

**Finance, Property and the Corporate Form:  
Making Sense of Our Entwined Mess  
LECO 3006  
Fall 2014**

Schedule: Monday & Wednesday – 1:50 to 3:30 pm  
25 August 2014 – 10 December 2014  
Room 102  
65 west 11<sup>th</sup> Street (Eugene Lang Building)

Instructor: Anthony Bonen ([bonea539@newschool.edu](mailto:bonea539@newschool.edu))  
Office Hours: Monday & Wednesday – 3:30 to 4:30 pm  
Room D-1119  
6 east 16<sup>th</sup> Street

Holidays (no class):  
9/1 – Labor Day (Monday)  
11/26 – Thanksgiving (Wednesday)

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Required Text:

Hirschman, Albert O. (1970). *Exit, Voice and Loyalty: Responses to Declines in Firms, Organizations and States*. Harvard University Press, Cambridge MA.  
(ISBN: 9780674276604)

Course Description:

The single most ubiquitous political-economic entity is a legal construct: the corporation. This course will explore the societal role of the corporation by critically analyzing the interrelation of the legal and economic theories that justify the corporation's particular manifestation in modern America. We will focus on three areas: (i) the historical development of the corporate form; (ii) the corporation's foundation in the theory of liberal property rights and contract theory, and; (iii) the treatment of corporate ownership in modern economic theory. Ultimately, our goal is to relate these areas to the behaviour of financial markets and theories of market (in)efficiency. The content overlaps with the literature in corporate governance, critical legal studies and the economic theory of the firm, but the broader framework will be the socio-economic approach of Albert O. Hirschman's *Exit, Voice and Loyalty* (1970).

Learning Outcomes:

Successful completion of this course will yield:

1. Broad knowledge of the legal and sociological issues surrounding corporate governance and its relation to economic theory;
2. In-depth understanding of a particular topic developed primarily through the research paper;
3. An ability to critically analyze and assess complex legal and economic arguments, and;
4. Enhanced presentation and discussion skills.

Evaluation Structure:

**40% - Participation and Discussion**

Students will be evaluated on the *quality* of their contributions to the weekly discussions. In addition, students will be assigned two presentations during the semester. The first is a short (5-15 minutes) summary of the week's readings. The second will be a student-led seminar on the topic and reading of her or his choosing, however suggested topics are available in the outline below. Presentations will begin in class on 10 November; students are strongly encouraged to choose a topic/reading relevant to the research paper.

**20% - Proposal for Paper (due 22 October 2014 at 1:50 pm)**

A 500-word summary of the planned research paper. Students should – but are not required – to discuss their topic ahead of time with the instructor. The proposal must include: (i) the research question to be explored; (ii) a tentative thesis statement, and; (iii) an indication of foundational sources.

**40% - Research Paper (due 12 December 2014 at 1:50 pm)**

A 4000- to 5000-word essay covering a topic relevant to the course.

Course Outline and Reading List:

**Week 1 (August 25 & 27) – Constituents of the Corporation**

*Readings:*

- Berle, Adolph A. (1931). "Corporate Powers as Powers in Trust", (1931) 44 *Harvard Law Review* 1049-1074.
- Dodd, E. Merrick (1932). "For Whom Are Corporate Managers Trustees?". 45 *Harvard Law Review* 1145-1163.

Questions: What is/was the legal relationship between corporate managers and shareholders? What underpins the argument for a fiduciary obligation of managers? Does it make sense to think of the corporation as a public entity or a private one? Why? How does this relate to ownership and contracting rights of corporate members?

## **Week 2 (September 3) – Modern Corporate Theory**

### *Readings:*

- Hansmann, Henry and Reinier Kraakman (2001). “The End of History for Corporate Law”. *Georgetown Law Journal*. January, 89: 439 – 468.

Questions: What is driving convergence across jurisdictions? What does the ‘end of history’ mean in terms of the debate between Berle & Dodd? What are the *forces of logic* for convergence identified by the authors? How does the social argument rely (implicitly or explicitly) on economic theory?

## **Week 3 (September 8 & 10) – Nexus v Property**

### *Readings:*

- Frank H. Easterbrook and Daniel R. Fischel. (1989). “The Corporate Contract” 89 *Columbia Law Review* 1416-1448.
- Armour, John and Michael J. Whincop. (2007). “The Proprietary Foundations of Corporate Law”. *Oxford Journal of Legal Studies*, 27(3): 429-465.

Questions: In these two approaches, what are the defining aspects of the corporations? How do they overlap and differ from one another? What is legal-economic position of shareholders in the two approaches, and how does this relate to the position of corporate creditors? Does personhood matter, why or why not? How do these corporate governance theories relate to financial market behaviour? What is the distinction between contracts “about property” versus contracts for “shared property”? Insofar as the *proprietary foundations* argument holds, which of Honoré’s incidents of ownership do shareholders embody?

## **Week 4 (September 15 & 17) – The Firm: Views from Economics**

### *Readings:*

- Coase, Ronald H. (1937). “The Nature of the Firm”. *Economica*. 4(16): 286-405.
- Alchian, Armen A. and Harold Demsetz. (1972). “Production, Information Costs, and Economic Organization”. *American Economic Review*. 62: 777-795.

Questions: According to the two theories, what problem(s) does the firm solve? What does Coase imply about the contractual and proprietary nature of the firm? What distinguishes economic activities internal to the corporation from those external to it? How does technology fit into either theory? What is role and importance of *uncertainty* in these two theories of the firm? What image of the *corporate form* emerges from these theories?

### **Week 5 (September 22 & 24) – Historical Developments and Misunderstandings**

*Readings:*

- O'Mellin, Liam Séamus (2006). "Neither Contract Nor Concession: The Public Personality of the Corporation". *George Washington Law Review*. 74: 201-259.
- Ireland, Paddy (1996). "Capitalism without the Capitalist: The Joint Stock Company Share and the Emergence of the Modern Doctrine of Separate Corporate Personality". *Legal History*. 17: 40-72.

Questions: Why did the 'concession' view die, and why did the 'contract' view persist? What distinguishes a private contract and "the" social contract; how does this relate to corporate personality? The focus on NPOs is important in general, but does this history matter to theories of for-profit corporations? According to Ireland, what effectuated the separation of the corporation from its shareholders? What is the legal distinction between partnerships and joint stock companies? Why did the emergence of the modern (London) Stock Exchange matter for corporate law theory and economic practice? Who owns the corporation?

### **Week 6 (September 29 & October 1) – MOVIE! *The Corporation* (2003)**

*No Readings*

Questions: What clear distinction (on legal, economic or social grounds), if any, can be made between the corporation as a profit-seeking entity versus an "externalizing machine"? How is the increasing privatization (i.e., the "enclosure movement") related to the concurrent wealth generation? Has the expansion of the corporate form altered social, inter-personal behaviour? How could this discussion be updated in light of social media's ubiquity? Are the problems raised in the film the result of the corporate form *per se* or how people within it have acted?

### **Week 7 (October 6 & 10) – Voice and Exit**

*Readings:*

- Hirschman. (1970). Chapters 1, 2 & 3 and Appendices A & B ("Introduction & Doctrinal Background", "Exit", "Voice")

Questions: What is the relevance of surplus and slack in how economists think about modern society? Why is the firm seemingly more stable in perfect competition than under imperfect conditions? Can quality-elasticity of demand be quantified? How do voice and exit signal and effect management? Why and at what point do the levels/volumes of exit and voice become hindrances to the organization? To society? Is there atrophy in the development of the art of voice?

### **Week 8 (October 13 & 15) – Loyalty**

#### *Readings:*

- Hirschman. Chapters 4, 7 & 9 and Appendices C & D. (“A Special Difficulty in Combining Voice and Exit”, “A Theory of Loyalty”, “The Elusive Optimal Mix of Exit and Voice”)

Questions: What is the special difficulty referred to in chapter 4? Are there examples of reversed positions of voice and exit in the special difficulty? When would a quality deterioration raise the surplus of a quality-conscious consumer? Why is there no “reversal” of exiting with only two goods or with a continuum of price-quality goods? In what ways does the degree of loyalty modulate the relative usefulness of exit and voice in organizations? How do organizations reinforce loyalty, and what are the possible effects? What, if any, relevance does the discussion of quality-reducing exit and public goods have to corporate governance and shareholder behaviour?

### **Week 9 (October 20 & 22) – Property Rights and Externalities**

#### **\*\*\* Paper Proposals Due on Wednesday at the beginning of class \*\*\***

#### *Reading:*

- Coase, Ronald H. (1960). “The Problem of Social Cost”. *Journal of Law and Economics*. 3: 1-44.
- Demsetz, Harold (1967). “Toward a Theory of Property Rights”. *American Economic Review*. 57(2): 347-359.

Questions: What defines an externality? What arguments does Coase provide to reject Pigou’s view of externalities and what does it assume about the generator of the externality? How does Coase’s Theorem relate to his (Coase, 1937) theory of the firm, and what externalities are possible within the firm? By what social processes do property rights emerge according to Demsetz? Is the process in accord with Coase? What is argument for social benefit (optimality?) of private ownership versus other arrangements? What “externality” does the corporate form solve? Where does Demsetz leave the proprietary foundations of the corporation and its assets?

### **Week 10 (October 27 & 29) – The Firm as Contract and as Property**

#### *Readings:*

- Jensen, Michael C. and William H. Meckling (1976). “Theory of the Firm: Managerial Behavior, Agency Costs and Ownership Structure”. *Journal of Financial Economics*. 3: 305-360.
- Grossman, Sanford J. and Oliver D. Hart (1986). “The Costs and Benefits of Ownership: A Theory of Vertical and Lateral Integration”. *The Journal of Political Economy*. 94(4): 691-719.

Questions: How does the contract theory of the firm specify the limit of the firm? What distinguishes it from external contracts? In Jensen/Meckling's theory, how do stock markets price affect or react to the firm's corporate structure? Is the efficient market hypothesis necessary, why or why not? What delineates internal and external firm relations in the property-based theory? Is there a role for the principal-agent dilemma in the Grossman/Hart view? How do the models treat the firm's investment and growth behaviour?

### **Week 11 (November 3 & 5) – Financial Markets, Deregulation and Expropriation**

Readings:

- Lazonick, William. (2007). "The US stock market and the governance of innovative enterprise". *Industrial and Corporate Change*. 16(6): 983-1035.
- Strine, Leo E. (2012). "Our Continuing Struggles with the Idea that For-Profit Corporations Seek Profits". *Wake Forest Law Review*. 47: 135–172.

Questions: Is Strine's conclusion that regulation – and not corporate law – should be used to reign in the excesses of corporate and investor actions? To what extent does shareholder value maximization as an ideology, as opposed to legal formalism, drive myopic or speculative behaviour? What, if any, barriers can or should a country impose barriers to hostile takeovers or M&A, in general? According to Lazonick why is a theory of innovative firm investment necessary for corporate governance? What other parties may have claims as 'residual claimants' and why does that matter? Which aspects of Lazonick's could be made to fit with 'nexus of contract' and/or shareholder value primacy arguments?

### **\*\*\* Student Presentations \*\*\***

### **Week 12 (November 10 & 12)**

Suggestions: The Contrarians

- Ireland, Paddy. (1999). "Company Law and the Myth of Shareholder Ownership", *Modern Law Review*. 62: 32-57.
- Lazonick, William. (2013). "The Financialization of the US Corporation: What Has Been Lost, and How Can It Be Regained?". *Seattle University Law Review*. 36: 857-909.
- Halpin, Andrew. (2007). "Disproving Coase's Theorem?". *Economics and Philosophy*. 23. pp. 321-341.

Student 1 & 2 (Monday):

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Student 1 & 2 (Wednesday):

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**Week 13 (November 17 & 19)**

*Suggestions:* More on Shareholders

- Margaret Blair. (2003). "Locking in Capital: What Corporate Law Achieved for Business Organization in the Nineteenth Century" 51 *UCLA Law Review* 387-455.
- Worthington, Sarah (2001). "Shares and shareholders: property, power and entitlement: Part 1 & 2". *Company Lawyer*. 22(9): 258-266.

Student 1 & 2 (Monday):

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- \_\_\_\_\_

Student 1 & 2 (Wednesday):

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- \_\_\_\_\_

**Week 14 (November 24)**

*Suggestions:* Production and Ownership Forms

- Shapley, S. and Martin Shubik (1967). "Ownership and the Production Function". *Quarterly Journal of Economics*. 81: 88-111.

Student 1 & 2 (Monday):

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- \_\_\_\_\_

**Week 15 (December 1 & 3)**

*Suggestions:* Mainstream Finance Theory

- Arrow, Kenneth (1964). "The Role of Securities in the Optimal Allocation of Risk-bearing". *Review of Economic Studies*. 31(2): 91-96.
- Sharpe, William F., 1964. Capital asset prices: a theory of market equilibrium under conditions of risk. *Journal of Finance* 19, 425.

Student 1 & 2 (Monday):

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Student 1 & 2 (Wednesday):

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- \_\_\_\_\_

**Week 16 (December 8 & 10)**

**\*\*\* FINAL RESEARCH PAPERS Due on Wednesday at the beginning of class \*\*\***

*Suggestions:* Liberal Property Rights Theory

- Schneiderman, David. (2006). "Property Rights and Regulatory Innovation: comparing constitutional cultures." *International Journal of Constitutional Law* . 4(2). pp. 380-381.
- Heller, Michael A. (1998-99). "The Boundaries of Property Rights." *Yale Law Journal*. (108). pp. 1163-1223.

Student 1 & 2 (Monday):

- \_\_\_\_\_
- \_\_\_\_\_

Student 1 & 2 (Wednesday):

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Class Policies:

**Absences:**

Attendance and participation are essential for this course. Therefore unexplained or unjustified absences will result in a lower overall grade. If a student's absence becomes a perpetual problem the instructor reserves the right to fail the student in spite of written performance.

**Lateness:**

Students should be on time for every class – which starts at 1:50pm sharp. Students arriving 10 minutes late (or more) will not be welcome in the class, and will be considered as absent.

**Late Submissions:**

No late research papers will be accepted without valid and proven exceptional reason. Late or un-submitted papers will receive a zero grade.

Resources:

The university provides many resources to help students achieve academic and artistic excellence. These resources include:

- ❖ The University (and associated) Libraries: <http://library.newschool.edu>
- ❖ The University Learning Center: <http://www.newschool.edu/learning-center>
- ❖ University Disabilities Service: [www.newschool.edu/student-disability-services/](http://www.newschool.edu/student-disability-services/)



In keeping with the university's policy of providing equal access for students with disabilities, any student with a disability who needs academic accommodations is welcome to meet with me privately. All conversations will be kept confidential. Students requesting any accommodations will also need to contact Student Disability Service (SDS). SDS will conduct an intake and, if appropriate, the Director will provide an academic accommodation notification letter for you to bring to me. At that point, I will review the letter with you and discuss these accommodations in relation to this course.

#### Academic Honesty and Integrity:

Compromising your academic integrity may lead to serious consequences, including (but not limited to) one or more of the following: failure of the assignment, failure of the course, academic warning, disciplinary probation, suspension from the university, or dismissal from the university.

Students are responsible for understanding the University's policy on academic honesty and integrity and must make use of proper citations of sources for writing papers, creating, presenting, and performing their work, taking examinations, and doing research. It is the responsibility of students to learn the procedures specific to their discipline for correctly and appropriately differentiating their own work from that of others. The full text of the policy, including adjudication procedures, is found at <http://www.newschool.edu/leadership/provost/policies/>

**Resources regarding what plagiarism is and how to avoid it can be found on the Learning Center's website:** <http://www.newschool.edu/learning-center/virtual-handout-drawer/>

At a minimum, please provide links to the Academic Honesty and Integrity Policy and the Intellectual Property Rights Policy, found at <http://www.newschool.edu/leadership/provost/policies/>

#### Other Useful Readings:

##### **Historical Development**

- Mitchell, Lawrence E. (2008). "Transcendental Value", Ch. 3 in *The Speculation Economy: How Finance Triumphed Over Industry*. Berrett-Koehler Publishers.
- Mitchell, Lawrence E. (2008). "The New Property", Ch. 4 in *The Speculation Economy: How Finance Triumphed Over Industry*. Berrett-Koehler Publishers

##### **Property Rights**

- Getzler, Joshua (1996). "Theories of Property and Economic Development." Author(s): Joshua Getzler Source: *Journal of Interdisciplinary History*. (26) 4. Spring. pp. 639-669.

- Heller, Michael A. (1998-99). "The Boundaries of Property Rights." *Yale Law Journal*. (108). pp. 1163-1223.
- Hart, Oliver and John Moore (1990). "Property Rights and the Nature of the Firm", *Journal of Political Economy*. 98(6): 1119-1158.
- Bonen, Anthony. (2009). "Of Volatility and Optimality in the Stock Market, or the bifurcated share under rational incentives". Unpublished MA Dissertation. *University of Kent at Brussels*.
- Dragun, Andrew and Martin O'Connor (1993). "Property Rights, Public Choice, and Pigovianism". *Journal of Post Keynesian Economics*. 16(1).

### **Corporate Control and the Efficient Market Hypothesis**

- Fama, Eugene. "The Behavior of Stock Market Prices". *Journal of Business*. vol. 38, 1965, pp. 34–105.
- Fama, Eugene F. (1998). "Market Efficiency, Long-Term Returns and Behavioral Finance". *Journal of Financial Economics*. vol. 49, no. 3, 1998. Pp. 283-306.
- Ruback, Richard S. Michael C. Jensen. (1983). "The Market for Corporate Control: The Scientific Evidence", *Journal of Financial Economics*. vol. 11, pp. 5-50.
- Fama, Eugene (1980). Agency Problems and the Theory of the Firm. *The Journal of Political Economy*. 88(2). April. pp. 288-307.
- Bhagwati, Jagdish. "The Capital Myth: The difference between trade in widgets and dollars". *Foreign Affairs*. vol. 77, no. 3, 1998, pp. 7-12.

### **Shareholder Primacy**

- Stout, Lynn (2012). *The Shareholder Value Myth: How Putting Shareholders First Harms Investors, Corporates, and the Public*. Berrett-Koehler Publishers, inc. San Francisco.
- Stout, Lynn A. (2002). "Bad and Not-So-Bad Arguments for Shareholder Primacy". 75 *Southern California Law Review* 1189-1209.
- Tusk, Dalia (2006). "Shareholders as Proxies: The Contours of Shareholder Democracy". 63 *Washington and Lee Law Review* 1503-1578.
- Letza, Steve *et al.*, (2004). "Shareholding versus Stakeholding: a critical review of corporate governance". 12 *Corporate Governance* 242-262.
- Ireland, Paddy (2005) "Shareholder Primacy and the Distribution of Wealth". 68 *Modern Law Review* 49-81.
- Preda, Alex. "The Sociological Approach to Financial Markets". *Journal of Economic Surveys*, vol. 21, no. 3 2007, pp 506-533.
- La Porta, Rafael Florencio Lopez-de-Silanes, Andrei Shleifer, Robert Vishny. (2000). "Investor protection and corporate governance." *Journal of Financial Economics*. 58. pp. 3-27.
- Bonen, Anthony (2008). "Outside-Inside: the Relationship between Financial Deregulation and Shareholder Primacy", *BSIS Journal of International Studies*.

### **International Perspectives and Approaches**

- Culpepper, Pepper D. (2005). "Institutional Change in Contemporary Capitalism: Coordinated Financial Systems since 1990". *World Politics*. vol. 57, January, pp. 173-199.
- Coffee, John C. (2011). "The Rise of Dispersed Ownership: The Roles of Law and the State in the Separation of Ownership and Control" 111 *Yale Law Journal* 1-82.
- Sassen, Saskia. "Territory and Territoriality in the Global Economy". *International Sociology*. vol. 15, no. 2, 2000, pp. 372-393.
- Roe, Mark J. (2000). "Political Preconditions to Separating Ownership From Corporate Control", 53 *Stanford Law Review* 539-603.
- Harmes, Adam. "Institutional investors and the reproduction of neoliberalism". *Review of International Political Economy*. vol. 5, no. 1, Spring 1998, pp. 92-121.
- Peter Gourevitch, 'The Politics of Corporate Governance Regulation', (2003) 112 *Yale Law Journal* 1829-1880.
- La Porta, Rafael et al. (1999). "Corporate Ownership Around the World". 54 *Journal of Finance* 471-517.
- Cohen, Morris. (1927-28). "Property and Sovereignty". *Cornell Law Quarterly*. 13. pp. 8-30.