A Contractarian Approach to Stakeholder Primacy

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Inspired by Alan Schwartz's contractarian approach to business law, we provide a framework for determining when corporate stakeholders should be able to opt out of legal rules in order to advance social goals beyond wealth maximization. We argue that, under this Schwartzian framework, shareholders and other corporate decisionmakers would be able to credibly opt out of legal rules intended for their own benefit but would not be able to opt out of rules intended to benefit other constituents. We then apply this framework to four bodies of business law: corporate law, antitrust, securities law, and bankruptcy.

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Introduction

For decades, academics have argued about whether and under what circumstances corporate decisionmakers should be able to consider interests beyond shareholder wealth maximization. Today, much of this scholarship focuses on corporate law and corporate governance under the banner of environmental, social and governance (ESG) principles. But this debate simply reprises the age-old arguments about corporate purpose: What is the goal of the corporate form? When should shareholders or other stakeholders be able to pursue pro-social interests? And who decides?

The academic literature has largely focused on day-to-day corporate decisionmaking: in the ordinary course of business, how, and to what extent, should managers be able to consider the interests of environmental, labor, and other non-shareholder constituents when deciding whether and how to pursue a project? While these questions are consequential, in our view the most difficult issues arise where the continued existence of the corporation is in question, or when the corporation is seeking to contract around laws designed to protect third parties that are not represented in the corporate decisionmaking process. For example, when a corporation is being acquired (or is filing for bankruptcy), should certain stakeholders be able to accept a lower payout in exchange for requiring that the acquirer (or reorganized company) protect the environment and maintain workplace protections? Should corporations be able to form a cartel if doing so leads to better outcomes for the environment or improves labor conditions? Should a corporation be allowed to give its workers an informational edge over the rest of the market in trading its shares?

This Symposium, in honor of Alan Schwartz's long and varied academic career, offers an opportunity to revisit these debates. Two trademarks of Schwartz's scholarship are his contractarian approach and his pro-efficiency leanings. While not directly adverse, stakeholderism has often been framed as a foil to the shareholder primacy paradigm, with classic law and economics scholars typically defending the latter on efficiency grounds. We explore the implications of applying Schwartz's contractarian lens to this ongoing debate.

For purposes of this discussion, we define stakeholder primacy as the practice of elevating the position of one or more stakeholder group above the level that would otherwise obtain under existing law. This could include considering the interests of customers when auctioning off a company. Or it could be allowing employees to use their superior information about a company to make money at the expense of other shareholders. Or it could be elevating the claims of involuntary creditors over those of lenders. Or finally, it could be using market power (obtained in contravention of the antitrust laws) to pay higher wages to workers.

All these examples illustrate how Schwartz's contractarian approach to business law can provide a framework for understanding whether and how corporate actors should be able to contract around business law. Applying the Schwartzian approach would suggest that, when business law is designed to protect corporate constituencies, those constituencies should be able to voluntarily give up those protections—and the financial returns that they are designed to safeguard—in order to pursue some prosocial interest. Under this framework, when a corporation is being acquired, shareholders should be able to accept a lower price in exchange for the acquirer agreeing to, for example, pursue environmental objectives or protect employee interests. In such circumstances, the shareholders are simply giving up an entitlement that belongs to them. By contrast, in the context of antitrust, shareholders should not be able to collude to protect the environment or improve labor conditions, since doing so involves giving up an entitlement—federal antitrust laws—that is designed to protect consumers and perhaps other non-shareholder constituents. If ESG provided an ability to opt out of the antitrust laws, it would put shareholders in a position of giving up something that never belonged to them.

I. Contractarian Stakeholder Primacy

A. Stakeholders versus Shareholders

The debate around shareholder primacy is one of the oldest debates in corporate law.[1] While it is impossible to summarize it all here, the question at its center is simple: should corporate managers be able to subordinate the interests of their shareholders to those of other groups? These groups, sometimes known as stakeholders, can include workers, suppliers, customers, local communities, and environmental interests. But the shareholder primacy paradigm answers this question in the negative: under that framework, when there is a conflict between the interests of shareholders and the interests of one or more stakeholder groups, the corporation's managers must pursue the former at the expense of the latter. There are, of course, limits to this—even the most ardent proponent of shareholder primacy would not condone illegal behavior—but in general, maximizing the value of the company for the benefit of shareholders comes first.[2] Stakeholderism, on the other hand, is a bit less precise, but if it is to mean anything at all, it must imply that at least some of the time, corporate managers must be able to (or perhaps required to) sacrifice shareholder value,

1. For a recent book defending shareholder primacy—i.e., the shareholder value maximization paradigm—see STEPHEN M. BAINBRIDGE, THE PROFIT MOTIVE: DEFENDING SHAREHOLDER VALUE MAXIMIZATION, (Cambridge Univ. Press 2023). For a review critiquing this position, see Ann M. Lipton, *Will the Real Shareholder Primacy Please Stand Up?* 137 HARV. L. REV. 1584 (2024).

2. One justification for this position is that other bodies of law, whether they be environmental law, labor law, consumer protection law, and the like, exist to protect these other constituencies. Having complied with all those rules, the corporation has discharged its obligations to those groups, and what remains is a duty to maximize shareholder value.

thereby subordinating the interests of shareholders, in order to benefit one or more stakeholder group.

This debate has traditionally focused on corporate law, presumably because corporate law is concerned with establishing and regulating the internal governance of corporations. While corporate managers (that is to say, directors and executive officers) of Delaware corporations owe fiduciary duties to the *corporation*, there is general consensus that shareholder primacy exerts a powerful influence over modern corporate law.[3] That is not to say that corporate managers cannot consider other constituencies, only that decisions that take those constituencies into account are generally couched in terms of stewarding the long-term value of the company.

The debate has come to other areas of law as well. As early as the 1980s, the debates in bankruptcy law between then-professor Elizabeth Warren and Douglas Baird, Thomas Jackson, and Alan Schwartz, centered around a closely related argument: that bankruptcy law should protect stakeholder interests as well as financial recovery in deciding whether and how to reorganize bankrupt companies. Naturally, the foil was creditors rather than shareholders, but because the benefits of creditor value maximization accrue to the shareholders both ex post (in the event that the company is ultimately able to repay its creditors in full) and ex ante (though a lower borrowing cost), skeptics of the stakeholder position were making arguments that closely resemble and promote the goals of shareholder wealth maximization And with the rise of "ESG,"[4] this set of considerations has expanded to other areas including securities law—see especially the debates over what has come to be known as the SEC's "climate rule"[5]—and antirust.[6]

3. *See, e.g.*, Leo E. Strine, Jr., *The Dangers of Denial: The Need for a Clear-Eyed Understanding of the Power and Accountability Structure Established by the Delaware General Corporation Law*, 50 WAKE FOREST L. REV. 761 (2015).

4. For the best discussion of ESG, and how it came to occupy its current central position, see generally Elizabeth Pollman, *The Making and Meaning of ESG*, 14 HARV. BUS. L. REV. 403 (2024).

5. Securities Act of 1933 Release No. 11275 / Securities Exchange Act of 1934 Release No. 99678, codified as 17 CFR 210, 229, 230, 232, 239, and 249. The rule was stayed due to ongoing litigation. Securities Act of 1933 Release No. 11280 Securities Exchange Act of 1934 Release No. 99908, April 4, 2024. On February 11, 2025, the Acting Chair made clear that the anticipated change in the composition of the Commission had put the future of the rule in jeopardy, and notified the court to that effect. Commissioner Mark T. Uyeda, *Acting Chairman Statement on Climate-Related Disclosure Rules*, SEC (Feb. 11, 2025), https://www.sec.gov/newsroom/speeches-statements/uyeda-statement-climate-change-021025. While the issue is still unresolved, it seems highly unlikely that the rule will ever go into effect.

6. For example, on August 4, 2022, the attorneys general of 19 states sent a letter to Larry Fink, the CEO of BlackRock, Inc. Among other things, the letter articulated concerns that BlackRock's ESG efforts could violate the federal antitrust laws. Letter to Mr. Laurence D. Fink, CEO, BlackRock, Inc. (Aug. 4, 2022), https://www.texasattorneygeneral.gov/sites/default/files/images/executive-management/BlackRock%20Letter.pdf.

B. Stakeholder Primacy and Lessons from Schwartz

A central lesson from Schwartz's work is that sophisticated parties can bargain for themselves, and, in general, should be allowed to do so. Schwartz's core contractarian commitments can be summarized briefly:

1. In the absence of externalities, people should be able to contract for what they want.
2. In the absence of externalities, it is paternalistic for a third party to impose its preferences on sophisticated parties.
3. Participants in capital markets are sophisticated and can contract to protect their interests.
4. Even when parties are sophisticated, there are certain situations in which it is possible for parties to act opportunistically.

That does not mean Schwartz was a rigid contractarian. He was attentive to holdup problems, especially in the context of renegotiation,[7] and also to the fact that his contractarianism applied primarily, if not exclusively, to sophisticated parties.[8] Still, Schwartz consistently defended the ability of sophisticated parties to contract to protect their own interests.[9] In fact, unlike many of his contemporaries, he did not think that holdup problems were fatal to the contractarian approach, but considered when and under what circumstances creditor control might offer an alternative to regulation.[10] To that end, he was a champion of default rules instead of mandatory rules,[11] and he advocated that specific legal subjects become more adopt more permissive frameworks that would allow parties to opt out to serve their interests.[12]

Often, Schwartz was decades ahead of contemporary business law scholars in anticipating developments in capital markets. Schwartz saw, for example, that private workouts would sometimes prove to offer a cheaper alternative to formal reorganization proceedings well before other

7. Alan Schwartz and Joel Watson, The Law and Economics of Costly Contracting, 20 J. L. ECON. & ORG. 2 (2004).

8. Antonio Bernardo, Alan Schwartz & Ivo Welch, *Contracting Externalities and Mandatory Menus in the U.S. Corporate Bankruptcy Code*, 32 J. LAW, ECON. & ORG. 395 (2016) (about when freedom of contract should be limited in bankruptcy contexts).

9. Alan Schwartz & Ron Gilson *Corporate Control and Credible Commitment*, 43 INT. REV. LAW & ECON. 119 (2015) (discussing the need for contracting to ensure commitment in corporate contexts); Alan Schwartz, *Bankruptcy Related Contracting and Bankruptcy Functions*, *in* RESEARCH HANDBOOK ON CORPORATE BANKRUPTCY LAW 363 (Barry Adler ed. 2020) (rejecting the creditors' bargain theory and showing how large creditors contract for control).

10. Alan Schwartz, *Bankruptcy Workouts and Debt Contracts*, 36 J. L. & ECON. 595 (1993)

11. Alan Schwartz & Robert Scott, *The Common Law of Contract and the Default Rule Project*, 102 VA. L. REV. 1523 (2016).

12. Alan Schwartz, *Bankruptcy Contracting Reviewed*, 109 YALE L.J. 343, 343 (1999) ("There should be few mandatory rules within bankruptcy systems.").

scholars, and he anticipated how creditor control would, over time, make workouts an even more attractive alternative to bankruptcy.[13]

At times, however, Schwartz's contractarianism went hand-in-hand with a preference for shareholder primacy. For example, one of the reasons Schwartz pushed against mandatory bankruptcy rules was that he thought that default rules would lead to lower capital costs.[14] But it is of course not always that case that shareholders and creditors will aim exclusively to maximize value. Indeed, given the enormous variety of companies in the world, it stands to reason that that there could exist some companies—and by that we mostly mean their shareholders—that really do care about some other constituency or constituencies. Given that it is worth considering how Schwartz's contractarian model could be applied to modern ESG debates.

C. Let Companies Opt Out of Rules for the Benefit of Shareholders

Then the question is, what contracts should shareholders be able to write? Under the Scwartzian framework, we think, the answer flows from two premises. First, that legal rules can confer entitlements and obligations on different parties. Second, parties cannot give or contract away a legal entitlement that belongs to someone else. Applying this to the realm of stakeholder primacy, it follows that a company and its shareholders should be able to give away their own entitlements, and only those entitlements.

Naturally, many (indeed most) legal rules are not quite so simple. They may confer an entitlement on one party with the aim of achieving some broader social goal. For example, labor law may be designed to protect workers, but also to promote overall economic efficiency. Another complication arises because legal rules may confer entitlements on multiple parties, such as when antitrust law allows the FTC, DOJ, and private individuals to enforce the federal competition laws. Still, at first approximation, we can at least make sensible arguments about which party (or parties) a legal rule is intended to benefit. Perhaps more importantly, we can coherently analyze whether allowing the holder of that entitlement to forego it in favor of another party would frustrate the purpose of the rule.

The Schwartzian framework that we explore is primarily conceptual, and many details would have to be resolved before it could be implemented. Nonetheless, and in keeping with the spirit of Schwartz's scholarship, we focus on high-level conceptual issues and try not to get bogged down with technical details related to implementation.

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13. Alan Schwartz, *Bankruptcy Workouts and Debt Contracts*, 36 J. L. & ECON. 595 (1993).

14. *See* Schwartz, *Bankruptcy Contracting Reviewed*, supra note 12, at 343 ("The only goal of a business bankruptcy law should be to reduce the cost of debt capital, which the law best does by maximizing the debt investors' insolvency state payoff.").

II. Contractarian Stakeholder Primacy in Four Parts

A. Corporate Law: Let Shareholders Decide

We begin with corporate law. For our purposes, the question is not whether shareholder primacy is the right model, at least as a default rule. The question is whether shareholders should be able to opt out of this rule if they so choose.[15]

As every student of corporate law knows, in practice, as long as a corporate decisionmaker (typically a board or directors) is unconflicted, the resulting decisions will be reviewed under the deferential business judgement rule.[16] As long as the decision is unconflicted and purports to be in interest of the corporation, managers can consider other constituencies besides shareholders, and the Delaware courts will not second guess it. In practice, this means that managers are free to consider the interests of stakeholders, and even to make decisions for their benefit, as long as those decisions are described in the right way.[17] If shareholders are unhappy with these decisions, they are free to use the two remaining levers at their

15. There is an active debate in Delaware corporate law about the extent to which Delaware companies can and should be able to tailor corporate governance. *See* Jill E. Fisch, *Stealth Governance: Shareholder Agreements and Private Ordering*, 99 WASH. U. L. REV. 913 (2022) (arguing that such tailoring should be limited to public documents like the charter). This debate came to the fore with the 2024 amendments to the Delaware General Corporation Law. For a discussion of the controversy and commentary surrounding these amendments, see *The Long Form*, THE CHANCERY DAILY (May 21, 2024), https://mailchi.mp/chancerydaily.com/2024-05-21-long-form-rjijrjfiojf3e3e3e322; *The Long Form - Special Edition*, THE CHANCERY DAILY (May 28, 2024), https://mailchi.mp/chancerydaily/the-long-form-special-edition-may-28.

16. In re Match Grp., Inc. Derivative Litig., 315 A.3d 446, 459 (Del. 2024) ("The default standard of review is the business judgment rule, which is a presumption that in making a business decision, the directors of a corporation acted on an informed basis, in good faith and in the honest belief that the action taken was in the best interests of the company. If the business judgment standard of review applies, a court will not second guess the decisions of disinterested and independent directors. The reviewing court will only interfere if the board's decision lacks any rationally conceivable basis, thereby resulting in waste or a lack of good faith." (cleaned up)). For arguments that some of the conditions of shareholder primacy do not apply to certain industries, Jonathan R. Macey & Maureen O'Hara, *The Corporate Governance of Banks*, ECON & POL'Y REV. 91, 102 ("[A] clear case can be made for bank directors being held to a broader, if not a higher, standard of care than other directors."): Aneil Kovvali & Joshua C. Macey, *The Corporate Governance of Public Utilities*, 40 YALE J. ON REGUL. 569, 574 (2023) ("Utility shareholders . . . are properly understood as creditors by another name. Like creditors, their losses are limited to the value of their investment while their recoveries are capped by regulatory price controls. While corporate governance mechanisms ensure that public utility companies are managed for the benefit of shareholders, it is the ratepayers who internalize the consequences of utilities' decisions"); Aneil Kovvali & Joshua C. Macey, *Private Profits and Public Businesses*, 103 TEX. L. REV. 711 (2026) (arguing that holdup problems in some industries create misaligned shareholder incentives).

17. *See* Revlon v. MacAndrews & Forbes Holdings, Inc., 506 A.2d 173, 182 (Del. 1986) (noting that a "board may have regard for various constituencies in discharging its responsibilities, provided there are rationally related benefits accruing to the stockholders"). For a discussion of the flexibility afforded to managers to consider stakeholder interests in the M&A context *outside* of the *Revlon* context, see Caley Petrucci & Guhan Subramanian, *Stakeholder Amnesia in M&A Deals*, 50 J. CORP. L. 87 (2024).

disposal: to sell their shares (thereby pushing down their price) or to vote for a different slate of directors at the next annual meeting.[18]

Where the rubber hits the road is the so-called *Revlon* context, when the board has decided to sell the company. At this point, the law is clear: the board's obligation is to maximize the deal price for the benefit of shareholders.[19] What if shareholders would prefer a different rule? In particular, suppose shareholders, either at the time of incorporation or when the company transitions from being closely held to dispersed ownership, get together and agree that they don't want *Revlon* to apply. Instead, they want management to be free to consider stakeholder interests *even* in the context of an auction, and *even* if doing so would reduce the payment to shareholders. Should the law permit them to do so, and, if so, how?

The sale of Twitter to Elon Musk has become a popular contemporary case study (though it's not clear that *Revlon* duties were ever at issue).[20] Commentators expressed concerns that Musk would run Twitter (now X) in a way that would harm stakeholders, including employees, suppliers, its customers (i.e., users of the platform), and society as a whole.[21] Yet from the shareholders' perspective, the deal was a no brainer,[22] representing a substantial premium over both the unaffected price.[23]

For our purposes, the question is not whether the Twitter board did the right thing, but rather whether a company should be able to commit, at the time that it is raising capital from prospective investors, not to behave as Twitter did. The Schwartzian paradigm provides a clear answer: of course. *Revlon* duties exist for the benefit of shareholders. The underlying economic rationale is to allow companies to raise capital as cheaply as possible by managing agency costs and maximizing payoffs to residual claimants at the point when option value is extinguished. But if shareholders want to voluntarily forego that right at the time of investment and with the

18. *See, e.g.,* Randall S. Thomas & Patrick C. Tricker, *Contested Director Elections and Management Proposals: A Review of the Empirical Literature*, 70 OKLA. L. REV. 9, 11 (2017) (noting that shareholders "can sell their shares, vote them where allowed, or sue the company and its management to enforce its officers and directors' fiduciary duties").

19. Revlon v. MacAndrews & Forbes Holdings, Inc. 506 A.2d 173, 182 (Del. 1986).

20. *See* Petrucci & Subramanian *supra* note 17.

21. *See generally* Ann M. Lipton, *Every Billionaire Is a Policy Failure*, 18 VA. L. & BUS. REV. 327, 373-80 (2024).

22. Of the nearly 460 million votes that were cast at the shareholder vote to approve the merger, over 453 million voted yes. In total, over 60% of outstanding shares were voted in support of the merger. Twitter, Form 8-K (Sep. 14, 2022), https://www.sec.gov/ix?doc=/Archives/edgar/data/1418091/000119312522244289/d403306d8k.htm

23. The merger consideration of $54.20 per share represented a premium of 38% above the closing price of Twitter's common stock on the last full trading day before Mr. Musk disclosed his approximately nine percent stake in the company. *Twitter*, Proxy Statement (Form DEFM 14A) (Jul. 26, 2022), https://www.sec.gov/Archives/edgar/data/1418091/000119312522202163/d283119ddefm14a.htm. By the time the deal closed, the consensus view was that the company was worth considerably less than that.

benefit of full disclosure, they must be better off by doing so.[24] What's more, it's hard to come up with a meaningful externality argument for restraining them. Schwartz's work therefore teaches us that there is little reason to be concerned that this will have a deleterious effect on the market.

Of course, precautions are necessary to guard against opportunism. First, we would need to be certain that *all* investors who buy into the company understand that they are doing so on these terms. Accordingly, initial consent must be unanimous among existing shareholders, which is why it may only be practical for closely held companies. And any prospective shareholder would have to be informed of the terms. Memorializing the fact in the company's charter—a publicly available document—should address this.

There are additional challenges with implementation. What if shareholders change their view midstream and decide that they no longer want to prioritize the relevant stakeholder interest? While flexibility in the face of changes circumstances is valuable, this also raises the possibility of opportunism: after all, whoever *sold* those shares to the current owner may have valued the continued prioritization of stakeholder interests and may have required a higher price in order to sacrifice it. This sort of commitment problem is both intractable and familiar. We do not pretend to have a solution for it here, since our focus here is on giving management the *option*, not on imposing an *obligation*. Still, one option would be to define the stringency of the precommitment device ex ante by stipulating a voting process that would allow the firm to change the ESG commitment at a later date.[25]

The other standard response to calls to allow management to prioritize stakeholders is that this is precisely what the public benefit corporation (PBC) form is intended to do. Introduced in Delaware in 2013, to date relatively few corporations have chosen to incorporate under statute.[26] To be sure, the PBC form has been subject to its own criticisms,[27] but as students of the Schwartzian school, we applaud this increase in the contracting space. But a Schwarzian approach would probably go further, and would allow shareholders of all corporations to credibly commit to allowing managers to consider stakeholder interests, even in an auction setting, while

24. *See also* Oliver Hart & Luigi Zingales, *Companies Should Maximize Shareholder Welfare Not Market Value*, 2 J.L. FIN. & ACCOUNTING 247 (2017).

25. For a fresh discussion of these commitment problems, see Patrick M. Corrigan, *The Corporate Governance Trilemma* (Working Paper, Apr. 2024), https://papers.ssrn.com/sol3/papers.cfm?abstract_id=4729606.

26. See Jens Damman, *Publicly Traded Public Benefit Corporations: An Empirical Investigation*, STAN. J.L. BUS. & FIN. (*forthcoming*). Perhaps it will take off. Anthropic, the prominent AI company founded by departing employees of OpenAI, has chosen this form. See Anthropic, *Making AI Systems You Can Rely On*, https://www.anthropic.com/company.

27. Damman, *supra* note 26.

respecting the rest of the Delaware General Corporation Law.[28] To be sure, it seems unlikely that many companies would adopt such a charter provision if it were available, but that's not a reason to prohibit it.

B. Antitrust Law: Not Shareholders' to Give

Antitrust law represents the opposite extreme. In response to a question for the record from Senator Ted Cruz in his capacity as a member of the Senate Judiciary Subcommittee on Competition Policy, Antitrust, and Consumer Rights in 2022, Lina Khan, Chair of the Federal Trade Commission stated unequivocally that "there is no ESG exemption to the antitrust laws."[29] Then-Chair Khan reiterated this point a few months later in an opinion piece in the Wall Street Journal.[30] Should there be?[31] For example, should companies be allowed to collude in order to set policies that benefit some stakeholder interest? Or should they be allowed to merge if such a merger would result in significantly greater market power, as long as the company pledged to use some of the monopoly profits to raise worker pay?

Here again, the Schwartzian paradigm provides a clear answer: of course not. Antitrust law isn't concerned with protecting shareholders—if anything, one of its primary functions is to prevent companies from obtaining high profits—which, of course, accrue to shareholders—by restricting production.[32] It follows from this that monopoly power is good for the shareholders of the monopolist, and that antitrust enforcement is adverse to those interests. Antitrust is instead designed to protect non-shareholder interests. Whether one thinks the federal antitrust laws should measure anticompetitive conduct by looking at "allocative efficiency,"[33] "consumer

28. Another possible response is to say that there are 49 other states, each with their own corporate law, to choose from. While charter competition has its own Schwartzian appeal, it does not entirely resolve the issue. There are many other very appealing aspects of Delaware corporate law; it would be a shame to have a take-it-or-leave-it attitude with respect to this provision.

29. Oversight of Federal Enforcement of the Antitrust Laws: Hearing Before S. Comm. on the Judiciary, 117th Cong. 13 (2022) (statement of Lina Khan)

30. Lina Khan, *ESG Won't Stop the FTC*, WALL ST. J. (Dec. 21, 2022), https://www.wsj.com/articles/esg-wont-stop-the-ftc-competition-merger-lina-khan-social-economic-promises-court-11671637135 ("Some in corporate America seem to think that the FTC won't challenge an otherwise illegal deal if we approve of its ESG impact. They are mistaken. The antitrust laws don't permit us to turn a blind eye to an illegal deal just because the parties commit to some unrelated social benefit").

31. Two recent student notes have argued for legal changes to allow them to do so. *See* Dailey C. Koga, *Teamwork or Collusion? Changing Antitrust Law to Permit Corporate Action on Climate Change*, 95 WA. L. REV. 1989 (2020); Peter Brigham, *The Case for Green Product Fixing: Reconciling Antitrust Law with Self-Regulation to Combat Climate Change*, 73 EMORY L.J. 241 (2023).

32. *See, e.g.*, Herbert Hovenkamp, *Antitrust and Platform Monopoly*, 130 YALE L.J. 1952, 1958 (2021) ("Antitrust policy is concerned with exercises of market power, which is the power to profit by reducing output below the competitive level and increasing prices unreasonably above cost.").

33. ROBERT H. BORK, THE ANTITRUST PARADOX: A POLICY AT WAR WITH ITSELF (1978).

welfare,"[34] or the "underlying structure and dynamics of markets,"[35] antitrust law is designed to protect customers and other stakeholders from anticompetitive business practices. It is not about protecting shareholders.

The obvious risk of allowing shareholders to invoke ESG to opt out of state and federal antitrust laws is that they would do so opportunistically to justify forming a cartel or engaging in some other anticompetitive conduct. Firms could, for example, agree to provide heightened employee protections not to protect workers but to raise costs, and therefore prices.[36] But even if a firm is genuinely committed to improving labor or environmental outcomes, the Schwartzian framework is again instructive: in such circumstances, if ESG agreements are a means to collude to raise prices, they effectively allow firms to contract away entitlements they never had to begin with. Revisiting the federal antitrust laws should be done through the political process.

In sum, the fact that shareholders may genuinely want to share some of those monopoly profits with some stakeholder group is irrelevant: those antitrust rules aren't meant to benefit shareholders, since profits obtained in contravention of standard antitrust law were never theirs to give away. That is the case even if the firm engages in activities that support environmental or labor interests.

C. Securities Law: Almost There

What about areas of law in which it is more difficult to precisely define whether a legal rule creates a defeasible entitlement? We start with the federal securities laws. In the standard account, one of the SEC's core missions is investor protection.[37] This suggests that shareholders (who are, after all, paradigmatic investors) should be able to deviate from the default rules as long as doing so doesn't materially undermine the regime's other missions (generally described as maintaining fair, orderly, and efficient markets and facilitating capital formation).[38]

And indeed, the securities laws already allow shareholders to opt out of many (albeit not all) of the portions of the securities regulatory regime intended for their benefit. The most obvious example is mandatory disclosure, which has been described as "the cornerstone of federal securities

34. Reiter v. Sonotone Corp., 442 U.S. 330, 343 (1979).

35. Lina M. Khan, Note, *Amazon's Antitrust Paradox*, 126 YALE L.J. 710, 717 (2017).

36. *See Climate Control: Exposing the Decarbonization Collusion in Environmental, Social, and Governance (ESG) Investing*, Committee on the Judiciary U.S. House of Representatives (June 11, 2024) (alleging "that a 'climate cartel' of left-wing environmental activists and major financial institutions has colluded to force American companies to 'decarbonize' and reach 'net zero'").

37. U.S. Securities & Exchange Commission, *About* (last visited Sep. 23, 2024), https://www.sec.gov/about ("The SEC's mission is to protect investors; maintain fair, orderly, and efficient markets; and facilitate capital formation").

38. *Id.*

law."[39] A crucial function of mandatory disclosure is that it provides shareholders with information that allows them to monitor and evaluate management.[40] At the same time, some commentators have argued that the need to report earnings and other financial information on a quarterly basis leads to managerial "short-termism" that causes managers to engage in behaviors that are harmful to stakeholders.[41]

To the extent that a group of shareholders believe this, they are in luck. Under current law, companies—and their shareholders—can effectively opt out of the mandatory disclosure regime by remaining (or, in the event that the company is already public, going) private,[42] something that leading scholars have argued has become increasingly common in recent years.[43] In practice then, shareholders are free to forego the benefits of mandatory disclosure if they really want to.

Of course, this choice imposes costs: private companies face restrictions that do not apply to public ones.[44] But given the other purposes of the securities laws, this seems like a reasonable compromise. If a company is really committed, it can choose to opt out of this default, but it bears some costs from doing so. While those costs might not be perfectly

39. Colleen Honigsberg, Robert J. Jackson Jr. & Yu-Ting Forester Wong, *Mandatory Disclosure and Individual Investors: Evidence From the Jobs Act*, 93 WA. U. L. REV. 293, 295 (2015).

40. For a canonical articulation of this, *see In the Matter of Franchard Corp.*, 42 S.E.C. 163 (July 31, 1964) ("Evaluation of the quality of management—to whatever extent it is possible—is an essential ingredient of informed investment decision. A need so important cannot be ignored, and in a variety of ways the disclosure requirements of the Securities Act furnish factual information to fill this need."). Of course, there are other rationales for mandatory disclosure. For example, by providing information about a particular company, mandatory disclosure makes *other* prices more efficient. *See generally* Elisabeth de Fontenay, *The Deregulation of Private Capital and the Decline of the Public Company*, 68 HASTINGS L.J. 445 (2017).

41. *See* Mark J. Roe, *Stock Market Short-Termism's Impact*, 167 U. PENN. L. REV. 71 (2018) (describing "[a] widely held view among Washington policymakers, the corporate judiciary, corporate executives, the media, and the public is that increasingly frenzied trading in the stock market, coupled with Wall Street's insatiable appetite for immediate profits, starves too many American firms and harms the economy. Jobs are lost and technological progress is stunted, while solutions are so easy to implement that one fumes at their absence").

42. While public company is not a formal legal classification, it is widely used by both scholars and market participants). The closest formal legal term is "reporting" issuers and "non-reporting" issuers. *See, e.g.*, de Fontenay, *supra* note 40, 453-54 n.29 and accompanying text (explaining the use of the terms "public" and "private" company as corresponding to reporting companies and publicly traded, and companies that are neither reporting companies nor publicly traded, respectively). We adopt these widely held meanings of "public" and "private" company for the purposes of this discussion.

43. *See, e.g.*, de Fontenay, *supra* note 40; Elizabeth Pollman, *Private Company Lies*, 109 GEORGETOWN L.J. 353 (2020).

44. For example, only public companies are allowed to list on public exchanges like the New York Stock Exchange (NYSE) or the NASDAQ, which provide significant liquidity *See* de Fontenay, *supra* note 40 at 456 ("Provided that they can satisfy the applicable listing standards, most U.S. public companies choose to list their stock on a major securities exchange such as the NYSE or NASDAQ, as this provides their shareholders and management with liquidity"). Private companies are also limited in how widely held their shares can be, although this has been relaxed in the context of employee ownership. *See* 15 U.S.C. § 78l(g). Finally, private companies face limitations as to how many non-accredited investors can purchase their shares. *See generally* 17 C.F.R. § 230.500 *et. seq.* (also known as Regulation D).

calibrated to reflect the loss in social value from the lack of disclosure,[45] there isn't an obviously better alternative.

Much of the rest of the regime is also consistent with the Schwartzian approach. After all, the securities laws essentially provide protections against fraud. For the most part, a company can do anything it wants, as long as it is up front about it. At least with respect to affirmative statements, it's hard to object to this.[46]

The one exception is insider trading. Under current doctrine, insider trading liability can attach under one of two (non-exclusive) theories. The first—and older—theory is the classical theory, which is premised on the idea that an insider with a fiduciary duty to the shareholders of a company defrauds those shareholders if she trades on the basis of material non-public information without first announcing her intention to do so.[47] Because this doctrine applied only to insiders of the company in which the trades took place, it was viewed as too limited. For example, what if a corporate insider learns that her company is about to announce a takeover bid? Under the classical theory, she could trade in the shares of target to her heart's content without fear of liability. Because of dissatisfaction around situations such as these, the SEC and the courts developed the misappropriation theory, which is premised on the idea that an insider defrauds the *source* of the information if she misappropriates it and trades on it without the permission of its rightful owner.[48]

How does this cash out in the ESG context? Suppose that a company wants to benefit its workers by allowing them to trade on information obtained in the course of their employment. The primary losers from these trades are, of course, the shareholders that the employees are trading against. After all, the employees will presumably use their informational advantage to make well timed highly profitable trades, generating large trading profits. These profits will come at the expense of "outsider" shareholders, who do not have this advantage. Interestingly, while companies can opt of out of the insider trading prohibitions under the *misappropriation* theory,[49] there is no clear doctrinal support for the ability to opt out of the prohibition under the *classical* theory.

This is particularly odd: the upshot is that (1) a company is free to allow its customers, suppliers, and other stakeholders (*except its workers*) to make money trading against its own shareholders, and (2) it's also free

45. See discussion *supra* note 40.

46. Of course, there may be other objectionable features, like the extent of the liability or the ubiquity of strike suits.

47. For the canonical case articulating the classical theory of insider trading, see *Chiarella v. United States*, 445 U.S. 222 (1980).

48. For the canonical case articulating the misappropriation theory of insider trading, *see United States v. O'Hagan*, 521 U.S. 642 (1997).

49. *Id.* at 659 n.9 ("[T]he textual requirement of deception precludes . . . liability when a person trading on the basis of nonpublic information has . . . obtained authorization from, the principal.").

to allow its workers (and other stakeholders) to make money trading against the shareholders of *other* companies, but (3) it is *not* free to let its workers make money trading against its *own* shareholders. This strikes us as illogical. While (1) and (2) can certainly be justified, it is hard to come up with any coherent theory that contains all three at the same time.[50] Surely it cannot be an argument about the integrity of the capital markets: it is hard to square such an argument with the fact that misappropriation-based insider trading theories are already contractarian in nature.

The obvious solution is to let companies—by which we mean the shareholders—opt out of the insider trading regime under *both* theories. Of course, as with the *Revlon* opt out discussed in Section III.A, this would have to be done by unanimous consent of all shareholders and recorded in a publicly available document like the charter.[51]

D. Bankruptcy Law: Which Stakeholders?

In theory, there are sets of stakeholders in bankruptcy that should be able to accept a lower payout if the reorganized firm agrees to pursue pro-social goals. In the context of bankruptcy, the Schwartzian approach to ESG would cash out through deviation from absolute priority rule or forcing (ex post) certain classes of creditors to subordinate their financial interests to make sure that environmental or labor interests receive some value to which they are not otherwise legally entitled.

The absolute priority rule is "the organizing principle of the modern law of corporate reorganizations."[52] When a firm files for bankruptcy, it must pay higher priority claims before paying those with a lower priority.[53] The creditors holding claims in the fulcrum position—those that are set to be paid in part, but not in full—determine the future direction of the

50. While it is formally true that the employee can trade as long as she discloses (purportedly an antifraud rule), this is tantamount to depriving her of the benefit of the information.

51. Even if the median retail investor never looks there, the usual arguments about informationally efficient markets apply here. If we depart from that paradigm, there are many parts of the securities regime that would be in more jeopardy than this one!

52. Douglas G. Baird, *Priority Matters: Absolute Priority, Relative Priority, and the Costs of Bankruptcy*, U. PA. L. REV. 785, 786 (2017).

53. For arguments that bankruptcy does not or should not follow absolute priority, see *id*. at 788 ("a reorganization regime that uses both is inherently unstable. Absolute priority is naturally suited for regimes in which the financially distressed firm is sold to the highest bidder. It is much less appropriate for a regime that puts a new capital structure in place without a market sale."); Anthony J. Casey, *The Creditors' Bargain and Option-Preservation Priority in Chapter 11*, 78 U. CHI. L. REV. 759, 765 (2011) (proposing that "when the present value of the firm is less than the face value of the senior debt, the senior creditor—rather than getting the entire firm—get[] the greater of (1) the non-bankruptcy liquidation value and (2) the entire firm net of the junior creditor's option value"); Anthony J. Casey & Joshua C. Macey, *The Hertz Maneuver (and the Limits of Bankruptcy Law)*, U. CHI. L. REV. ONLINE ("The real bankruptcy problem, then, is not that retail investors are incapable of making informed bets, but that bankruptcy law makes it difficult for stockholders and unsecured creditors to make long-term bets about a company's future value. From this perspective, relative priority begins to look like a form of investor protection that facilitates investment in a firm's long-term value.").

company. This can occur through a formal sale or by voting to approve a plan of reorganization. Because these creditors are the residual claimants, the wealth maximization paradigm in bankruptcy shifts from maximizing shareholder value to maximizing the value of the claims of the fulcrum creditors. Accordingly, a Schwarzian approach would suggest that they should be able to require that the reorganized company pursue goals other than wealth maximization—even if that means accepting a lower payout.

But problems arise in practice. One could, of course, simply allow creditors that occupy the fulcrum position to make prosocial commitments once the firm files for bankruptcy. Alas, though, any ex post approach is vulnerable to opportunism. It is possible that a creditor genuinely wants to pursue broad social objectives. But it is also possible that a creditor is simply threatening to destroy value in order to secure bargaining concessions from other creditors.

Opportunism is especially concerning in the context of bankruptcy, since bankruptcy gives creditors tools that allow them to force equally-situated creditors to accept a plan of reorganization even if they object to the plan. Perhaps most importantly, one class of creditors can "cramdown" a bankruptcy plan—it can force impaired creditors with equal priority to accept a plan even if they object to the proposed plan—so long as the bankruptcy plan is "fair and equitable" and does not "discriminate unfairly."[54] Thus, if bankruptcy allowed fulcrum creditors to decide to pursue social objectives *after* the firm became insolvent, it would empower some fulcrum creditors to force other impaired creditors to accept a loss beyond what they are entitled to under the absolute priority rule. This would violate the animating principle of this Essay, which is that corporate stakeholders should not be able to give up entitlements that belong to other stakeholders.

This suggests that firms that want to contract around the absolute priority rule must precommit to doing so. But precommitment devices turn out to be especially difficult to administer in bankruptcy. For starters, firms do not know ex ante which creditor group will occupy the fulcrum position, how much the firm will be worth, or how much creditors will have to sacrifice financially to pursue non-welfare maximizing pursuits. This creates familiar contracting challenges. It is difficult to specify ex ante what the firm should do when contracting parties possess incomplete information about the firm's future value.[55] In the context of bankruptcy, this uncertainty

54. 11 U.S.C. § 1129(b).

55. Alan Schwartz, *A Contract Theory Approach to Business Bankruptcy*, 107 YALE L.J. 1807, 1809 (1998) (arguing that bankruptcy itself should be limited to situations in which contracting fails); Anthony J. Casey, *Chapter 11's Renegotiation Framework and the Purpose of Corporate Bankruptcy*, 120 COLUM. L. REV. 1709, 1715 (2020) (arguing that bankruptcy is best understood as a solution to incomplete contracting); Vincent S.J. Buccola, *Bankruptcy's Cathedral: Property Rules, Liability Rules, and Distress*, 114 NW. L. REV. 705, 724 (2019) (making similar arguments to support a theory of bankruptcy as appropriate when, for a variety of reasons, means property rights should be treated as liability rights for firms in financial distress).

means that firms may not be able to specify early on the terms of a prosocial commitment, since they have very little information about the costs of future tradeoffs. If the firm turns out to be worth very little, stakeholders may not be willing or able to sacrifice financial returns in the pursuit of other social interests.

This issue is not fatal. After all, firms could put specific prosocial goals in the charter and in debt contracts. Still, it suggests that uncertainty surrounding the circumstances of financial distress might either make it extremely costly for firms to precommit to pursuing non-welfare maximizing goals in bankruptcy, or that firms will be reluctant to make binding, enforceable commitments that would dramatically increase the cost of debt.

Moreover, unless a precommitment device is binding or at least relatively immutable, ex ante prosocial bankruptcy commitments could exacerbate the very contracting problems bankruptcy is intended to resolve. Bankruptcy is designed to prevent the collective action problem that arises when creditors know they will not be paid in full. When firms are in distress, creditors may pursue remedies privately to try to make sure that they are repaid. This race to the courthouse may dismantle firms that are more valuable as a going concern, ultimately harming creditors as a group. Bankruptcy's core provisions such as the automatic stay and the absolute priority rule are designed to prevent this race to the courthouse to preserve the firm's value as a going concern. Without a precommitment device, creditors who offer to lend money to distressed firms may simply abandon their promises to environmental and labor interests when the firm enters distress. If even a few creditors did this, that would create pressure on all creditors, since the creditors who abandoned their prosocial commitments would effectively be trying to jump the line.

Without a precommitment device, it is unlikely that any prosocial commitments would have teeth. For example, if early debt contracts included covenants that stipulated that the creditors will respect environmental or labor interests in bankruptcy, creditors who offer financing to distressed firms may refuse to make such promises out of concern about the firm's solvency. While such creditors may be responding to the realities of financial distress, they would also effectively be trying to jump the line by refusing to extend credit to a firm that honors its prosocial commitments. That, of course, would make all creditors reluctant to enter into such contracts and create pressure for those who agreed to consider prosocial goals to try to renegotiate their contracts to avoid being front run by other creditors.

A final challenge is that there needs to be some mechanism to protect the entitlements of tort, environmental, and other nonadjusting creditors. While some creditors are able to contract to protect their interests, nonadjusting creditors such as tort victims and some environmental claimants are typically unable to do so.[56] Instead, these claimants are entirely reliant on the absolute priority rule to vindicate their financial interests. Unlike contractual creditors, they are unable to object to ex ante contracts that agree to accept a lower payout in exchange for pursuing non-welfare maximizing goals. If contractual creditors agree to redistribute firm value to labor and environmental interests, especially if those interests are not formally represented in the bankruptcy context (such as agreements to pay higher wages in the future or invest in climate mitigation programs), the creditors could reduce the firm's value as a going concern. That, in turn, could leave tort and environmental claimants who are formally entitled to some of the firm's value to receive less than they would have if the firm pursued a welfare maximization approach in bankruptcy.

If contractual creditors agree to a reorganization plan the decreases overall firm value, they could reduce the compensation owed to nonadjusting creditors who never agreed to accept lower recoveries. In this way, creditors who precommit to pursuing certain social goals in bankruptcy may in fact be agreeing to give up entitlements that belong to tort and environmental claimants, violating our rule against negotiating with other people's entitlements. It would be perverse if, in trying to allow contractual creditors to pursue broad social goals, bankruptcy authorized carve outs to the absolute priority rule that allowed financial creditors to threaten to redistribute money on behalf of individuals who were harmed by corporate misconduct and corporate pollution and who never agreed to lower recoveries.

Even this problem is not completely intractable. Theoretically, it might be possible to determine how much tort and environmental claimants are owed and stipulate that any prosocial bankruptcy plan not result in those claimants taking a loss, or, in the alternative, that those claimants vote to accept the prosocial plan. That is not impossible, but it means that deviations from the absolute priority rule requires a precommitment device that can be vetoed by any nonadjusting creditors who did not agree to the prosocial bankruptcy approach.

In short, it is conceivable that bankruptcy could accommodate deviations from the absolute priority rule. To do so, a firm would have to precommit such that all contractual creditors were bound by the prosocial commitment. Otherwise some creditors might opt out, potentially leading to a race to the courthouse among all creditors. But even with a precommitment device, bankruptcy needs a mechanism to ensure that contractual creditors do not invoke prosocial goals to give up entitlements that belong to nonadjusting creditors. This likely requires that nonadjusting creditors are either paid in full or vote to accept the prosocial plan of reorganization.

56. For a discussion of this issue, see Joshua C. Macey & Jackson Salovaara, *Bankruptcy as Bailout: Coal Company Insolvency and the Erosion of Federal Law*, 71 STAN. L. REV. 879 (2019).

Conclusion

We have provided a Schwartzian framework for understanding when and under what circumstances corporate stakeholders should be able to contract around business regulations. Under this Schwartzian approach, corporate stakeholders would be able to contract around business regulations designed to protect themselves, but would not be able to give up entitlements that belong to other corporate constituents. Under this approach, at least in theory, shareholders would be able to contract around Revlon but not antitrust. To be sure, many important administrative and conceptual details would have to be ironed out before the framework could be adopted in practice. These include ensuring that stakeholders are in fact able to protect their interests, determining which constituencies in fact possess the relevant legal entitlements, and preventing certain stakeholders from invoking ESG opportunistically to holdup potential welfare-enhancing deals.