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FEDERAL CORPORATE CHARTERING FOR BIG BUSINESS:
AN IDEA WHOSE TIME HAS COME?*

JOEL F. HENNING**

AMERICA WAS born in resistance to the unbridled power of *government*. Thus the Constitution principally addressed itself to limiting, checking and balancing government power. In 1789 there was no big business. Corporations, when chartered at all, were chartered individually by state legislative act, usually to accomplish specific public purposes, such as building bridges or highways.¹

The Industrial Revolution created a demand for corporate structures to facilitate the accumulation and utilization of capital, but the process of securing a charter by special legislation was cumbersome, expensive and occasionally corrupt.² The states responded by passing general incorporation laws providing virtually automatic corporate chartering.³ From that point, nature took its course until America's super-corporations now rival, if not exceed, any government in the world in power and influence. For example, the two hundred biggest companies control about two-thirds of U.S. manufacturing assets. One hundred seventy corporate giants reported sales of one billion dollars or more in 1970. Eighteen had sales of more than four billion dollars. Four corporations earned more than one billion dollars in profit.⁴

* *The editors of this journal asked me to elaborate on a short article of mine published in the Washington Post proposing a dual system of corporate chartering. The subject is one that will, I hope, increasingly attract the attention of legal scholars as well as policy makers.*

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1. A. BERLE JR., and G. MEANS, *THE MODERN CORPORATION AND PRIVATE PROPERTY*, 218-30 (1932).

2. J. HURST, *THE LEGITIMACY OF THE BUSINESS CORPORATION IN THE LAW OF THE UNITED STATES 1780-1970*, 133-39 (1970).

3. A. BERLE and G. MEANS, *supra* note 1, at 135-37.

4. Figures quoted from FORBES, *Annual Directory Issue*, May 15, 1971.

I. MISDIRECTED EFFORTS TO CONTROL CORPORATE POWER

The manner in which these super-corporations are established, the relative rights and duties of those participating in them (directors, officers, stockholders, creditors, employees, customers, etc.) and the delimitation of their powers *vis-à-vis* the external world are obviously matters of public importance. However, the dispersal among fifty states of responsibility to make the rules has discouraged initiative for reform. On the contrary, a disagreeable change in one state's laws still will cause corporate managers to re-incorporate in a more accommodating state. Currently, Delaware is the most alluring jurisdiction.

The sovereign state of Delaware is in the business of selling its corporation law. This is profitable business, for corporation law is a good commodity to sell. . . . The consumers of this commodity are corporations, and . . . Delaware, like any other good businessman, tries to give the consumer what he wants. In fact, those who will buy the product are not only consulted about their preferences, but are also allowed to design the product and run the factory.⁵

State incorporation law has clearly failed to control corporate power. Because of the venal scramble for corporate business at the state level, this failure can only be corrected at the federal level. But the federal record on economic regulation is hardly better than that of the states. Critics will legitimately ask if any real benefit can be achieved by adding even more tentacles to the federal octopus. There are already an ever-expanding number of federal laws affecting corporations. Some attempt to preserve or restore free market conditions, others attempt to impose public policy through direct regulation of enterprises. Neither category has been an unqualified success.

In the anti-trust field, eighty years of enforcement under the Sherman Act, the Clayton Act and their progeny has proceeded simultaneously with startling increases in industrial concentration.⁶ While the anti-trust laws have worked reasonably well in the areas of price-fixing, bid-rigging and market allocation,⁷ they have failed

5. Note, *Law for Sale: A Study of the Delaware Corporation Law of 1967*, 117 U. PA. L. REV. 861 (1969).

6. R. BARBER, *THE AMERICAN CORPORATION*, 173-74 (1970). M. GREEN *et al*, *THE CLOSED ENTERPRISE SYSTEM, A NADER TASK FORCE REPORT ON ANTI-TRUST ENFORCEMENT* (1971); *cf.* Posner, *Nader on Anti-Trust*, *NEW REPUBLIC*, June 26, 1971.

7. R. BARBER, *THE AMERICAN CORPORATION*, at 172-73 (1970).

to significantly deter the extraordinary concentration of American industry. As Professor Barber has written:

Under the very nose of anti-trust, U. S. industry has been thoroughly oligopolized and the share of productive wealth held by a relatively very few corporations . . . has continued to increase.⁸

In the area of conglomerate mergers, the record of anti-trust enforcement is even more dismal. Recent revelations concerning the cases involving ITT suggest that rigorous conglomerate anti-trust enforcement is subject at best to strong political influence, at worst to outright bribery.⁹

The regulatory agencies have been at least as disappointing in performance as federal anti-trust policy.¹⁰ In many cases they have been set adrift with fuzzy delegations of authority to regulate complex industries "in the public interest."¹¹ They are subject to pressures from the White House, from Congress and from the industries they are supposed to regulate. They have not, as yet, found an effective means of systematically channelling the voice of the public into their decision-making processes. In addition, the various agencies are often in conflict with one another. Our federal highway subsidy program, for example, was a principal cause of the decline in railroad service.¹²

Why has government regulation of corporations largely failed? The final answer to this question must await the judgment of economic and political historians in generations to come. Those interested in public policy, however, must attempt to at least find some tentative answers to this question. Perhaps the basic problem is that we have misconceived the nature of the large corporation. This problem was clear to Professors Berle and Means forty years ago when they published their seminal work, *The Modern Corporation and Private Property*.¹³ The corporation, they pointed out:

8. *Id.* at 175.

9. *See, e.g., ITT's Battle to Keep Hartford*, BUSINESS WEEK, March 11, 1972, at 32-33.

10. *See, e.g., L. KOHLMEIER, JR., THE REGULATORS* (1969).

11. T. LOWI, *THE END OF LIBERALISM* 128-56 (1969).

12. J. DAUGHEN and P. BINZEN, *THE WRECK OF THE PENN CENTRAL*, 209 (1971).

13. A. BERLE and G. MEANS, *supra* note 1.

[c]alls for analysis, not in terms of business enterprise but in terms of social organization. On the one hand, it involves a concentration of power in the economic field comparable to the concentration of religious power in the medieval church or of political power in the national state. On the other hand, it involves the interrelation of a wide diversity of economic interests—those of the 'owners' who supply capital, those of the workers who 'create,' those of the consumers who give value to the products of enterprise, and above all those of the control who wield power.¹⁴

Berle and Means saw the inherent conflict that surrounds such enterprises. Those who wield the power desire to preserve and enlarge it. At the same time, however, those who are affected by these powerful institutions increasingly demand that corporate power be used for the benefit of all concerned. This phenomenon applies equally to religious, political and economic institutions. In the last few decades the growth of the modern corporation has reached the point where Professor Berle was prompted to state that, "some of these corporations are units which can be thought of only in somewhat the way we have heretofore thought of nations."¹⁵

However, we have not attempted to control the super-corporations in the same way that we have controlled the power of government. Through anti-trust policy and the regulatory agencies federal regulation of corporations has proceeded by a series of attempts to prohibit specific acts. A very different approach to the control of governmental power was taken by the founding fathers in drafting the U.S. Constitution. They chose to reorganize, regularize and disburse government power rather than to prohibit specific acts.¹⁶

II. THE ALTERNATIVE: A NEW LAW OF CORPORATIONS

It would therefore seem sensible to attempt the creation of a new "law of corporations." Such a law, as Professors Berle and Means suggested, "might well be considered as a potential constitutional law for the new economic state. . . ."¹⁷ A federal business corporation act might be the appropriate vehicle for this new institutional approach to the problem of corporate power. It would be a means of controlling the power of big business by establishing

14. A. BERLE and G. MEANS, *supra* note 1, at 352-53.

15. A. BERLE, JR., *ECONOMIC POWER AND THE FREE SOCIETY*, 15 (1957).

16. This analysis was developed in an interesting and important essay by Chayes, *The Modern Corporation and the Rule of Law*, in *THE CORPORATION IN MODERN SOCIETY*, p. 25-45 (E.S. Mason ed. 1959).

17. A. BERLE and G. MEANS, *supra* note 1, at 357.

and enforcing a reasonable set of corporate institutional arrangements. Without minimizing the enormous conceptual challenge that such a project suggests, the remainder of this essay is an attempt to touch on some of the basic issues that might be involved.

The notion of federal chartering is not new. At the Constitutional Convention James Madison proposed unsuccessfully that Congress be empowered to charter corporations. Presidents Roosevelt, Taft, and Wilson all advocated federal chartering or licensing. President Taft wrote:

No other method can be suggested which offers federal protection on the one hand, and close federal supervision on the other, of these great organizations that are in fact federal because they are as wide as the country and are entirely unlimited in their business by State lines.¹⁸

The Depression brought renewed interest in the concept from Senators Borah and O'Mahoney, but after extensive hearings their proposals were defeated.¹⁹

Senator O'Mahoney remained convinced that such legislation was needed. In his final statement on the matter he said:

It is idle to think that huge collective institutions which carry on our modern business can continue to operate without more definite responsibility toward all the people of the Nation than they now have. To do this it will be necessary in my judgment, to have a national chartering system for all national corporations²⁰

The drafting of a federal business corporation act will profoundly challenge the skill of lawyers and legislators. Complex issues must be resolved such as the relative fiduciary obligations of inside and outside directors, shareholder rights, employee rights, accounting standards, and a host of others. This is not the place to delve into substantive details of the proposed legislation. But a few possible features of the legislation are worth brief discussion: (A) a new approach to anti-trust policy, (B) a comprehensive system of disclosures and (C) a limited federal interest, pursuant to which only the biggest corporations would require federal charters.

18. Reuschlein, *Federalization—Design for Corporate Reform in a National Economy*, 91 U. PA. L. REV. 91, 106, n.74 (1942). See pages 106-7 for brief review of history of attempts to implement federal incorporation schemes.

19. *Id.* at 107.

20. Quoted by Ralph Nader, *The Case for Federal Incorporation*. Statement presented at Conference on Corporate Accountability, Washington, D.C., October 30-31, 1971, at 9.

A. INDUSTRIAL DE-CONCENTRATION

Industrial de-concentration can be approached in ways other than after-the-fact litigation based on the existing anti-trust laws. If a workable formula can be developed, the federal business corporation act could include anti-trust standards that must be met prior to the issuance or renewal of a federal charter. The act may, for example, require that no corporation be chartered to serve more than twelve percent of any relevant market, as recommended by the Neal Task Force Study commissioned by President Johnson.²¹ The act might also prohibit stock or asset acquisitions, except under appropriate circumstances. It should certainly restrict anti-competitive corporate interlocks.

B. DISCLOSURE

In order to make rational policy in domestic and international affairs we support several intelligence agencies, at least one of which, the CIA, is reputed to have a budget larger than that of the State Department. But we have compelled our economic regulators to grope blindly with little systematic access to relevant data. If a free market economy is to work, information must be freely available. Businessmen tend to turn this axiom on its head, defending corporate secrecy as the fundamental requisite of free enterprise. However, when a company expands into divisions, subdivisions, and especially when it conglomerates, its public reporting becomes less and less useful to investors, suppliers, customers and potential competitors. It goes without saying that consumers, the media, scholars and the government itself are equally at a loss to know what corporations are doing and planning.

In short, we do not know much about corporations. Therefore, the act should require substantially more financial disclosure, product information and social data from corporations. The earnings of separate products and subsidiaries, now largely hidden, the results of product safety and durability tests, the ingredients of food and beverages, the racial composition of work forces, the costs of pollution, job dislocations, research and development, etc., all can be disclosed without critically impairing the honest competitive ad-

21. N.Y. Times, May 22, 1969, at 1, col. 7.

vantages of one business over another. The SEC appears to be moving in the same direction within its limited jurisdiction.²²

A comprehensive set of disclosure requirements, reaching into all aspects of corporate operations will make it possible for the government and the public to make rational decisions in all aspects of corporate enterprise.²³ In the course of time, policymakers will know considerably more about corporations and will thus be in a substantially improved position to determine what areas of enterprise should be left free of any political interference, what areas now constrained by regulation should be freed, and vice-versa.

C. LIMITED FEDERAL INVOLVEMENT

The political problems of achieving a federal business corporation act, as well as some of the practical problems, can perhaps be minimized by attempting to "federalize" only the very biggest corporations. This approach seems better suited to our federal system of government, more appealing to those who believe activities with local impact should be subject to local control, and more politically manageable in the short run. It is modeled in part on our dual banking system, under which banks can operate under state or federal charter. Obviously, the dual banking system is far from perfect and has from time to time been subject to intense criticism. It has not prevented panics, depressions, recessions and inflations. It developed through a series of historical accidents,²⁴ but it nevertheless provides an interesting model.

The smallest of our corporations may have a relatively confined impact on their local communities. The biggest, however, are truly national and international institutions. Such a system would mean that those wishing to start a new and modest venture would not have to travel to the formidable bureaucracy of Washington. However, enterprises with profound national and international impact would be required to conform to structural and institutional stand-

22. *Its Getting Tougher to Lie*, N.Y. Times, March 26, 1972, (Financial Section) at 1.

23. See, e.g., Mueller, *Corporate Disclosure and Federal Incorporation*. Statement presented at Conference on Corporate Accountability, Washington, D.C., October 30-31, 1971.

24. T. THOMPSON, *CHECKS AND BALANCES, A STUDY OF THE DUAL BANKING SYSTEM IN AMERICA* (1962); W. BROWN, *THE DUAL BANKING SYSTEM IN THE U.S.* (1968).

ards developed to meet the special problems that their size and power generate.

A dual system would reflect continued faith in federalism and in the power and ability of local communities to control activities of local impact. It would prevent the creation of another gargantuan federal bureaucracy that would have little chance of effective operation because of its sheer size. It would seem as absurd for the federal government to attempt control of a corporation with assets of one million dollars or less as for the federal government not to control a corporation with assets of one billion dollars or more. Federal anti-trust, securities, trade, consumer and environmental protection laws would continue to apply to all corporations regardless of their incorporation under state or federal jurisdiction. Conversely, state and local laws and taxes would still be imposed upon the local operations of national corporations.

Perhaps, therefore, national franchises in general need be required only of the two hundred largest industrial corporations, which alone control sixty percent of our manufacturing assets.²⁵ In addition, however, a national franchise should be required of a smaller corporation if it wishes to do a significant amount of business with the federal government, to operate subsidiaries or factories in foreign countries, or to engage in certain industries where there is an overriding federal interest, such as energy and interstate transportation.

The dual system of corporate chartering would be necessarily different from banking in at least two respects. First, regardless of size, banks may elect to operate under state charter. At least for the five hundred largest industrial corporations, national charters must be required if the dual system is to work in the corporate context. The second difference has to do with tenure of national charters. National banking charters are perpetual. National corporate charters should extend for a limited number of years and should be renewable upon a showing of fiscal and social responsibility. One would suppose that a company which lost its right to federal incorporation could apply for a state charter. Of course, a large industrial corporation would have to split into many small

25. R. BARBER, *supra* note 7, at 21.

units to avoid the requirement of a national charter for corporations of substantial size.

The principle of rigorous external examination and supervision, now firmly embedded in the banking community, ought to be transferable to the corporate community. Frequent external examination of national corporations by the federal government might even influence the states, and similar examinations would be instituted in the state segment of the dual system. This appears to have occurred in the banking community, where state banks caused their home states to institute supervisory systems comparable to that for federal banks. The public may feel insecure in dealing with corporations chartered by the states if they were not as carefully examined and audited as national corporations. There is no reason why such audit must be confined to the historical indices of success and failure. It could involve examination of a corporation's responsibilities to hire and promote members of minority communities, to refrain from polluting the environment and to manufacture socially useful products.

Obviously, action to neutralize corporate political power must precede fundamental reforms in corporate law and regulation, such as the one under discussion. It would be naive to minimize the difficulty of rescuing politics from the dominance of business.²⁶ The process may have modestly begun, however, with the first tentative steps now being taken toward election reform.²⁷ If virtually all campaign costs were limited and subsidized by the federal government, the influence of wealth on politics would not be eliminated, but it might sufficiently be reduced to permit growing public interest in consumer and environmental issues to compete with the interests of business for the attention of our politicians.

III. PRAGMATIC ALTERNATIVES TO THE FUNDAMENTAL APPROACH

Political feasibility notwithstanding, there are those who reject a fundamental, structural approach to corporate reform, on the ground

26. M. MINTZ & J. COHEN, *AMERICA, INC.* (1971).

27. *The Wall Street Journal*, January 20, 1972, at 2, col. 1. The bill imposes limits on television, radio and newspaper advertising by candidates for federal offices. It also requires disclosure of contributors' names when contributions exceed one hundred dollars.

that better alternatives exist. Some men who have held high office in business and government believe the better alternative is to surrender society to the corporation. George Ball has written:

While the structure of the multinational corporation is a modern concept, designed to meet the requirements of a modern age, the nation state is a very old-fashioned idea and badly adapted to serve the needs of our present complex world.²⁸

Others are equally prepared to surrender to the managers of the conquering corporations but prudently throw themselves upon their mercy, pleading for "corporate social responsibility." In the absence of effective political statesmanship, they urge business managers to assume economic statesmanship, to balance the interests of all corporate constituencies and the general public, and to operate their enterprises with the public interest in mind. These suppliants ignore Lord Acton's rule concerning power in the hands of unaccountable, self-perpetuating rulers. They also conveniently overlook the palpable evidence of corporate irresponsibility in our air, water, and food, on our highways, railroads and television sets, and in our sacked and gradually abandoned cities.²⁹

Still other spokesmen acknowledge the ascendancy of the corporation over the state, but would transform the corporate autocracies and oligopolies into democratic political institutions. To these idealists still cherishing their high school civics, the problem is simple: If the old social contract with government has not been fulfilled, enter into a new one with the super-corporations. What could be more American? It's as simple as signing a new football coach. How ironic that those who caution against simple-minded attempts to impose our very particular democratic framework on other nation states, as in Vietnam, see no problem in imposing it on economic enterprises with values and goals at least as remote. Well-intentioned, (as always) these missionaries refuse to believe that the genius of American political democracy is not, like a McDonald's hamburger franchise, capable of flourishing anywhere.³⁰

28. Ball, *The Promise of the Multinational Corporation*, FORTUNE, June, 1967, at 80.

29. Henning, *Corporate Social Responsibility: A Shell Game for the '70's?* in CORPORATE POWER IN AMERICA, (M. Green ed. scheduled for publication in fall, 1972).

30. Henning, *Reforming the Corporations Is Not Enough*, Washington Post, August 29, 1971, at 85.

There is another group that sees the problem merely as one of transferring ownership to the public sector. Ownership, alas, is not the fundamental problem. Public ownership can result in a range of systems from state capitalism to decentralized socialism. Obviously, America's current level of economic concentration suggests that the former is more likely to result from total state control. Merely changing ownership will not result in an equitable and socially salubrious distribution of corporate resources. The problem is not ownership but accountability. Soviet lakes are polluted, too. Eliminating what remains of our market economy would require the substitution of planning, which has not been enormously successful anywhere and has in some instances been a fiasco. Goals seem to be reached most often in planned economies when they have been set by industrial managers, based on the narrow interests of their enterprises, a system only slightly different from our present one.³¹

Others concede the dangers of statism and therefore propose dismembering, smashing, atomizing the economy—doing for ourselves what Morgenthau proposed we do for Germany after World War II. This is a hopeless vision. It would not conceivably work unless the entire world agreed to return to a state of pre-industrial nature. No doubt, then, the whole thing would begin all over again.

IV. CONCLUSION

Finally, many reject a fundamental approach to corporate reform, alleging that such reforms are anti-capitalist, anti-profit, anti-American. There is no way to avoid such criticism, but it may, nevertheless, be useful to remind these critics that Germany has experienced the most dramatic economic development, largely within its private sector, while deliberately and thoroughly reforming its corporate law. Violent political developments have provided German reformers the opportunity to propose substantial changes, many of which have been enacted into law.³² Perhaps we can accomplish as much here in a more peaceful and humane context.

31. S. COHEN, *MODERN CAPITALIST PLANNING: THE FRENCH MODEL* (1969).

32. Vagts, *Reforming the 'Modern' Corporation: Perspectives from the German*, 80 HARV. L. REV. 23, 25 (1966).