Corporate Power, Law, and the Multinational Corporation: A Contemporary Reading of *Dodge v. Ford*

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Treating Dodge v. Ford as the precedent which serves as a symbol for legal control of corporate activity, Professor Deutsch analyzes the political forces which led to that decision. He also surveys political forces and legal precedents which may render such legal control ineffective in connection with multinational corporate entities.

Henry Ford symbolizes many things in the history of the United States. Developer of the automobile, implementer of projects to end international conflict, family patriarch, opponent of labor unions, he represents an individualism which manifested itself in a variety of political and economic forms during the 19th century. In political terms, the 19th-century movement characterized as Progressive advocated "direct" democracy at home (symbolized by such reforms as the initiative, the referendum, and election of judges) and attempted to restrict involvement in international affairs to "principled" uses of national power like the convening of conferences and formulation of agreements in pursuit of such ends as the renunciation by nations of the right to resort to arms.

Corporations were regarded as dangerous entities by Progressives because the accumulation of capital made possible by the corporate structure was perceived as permitting persons in control of such entities to wield inordinately large amounts of economic power. It was this perception that led the Michigan Supreme Court in *Dodge v. Ford Motor Co.*,[1] in response to Henry Ford's plan to expand his production facilities while reducing the selling price of his cars, to warn:

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1. 204 Mich. 459, 170 N.W. 668 (1919).

> The difference between an incidental humanitarian expenditure of corporate funds for the benefit of the employees, like the building of a hospital for their use and the employment of agencies for the betterment of their condition, and a general purpose and plan to benefit mankind at the expense of others, is obvious. There should be no confusion (of which there is evidence) of the duties which Mr. Ford conceives that he and the stockholders owe to the general public and the duties which in law he and his codirectors owe to protesting, minority stockholders.[2]

The Michigan Supreme Court recognized that "[i]n view of the fact that the selling price of products may be increased at any time, the ultimate results of the larger business cannot be certainly estimated. The judges are not business experts."[3] As a result, while it did force the payment of dividends, which Ford had attempted to discontinue, the court refused to enjoin the building of River Rouge. Invocation of the business judgment rubric had effectively shielded corporate activity from judicial control.

It is the purpose of this Article to demonstrate that in today's world it is the concepts underlying the business judgment rubric which provide an effective shield against judicial intervention. Defined in terms of long-run profit maximization, that rubric gives to decisions an advantage shared by all actions described in quantifiable terms: that of appearing to be sufficiently certain and objective for direct comparison with alternatives. The "direct" democracy espoused by the Progressive movement was based on a belief that political systems, like economic ones, were legitimate only when founded on such direct comparisons; and that the selection of judges by appointment was inadequate precisely because the power to interpret judicial precedents was sufficiently great that individuals wielding it should be selected by the direct comparisons involved in the electoral process.

I.

Current attempts to limit corporate power are focused on defining standards of "fairness" with which persons in control of corporations must comply. Two recent decisions of the Delaware Supreme Court are illustrative of such attempts. In *Singer v. Magnavox Co.*,[4] that court held that the merger of a parent corporation with its

2. *Id.* at 506-07, 170 N.W. at 684.
3. *Id.* at 508, 170 N.W. at 684.
4. 380 A.2d 969 (Del. 1977).

eighty-four-percent-owned subsidiary would be fair only if the evidence supported a corporate purpose other than the elimination of the minority interest. In *Tanzer v. International General Industries, Inc.*,[5] the court held that a merger which conveyed a benefit to the parent corporation sufficed to meet such a standard, but the case was remanded for a determination of the "entire fairness" of the transaction. The scholarly comment was: "Just how such a reexamination is to be carried out remains something of a mystery."[6] Such a reaction is strikingly reminiscent of the Progressive distrust of the lack of certainty characteristic of common law. The most likely outcome of the *Tanzer* order is that the remand will control corporate behavior by making settlement cheaper than the cost of future litigation, and the merger will bear the extra cost of settlement.

Delaware cases, though perceived as defining the standard to be applied to parent-subsidiary relationships, also raise the issues presented by multinational corporate activities. In 1971, the Delaware Supreme Court reversed a determination by the Chancellor[7] that the test of "intrinsic fairness" had been violated by the payment of dividends to a parent by its subsidiary. In reversing, the court defined "the basic situation for the application" of that test as "one in which the parent has received a benefit to the exclusion and at the expense of the subsidiary"[8] and noted that "[t]he plaintiff [subsidiary] proved no business opportunities which came to [it] independently and which [the parent] either took to itself or denied to [the subsidiary]."[9] Responding to the claim that the magnitude of the dividends deprived the subsidiary of resources needed for its own development, the court pointed to the fact that "all of [the subsidiary's] operations have been conducted in Venezuela, and [the parent] had a policy of exploiting its oil properties located in different countries by subsidiaries located in the particular countries."[10]

The holding that the standard of fairness had been met thus seems based on a finding of historical regularity—the demonstration by the parent that it had consistently followed a policy of utilizing separate corporate subsidiaries to pursue business opportunities in separate national communities. Such a position would obviously

5. 379 A.2d 1121 (Del. 1977).

6. Brudney and Chirelstein, *A Restatement of Corporate Freezeouts*, 87 YALE L.J. 1354, 1365 (1978).

7. Levien v. Sinclair Oil Corp., 261 A.2d 911 (Del. 1969).

8. Sinclair Oil Corp. v. Levien, 280 A.2d 717, 720 (Del. 1971).

9. *Id.* at 722.

10. *Id.*

have been both easier to argue and more difficult to refute if each separate nation had enacted a law restricting business opportunities located within its boundaries to corporate entities that accepted local participation in some designated form. While such policies have recently been proclaimed by many nations, they have been accompanied by a concern that their implementation is in many cases responsive to what the governments involved perceive to be satisfactory to one or more multinational corporate entities.

Nor is the issue of the political impact of the economic power of multinational corporations restricted to its effect on governmental policy. Assume, for example, in connection with a question of plant location, that the majority of the inhabitants in the immediate vicinity of the proposed location are in fact perceived as a cohesive and threatening minority in the larger political unit with which negotiations concerning the plant are being conducted. As soon as employment demands made by the local residents are regarded as entailing costs in addition to those imposed by the demands of the larger political unit, the corporate entity, in deciding which demands to meet, will necessarily be taking actions with significant domestic political repercussions.

In general terms, the corporate response, if accepted, will be defining the nature of the community capable of making such demands in the future. The Progressive concern with corporate power thus becomes, not the question of the nature of political control of corporate economic behavior, but the issue of the extent to which economic behavior should be permitted to define the political unit possessing the potential for control.

II.

The political concepts in terms of which decisions such as those adumbrated above are made cannot without significant loss be quantified. As a result, the bases for those actions cannot directly be compared to quantifiable types of data. This loss, because it makes direct comparisons impossible, presents insuperable obstacles to the implementation of the "direct" democracy espoused by Progressives. More importantly, lack of quantifiability precludes any requirement that the concepts on which those actions are based be given precisely the same meaning by different individuals; and the resultant variations in individual definitions necessarily produce potential gaps in communication among the individuals making such decisions.

Social science theorists in the 1950's ascribed the origin of such a situation to the replacement of *Gemeinschaft* by *Gesellschaft*. *Gemeinschaft*, for this purpose, can be defined as the situation in which the economic organization deemed socially necessary is perceived by the individual as sufficiently small in scale itself to provide a basis for community. Mass production, on the other hand, involves economic organization on a scale perceived as antithetical to the expression of individual skill that constitutes the basis for community participation. The specialization required by such organization divides many business decisions into a variety of aspects, each involving a specialized field of knowledge. Because only some of those aspects are capable of quantification without significant loss, however, this process necessarily produces the gaps in communication described above.

In terms of the *Dodge v. Ford* precedent, it is clear that the mass assembly techniques which made possible Ford's plans for River Rouge necessarily supplanted craft skills and techniques perceived as sufficiently small in scale to provide the basis for *Gemeinschaft*. The resultant emphasis on the volume of production, rather than quality or diversity, also produces significant social effects when viewed from the standpoint of consumption. Expanded application of mass production techniques substantially raises the cost of goods readily distinguishable from those generally available, a fact that renders the use of conspicuous consumption as a mechanism for personal identity increasingly difficult. Thus, as demonstrations staged for the mass media make clear, personal identity has in more and more instances become defined through public recognition of self as a member of a group devoted to a given aim.

The implication for law of this social phenomenon—the shift in focus from the individual to the group—constitutes one of the reasons *Brown v. Board of Education*[11] can be characterized as a landmark decision in the jurisprudence of the United States. Not only was that decision the result of a carefully-organized group campaign of litigation,[12] but the grade-a-year desegregation programs upon which settlements were often based also denied to given individual plaintiffs the very right to an integrated education for which suit was being brought.

The significance of self-conscious group legal activity in connection with United States politics can most clearly be portrayed in con-

11. 347 U.S. 483 (1954).

12. Vose, *Litigation as a Form of Pressure Group Activity*, 319 ANNALS 20 (1958).

nection with *Smith v. Allwright*.[13] In that case, the Supreme Court held unconstitutional attempts to exclude persons on the basis of race from participating in primary elections conducted by the Texas Democratic Party, which was treated by the applicable state law as a private voluntary institution. Herbert Wechsler condemned that decision as unprincipled because it seemed to him necessarily to bar the organization of political parties exclusively on the basis of religious, economic, or social classifications or ideologies.[14] In a review of Wechsler's argument, Professor Ernest Brown denied that the Supreme Court's decision entailed what he agreed would be an impermissible limitation on the formation of political organizations:

> Cause and effect are difficult to establish in political institutions, but it is at least a tenable thesis that the system of legally significant primary elections is an outgrowth of a party system in which the major parties, to which primaries significantly relate, have historically been amorphous, heterogeneous, and heterodox. In dealing with an institution in what is, I should think, its predominant historical and functional context, it seems questionable that *Smith v. Allwright* can be considered unprincipled because it did not anticipate possibilities lying in a hypothetical, and different, future.[15]

As a result of awareness of the advantages inherent in organized litigation, possibilities, characterized as hypothetical by Brown, are rapidly brought to court in an attempt to test the outermost limits of an announced judicial policy. The result of this phenomenon—the loss of the characteristic of randomness in the flow of litigation—is to make it more difficult for judicial decisions to be accepted as promulgating generally applicable standards, a problem explored in the next Section in the context of constitutional standards that must be met by domestic political efforts to control economic activity.

III.

Given the difficulties encountered by federal and state judges in promulgating workable standards of implementation, it has become clear that certain language in Warren Court decisions in areas such as reapportionment must in the future be construed narrowly. What has not been clear is the extent to which this process of qualification

13. 321 U.S. 649 (1944).

14. H. WECHSLER, *Toward Neutral Principles of Constitutional Law*, PRINCIPLES, POLITICS AND FUNDAMENTAL LAW 3, 30-40 (1961).

15. Brown, Book Review, 62 COLUM. L. REV. 386, 391 (1962).

may make social control of economic activity an increasingly difficult task.

United States Trust Co. v. New Jersey,[16] a declaratory action on behalf of bondholders, involved a challenge to New York and New Jersey statutes which repealed a prior statutory covenant limiting the ability of The Port Authority of New York and New Jersey to subsidize rail passenger transportation. The United States Supreme Court, finding the legislation to be violative of the Contract Clause of the United States Constitution,[17] reversed the New Jersey Supreme Court's *per curiam* affirmance of the trial court's ruling that the statutory repeal was a reasonable exercise of New Jersey's police power. Mr. Justice Brennan, with whom Mr. Justice White and Mr. Justice Marshall joined in dissent, argued that "[t]oday's decision. . . . by creating a constitutional safe haven for property rights embodied in a contract . . . substantially distorts modern constitutional jurisprudence governing regulations of private economic interests,"[18] and that "[d]ecisions of this Court for at least a century have construed the Contract Clause largely to be powerless in binding a State to contracts limiting the authority of successor legislatures to enact laws in furtherance of the . . . collective interests of the polity."[19]

The lengthy case survey in terms of which the *United States Trust Co.* dissent attempts to establish the last proposition[20] is reminiscent of the canvassing of "political question" decisions undertaken by Mr. Justice Brennan in 1962 in *Baker v. Carr*[21] to establish the proposition that "the complaint's allegations of a denial of equal protection present a justiciable . . . cause of action."[22] The Frankfurter dissent in *Baker v. Carr* argued:

> The Court today reverses a uniform course of decision established by a dozen cases, including one by which the very claim now sustained was unanimously rejected only five years ago. . . . Disregard of inherent limits in the effective exercise of the Court's judicial Power not only presages the futility of judicial intervention in the essentially political conflict of forces by which the rela-

16. 431 U.S. 1 (1977) [hereinafter cited as *United States Trust Co.*].

17. "No State shall . . . pass any . . . Law impairing the Obligation of Contracts. . . ." U.S. CONST. art. I, § 10, cl. 1.

18. *United States Trust Co.*, 431 U.S. at 33.

19. *Id.*

20. *Id.* at 45-61.

21. 369 U.S. 186, 210-37.

22. *Id.* at 237.

> tion between population and representation has time out of mind been and now is determined. It may well impair the Court's position as the ultimate organ of "the supreme Law of the Land" in that vast range of legal problems, often strongly entangled in popular feeling, on which this Court must pronounce.[23]

The basis for the Frankfurter warning was that more than one line of precedent is arguably applicable to almost every case accepted for decision by the Supreme Court. As a result, almost every decision requires that cases held not to govern the situation being adjudicated must be reinterpreted in ways consistent with the result arrived at. Decisions that require significant reinterpretation of prior precedents threaten damage to the image largely responsible for public acceptance of the binding nature of the Court's opinions: the perception that the holding represents a conclusion derived from a reasonably stable set of rules embodied in judicial precedents.

Thus, whether or not one agrees with the decision reached, it seems important that the majority in *United States Trust Co.* holds that "[t]he trial court's 'total destruction' test is based on what we think is a misreading of *W. B. Worthen Co. v. Kavanaugh*, 295 U.S. 56 (1935),"[24] whereas the dissent states:

> The Court, as I read today's opinion, does not hold that the trial court erred in its application of the facts of this case to Mr. Justice Cardozo's formulation. Instead, it manages to take refuge in the fact that *Kavanaugh* left open the possibility that the test it enunciated may merely represent the "outermost limits" of state authority. . . . This, I submit, is a slender thread upon which to hang a belated revival of the Contract Clause some 40 years later.[25]

As argued in the prior Section, perhaps the most significant impact of self-conscious group utilization of the legal process is that it will henceforth take considerably less than a generation to test the meaning of a judicial declaration concerning "outermost limits." The next Section of this Article delineates one possible result of the changed perception of law resulting from this fact in connection with multinational corporate activities.

IV.

A 1968 Second Circuit decision, construing Rule 10b-5 of the

23. *Id.* at 266-67.
24. 431 U.S. 1, 26 (1977) (footnote omitted).
25. *Id.* at 57 (emphasis added).

Securities Exchange Act of 1934[26] as imposing stringent limitations on securities transactions involving controlled corporations, indicated to the dissenters the dangers in utilizing litigation costs as a control device:

> What this amounts to is giving *carte blanche* to every holder of a few shares in any corporation whose stock is traded on the New York or American stock exchanges to give his imagination full rein in the making of any sort of extravagant charges, no matter how ill founded in fact they may be, and then, when faced with a summary judgment motion based upon personal knowledge and documentary proof, say simply "I know nothing whatever about the matter but hope my lawyer will find something if we conduct extensive discovery proceedings and compel the defendants to produce their complete files." This, while doubtless not so intended, is in my judgment nothing short of a standing invitation to blackmail and extortion. It is perfectly apparent that the expense of such discovery proceedings to the defendants, especially when they are foreigners as in this case, will be enormous; and a plaintiff and his lawyer under these circumstances would seem to have some justification for hoping they will be bought off in one way or another, despite the falsity of the allegations in the complaint.[27]

The opinion in question, *Schoenbaum v. Firstbrook*, was rendered on rehearing *en banc* and involved Banff Oil Ltd., a Canadian corporation, and Aquitaine Company of Canada, Ltd., the wholly-owned subsidiary of a French corporation. In February of 1964, Aquitaine acquired control of Banff and designated three of its representatives to sit on Banff's eight-person board of directors. In the following month, the two corporations agreed to conduct joint explorations for oil, and in December of that year, Banff's board of directors voted to offer 500,000 shares of Banff treasury stock to Aquitaine. A test well struck oil on February 6, 1965.

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26. It shall be unlawful for any person, directly or indirectly, by the use of any means or instrumentality of interstate commerce, or of the mails or of any facility of any national securities exchange,
    (a) To employ any device, scheme, or artifice to defraud,
    (b) To make any untrue statement of a material fact or to omit to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading, or
    (c) To engage in any act, practice, or course of business which operates or would operate as a fraud or deceit upon any person,
    in connection with the purchase or sale of any security.
17 C.F.R. § 240.10b-5 (1969).

27. Schoenbaum v. Firstbrook, 405 F.2d 215, 221 (1968), *cert. denied*, 395 U.S. 906 (1969).

The petition for rehearing *en banc* sought reconsideration of the issue whether, as the trial judge had held, the defendants were entitled to summary judgment in a derivative action on behalf of Banff. The plaintiffs there had alleged "that the defendants, knowing of the oil discoveries and the consequent increase in value of Banff stock, sold [all] of that stock to Aquitaine . . . at vastly inadequate prices as a result of a conspiracy . . . to enrich Aquitaine . . . at the expense of Banff."[28]

In the dissent's view, the *en banc* reversal of the panel's upholding of the trial judge's grant of summary judgment was based upon an erroneous assumption of fact:

> We proceeded in the panel opinion upon the assumption that both parties to the transaction of purchase and sale of the Banff treasury stock knew Banff had struck oil because Judge Cooper proceeded upon the same hypothesis. In retrospect it is now apparent that it was a mistake to have made this contrary-to-fact assumption as it has thrown the whole case out of focus.[29]

It is likely, however,[30] that the crucial fact was that the corporations were "taking advantage of [an] Alberta law permitting . . . withhold[ing] [of] information concerning [the oil] discovery for one year";[31] that the *en banc* holding was based on a perception of foreign law being utilized in an attempt to justify a deviation from the directives embodied in United States securities legislation.

Even if one assumes that *Schoenbaum v. Firstbrook* is in fact a holding that United States securities legislation overrides inconsistent foreign law, its current significance is that "[t]he court en banc has not reviewed the [panel] decision . . . on the issue of jurisdiction . . . and that decision stands as the holding of the court."[32] The

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28. *Id.* at 218.

29. *Id.* at 220.

30. *See, e.g.*:

> It is argued that the agreement to sell Banff stock to Aquitaine was entered into before the results of the oil exploration were known. However it is by no means clear that the letter of Aquitaine's president dated January 5, 1965 resulted in the formation of a binding contract. Moreover in the absence of an opportunity for discovery procedures it cannot be accepted as true that on January 5, 1964 [sic] or at the earlier date in December, 1964 when Banff made the offer to sell, the parties were not in possession of sufficient information as to the true value of Banff stock to make the sale at market price a fraud on Banff. In addition, whether Aquitaine's acquisition of the Banff stock on the eve of the completion of the first oil well constituted overreaching presents an issue to be resolved only after an opportunity for further investigation.

Id. at 220.

31. *Id.* at 221.

32. *Id.* at 217 (emphasis added).

dissent argued that the difficulty with *Schoenbaum v. Firstbrook* was that it "transform[ed] a simple cause of action against directors for waste or the use of bad judgment in the sale of corporate assets into a federal securities fraud case by judicial fiat,"[33] a holding that would be reversed by the Supreme Court's decision in *Blue Chip Stamps v. Manor Drug Stores*.[34] The holding on jurisdiction, however, imposed the costs connected with the possibility of federal securities litigation solely on the basis of the act of listing securities on a national securities exchange:

> [T]he district court found that the only harm alleged was to the foreign corporation on whose behalf plaintiff brought the action. We do not agree. A fraud upon a corporation which has the effect of depriving it of fair compensation for the issuance of its stock would necessarily have the effect of reducing the equity of the corporation's shareholders and this reduction in equity would be reflected in lower prices bid for the shares on the domestic stock market. This impairment of the value of American investments by sales by the issuer in a foreign country, allegedly in violation of the Act, has in our view, a sufficiently serious effect upon United States commerce to warrant assertion of jurisdiction for the protection of American investors and consideration of the merits of plaintiff's claim.[35]

If costs of litigation are perceived as outweighing the benefits conferred by such listing, one possible remedy would be simply to leave the jurisdiction. Any given national legal system, in other words, can enforce substantive domestic policies on multinational transactions only so long as the advantages of that system are perceived as outweighing the costs entailed in leaving the jurisdiction. To a considerable extent, multinational corporations could contract out of all legal systems simply by expending the resources required to obtain more precise drafting of contractual agreements explicitly dealing with the widest array of possibilities, and accepting the costs of resort to arbitration. Indeed, existing forum selection clauses demonstrate awareness of the possibility of treating choice of law as an aspect of a transaction subject to corporate control. The Supreme Court's decision in *M/S Bremen v. Zapata Off-Shore Co.*[36] explicitly recognized that such a clause could effectively block the enforcement of substantive domestic social policy.

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33. *Id.* at 220.
34. 421 U.S. 723 (1975).
35. Schoenbaum v. Firstbrook, 405 F.2d 200, 208-09 (1968) (footnote omitted).
36. 407 U.S. 1 (1972).

The Bremen was a tug owned by a German corporation, which was towing respondent's ocean-going drilling rig under a contract exculpating it from liability for damages and providing that "[a]ny dispute arising must be treated before the London Court of Justice."[37] When the rig was damaged in international waters in the middle of the Gulf of Mexico, respondent, a United States corporation, commenced suit in admiralty in a United States District Court.

Vacating the judgment of the Court of Appeals, which had "suggested that enforcement [of the forum selection clause] would be contrary to the public policy of the forum under [an earlier Supreme Court decision barring exculpatory clauses],"[38] the Supreme Court held that the earlier decision "rested on considerations with respect to the towage business strictly in American waters, and those considerations are not controlling in an international commercial agreement."[39] It then quoted with approval the dissent in the Court of Appeals, which argued that the policy promulgated by the earlier Supreme Court decision should be extended to multinational transactions only if it is demonstrated that no business judgment has been made on the contractual clause at issue:

> [T]wo concerns underlie the rejection of exculpatory agreements: that they may be produced by overweening bargaining power; and that they do not sufficiently discourage negligence. . . . Here the conduct in question is that of a foreign party occurring in international waters outside our jurisdiction. The evidence disputes any notion of overreaching in the contractual agreement. And for all we know, the uncertainties and dangers in the new field of transoceanic towage of oil rigs were so great that the tower was unwilling to take financial responsibility for the risks, and the parties thus allocated responsibility for the voyage to the tow. It is equally possible that the contract price took this factor into account.[40]

Given the increasing significance of the multinational activities of corporate entities, the *Bremen* decision threatens substantially to dilute even the symbolic content of *Dodge v. Ford* as a citation of authority for the possibility of legal control of corporate action.

37. *Id.* at 2.
38. *Id.* at 15.
39. *Id.* at 15-16.
40. *Id.* at 16.