895 ("Since the rise of the law and economics movement, dominant thinking about the nature of the corporation has coalesced around an aggregate theory of the corporation that sees the corporation as a 'nexus of contracts.'"); Charles R.T. O'Kelley, *The Entrepreneur and the Theory of the Modern Corporation*, 31 J. CORP. L. 753, 763 (2006) ("Though it is impossible to date precisely, the Nexus-of-Contracts Paradigm achieved dominance in the field of corporation law near the end of the 1970s."); Susan J. Stabile, *A Catholic Vision of the Corporation*, 4 SEATTLE J. SOC. JUST. 181, 211 n.48 (2005) ("The law and economics view, which sees the corporation as a nexus of contracts, has been the dominant model for thinking about the regulation of corporations.").

218. *See* William W. Bratton, Jr., *The "Nexus of Contracts" Corporation: A Critical Appraisal*, 74 CORNELL L. REV. 407, 464 (1989) ("Whatever the future interplay of theory and power, the concepts that make up theories of the firm—entity and aggregate, contract and concession, public and private, discrete and relational—will stay in internal opposition. This tendency toward contradiction should be accepted, not feared."); David Millon, *Theories of the Corporation*, 1990 DUKE L.J. 201, 262 ("Confronted with important political challenges, theories of the corporation have always been fundamentally indeterminate."); Fenner L. Stewart, Jr., *Indeterminacy and Balance: A Path to a Wholesome Corporate Law*, 9 RUTGERS BUS. L. REV. 81, 85 (2012) ("[T]his article recommends focusing upon the indeterminacy of corporate legal theories.").

drawbacks. The artificial entity theory celebrates the role of the state in creating the corporation, while underplaying the separate identity of the entity and the roles of the individuals organizing, operating, and owning it.[219] The real entity theory celebrates the existence of the corporation as a distinct entity, while underplaying the role of the state in creating it, and the roles of the individuals organizing, owning, and operating it.[220] Finally, the aggregate theory celebrates the roles of the individuals organizing, operating, and owning the corporation, while underplaying the role of the state in creating the entity and the existence of the corporation as a distinct entity.[221] The metaphysical inquiry into the essential nature of the corporation is at heart the search for a coherent definition of the corporation, and each of the theories seems thin.

Some have argued that the best way to gain a robust understanding of the corporation is to embrace all of the prevailing theories of the corporation simultaneously.[222] Embracing all of the prevailing theories simultaneously is problematic, however, because the theories do contradict each other. For example, the artificial entity theory and the real entity conceive of the corporation as a distinct entity,[223] but the aggregate theory conceives of the corporation as nothing more than a collection of individuals.[224] In terms of corporate rights, the artificial entity theory suggests that all rights of the corporation are given and defined by the state.[225] However, the natural entity theory claims that corporate rights derive from the separate identity of the

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219. *See supra* Part IV.A (explaining artificial entity theory).

220. *See supra* Part IV.B (explaining real entity theory).

221. *See supra* Part IV.C (explaining aggregate theory).

222. *See supra* note 218 and accompanying text.

223. *See supra* note 192 and accompanying text (explaining that under the artificial entity theory, the corporation is a distinct entity that is created by the state); *supra* notes 203–04 and accompanying text (discussing that under the real entity theory, the corporation is a separate entity created by the group identity of the individuals composing it).

224. *See supra* note 214 and accompanying text (stating that under the aggregate theory, the corporation has no separate identity from the individuals composing it).

225. *See supra* note 194 and accompanying text (discussing that under the artificial entity theory, the rights of the corporation are defined by the government that provided for the corporation's existence).

group,[226] and the aggregate theory argues that corporate rights are derived from the individuals organizing, operating, and owning the corporation as they interact with other participants in the firm and with parties outside of the corporation.[227] Put simply, accepting the indeterminacy of the corporation means accepting conflicting theories that cannot be meshed into a coherent understanding of the corporation.

Famously, in *The Historic Background of Corporate Legal Personality*,[228] an article published in 1926, John Dewey wrote, "The fact of the case is that there is no clear-cut line, logical or practical, through the different theories which have been advanced and which are still advanced in behalf of the 'real' personality of either 'natural' or associated persons."[229] As a consequence, he concluded:

> As far as the historical survey implies a plea for anything, it is a plea for disengaging specific issues and disputes which arise from entanglement with any concept of personality which is other than a restatement that such and such rights and duties, benefits and burdens, accrue and are to be maintained and distributed in such and such ways, and in such and such situations.[230]

In short, he advocated to retreat from the debate by embracing all of the prevailing theories of corporate personality at once, despite the incoherence of that position.[231] Remarkably, many scholars adopted his position, and the debate over corporate personality did not re-intensify until the early 1980s, when luminaries of the law

226. *See supra* note 205 and accompanying text (explaining that under the real entity theory, the rights of the corporation emerge from the separate identity of the group).

227. *See supra* note 215 and accompanying text (explaining that under the aggregate theory, the rights of the corporation are derived from the rights of the individuals organizing, owning, and operating the entity).

228. John Dewey, *The Historic Background of Corporate Legal Personality*, 35 YALE L.J. 655 (1926).

229. *Id.* at 669.

230. *Id.*

231. *See id.*

and economics movement reinvigorated the debate through advocacy for the aggregate theory of personality.[232]

John Dewey's proposal to embrace the indeterminacy of the corporation is remarkably seductive. At heart, each of the prevailing theories is an attempt to define what a corporation is. The problem is that each theory is descriptively thin, downplaying some attributes and favoring others.[233] Despite the incoherence, embracing all of the theories helps to offer a thicker definition of the corporation. In addition, by ignoring the question of what a corporation is, one has time for other pursuits, whatever those might be. However, taking such a path seems wrong for a variety of reasons. First, backing away from any intellectual pursuit simply because it is difficult is not acceptable. Otherwise, a myriad of human problems would never be solved. Second, theories of the corporation matter now in a way that they have not in the past. As cases like *Citizens United*[234] and *Hobby Lobby*[235] demonstrate, the legal rights of corporations are evolving.[236] For litigation of these issues to occur properly, society must know what corporations are in the first place. Third, none of the prevailing theories of the corporation, even if joined together, provide a complete answer of what is a corporation. Fourth, a better theory of the firm, collaboration theory, exists.

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232. *See* Pollman, *Reconceiving Corporate Personhood*, *supra* note 31, at 1650 ("Many commentators view John Dewey's 1926 Yale Law Journal article as having put an end to the corporate personhood debate."); David A. Skeel, Jr., *Corporate Anatomy Lessons*, 113 YALE L.J. 1519, 1527 (2004) ("[T]he debate [over the essential nature of the corporation] is often viewed as having ended when the pragmatist philosopher John Dewey published an article in this journal arguing that the various views collapsed into each other, and each could be used to support any outcome on a particular issue."); Linda Sugin, *Theories of the Corporation and the Tax Treatment of Corporate Philanthropy*, 41 N.Y.L. SCH. L. REV. 835, 866 n.144 (1997) ("The indeterminate nature of normative content in theories of the corporation was argued by John Dewey in 1926. . . . Dewey's article may have been responsible for the sudden end of debate on the issue . . . .").

233. *See supra* Part IV.A–C (providing an overview of the prevailing essentialist theories of the corporation).

234. Citizens United v. FEC, 558 U.S. 310 (2010).

235. Burwell v. Hobby Lobby Stores, Inc., 134 S. Ct. 2751 (2014).

236. *See* Pollman, *supra* note 187, at 642 ("A new dynamic between federal corporate rights and state corporate law has emerged . . . [w]ith the Court's recent decisions in *Citizens United v. Federal Election Commission* and *Burwell v. Hobby Lobby Stores, Inc.* . . . .").

V. Collaboration Theory

In developing an essentialist theory of the corporation, one is trying to define what is a corporation. Each of the prevailing theories offers an incomplete definition of the corporation. As previously discussed, each of the theories emphasizes certain aspects of the firm, while underemphasizing other aspects.[237] The problem, however, is much deeper than that. Each of the theories explains how the corporation exists but fails to explain why the corporation exists. A proper theory of the corporation should do both.

To state this issue a bit more concretely, consider how to define a bridge. One could define a bridge as an artificial entity created by the government. This would be the artificial entity theory of the bridge.[238] One also could also define a bridge simply as an object that exists. This would be the real entity theory of the bridge.[239] Finally, one could define a bridge as a sum of its parts in a certain arrangement. This would be the aggregate theory of the bridge.[240] The problem is that none of these theories offers a robust and proper definition of what a bridge happens to be. A better definition of a bridge would be "[a] structure spanning and providing passage over an obstacle."[241] This definition provides an explanation of how a bridge exists, i.e., as a "structure," and why a bridge exists, i.e., "providing passage over an obstacle."[242] In the absence of answering both questions, one has not created a fully formed definition of a bridge. The same is true with trying to develop an essentialist theory of the corporation. This is especially true if you want to draw normative implications from a theory of

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237. *See supra* Part IV.D (discussing the reasons for embracing the indeterminacy of the corporation).

238. *See supra* Part IV.A (providing an overview of the artificial entity theory of the corporation).

239. *See supra* Part IV.B (providing an overview of the real entity theory of the corporation).

240. *See supra* Part IV.C (providing an overview of the aggregate theory of the corporation).

241. *Bridge*, WEBSTER'S II NEW COLLEGE DICTIONARY 138 (1995).

242. *Id.*

the corporation.[243] A more robust theory of the corporation yields more robust normative conclusions.

Collaboration theory answers the questions of both how and why corporations exist. Under this theory, which I have developed, the corporation is a collaboration among the government and the individuals organizing, operating, and owning the corporation.[244] As a result, this theory explains *how* the corporation exists—as a collaboration. Collaboration theory also explains *why* the corporation exists. A collaboration can be defined as a common effort between or among multiple entities to accomplish a task or project.[245] In regard to for-profit corporations, the common project among the government and those organizing, operating, and owning the entity is economic development and economic gain. The interests of the parties do diverge somewhat. The state government is interested in societal economic development and economic gain,[246] but the individuals organizing, operating, and owning the corporation are looking for personal economic development and gain.[247] However, parties often enter into

243. *See infra* Part VI.A–B (discussing some of the normative implications of collaboration theory).

244. Collaboration theory may be defined to include other parts, such as creditors, customers, and the general public. The exact scope of the collaboration and relationships among collaborating parties will be left for another day.

245. *See Collaborate,* MERRIAM-WEBSTER'S COLLEGIATE DICTIONARY 243 (11th ed. 2006) (providing a definition of the term "collaborate").

246. *See* Andrew I. Gavil, *Competition and Cooperation on Sherman Island: An Antitrust Ethnography*, 44 DEPAUL L. REV. 1225, 1242 (1995) (reporting that emergence of the modern corporation resulted from "a conscious government policy of promoting economic growth, combined with the realization that the needs of technological progress, particularly in transportation and communication, demanded a more widely available cooperative mechanism for raising capital"); H. C. Robinson, *Shifted Personhood: Corporations, Technology, and Law on the Path to* Citizens United *and Current Electoral Politics in the U.S.*, 18 U. PA. J.L. & SOC. CHANGE 403, 405 n.9 (2016) ("By the end of the eighteenth century, the new American states had become involved in the process of promoting economic development by granting corporate charters and franchises to private investors."); Carl J. Schramm, *Law Outside the Market: The Social Utility of the Private Foundation*, 30 HARV. J.L. & PUB. POL'Y 355, 364 (2006) ("State legislatures . . . replaced 'special' incorporation statutes with 'general' incorporation laws to make it easier for people to pursue commercial aspirations, opening the door to greater economic participation.").

247. *See supra* note 122 and accompanying text (explaining that for-profit corporations are created and are to be managed primarily to make a profit for shareholders).

arrangements referred to as collaborations with far more divergent interests than those collaborating within the corporate form.[248]

Collaboration theory also offers a fuller view of the corporation in other ways as well. For example, collaboration theory clarifies why corporations have separate entity status. This theory achieves this by building upon the work of Otto von Gierke, who argued that groups have identities that are separate and distinct from the individuals composing them.[249] As mentioned above, Gierke's work helped popularize the real entity theory during the nineteenth and early twentieth centuries.[250] Collaboration theory takes Gierke's work one step further by arguing that because collaborations allow individuals to achieve more than they ever could on their own that the corporation should be viewed as having a separate and distinct status from the government and the individuals organizing, operating, and owning the entity.[251]

Collaboration theory also explains why the government has the ability to regulate the rights of corporations to a greater degree than actual human beings. Because the government is a collaborator in the entity, it has the ability to guide its existence

248. *See* Aaron X. Fellmeth, *Conception and Misconception in Joint Inventorship*, 2 N.Y.U. J. INTELL. PROP. & ENT. L. 73, 77 (2012) ("Collaborations frequently involve teams from industry and universities or government agencies joining forces to advance technology despite divergent economic interests."); Nancy J. Knauer, *Learning Communities: A New Model for Legal Education*, 7 ELON L. REV. 193, 212 (2015) ("The collaborative co-production of knowledge requires divergent thought and is based on the combined efforts of a diverse range of participants."); Gerald P. López, *Transform—Don't Just Tinker with—Legal Education (Part II)*, 24 CLINICAL L. REV. 247, 312 (2018) ("[W]e perhaps learn most when we collaborate with others who see the world differently, [and] go about their practices in ways different and even divergent from our own . . . .").

249. *See supra* note 208 and accompanying text (discussing Otto von Gierke's work on group identity).

250. *See supra* Part IV.B (discussing Otto von Gierke's role in the rise and dominance of the real entity theory of the corporation during the nineteenth and early twentieth centuries).

251. *See generally* MORTEN T. HANSEN, COLLABORATION: HOW LEADERS AVOID THE TRAPS, BUILD COMMON GROUND, AND REAP BIG RESULTS (2009); EVAN ROSEN, THE CULTURE OF COLLABORATION: MAXIMIZING TIME, TALENT AND TOOLS TO CREATE VALUE IN THE GLOBAL ECONOMY (2009); KEITH SAWYER, GROUP GENIUS: THE CREATIVE POWER OF COLLABORATION (2007); LEIGH THOMPSON, CREATIVE CONSPIRACY: THE NEW RULES OF BREAKTHROUGH COLLABORATION (2013).

through law and regulation.[252] In a myriad of different areas, collaboration theory has normative implications. A complete discussion of all these areas is beyond the scope of this Article, but a significant amount can and will be said about collaboration theory's application to tax avoidance.

VI. Collaboration Theory and Tax Avoidance

One of the major problems with the prevailing theories of the corporation is that their normative implications are very limited.[253] The artificial entity theory, real entity theory, and aggregate theory each have some descriptive appeal, but they fail to fully describe the corporation.[254] As a consequence, in attempting to resolve fundamental issues regarding the corporation, each of these theories often provides little or no guidance. With tax avoidance, for example, one might argue that the artificial entity theory suggests corporate managers should not engage in tax avoidance because of the close relationship with the state, but such an argument would be attenuated at best.[255] The real entity theory and aggregate theory seem to be no help in answering questions relating to tax avoidance at all.[256]

Collaboration theory does a much better job providing guidance as to whether corporate managers should engage in tax avoidance activities. As will be explored in the remainder of this Part, two viable models for addressing tax avoidance issues can be derived from collaboration theory.[257] However, between these two models, this Article argues that collaboration theory should be

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252. *See supra* note 245 and accompanying text (describing collaboration as a "common effort" which suggests that all parties have a role to play in shaping that collaboration).

253. *See supra* Parts IV.A–C (providing an overview of the prevailing essentialist theories of the corporation).

254. *See supra* notes 237–247 and accompanying text (noting the deficiencies of the prevailing essentialist theories of the corporation).

255. *See supra* Part IV.A (explaining the artificial entity theory of the corporation).

256. *See supra* Part IV.B (explaining the real entity theory of the corporation).

257. *See infra* Part VI.A (giving an overview of the good faith model); *infra* Part VI.B (giving an overview of the profit seeking model).

understood to preclude corporate managers from engaging in aggressive tax avoidance and perhaps any tax avoidance at all.[258]

A. The Good Faith Model

As previously explained, collaboration theory posits that the corporation is a collaboration among the government and the individuals organizing, operating, and owning the entity.[259] Although the collaboration makes the corporation much more substantial and robust than most contractual relationships, the relationship among the government and the individuals organizing, operating, and owning the firm is contractual in nature.[260] Importantly, under the aggregate theory, which has been refined into the nexus of contracts theory, the focus is on the contractual relationship among the individuals organizing, owning, and operating the firm.[261] Collaboration theory is different because it shifts and expands the focus to include the government.[262]

The contractual underpinnings of collaboration theory offer one model for corporate managers deciding whether to engage in tax avoidance, which I will term the "good faith model." Implicit within every contractual relationship is a duty of good faith that requires parties to treat each other well within the scope of their agreement.[263]

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258. *See infra* Part V.C (arguing that the good faith model should always be chosen over the profit seeking model in instances related to tax avoidance).

259. *See supra* Part V (explaining collaboration theory).

260. *See supra* note 124 and accompanying text (explaining the contractual nature of the corporate form).

261. *See supra* Part IV.C (explaining the aggregate theory of the corporation).

262. *See supra* Part V (providing an overview of collaboration theory).

263. *See* U.C.C. § 1-304 (AM. LAW. INST. 2004) ("Every contract or duty within [the Uniform Commercial Code] imposes an obligation of good faith in its performance and enforcement."); RESTATEMENT (SECOND) OF CONTRACTS § 205 (AM. LAW INST. 1981) ("Every contract imposes upon each party a duty of good faith and fair dealing in its performance and its enforcement."); Matthew T. Bodie, *The Best Way Out Is Always Through: Changing the Employment At-Will Default Rule to Protect Personal Autonomy*, 2017 U. ILL. L. REV. 223, 232 ("Common-law contract doctrine presumes that each contract has an implied duty

Similarly and relatedly, within business forms, collaborators have an obligation to treat each other with a duty of good faith within the scope of their relationship. As Benjamin Cardozo described it in *Meinhard v. Salmon*,[264] while he was serving as Chief Judge of the New York Court of Appeals at the time of the opinion: "Joint adventurers, like copartners, owe to one another, while the enterprise continues, the duty of the finest loyalty. . . . Not honesty alone, but the punctilio of an honor the most sensitive, is then the standard of behavior. As to this there has developed a tradition that is unbending and inveterate."[265] Under collaboration theory, the parties composing the firm are bound by duties of good faith that emanate from the contractual relationship of the parties and from the business form itself.

As a result, corporate managers should not deprive the government of the tax revenue that it hoped to generate through the creation of the corporation. As previously discussed, under collaboration theory, the collaboration is defined as a common effort between or among multiple entities to accomplish a task or a project.[266] In regard to for-profit corporations, the common project is economic development and economic gain for the parties involved.[267] When corporate managers engage in tax avoidance, they violate the duty of good faith by treating the government abusively, and they frustrate at least one of the government's purposes for entering the contract, i.e., to procure funds via taxation for purposes of maintaining and improving the state.[268]

B. The Profit Seeking Model

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of good faith and fair dealing."); Andrea M. Matwyshyn, *Privacy, the Hacker Way*, 87 S. CAL. L. REV. 1, 54 (2013) ("Courts have recognized that every contract imposes the duty of good faith and fair dealing to protect the parties' reasonable expectations. This approach serves to legally solidify the idea that rules of exchange should reflect reasonable business conduct.").

264. 164 N.E. 545 (N.Y. 1928).

265. *Id.* at 546.

266. *See supra* Part V (explaining collaboration theory).

267. *See supra* note 122 and accompanying text (discussing the purpose of a for-profit corporation, which is to make a profit).

268. *See supra* note 53 and accompanying text (discussing that tax avoidance is one potential way to improve a corporation's financial performance).

Tension certainly exists between the implied duties of good faith within the firm and the deal that the government has struck with the individuals organizing, operating, and owning the corporation.[269] The state and the individuals organizing, operating, and owning the corporation have expressly agreed to create a for-profit corporation, which must seek profit.[270] Because lowering a corporation's tax burden is one of the ways of improving the financial performance of the firm,[271] a second potential model emerges under collaboration theory as to how corporate managers should make decisions regarding whether to engage in tax avoidance.

Under this model, the analysis hinges on whether a cost benefit analysis demonstrates that the tax avoidance strategy is beneficial to the corporation. This model, which I will term the "profit seeking model," involves four scenarios. In the first scenario, the costs of the tax avoidance activity outweigh its benefits. At first blush, this might seem impossible because tax avoidance has been defined as structuring business transactions to reduce a firm's tax obligations in a manner that technically complies with the law, but violates the spirit or underlying policies of the law.[272] Because tax avoidance is by definition legal, one might believe that its benefits would always outweigh its costs. However, tax avoidance has a variety of potential costs associated with it. These include increased government scrutiny of the corporation's operations[273] and public scorn of the corporation for not shouldering its tax burden.[274] In addition, some tax avoidance schemes may simply be too expensive for certain corporations to

269. *See supra* note 263 and accompanying text (discussing the implied fiduciary duties of good faith within the corporation).

270. *See supra* note 122 and accompanying text (explaining that for-profit corporations exist to make a profit).

271. *See supra* note 53 and accompanying text (explaining one of the benefits associated with tax avoidance).

272. *See supra* Part II.A (defining tax avoidance).

273. *See supra* note 59 and accompanying text (explaining that one result of corporate tax avoidance is increased scrutiny of corporate operations).

274. *See supra* note 62 and accompanying text (explaining that the public has become increasingly critical of corporations failing to pay their fair share of taxes through the use of tax avoidance).

undertake.[275] For example, a small corporation in Nebraska is unlikely to go through the time and expense of setting up foreign subsidiaries to obtain a favorable tax rate on a portion of its income. Under the profit seeking model, based upon the profit seeking nature of the corporation, corporate managers should refrain from engaging in the tax avoidance strategy when its costs exceed its benefits.

In the second scenario, the tax avoidance activity is cost neutral. In this scenario the cost of setting up the tax avoidance scheme or the negative repercussions of the tax avoidance scheme are equal to any benefit that could be reaped. Under the profit seeking model of the corporation, the agreement that the individuals organizing, operating, and owning the corporation is that they will seek a profit.[276] What is confounding about scenario two is that any cost or benefit cancel each other out. At this point in the profit seeking model, the fiduciary duties discussed in the previous section would come into play to tip the scales in favor of not undertaking the tax avoidance activity because the express agreement to seek profits within the corporation would provide no guidance, and as a consequence, the state should be allowed to obtain the tax revenue.[277]

In the third scenario, the cost benefit analysis is uncertain, and the tax avoidance activity may lead to an economic benefit, or it may lead to a loss. Although debatable, the tax avoidance activity once again should not be undertaken. When the cost benefit analysis is uncertain, the duties of good faith that emanate from contractual nature of the collaboration and the business form itself should be enough to require corporate managers not to engage in the tax avoidance activity. The government has allowed

275. *See* Alexia Fernandez Campbell, *The Cost of Corporate Tax Avoidance*, ATLANTIC (Apr. 14, 2016), https://www.theatlantic.com/business/archive/2016/04/corporate-tax-avoidance/478293/ (last visited Feb. 18, 2019) (reporting on how large corporations avoid taxes through offshore accounts and shell companies, while smaller corporations end up paying the full tax rate) (on file with the Washington and Lee Law Review).

276. *See supra* note 122 and accompanying text (explaining that a for-profit corporation is designed to seek profit).

277. *See supra* Part VI.A (discussing the duties of good faith at play within collaboration theory based upon the contractual nature of the corporation and emanating from the business form).

for the creation of the corporation in part as a means of generating tax revenue, and when in doubt, corporate managers, rather than engaging in tax avoidance, ought to err on the side of allowing the government to collect revenue.

Finally, in the fourth scenario, the cost benefit analysis suggests a clear financial benefit to the firm through undertaking the tax avoidance activity. Under the profit seeking model, one would have to argue that because the corporation exists to make a profit, that the tax avoidance activity must be undertaken.[278] However, as will be explained in the next section, this view of the collaboration between the government and individuals organizing, operating, and owning the corporation is too simplistic.

C. Choosing the Good Faith Model

At first blush, collaboration theory seems problematic because it seems to suggest that both the good faith model and profit seeking model are appropriate for corporate managers to use in determining whether to engage in tax avoidance. In some instances, this does not matter. When the costs of tax avoidance outweigh the benefits, when the tax avoidance strategy is cost neutral, and when the cost benefit analysis is uncertain, both models suggest that tax avoidance activities should not be undertaken.[279] The problem arises in regard to tax avoidance activities with a clear financial benefit because the profit seeking model suggests that they should be undertaken, and the good faith model suggests the reverse.[280]

Resolving this problem turns on the deal that the individuals organizing, operating, and owning the corporation struck with the state in collaborating to form the corporation. In general, that deal is to seek profit because the common project, which is the basis of

278. *See supra* Part II.B (discussing the potential benefits of tax avoidance, including improving the financial performance of the corporation).

279. *See supra* Part VI.A–B (describing the good faith model and the profit seeking model).

280. *See supra* Part VI.A–B.

the collaboration, is economic development and economic gain.[281] The individuals organizing, operating, and owning the corporation are seeking their own economic development and economic gain, and the government is seeking societal economic development and economic gain. As a result, the corporate managers are required to seek profit. Elsewhere, I have argued that the profit seeking model requires corporate managers to decline to engage in socially responsible acts, if the financial benefit to the corporation is clear.[282] If the government is unhappy about the acts, then it has the ability to pass positive law to alter the cost-benefit analysis.[283] Therefore, in general, the profit seeking model should be preferred over the good faith model.

However, in regard to tax avoidance, the good faith model should be preferred to the profit seeking model. This means that tax avoidance is to be avoided in all circumstances. This includes circumstances in which a clear financial benefit exists from the tax avoidance activity, i.e., circumstances involving tax avoidance activities that the profit seeking model would require corporate managers to pursue. In short, tax is different. The reason for this is the deal that is struck between the government and the individuals organizing, operating, and owning the corporation. A for-profit corporation unsurprisingly exists to make a profit,[284] and under collaboration theory, the government and the individuals organizing, operating, and owning the corporation have created the entity for purposes of economic development and economic gain. When corporate managers engage in tax avoidance, they frustrate one of the government's main reasons for collaborating within the corporate form (i.e. to procure funds via taxation for purposes of maintaining and improving the state).[285] Therefore,

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281. *See supra* note 122 (explaining that the reason for the existence of for-profit corporations is to make a profit).

282. *See* Chaffee, *Corporate Social Responsibility*, *supra* note 38, at 377 (exploring the application of collaboration theory to corporate social responsibility).

283. *See id.* ("Through regulation, regulators can change the cost-benefit analysis that leads corporations to engage in socially reprehensible behavior . . . .").

284. *See supra* note 122 and accompanying text (discussing the purpose of a for-profit corporation).

285. *See supra* Part V (providing an overview of collaboration theory, including the government's reasons for engaging in the collaboration).

this Article takes the position that in regard to tax avoidance issues, the good faith model is the correct model to use because it correctly reflects the deal that the individuals organizing, operating, and owning the corporation struck with the government.

D. Lingering Concerns About the Good Faith Model

Although the good faith model is the appropriate method of applying collaboration theory to tax avoidance decision-making, a few lingering concerns can be raised, including why the corporation should limit tax avoidance in regard to the federal government, when the state government allows for its incorporation; why tax minimization is permissible, while tax avoidance is not; and how to limit or eliminate tax avoidance, when it has a relatively vague definition. Each of these concerns will be addressed in turn.

The good faith model of applying collaboration theory to corporate tax avoidance creates questions as to why the corporation should refrain from tax avoidance in regard to the federal system of taxation because the collaboration is among the state government and the individuals organizing, operating, and owning the corporation. In terms of the corporation's state tax burden, the good faith model speaks directly as to why the corporation should not engage in tax avoidance.[286] This is because incorporation occurs at the state level in the United States.[287] The

286. *See supra* Part VI.A (explaining the good faith model).

287. *See* M. Thomas Arnold, *"It's Déjà Vu All Over Again": Using Bounty Hunters to Leverage Gatekeeper Duties*, 45 TULSA L. REV. 419, 424 (2010) ("Corporation law historically has been a matter of state law. Most corporations are formed under state law and are, for the most part, governed by state law."); Justin Blount, *Creating A Stakeholder Democracy Under Existing Corporate Law*, 18 U. PA. J. BUS. L. 365, 381 (2016) ("In the United States, corporations are creatures of statute, created almost exclusively at the state level, with Delaware being the most popular state of incorporation."); Elizabeth Kingsley & John Pomeranz, *A Crash at the Crossroads: Tax and Campaign Finance Laws Collide in Regulation of Political Activities of Tax-Exempt Organizations*, 31 WM. MITCHELL L. REV. 55, 60 (2004) ("Nonprofit corporations or associations, like their for-profit counterparts, are creatures of state law.").

issue then becomes why the corporation should not engage in aggressive tax avoidance in regard to its federal taxes as a means of improving the firm's financial performance because the federal government is not a direct party to the collaboration. The obligation not to engage in tax avoidance on the federal level is derivative of the duty to the state government. The state government entered the collaboration with the individuals organizing, operating, and owning the corporation for purposes of economic development and economic gain.[288] A strong federal system helps to enable these pursuits through, for example, maintaining a strong national economy and maintaining a strong system of national defense.[289] Notably, the need for a strong national government to help to protect and enhance the states was one of the animating reasons for the transition from the Articles of Confederation to the Constitution, which provides the federal government with the power to tax.[290] As a result, the obligation not

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288. *See supra* Part V (providing an overview of collaboration theory).

289. *See* Swati Agrawal, *Trusts Betrayed: The Absent Federal Partner in Immigration Policy*, 33 SAN DIEGO L. REV. 755, 793 (1996) ("Division of power between the state and federal governments fosters efficiency of governance. Efficient distribution of power means that the federal government is . . . responsible for harmonizing and unifying policy regarding foreign and interstate relations . . . ."); Kevin Hopkins, *The Politics of Misconduct: Rethinking How We Regulate Lawyer-Politicians*, 57 RUTGERS L. REV. 839, 885 (2005) ("The Framers of the Constitution's selection of a federalist form of government was a compromise that was designed both to insure the existence of a strong central government, which was lacking under the Articles of Confederation, and to accommodate and protect the interests of the existing state governments."); David M. Schizer, *Fiscal Policy in an Era of Austerity*, 35 HARV. J.L. & PUB. POL'Y 453, 485 (2012) ("[S]tates do not have the same responsibilities [as the federal government] (for example, for national defense), and usually can depend on help from the federal government in an emergency.").

290. *See* Eric Engle, *Is Bitcoin Rat Poison? Cryptocurrency, Crime, and Counterfeiting (CCC)*, 16 J. HIGH TECH. L. 340, 358 (2016) ("An essential failing of the articles of confederation of the United States, the constitutional precursor to the current United States constitution, was finance: the articles of confederation provided no independent taxation power to the confederal government . . . ."); John T. Plecnik, *The New Flat Tax: A Modest Proposal for a Constitutionally Apportioned Wealth Tax*, 41 HASTINGS CONST. L.Q. 483, 506 (2013) ("It is uncontroverted that the principal reason for adopting the Constitution in lieu of the old Articles of Confederation was to enhance the taxing power of the federal government."); Steven J. Willis & Hans G. Tanzler IV, *Affordable Care Act Fails for Lack of Uniformity*, 27 U. FLA. J.L. & PUB. POL'Y 81, 86 (2016) ("The Constitution is substantially about the taxing power: the Articles of Confederation failed, at least in part, because Congress had no power to tax.").

to engage in federal tax avoidance is in fact derivable from the duties owed to the state under collaboration theory. One would have a hard time arguing that the states would be able to engage in effective economic development if the federal government is starved of funds through corporate tax avoidance.[291]

A second concern regarding the application of collaboration theory to tax avoidance using the good faith model is that it creates questions as to why tax minimization is permissible, while tax avoidance is not. If depriving the government of revenue as a result of tax avoidance strategies is not permissible, depriving the government of revenue as a result of tax minimization strategies appears to be troubling as well because tax minimization also deprives the government of revenue.[292] The difference, however, is that tax minimization is both legally permissible and acceptable by the government.[293] As explained earlier, for purposes of this Article, tax minimization occurs when a taxpayer reflectively makes tax compliance decisions with the goal of reducing that taxpayer's tax burden within the intended scope of the law.[294] In contrast, tax avoidance means the structuring of business transactions to reduce a firm's tax obligations in a manner that technically complies with the law but violates the spirit of the law.[295] Under collaboration theory, tax minimization is permissible, while tax avoidance is not, based on the deal that has been struck between the government and the individuals organizing, operating, and owning the corporation.[296] In terms of

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291. *See* ROBERT JAY DILGER, CONG. RESEARCH SERV., R40638, FEDERAL GRANTS TO STATE AND LOCAL GOVERNMENTS: A HISTORICAL PERSPECTIVE ON CONTEMPORARY ISSUES 1 (2018), https://fas.org/sgp/crs/misc/R40638.pdf ("In [Fiscal Year] 2018, the federal government is expected to provide state and local governments about $728 billion in federal grants encompassing a wide range of public policy areas . . . .").

292. *See supra* Part II.A (discussing tax minimization as a means of lowering a corporation's tax burden).

293. *See supra* Part II.A (exploring the spectrum of tax compliance behavior, which includes tax avoidance).

294. *See supra* Part II.A (providing a definition of tax minimization).

295. *See supra* Part II.A (providing a definition of tax avoidance).

296. *See supra* Part VI.A (describing the contractual underpinnings of collaboration theory and the good faith obligation tied to those underpinnings).

the deal struck, the idea is that to reap the benefits of the collaboration, the individuals organizing, operating, and owning the corporation will comply with the law.[297] In regard to tax minimization, as defined in this Article, the individuals organizing, operating, and owning the corporation are in full compliance with the letter and spirit of the law.[298] In regard to tax avoidance, those individuals are not.[299] Although those individuals are violating only the spirit of the law through tax avoidance, one would have a difficult time arguing that the deal struck with the government was that those individuals could be abusive to the laws and regulations of the government.

A third and final complaint that could be lodged against the good faith model and collaboration theory in general as applied to tax avoidance is that it does not provide a bright-line standard for purposes of helping corporate managers make tax compliance decisions. The spectrum of tax compliance behavior discussed above does not provide crisp, clean categories of tax compliance behavior because these categories blend and blur into each other.[300] As a consequence, in the business world, one may have difficulty distinguishing tax avoidance from tax minimization or tax avoidance from tax evasion.[301] Although a bright-line standard would be nice, legal mandates upon the business world are often not crisp and clear. For example, the fiduciary duties discussed above have filled reporters with cases in which courts struggle with

297. *See supra* Part VI.A (noting that, since the government is an essential part of the overall collaboration, corporations should not deprive the government of expected tax revenue).

298. *See supra* Part II.A (defining the term "tax minimization" and providing examples of this behavior).

299. *See supra*Part II.A (defining the term "tax avoidance" and comparing this behavior to other behaviors within the spectrum of tax compliance).

300. *See supra* Part II.A (defining tax avoidance through a discussion of the spectrum of tax compliance behavior).

301. *See* Marjorie E. Kornhauser, *Legitimacy and the Right of Revolution: The Role of Tax Protests and Anti-Tax Rhetoric in America*, 50 BUFF. L. REV. 819, 874 n.153 (2002) ("The difference between tax avoidance and tax evasion is that the latter is illegal, while the former is just smart tax planning. The boundary between the two is blurry."); Leandra Lederman, *The Interplay Between Norms and Enforcement in Tax Compliance*, 64 OHIO ST. L.J. 1453, 1454 n.1 (2003) ("[T]he line between illegal tax evasion and legal tax avoidance is sometimes blurry.").

their contours and implementation.[302] Although collaboration theory may not provide perfect guidance in regard to what to do in making tax strategy decisions, applying the theory in this context still demonstrates that a legal mandate exists not to engage in tax avoidance, and it provides more guidance than simply ignoring the true nature of the firm.

VII. Conclusion

As a result of recent tax reform, the permissibility of tax avoidance is a hot legal issue. The essential nature of the corporate form offers an excellent place to begin in understanding when and to what extent engaging in tax avoidance is mandated. This approach has not been taken before in the existing literature. By understanding the corporation as a collaboration between the government and the individuals organizing, operating, and owning the corporation, the impermissibility of aggressive corporate tax avoidance becomes apparent. Collaborators in business ventures owe each other a duty of good faith, and the contractual nature of the corporation carries with it a duty of a good faith as well. As a result, the notion becomes fanciful that depriving the government of revenue through aggressive corporate tax avoidance strategies is required or even permissible. Tax avoidance is by definition violating the spirit of the law, and it is an affront to the collaboration that forms the foundation of the corporate form because it frustrates one of the government's purposes for entering the collaboration (i.e. gaining revenue).

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302. *See supra* Part III.B (discussing the fiduciary duties corporate managers owe to the corporation and its stockholders).