

Do the Capital Markets Compel Limited Liability?

A Response to Professor Grundfest

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I. INTRODUCTION¹

We had hoped that our recent article² exploring a rule of pro rata shareholder liability for corporate torts would spark renewed interest in the limited liability doctrine. Indeed, we concluded that article by inviting limited liability proponents to redress the balance of the argument. We therefore enthusiastically welcome the spirited defense of limited liability offered by Professor Joseph Grundfest in this issue of *The Yale Law Journal*³ and by his colleague, Professor Janet Cooper Alexander, in a forthcoming article in the *Harvard Law Review*.⁴

We predicted in our original article that the strongest arguments supporting limited liability would have little to do with the particular concerns of corporate law or the requirements of the corporate form. Rather, they were likely to rest on a belief that investors would be able to evade a pro rata liability regime, or that the difficulties of extraterritorial enforcement would preclude effective adoption of such a regime in any single jurisdiction.

Judging from the arguments of our critics, our prediction was on the mark. For what these critics do *not* argue is as important to us as what they do. They do not make an affirmative policy case for limited liability, nor do they defend the traditional corporate law view that breaching the limited liability rule might cripple the corporate form or impair the liquidity of the securities market. Instead, they focus on the difficulties of implementing a proportionate liability regime. Professor Grundfest accepts *arguendo* the policy rationale for proportionate liability but contends that enforcement constraints arising from the dynamism of the capital markets will doom any effort to escape the status quo.

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1. Professor Grundfest has revised his footnotes to comment on an earlier draft of this Response. We, in turn, have added to our footnotes to clarify our Response in light of Professor Grundfest's comments.

2. Henry Hansmann & Reinier Kraakman, *Toward Unlimited Shareholder Liability for Corporate Torts*, 100 YALE L.J. 1879 (1991).

3. Joseph A. Grundfest, *The Limited Future of Unlimited Liability: A Capital Markets Perspective*, 102 YALE L.J. 387 (1992).

4. Janet Cooper Alexander, *Unlimited Shareholder Liability Through a Procedural Lens*, 106 HARV. L. REV. (forthcoming Dec. 1992).

Professor Alexander argues that prevailing doctrine concerning conflicts of laws and personal jurisdiction would block the adoption of a proportionate liability regime at the state level, although she shows how pro rata shareholder liability might be implemented as a matter of federal law. We take it as a measure of progress in the debate over limited liability that we are thus invited to defend our views on the terrain of enforcement and procedure and not on the substantive terrain of tort or corporate law.

Although we take the criticisms of Professors Grundfest and Alexander seriously, we remain unconvinced. In this Response, we attempt to show that Professor Grundfest's description of the difficulties of enforcing a pro rata liability rule against public shareholders are less daunting than he suggests. We respond to Professor Alexander in greater detail elsewhere.⁵

II. PROFESSOR GRUNDFEST'S CRITIQUE OF UNLIMITED LIABILITY

Professor Grundfest's central claim is that an unlimited liability regime of the type we propose—a regime assigning tort liability in excess of a corporation's value to its shareholders pro rata—would be irrelevant in today's capital markets. In essence, this is because capital markets would “generat[e] a large clientele of investors who are de facto attachment-proof in actions seeking recovery of proportionate damages.”⁶ These nonassessable investors would specialize in holding the equity securities of corporations having high expected tort costs. Most other investors—those with potentially assessable assets—would confine their investments to low-risk equities. Then, through a variety of arbitrage techniques, both classes of investors would assemble investment portfolios with substantially the same risk and return characteristics that they would have achieved under a limited liability regime.

The critical step in this argument is the first one: the claim that the capital markets will always be able to generate a large pool of nonassessable shareholders capable of holding the bulk of the equity securities of firms having high tort risks. Conversely, the last point—the market's ability to use arbitrage to construct balanced portfolios—is largely irrelevant. A proportionate liability regime stands or falls on whether it can maintain, for most corporations running high tort risks, a core of equity holders who are in fact assessable for the corporation's excess tort liability. If this can be done, then the market's ability to construct balanced portfolios is a benefit rather than a burden to unlimited liability, since it assures that the resulting tort risks can be efficiently diversified. In contrast, if very large pockets of nonassessable shareholders remain, unlimited liability in tort is unlikely to work even if those shareholders are unable to

5. Henry Hansmann & Reinier Kraakman, *A Procedural Focus on Unlimited Shareholder Liability*, 106 HARV. L. REV. (forthcoming Dec. 1992).

6. Grundfest, *supra* note 3, at 389 (citation omitted).

achieve the same degree of portfolio diversification that they could achieve with limited liability.⁷

Thus we will focus on Professor Grundfest's claim that there will always be a sufficiently large pool of nonassessable shareholders to defeat unlimited liability. Despite his arguments, we believe that relatively straightforward legal measures have substantial promise for preserving the core of assessable shareholders required by a proportionate liability regime.

To settle the issue, it is necessary to take a closer look at just how the capital markets might generate nonassessable shareholders. Professor Grundfest proposes, by our count, four methods. Two of these involve schemes, undertaken either by high risk corporations or by market intermediaries that purchase the securities of such corporations, to issue securities designed to be nonassessable regardless of who holds them. The remaining two methods turn on purportedly unavoidable limitations on the enforcement of shareholder liability: the high costs of collecting from small investors and the impossibility of collecting from offshore investors. We shall suggest here some measures that might limit each of these sources of nonassessable shareholders, saving the most difficult case—that of the offshore investor—for last.

A. *Evasion by Design: Schemes to "Launder" Equity*

Professor Grundfest argues that, even without attempting to spirit risky equity overseas, a corporation could externalize tort costs by minimizing its outstanding equity shares and raising the bulk of its capital by selling equity substitutes in addition to ordinary debt securities. These substitutes would include convertible bonds, warrants, and other hybrid securities that, although not formally equity shares and thus presumably not subject to unlimited liability, have many of the characteristics of such shares.

Equity substitutes and debt do not themselves evade unlimited liability, but merely concentrate liability on a smaller pool of equity. Equity substitutes and debt become troublesome for an unlimited liability regime only when accompanied by a decline in the aggregate assessable assets of equity holders. This may occur, however, if the pool of equity capital is reduced sufficiently to permit a substantial fraction of that capital to be placed in the hands of equity holders who can escape the effective jurisdiction of the courts or who lack sufficient assets to satisfy a liability judgment.

7. A fairly well-diversified portfolio could be constructed using only the equities of risky firms, since such tort-prone industries as oil, chemicals, pharmaceuticals, and tobacco have little in common apart from their exposure to tort liability. We do not dispute Professor Grundfest's observation that *optimal* diversification would require a portfolio that includes the return characteristics of both high and low risk firms. *See* Grundfest, *supra* note 3, at 400 n.53. Rather, our point is that the incremental diversification gain achievable by arbitrage between holders of high and low risk equities is a secondary issue. The central issue is the size of the pool of nonassessable shareholders who are able to profit from investing in high risk firms—and in doing so undermine a proportionate liability regime—even without access to sophisticated arbitrage transactions.

An extreme form of this evasion strategy, in which a few high rollers take tort-prone corporations private with the aid of debt financing or other equity substitutes, is discussed at length in our original article.⁸ Such a strategy is an obvious threat to a proportionate liability regime. Yet, as we argued previously, it is not an insurmountable one. The supply of high rollers with just the right combination of capital, risk preference, and management expertise to pursue this strategy is likely to be very limited.

Beyond this, a court should have little difficulty identifying an opportunistic recapitalization in which, to avoid tort liability, an issuer shrinks its traditional equity base to a small pool of attachment-proof shareholders while employing equity substitutes and debt to serve the risk bearing and control functions normally served by common stock.⁹ Confronted with such a blatant evasion tactic, a court need only recharacterize some or all of the equity substitutes as constructive equity for purposes of pro rata tort liability. Indeed, since convertible securities are generally the best equity substitute, we suspect that most evasion efforts could be controlled adequately if the courts stood ready to characterize convertible securities as constructive equity, at their stated conversion ratios, whenever those securities appear to have been used to evade tort liability.¹⁰ In some cases, however, it might be necessary to go further and treat debt securities as constructive equity as well. This would be appropriate where, for example, individuals who own no common stock in the firm but exercise substantial

8. Hansmann & Kraakman, *supra* note 2, at 1911-13.

9. Professor Grundfest argues in response that it would be difficult for courts to identify efforts to evade (not avoid) tort liability through the use of equity substitutes because it would be "trivially easy" for high risk firms "to generate legitimate rationales for the use of equity substitutes"—most notably the rationale that equity substitutes shorn of the risk of liability are a cheaper source of capital than equity itself. See Grundfest, *supra* note 3, at 414 n.105. This argument misconceives how extensive reliance on equity substitutes would have to be before a risky corporation could evade the bulk of its excess tort liability.

Displacing 50% or even 90% of the existing equity of a large corporation might not save a penny in tort costs if the personal assets of hundreds or thousands of remaining shareholders continued to be exposed to tort liability. An even more dramatic substitution effort—one that eliminated the market for a corporation's equity entirely—could reduce the pool of assessable shareholder assets below the expected damages of a catastrophic tort. Such an effort, however, would have two other effects. First, destroying the market for a public corporation's equity would also eliminate the foundation for conventional equity substitutes such as convertible debt. Second, shifting virtually all of a corporation's risk to equity substitutes would require a commensurate shift in control over corporate policies to the holders of the equity substitutes.

We submit that in the wake of a catastrophic tort, a court confronted with changes of this magnitude in a corporation's capital structure, securities market, and governance structure would have good reason to suspect an effort to evade liability. In particular, the rationale that such dramatic changes were undertaken to lower capital costs would not sit well when it was painfully obvious that tort victims were to be an important source of the cost savings. Perhaps a court would not always recharacterize equity substitutes as equity even in these circumstances, but the legal risk that it might do so would act as a powerful deterrent to such a costly evasion effort. In addition, the restructuring necessary to effect such an evasion strategy must play out in the context of public corporations and the public market, not in the context of closely held corporations where the analogous equity characterization problem typically arises in tax.

10. Contrary to Professor Grundfest's suggestion, *supra* note 3, at 415, recharacterizing equity substitutes as constructive equity in response to deliberate attempts to evade liability is not equivalent to establishing minimum capitalization levels. Such recharacterizations would presumably be rare. They would be directed toward distorted capital structures with no plausible justification except the evasion of liability, and they would turn not simply on the amount of equity retained by a corporation but also on the dispersion and assessable assets of remaining equity holders.

control over it as directors or officers hold large quantities of subordinated debt.¹¹

This same point applies to Professor Grundfest's second proposed evasion scheme: an effort by market intermediaries to create specialized holding structures (or investment funds) to separate returns on equity from the risk of paying excess tort damages under a proportionate liability rule. Such a fund would hold no assets except stock in a single risky firm. In addition, it would issue no equity itself that might absorb the personal liability attaching to its investment shares. An investment bank might create a fund to purchase the stock of a tort-prone corporation with capital raised by selling a combination of debt and options or warrants to solvent investors. Investors in the fund could thus hope to divide the returns from risky equity free of the danger of tort liability.

This is a clever scheme, but it has one shortcoming. No court would accept such a fund at face value because its sole function would be to evade tort liability.¹² In the event of an actual tort, a court would—or at least should—assign the full liability of the fund's equity holdings to its investors. This would not require sophisticated calculations. A crude apportionment rule—such as assigning liability according to the dollar amounts invested in the fund—would suffice, since all investors in the fund, regardless of the form of their investment, would be joint participants in a scheme to evade tort liability. Even more to the point, because investors would expect a court to apportion liability among them in one way or another, it is unlikely that a market intermediary could profitably launch such a laundry fund in the first place.¹³

B. *Passive Evasion and the Limits of Enforcement*

Quite apart from such deliberate schemes to evade proportionate liability, Professor Grundfest correctly points out that there may be classes of equity holders in risky corporations who can evade liability assessments because of more general constraints upon the ability of courts or plaintiffs to enforce such assessments. Professor Grundfest identifies two classes of shareholders who could

11. Subordinated debt might be characterized as equity at face value. There would be no reason to be overly fussy in allocating liability among different classes of security holders. The parties themselves could not complain about a judicial allocation of liability, since they would have intentionally failed to allocate tort risks among themselves beforehand. In addition, the prospect of a court imposing an allocation of liability rather than allowing tort victims to go uncompensated would probably deter such evasive recapitalizations in the first instance.

12. Prior to the introduction of federal deposit insurance in the 1930's, courts had little difficulty thwarting analogous evasion strategies while enforcing double liability against shareholders under federal banking law. See Jonathan R. Macey & Geoffrey P. Miller, *Double Liability of Bank Shareholders: History and Implications*, 27 WAKE FOREST L. REV. 31, 39-55 (1992).

13. Contrary to Professor Grundfest's suggestion, *supra* note 3, at 411-14, under a proportionate liability regime there should be no need to regulate options, futures, and other derivative securities not issued by a risky corporation or by a holder of such a corporation's equity shares. In particular, there should be no need to attempt to impose excess tort liability upon the holders of such derivative securities.

be passive evaders of this sort: (1) small domestic shareholders and (2) offshore investors residing in jurisdictions that refuse to enforce excess liability judgments.

Small domestic shareholders, Professor Grundfest argues, are likely to escape damage assessments under a proportionate liability rule because they will owe too little to justify the costs of collecting from them. To support his estimate of these costs, Professor Grundfest relies upon the work of Professor Alexander, who has developed a procedural critique of our proportionate liability proposal. In this critique, Professor Alexander assumes, among other points, that the collection procedure would be predicated on state law and, hence, subject to the multiple jurisdictional and procedural constraints that this would entail.

We do not dispute that litigation and collection efforts may involve large costs if the procedural backdrop to a proportionate liability regime remains more or less what it is today. However, in attempting to sketch a workable proportionate liability regime, we see no reason to make such an assumption. Procedural reform on the federal level could assure that claims arising from a catastrophic tort are all litigated in a single court. Federal legislation could assure that all shareholders are directly liable for any unsatisfied portion of the tort debt of corporations in which they own shares (so as to preclude shareholders from relitigating the merits of tort claims). Similarly, federal legislation could shift the legal costs of collecting on a valid tort debt to shareholders and deter even the smallest shareholder from ignoring a judgment. To be sure, these reforms would not be easy to shepherd through Congress, but then neither would a federal rule of proportionate liability in the first instance. The issue at this stage of the debate is not political feasibility, but the relative merits of liability regimes. We see no reason in principle why litigation and collection procedures could not be streamlined, particularly with the aid of a cost-shifting rule, to ensure effective collection against the vast majority of solvent domestic shareholders.

Professor Grundfest's second class of passive evaders—offshore shareholders—presents the most difficult challenge to a proportionate liability regime.¹⁴ No amount of domestic law reform can aid collection against a foreign shareholder whose home jurisdiction refuses to enforce an excess liability judgment. The issue, then, is whether a countermeasure can be devised that will not excessively burden the participation of American corporations in international equity markets.

Our original article proposed an insurance-based regulatory solution to the analogous problem of a foreign corporation that is domiciled in a limited liability jurisdiction and wishes to conduct business in the United States.¹⁵ With modifications, such a solution could also be applied to the foreign shareholders of a domestic corporation.

14. We recognized this in our original article. See Hansmann & Kraakman, *supra* note 2, at 1922, 1933.

15. *Id.* at 1923 n.112.

For example, one could identify risky industries—perhaps by broad industrial classifications, such as pharmaceuticals or chemical manufacturing—where potential tort costs appear large enough to make evading a proportionate liability rule through extensive foreign shareholdings attractive. One could then require, for example, that at least 60%¹⁶ of all shareholders in such corporations be (a) U.S. residents, (b) institutional shareholders with substantial (or, equivalently, well-diversified) assets in the U.S., or (c) individuals or well-capitalized institutional investors resident in foreign countries that, by treaty, grant U.S. courts personal jurisdiction for purposes of excess liability judgments. To provide further flexibility, exemptions from the 60% rule might be granted for companies purchasing large amounts of liability insurance, as we suggested in our article.¹⁷ The amount of insurance would not have to be chosen with any precision, but could be set crudely on the high side—say, as a large multiple of the company's total invested capital and/or annual expenditures—to make it worthwhile for nearly all corporations to avoid the insurance requirement.¹⁸ Such a regulation would not prevent citizens of any country from investing to whatever extent they wish in the securities of any company affected by the regulation. It would merely encourage such investors, when not personally subject to the jurisdiction of U.S. courts, to channel their investment through well-capitalized vehicles that are themselves either resident in the U.S. or subject to the jurisdiction of U.S. courts.¹⁹

16. We suggest the figure of 60% arbitrarily on the assumption that it would probably suffice to discourage a tort-prone corporation from engaging in excessively opportunistic creation of tort risks. Upon closer consideration, 50% or 80% might appear to be a more appropriate figure.

17. Hansmann & Kraakman, *supra* note 2, at 1923 n.112.

18. Professor Grundfest raises two objections to the solution we have sketched to the problem of nonassessable foreign investors. He argues that our proposal “may violate” bilateral treaty obligations to afford foreign companies “no less favorable” treatment than that accorded domestic companies. Grundfest, *supra* note 3, at 424 n.149. We fail to see the force of this argument since our proposal is not designed to treat companies with extensive foreign ownership unequally but merely to avoid giving such companies an advantage—the opportunity to externalize tort costs—that would be unavailable to predominately American owned companies.

Professor Grundfest also argues that unless our proposal were further elaborated, it could easily be evaded by foreigners who establish a domestic investment vehicle whose assets are invested exclusively in the shares of a risky U.S. corporation. *Id.* On this point, Professor Grundfest is correct. Further elaboration of our proposal would be necessary to take account of this potential for evasion. We do not purport to draft regulations in this Response, however, but instead to sketch the outlines of a solution. Nonetheless, the particular problem of foreign owned U.S. investment companies can easily be solved by a simple elaboration of our proposal. Our regulations need only specify that investment intermediaries qualify as “U.S. residents” (for purposes of exclusion under (a) of our proposal) only to the extent that their beneficial owners are U.S. residents. In this case, shares in a risky corporation held by a foreign owned U.S. investment company would receive the same treatment as shares held directly by nonassessable foreign investors, at least for purposes of administering the ownership based insurance trigger outlined above. Of course, if the foreign owned investment company were well-capitalized or diversified, it would be treated on a par with U.S. residents under section (b) of our proposal. More generally, according identical treatment to direct and indirect foreign ownership of risky equities is simply an application of the broader principle that a proportionate liability regime must see through intermediary ownership structures to prevent opportunistic evasion of tort liability. See Hansmann & Kraakman, *supra* note 2, at 1905 n.74.

19. A further refinement might be to assign all of the excess liability of corporations with substantial overseas equity ownership (say, between 20% and 40% foreign ownership) to the remaining equity holders who are subject to the jurisdiction of the U.S. courts. These corporations would then have an incentive to

There is insufficient space here to develop and evaluate in detail this or other potential regulatory schemes for preventing the opportunistic exportation of shareholdings in risky firms to foreign jurisdictions that are beyond the reach of U.S. courts. We simply wish to emphasize that Professor Grundfest does not carefully examine the potential for such regulation, much less demonstrate convincingly that regulation would not be feasible. Rather, he describes several other, unrelated efforts at financial regulation or taxation that have been hampered by the flexibility of financial markets and infers from them that “efforts to regulate behavior through the manipulation of financial market prices are often misguided and will generally fail to achieve their desired purposes.”²⁰ The intended content and scope of the quoted proposition are unclear to us. We can only say that the various examples of regulation that Professor Grundfest examines (including, conspicuously, the regulation of Japanese insurance companies with which he begins his article²¹) generally provide little evidence concerning the feasibility of the type of regulation required to enforce unlimited liability, and at least one of those examples—the corporate income tax—actually offers a hopeful prognosis for such regulation.²²

reapportion corporate distributions in favor of domestic shareholders in order to equalize returns across both classes of shareholders.

20. Grundfest, *supra* note 3, at 390-91.

21. If Japanese regulators did not immediately prevent insurers from evading capital requirements by buying dividends through the simple transactions that Professor Grundfest describes, presumably it was because they failed to try. It takes little imagination to think of regulatory strategies that would have made evasion much more difficult, such as including in the definition of “current income” only dividends and interest received on securities held by the insurance company for at least six months. We suspect that few analysts would wish to draw from this example even the very modest generalization that the protean character of capital markets requires that all net capital requirements for insurance companies and banks be abandoned as futile, much less any broader conclusions about regulatory incapacity.

Professor Grundfest responds to this argument by claiming that when Japanese regulators required that insurance companies make annual payments out of current income, they were not imposing a capital preservation requirement. *Id.* at 394-95 n.24. Yet it is difficult to imagine any other motivation for such a restriction, and he offers none. Professor Grundfest also suggests that if Japanese regulators had required a six-month holding period, insurance companies could have attempted a different evasive response based on the purchase of high yield securities. *Id.* This alternative evasion strategy, however, can threaten any minimum capital requirement—and it is precisely to thwart this kind of tactic that minimum capital requirements are generally accompanied by restrictions on the types of assets a regulated firm can hold.

22. It is a familiar point that there is no coherent economic rationale for allowing corporations to deduct interest but not dividends when computing their corporate tax liability. One might, therefore, conclude that any tax system so structured would not produce any revenue since corporations would design financial instruments and structures that would take advantage of this inconsistency in the tax system. And in fact, as Professor Grundfest points out, there has evidently been significant restructuring of corporate financing to avoid these taxes. Nevertheless, even after a century of this highly arbitrary tax system, U.S. corporations continue to distribute a substantial share of their net earnings in the form of dividends and the federal government continues to collect sizeable revenues from the corporate income tax. Note, moreover, that it is easier to avoid the corporate income tax by substituting debt for equity than it is to avoid unlimited liability: replacing equity with debt reduces taxes in direct proportion to the amount of debt employed, yet it simply concentrates all excess tort liability in the hands of the remaining equity holders.

Professor Grundfest claims in response that the hopeful prognosis we infer from the corporate tax analogy is mistaken. *Id.* at 415 n.108. His discussion misconceives our analogy. We argue that the tax experience strongly supports our view that corporations will not reconfigure their capital structures to eliminate traditional equity in response to proportionate liability. The agency problem associated with substituting debt for equity, which Professor Grundfest helpfully describes in his footnote, is further theoretical support for our view.

III. CONCLUSION

In sum, Professor Grundfest has proposed four ways in which equity holders might evade a proportionate liability regime. Two of these evasion routes presuppose active evasion schemes (equity laundering by market intermediaries or corporate issuers), and two depend upon purported limitations on the enforcement apparatus underlying proportionate liability. We propose legal measures to block each of these evasion routes: most simply (and cheaply), ex post judicial intervention to deter outright evasion schemes by corporate issuers and market intermediaries; less simply (and cheaply), regulatory measures to facilitate collection from small domestic shareholders and to discourage a wholesale flight of equity in risky firms beyond the reach of U.S. courts. None of these measures would be perfect or costless. In particular, keeping track of the foreign ownership of risky U.S. corporations would impose modest reporting and monitoring costs on both U.S. firms and foreign shareholders (although such costs could largely be avoided if foreigners traded through resident intermediaries).

Our original article, however, did not claim that proportionate liability would be costless. We argued that a regime of pro rata shareholder liability would be a pragmatic, workable way to avoid externalization of tort costs without forcing basic structural change on our systems of corporate governance and finance. Nothing in Professor Grundfest's appreciative account of the dynamism of capital markets jeopardizes the feasibility of a proportionate liability regime.²³ There may be novel liability evasion strategies—different from those that either Professor Grundfest or we have yet imagined—that could definitively defeat unlimited shareholder liability. They have yet to be introduced into the debate.²⁴

On inspection, then, it appears that Professor Grundfest does not disagree with our tax analogy. Rather, he makes an altogether different point: corporations can evade proportionate liability not by eliminating equity but by attracting nonassessable equity holders. This claim is indeed the chief point of contention between Professor Grundfest and us. The bulk of our Response is devoted to arguing that a regime of proportionate liability can adequately control the pool of nonassessable shareholders.

23. Professor Grundfest points to the fact that Lloyds of London is considering the adoption of limited liability for its investors ("names") as additional evidence weighing against the introduction of a proportionate liability scheme for corporate torts. This example is, however, inapposite. It clearly involves a choice of liability regimes in a contractual setting. As our article recognized, there are compelling reasons for retaining limited liability as the default rule governing the relationship between shareholders and contract creditors of the corporation. See Hansmann & Kraakman, *supra* note 2, at 1919-20.

24. In his conclusion, Professor Grundfest hints that possible disruptions in the international product markets occasioned by the adoption of proportionate liability—specifically the increased cost of American made goods—might equal or exceed in importance the obstacles to proportionate liability arising from the international capital markets. Two points should be made in response. First, to the extent that one concludes that tort liability unfairly disadvantages American manufacturers, a rule of limited liability is an arbitrary device for reducing liability costs. Direct reform of tort law would be a far superior approach to lowering the liability costs of U.S. firms. See *id.* at 1916-19. Second, the kind of catastrophic torts that are most likely to bankrupt public corporations are those involving serious injury to employees or the environment. If foreign producers wish to subsidize foreign products at the expense of their employees or their environment, we are far better off accepting their decision than we are in trying to match it by pursuing a similarly destructive tort policy at home.

To stand by our views on the feasibility of proportionate shareholder liability for public as well as closely held corporations is not to become unqualified advocates of such a regime. There is still the complex empirical task of weighing costs against benefits. We have acknowledged that a regime of unlimited liability would impose numerous costs, including transition costs, ancillary regulatory costs, and the indirect social costs of efforts to evade liability. Maybe such a regime would not be worth the candle. Maybe it would. That question can be answered only after tallying up all of its costs and comparing them to the costs of doing nothing—or, alternatively, to the costs of directly regulating the products and processes of a myriad of individual firms operating in a broad variety of different industries.