Shareholders, Unicorns and Stilts: An Analysis of Shareholder Property Rights

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SHAREHOLDERS, UNICORNS AND STILTS: AN ANALYSIS OF SHAREHOLDER PROPERTY RIGHTS

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Shareholders’ rights advocates argue that shareholders have the right to control the corporation. This article examines the basis for the claims. It begins with an analysis of rights, then moves to an analysis of legal rights, which is followed by an analysis of property rights as a species of legal rights. The article then examines the historical context, rationale and development of shareholder rights which leads to the analysis of current shareholders’ rights. It concludes with some comments and suggestions concerning future development of corporate governance thinking.

A. INTRODUCTION

“Shareholders’ rights” is the rallying cry for shareholders’ rights advocates, including lawyers, economists, investment bankers and law-and-economics scholars.1 It is a call to action, a challenge to opponents, and a warning to any party interested in a critical examination of the corporation and corporate law.2 Rights have become the ultimate weapon in many battles and have proliferated exponentially through the twentieth century.3 In fact, rights talk is so common that some scholars fear an appeal to rights is losing all significance.4 A demand for shareholders’ rights is a demand of shareholders against corporate directors, government, employees and other suppliers, for recognition and for control of

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2 Shareholder’ rights advocates are shareholder primacy advocates. For an example of a rather hostile address of non-shareholder primacy theorists, see E Sternberg, “The Defects of Stakeholder Theory” (1997) 5 Corporate Governance 1.
the corporation and the corporate agenda, and it brooks no challenge, for it is a matter of "Rights!"

The article is divided into three parts. The first part is an examination of the concept of rights in both moral and legal terms. This part discusses the nature of rights and looks to the basis of the moral strength of the rights claim. It argues that rights claims are fundamentally moral claims and that in certain instances these moral claims have been given a legal form. The legal form of rights does not necessarily carry with it the moral force of moral rights, and in such cases are rather weak rights claims. This examination sets the foundation for the analysis of property rights. The second part of the article examines the particular type of right, property rights. The argument in this part has two main thrusts. First, property rights, it is argued, are a weaker right, not in the least because of the amorphous and debated nature of property itself. Essentially, the argument is that "property rights" and "property rhetoric" have no justificatory force. The second is that even if property rights are given to have a justificatory force, shares fit only awkwardly the legal paradigm of "property". Accordingly, where one grants justificatory force to property rights, it is questionable how valid this force is with respect to shares, and further, to what extent these rights should be enforced as against other rights claimants. In essence, the argument is that shareholders cannot rely on the justificatory force of "property rights" in their claim for supremacy in the corporation. In the third part of the article, the argument turns to an examination of shareholders’ core rights—the rights to dividends, vote and residue. These rights are given a critical review which leads to the conclusion that shareholders’ rights cannot be justified by entitlement to the underlying assets of the company. In other words, a justification, which may once have had some historical validity, given the changes in the law over the last century and one half, no longer does. In sum, this latter part of the article leads to the conclusion that shareholder rights lack a clear historical, theoretical or economic foundation, and hence lack a good justification.

B. INTRODUCTION TO RIGHTS

Rights—what are they? Whenever they are raised, the nature of the debate changes. No longer is the debate a mere dispute between holders of opposing points of view. Rather, it becomes something deeper, more fundamental. As Sumner observes: "The normative function of the language of rights is to form one kind of urgent or insistent demand." In other words, whatever rights may be, they are not some type of ordinary thing like ketchup or contracts. They are an out of the ordinary—or extraordinary—type of thing.

5 Sumner, supra n 3, 15.
One hears of moral rights, legal rights, conventional rights, my rights, your rights, human rights, shareholder rights, civil rights, universal rights and rights with every type of qualifier imaginable. In all this discussion, the effort is seldom made to define exactly what type of claim is being made or what rights are. Worse, when the discussion is turned to the topic of defining rights, one finds a horribly complicated, convoluted debate with much heat and noise, but very little light. HLA Hart observed that “The notion of a legal rights has proved in the history of jurisprudence to be very elusive.” Some philosophers argue along the lines of semantics, looking for the appropriate understanding of words like “ought” and “should”, and the grammatical understanding of the word. They ask: is it a noun, or a collective, or a fact, or a signifier of something?

Other philosophers ask to what type of “fact” does the term refer. Still other philosophers, taking a linguistic analysis approach, argue that rights cannot be fully analysed because rights are a fundamental or foundational concept. Jurists examine rights in the context of legal claims. For example, a jurist will ask: “Does x have the right to possession of y?” Social reformers argue about rights to jobs and rights to education. Politicians accuse one another of human rights violations, referring equally to putting a ballot in a box and to executing one’s own citizens. In addition, just to ensure there are no positions left uncovered, mention must be made of a whole group of philosophers and jurists who deny the existence of rights.

From this medley, it is difficult, if not impossible, for the uninitiated to tease out an understanding of the notion or sketch the outlines of the debate—let alone make an application to a specific case such as shareholders—without a considerable expenditure of time and effort. Once the effort is made, however, it opens up a fascinating arena of human intellectual activity and interaction where one finds some of the most interesting and profound questions about the

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3. This is the approach taken by B Russell and L Wittgenstein, discussed in White, supra n 7, 9–10.
4. Ibid.
5. Discussed in more detail infra.
6. See generally views identified with liberalism of Rawls, Dworkin and Rorty.
9. Eg Duguit, cited in Hart on Bentham, supra n 6, 126, the pragmatists in general discussed infra and some linguistic analytic philosophers who are sceptical about rights talk as merely tautological.
organisation and governance of society being debated, discussed and developed. In such a short article obviously a comprehensive or a critical review of rights cannot be offered. Therefore only a bare outline of the discussion will be sketched out.

Rights in the western tradition go back at least as far as the Middle Ages. In that context, the discussion was focused on what is sometimes considered to be the corollary of rights, namely, duties. The duties of medieval peoples’ attention were those owed to the feudal lords and religious duties. On occasion, medieval lawyers raised the idea as a defence against encroachment by the authorities on “liberties”. In the seventeenth and eighteenth centuries, further discussion by commentators such as Blackstone developed rights theory by using expressions such as “the liberties of Englishmen” and “natural rights”. At that point, which is the true starting point for a discussion of western rights, the discussion was taken up by some of England’s pre-eminent philosophers, such as John Locke, and later by Jeremy Bentham, among others.

Whatever else one may say about rights, they are in the nature of an imperative or a normative, and as such, put the object of rights beyond the scope of discussion. As Richard Rorty, puts it:

“rights talk . . . makes political morality not a result of political discourse—of reflection, compromise, and choice of the lesser evil—but rather an unconditional moral imperative: a matter of corresponding to something antecedently [sic] given, in that the will of God or the law of nature is purportedly given.”

They are not subject to negotiation and discourse, and are given prior to any argument.

C. DISCOURSE ON RIGHTS THEORY

In the broadest definition, a discussion about rights is a discussion about moral rights. Moral rights are not in the nature of moral rules or moral advice. Moral

16 Benn, ibid.
rights, particularly as expressed in the human rights discussion, proceed from a purportedly universal objective notion of what it means to be human.\textsuperscript{20} They are expressive conceptually of such views as Kant’s elevated view of human nature: what fundamental conditions are necessary or must society aspire to in order to offer basic recognition to humans as a rational moral beings? Rights also address the issue of what limitations may be justly put on humans as rational moral beings. And from the perspective of limitations, the question is: what limitations are consistent with those aspirations? Or, what type or level of justification is an acceptable or necessary justification before one can curb another’s efforts to achieve those aspirations? One can develop a basic moral theory of rights from one’s answer to these questions\textsuperscript{21} and in turn create a platform for judging laws and government action as being in support of or contrary to rational moral beings’ rights.\textsuperscript{22}

Any investigation into rights theory leads rather promptly one to two main approaches: one based on a particular view of human nature, the other based on the existence of the state. One important approach to moral rights is Natural Rights theory. This theory, although often traced back through Aquinas to Aristotle,\textsuperscript{23} finds a seminal statement in John Locke. Locke holds that rights are inherent to human beings. As he puts it all, “men are born free and equal”\textsuperscript{24} Locke states: “The Natural Liberty (italics in original) of Man is to be free from any Superior Power on Earth . . . but to have only the Law of Nature for his Rule.”\textsuperscript{25} For Locke, rights can neither be granted nor denied, and the proper role government, as the instrument of society, is to not interfere with the exercise of those rights. The argument goes that, just as a beating heart and breathing are natural to being human, so too are rights. As can be seen from the above quote, Locke’s main concern was limiting the rights of the monarchical government in control of the country’s resources.\textsuperscript{26} So, as the monarch does not have legitimate


\textsuperscript{24} Locke, Second Treatise on Government, ch II, para 5 (hereinafter “Second Treatise”) and carried forward by HLA Hart, “Are There Any Natural Rights” (1953) 44 The Philosophical Review 175, reprinted in D Lyons (ed), Rights (Belmont, CA, Wadsworth, 1979), 14.

\textsuperscript{25} Locke ibid, ch IV, para 22.

\textsuperscript{26} Locke’s historical context is critical for understanding his views. See J Williams, “The Rhetoric of Property” (1998) 83 Iowa Law Review 277, 281–83.
control over the biological functioning of subjects, its legitimate control over other aspects of subjects’ lives are limited to those non-rights bearing aspects. This view has been taken up most forcefully in recent discussion by John Rawls.27

The alternative, antithetical view, that rights are granted by the state, was advanced nearly a century later by fellow British philosopher, Jeremy Bentham. Bentham was a conservative who supported the government. From this perspective, Bentham rightly criticised Locke’s view of rights which was used as a philosophical basis for the overthrow of the government.28 Accordingly, from Bentham’s perspective, rights are the grant of society and have no existence outside of society’s legal system.29 They are the creation of the law, and law owes its origins to government and, more importantly, to governmental enforcement. Hence the idea of rights existing apart from and as a challenge to government is a non-sequitur. He opposed any idea of rights, moral or otherwise, outside of the legal system. This view is advanced currently most vigorously by American pragmatists30 and the Realist school.31

These early starts on a theory of rights by no means ended the debate. Rather, they started a whole line of thinking taken up in the States of America in political and jurisprudential foment, leading to the founding of the US as a new country in 177632 and continuing unabated into the present. No less worthies than Ronald Dworkin33 and Richard Posner34 are engaged in the debate, as were John Rawls35 and HLA Hart36 until their deaths.

Mention must be made of an important school of thought completely at odds with the foregoing view of rights, embodied particularly in pragmatist school in the US and the deconstructionists in Europe. This view, consistent with anti-essentialist doctrine,37 denies that rights exist. As Alasdair MacIntyre puts it,
a belief in human rights “is one with belief in witches and unicorns”.38 To the extent that rights are acknowledged or discussed by pragmatists, they fall into a category of things to be analysed and allocated along the lines of economic efficiency. Jurists who belong to this school, such as Posner,39 view rights language as one aspect of law concerning the proper means of determining allocation of costs.40

Finally, mention must be made of the Critical Legal Studies school (CLS)—the modern legal realists.41 This school views law and all its components as philosophical views enforced through political structures. Accordingly, rights for CLS are neither morally based nor non-existent per se. Rights discourse, says Kennedy, “is internally inconsistent, vacuous, or circular. Legal thought can generate plausible rights justifications for almost any result.”42 Rights among these scholars are merely another means of imposing one groups’ values upon another.

One way to clarify rights discussion is by returning to Locke’s thinking,43 which was later further clarified as creating a distinction between first- and second-order rights.44 First-order rights are the rights we each presumably have in the state of nature. These are the rights enshrined in the first four articles of the Universal Declaration of Human Rights. They include such rights as the rights to life, liberty and security of person, and carry a moral imperative recognised particularly in the west.45 Second-order rights in Lockean terms are the State’s right to punish people who breach first-order rights. These second-order rights, which are rights to State provided services have been expanded to include such rights as the right to employment, education and social services.46 Second-order rights do not carry the same moral imperative as first-order rights in the west, where such things as employment, education and

38 A MacIntyre, After Virtue: A Study in Moral Theory (Notre Dame, IN, University of Notre Dame Press, 1988), 69.
39 Posner is a bit of a difficult pragmatist. He does not follow the philosophical traditions of pragmatists William James or John Dewey but identifies himself as a pragmatist in the sense usually understood by the layperson.
40 See, eg Economic Analysis of Law and The Economics of Justice, supra n 34.
45 There has been an ongoing debate as to whether human rights are truly universal or merely a western notion. C Hansen, “Do Human Rights Apply in China: A Normative Analysis of Cultural Difference” (1994) 24 Hong Kong Law Journal 387.
46 These rights are also found in the Universal Declaration of Human Rights, Arts 21–26.
social services are within the grasp of the vast majority and hence viewed as the deserved fruits of individual effort.47

We have only briefly examined the origins and idea of rights with no substantive discussion about the contents of these rights. At this point, the views diverge to an even greater degree and following their varying directions will not add to an understanding of legal rights, to which we now turn. In summary, if one is to accept the existence of rights and those rights are independent of the legal system, rights are a moral claim that, as Dworkin puts it, “trump utility”.48 In this sense, moral rights are first-order rights.

D. DISCOURSE ON LEGAL RIGHTS49

Shareholders’ rights advocates do not simply advocate a moral rights claim. The strength of their claim rests on the support that law provides for their rights. We turn now to examine the nature of legal rights. Legal rights find a foundation on both moral50 and societal bases,51 but as the foundation is weak, legal rights awkwardly straddle moral and societal views, and unsurprisingly are dismounted at times by both views. There is no escape from dealing with rights, however, because rights are central to legal discourse. In fact, one approach to understanding law is that it is adjudicating competing rights claims.52 Legal rights are especially contentious because they set limits on the will of the majority or those with power, and such limitations are not readily accepted by either the majority or the powerful. As Dworkin puts it, “A right against the Government must be a right to do something even when the majority thinks it would be wrong to do it, and even when the majority would be worse off for having it done.”53

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47 See Rorty’s scathing critique of the left and liberalism in the US in Simon, supra n 4.
49 The discussion will focus exclusively on rights in the Anglo tradition from this point forward. Legal rights in German law and French law take on a different character: see the discussions of C Dietel “das Recht” and “subjectives Rechten” in Dictionary of Legal, Commercial and Political Terms (Munich, CH Beck, 1983) and of G Cornu, “le Droit objectif” and “les droits subjectifs” in G Cornu, Vocabulaire Juridique 6em (Paris, Presses Universitaires de France, 1996) concerning German and French views respectively.
51 This is essentially the Positivist claim.
53 This anti-majoritarian aspect is at the heart of Dworkin’s view of rights. The quote is from Dworkin, supra n 22, 194.
Finally, for some, the legal system is ultimately concerned solely with the efficient allocation of rights. An analysis of legal rights finds that jurists assume three things: a legal system, the existence of rights and justification for rights—usually a moral justification—as a starting point. Hart wrote: "the concept of a right belongs to that branch of morality which is specifically concerned to determine when one person’s freedom may be limited by another’s". Legal rights analysis is therefore confined to understanding the term within a legal system.

As previously noted, Bentham viewed rights as the creation of the state, in other words, as a creation of law. Bentham identified two types of rights: those he described as “permissive”, which are not legal obligations but simply rights to do or not do an action; and (2) those he described as “coercive”, being legal obligations calling for the mandatory acts and mandatory forbearance of others. For Bentham, rights holders were the recipients of a benefit. Much discussion has followed from Bentham’s reasoning on rights, and despite an earlier view that the former “permissive” rights could not count for much, such rights have become a major focus on much subsequent debate. For Bentham, whatever else rights may be, they were clearly the product of a government created legal system.

Nearly 100 years after Bentham’s death, in 1832, legal rights theory made its next significant advance through the work of Wesley Hohfeld. Hohfeld’s analysis of rights and correlative duties remains an important starting point for much contemporary discussion. Hohfeld was particularly concerned with rights in their juridical context and developed his theory of rights as such may exist in a system of rules—legal or non-legal. Hohfeld’s theory, published in 1919, identified four types of rights, each set apposite to a “jural correlative”. The rights and jural correlatives are: claim and duty; privilege and no-right; power and liability; and immunity and disability.

The first set, claim and duty, addresses the situation in which one party has a claim to have something done and the other party has a duty to do it. This

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54 See, eg Posner, supra n 34.
55 Natural Rights, supra n 24, 16.
56 The interesting collision of moral and legal rights finds its most vocal expression in the civil disobedience literature. See, eg Dworkin, supra n 22.
57 My discussion of Bentham throughout this article relies heavily on Hart on Bentham, supra n 6.
58 Hart on Bentham, ibid.
59 This aspect of Bentham’s theory was subjected to Hart’s critical eye, and arguably did not survive the scrutiny. As Hart pointed out, a third party can be the beneficiary of a duty on the second party who received the duty by contracting with the first party. See Hart on Bentham, supra n 6, 125.
60 Early doubt about the importance of the permissive right noted by Hart on Bentham, supra n 6, 128, and for the importance of the concept since Hart’s article, any survey of the absolutist property rights advocates’ literature will suffice.
61 Sumner, supra n 3, 20.
relation provides the claiming party with a right. The second set of correlatives, privilege and no-right, is the situation in which a person is at liberty to do or not to do something, the correlative of which is a person not having that liberty.

Hohfeld states that power and liability correlatives address the ability to change juridical relations—i.e., one party’s power to create or do something that changes another party’s liabilities by operation of law. The final correlatives, immunity and disability, deal with parties’ immunity from the effects of law or judicial pronouncements, and another party’s inability to change the first party’s jural relations. Since Hohfeld’s time, rights theorists have tended to collapse his power rights and immunity rights into his first two categories of liberty rights and claims rights, with an emphasis on claim rights—that is, the rights to claim the benefit of another’s duty.

Hohfeld’s idea is that having a right puts one at an advantage, and this view is labelled by later theorists as the “benefit theory.” Despite various critiques, the theory continues to hold explanatory power in terms of normative rights discussions. This view has been taken up by scholars such as MacCormick and Raz, who are of the view that the essence of legal rights is the protection of a party’s interests by imposing corresponding duties on other parties. The theory’s philosophical basis is prudential: that is to say, it places a duty on everyone to refrain from interfering because only by doing so, will one have the benefit of rights. This theory is discussed in the literature as “interest or benefit theory.”

Following Bentham’s vein is Hart’s theory. Like Bentham, Hart holds that rights holders have two basic types of rights: (1) permissions—which Hart dubs “bilateral” because the right or permission includes the right to act as well as the permission not to act; and (2) duties owed to one which can be enforced or

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64 My summary is based on Benn’s analysis, supra n 15.
65 See, eg P Jones, Rights (Basingstoke, Macmillan, 1994).
66 Sumner, supra n 3, 45.
67 See, eg Sumner, supra n 3, 32–54; Hart, supra n 23; and A Hagerstrom, Inquiries into the Nature of Law and Morals (Uppsala, Almqvist & Wiksell Boktryckeri Aktiebolag, 1953) CD Broad (trans), cited in Benn, supra n 15.
68 See, eg Sumner’s discussion supra n 3, 18–33.
71 Campbell, supra n 30, states that this view is held by Austin, MacCormick and Raz.
72 Sumner, supra n 3, 45.
73 Hart on Bentham, supra n 6.
waived. In this view, Hart fits in with the group of philosophers who believe that legal rights concern choice and control or a “claim” over corresponding duties and that the issue of rights is “so to determine what actions may appropriately be made to subject of coercive legal rules.” This view is premised on a particular view of human nature as having an innate capacity for freedom. Hart describes rights as flowing from this one natural right: “the equal right of all men to be free.” Hart’s view is that legal rights are rights to choose or control a corresponding duty and unsurprisingly, the rights theory is called the “choice or will theory.”

An altogether different approach to legal rights has been developed by the moral philosopher and legal scholar, Ronald Dworkin. Dworkin’s view is that rights are primary points or claims in a discussion and stand out from and above all other claims. For Dworkin, given the moral basis for rights, they are essentially non-negotiable. As he puts it, they are an expression “too central to personality, too much at the core of liberty” to be negotiated away on some supposed benefit to others.

Dworkin’s arch-rival is the pragmatist Richard Posner. Posner’s view of rights has little to do with any of the theories of legal rights just discussed. Essentially, following the work of R Coase, Posner has developed a legal theory based completely on the economic costs of rights. Legal rights are little more than tools for expressing or identifying a cost that should be acknowledged or

74 Ibid.
75 Hart, supra n 24, 16.
76 Ibid, 14.
77 Sumner, supra n 3, 46. Note that Campbell, supra n 50, views Wellman as another jurist who adopts this view.
79 Dworkin’s view is particularly valuable in an analysis of constitutional rights; however, in broader discussions of rights, it appears to lack balance for rights lesser significance.
81 R Rorty, perhaps more representative of American pragmatist philosophers, completely upsets the situation declaring, that rights talk in the political discourse is “a pointless importation of legal discourse into politics”. In other words, there are no rights except legal rights, supra n 19, 302.
83 Interestingly, the pragmatist Rorty distances himself from both Dworkin, whom he views as a pragmatist, and Posner, putting them in the same group, writing, “For myself, I find it hard to discern any interesting philosophical differences between . . . Dworkin and Posner; their differences strike me as entirely political”. In “The Banality of Pragmatism and the Poetry of Justice”, in M Brint and W Weaver (eds), Pragmatism in Law and Society (Boulder, CO, Westview Press, 1990), reprinted in Philosophy and Social Hope, supra n 37, 94.
addressed by the legal system, whose job it is to evaluate and allocate those costs in a wealth maximising manner.\textsuperscript{85} In fact, Posner has described rights as “law’s metaphysical balloons”.\textsuperscript{86}

None of these explanations of legal rights, however, move beyond the moral or systemic approaches to rights. They provide no information about content of legal rights or their appropriate use in legal disputes. Regardless of their origin or nature, all parties recognise legal rights—as each defines them—as a critical tool in legal analysis. Shareholders’ rights advocates stake their legal rights claim on the basis of their property in shares. Accordingly, we now turn to examine property rights.

\textbf{E. Property Rights}\textsuperscript{87}

One especially important area of legal rights, particularly in a capitalist economy, is the area of property rights.\textsuperscript{88} Property law forms the basis for claims concerning the control of resources, capital and the means of production. It is a notoriously difficult area of law, perhaps in part because it is really a subspecies or particularisation of the complex area of Rights just discussed.\textsuperscript{89} Rather than a complete canvassing of all the theories of property law, this article will attempt to identify some core concepts of property to create a paradigm of property that resonates with the shareholder property rights advocates’ discourse.\textsuperscript{90}

Perhaps the best place to start is with Blackstone’s famous comment:

“There is nothing which so generally strikes the imagination, and engages the affections of mankind, as the right of property: or that sole and despotic dominion

\footnotesize{\textsuperscript{85} Posner, \textit{Economic Analysis of Law}, supra n 34.}


\footnotesize{\textsuperscript{87} As will be discussed within, the nature and role of property rights in western legal systems remains radically undecided.}

\footnotesize{\textsuperscript{88} Berle and Means observed “[property] the very foundation on which the economic order of the past three centuries has rested”, in \textit{1932 (New York, The Macmillan Company, 1932), 7–8, quoted in C Holderness, “Joint Ownership and Alienability” (2003) 23 \textit{International Review of Law and Economics} 75.}

\footnotesize{\textsuperscript{89} In a surprisingly passed over comment, Hart identifies rights as “moral property”. Hart, \textsuperscript{89} supra n 24, 19. He says they are “typically conceived of as possessed or owned by or belonging to individuals”.}

\footnotesize{\textsuperscript{90} Discussion will be restricted exclusively to legal analysis of property and only venture briefly into a Law and Economics analysis.}
which one man claims and exercises over the external things of the world, in total exclusion of the right of any other individual in the universe.\textsuperscript{91}

There are three things worthy of note in Blackstone’s comment: (1) property is absolute; (2) it can be equated with a thing; and (3) it is exclusive. This little area of the universe over which a person has absolute dominion—or “property rights”, as Blackstone has it—in fact expresses views found roughly in his predecessor, Locke, and carries sentiments surprisingly common in contemporary thought.

1. Is Property Absolute?

Locke posited two founding points for his argument for property rights: a general gift from God to all “mankind” and from a supposed State of Nature.\textsuperscript{92} God, says Locke, gave the earth and all its resources to mankind in general for his sustenance. From this position, with an intermediary step in which humans apply labour to common property, or “mix” labour with commons, he ends up with a theory of private property.\textsuperscript{93} Essentially, Locke’s view is that one appropriates from the wild or from the commons, to create private property.\textsuperscript{94} That which has been appropriated/tamed/claimed from the commons is the private property of the appropriator/tamer/claimer.

He justifies this argument by basing the common–private distinction on the hypothetical, wild state in which each human chooses to declare a truce with the natural war in order to create a society, to surrender the right to unmitigated warfare for the mutual benefits of peace. Locke supposed that individuals came to society of their own accord, with free will, as independent free moral agents, and thus maintained that status and corollary rights against the society which they formed. For Locke, then, the fundamental justification for private property is that it is God-given to each individual for the purpose of sustenance and so its coordination with or by the state can only be with the consent of the individual.

Although popular and enduring, Locke’s argument for private property—mixing one’s labour with nature’s common resources—suffers from some fundamental flaws.\textsuperscript{95} For example, why is it that mixing one’s labour should

\textsuperscript{91} Blackstone, supra n 17. Obviously his statement is by no means a complete statement of Blackstone’s position. Indeed, as F McDonald observes, “he [Blackstone] devoted the next 518 pages of Book 2 . . . to qualifying and specifying the exceptions to his definition”. Quoted in J Williams, supra n 26, 281.
\textsuperscript{92} This claim is made in his First Treatise, para 26. Locke’s major discussion of property is in his Second Treatises on Government, supra n 24, ch 5 paras 24–51.
\textsuperscript{94} Williams, supra n 26, 284–88.
\textsuperscript{95} My critique of Locke is based on McGregor, supra n 92, and G Sreenivasan, The Limits of Lockean Rights in Property 11 (Oxford University Press, 1995).
create private property instead of adding to the common.\textsuperscript{96} A further criticism advanced by Kant is that in order to mix one’s labour with something, one must appropriate it. If one appropriates it before one has mixed one’s labour, one fails to have the essential Lockean right to appropriate it in the first place.\textsuperscript{97}

Another argument in support of the mixing theory is based on the view that the value added by the labour may be disproportionately higher to the nominal value of the thing in its natural state. This argument too, however, is specious as some people may well value a thing in its natural state more than after mixing,\textsuperscript{98} and it still fails to explain why it entitles the labourer to appropriation as opposed to entitling society to the benefit with the labour merely adding to the commons. This problem with Locke’s argument was recognised by, among others, John Stuart Mill.\textsuperscript{99} Finally, one must mention Locke’s own recognition of the limitations on acquisition rights. Locke held that acquisition was justified only so long as “there is enough and as good left in common for others”.\textsuperscript{100} He further proposed that private property holds legitimacy only within the further, somewhat awkwardly put, limit of “As much as anyone can make use of to any advantage of life before it spoils”.\textsuperscript{101}

Contemporary property rights theorists who hold that property rights are fundamental and absolute\textsuperscript{102} develop their position from Locke after having jettisoned his proposed limitation. Their view, like Locke’s, is that property rights are natural or “God-given”, and as such should have the least interference from the state. Again, one can turn to Blackstone for a basic expression of the position: “so great moreover is regard of the law for private property that it will not authorise the least violation of it; no, not even for the good of the whole community”.\textsuperscript{103} Many of these theorists have developed stronger views since Regulatory Takings legislation developed in the United States since the 1970s.\textsuperscript{104} Their views have considerable overlap of the simplified view of property as

\textsuperscript{96} R Nozick (\textit{supra} n 44, 175) makes this criticism observing, “If I own a can of tomato juice and spill it in the sea so that its molecules (made radio active so I can check this) mingle evenly throughout the sea, do I thereby come to own the sea, or have I foolishly dissipated my tomato juice?”


\textsuperscript{98} McGregor, \textit{supra} n 93, 402.


\textsuperscript{100} \textit{Second Treatise}, \textit{supra} n 24, ch 5, para 27.

\textsuperscript{101} Ibid, para 31.


\textsuperscript{103} Commentaries 135.

\textsuperscript{104} R Epstein notes that governmental takings have been a concern since the nineteenth century at least in “The ‘Necessary’ History of Property and Liberty” (2003) 6 \textit{Chapman Law Review} 1, available at http://articles.ssrn.com/sol3/delivery.cfm/SSRN_ID396600_code030421570.pdf?abstractid=396600, accessed on 3 June 2005. It seems, however, that the current interest and response has resulted from the more recent legislation.
“thing”—discussed below—over which those with property rights have control.105

A second group of property rights theorists take a somewhat more restrained approach. 106 This group usually starts with Hohfeld and his famous “bundle of rights” paradigm—being an application of his rights theory discussed previously—and then turns to Honore to make a problematic combination of the two systems.107 Hohfeld wrote:

“Suppose, for example, that A is fee-simple owner of Blackacre. His ‘legal interest’ or ‘property’ relating to the tangible object that we call land consists of a complex aggregate of rights (or claims), privileges, powers, and immunities.”108

Hohfeld’s contribution, unfortunately still in a preliminary stage at the time of his death,109 is his idea that property is an aggregate of rights concerning jural relations between parties.110 As a set of relationships between parties, it is exceedingly difficult to view property as absolute. Legal relationships, like all other human relationships, tend to be fluid and dynamic.

Honore, by way of contrast, identified “ownership” as the fundamental issue in property: that is to say, property is a matter of having “incidents”. Honore identified the following as the incidents of ownership: the right to possess, the right to use, the right to manage, the right to the income of the things, the right to the capital, the right to security, the rights or incidents of transmissibility and the absence of term, the prohibition of harmful use, the liability to execution and the incident of residuarity.111 Honore observes that the standards of ownership apply “to the person who has the greatest interest in a thing admitted by a mature legal system”.112 In contrast to Hohfeld’s relational view, Honore views property rights as ownership of “rights to a thing”. 113 Honore’s view too challenges the Blackstone notion of property as absolute. His hodgepodge of rights forming ownership creates an uncertain bundle of which one can never be sure of having all possible rights.

105 See discussions on various popular and expert views of property in Williams, supra n 26, and a revealing article by M Duncan, “Reconceiving the Bundle of Sticks: Land as a Community-based Resource” (2002) 32 Environmental Law 773.

106 Interestingly, both camps claim to be in the dominant position. Penner, supra n 93, notes the bundle of rights as the dominant paradigm, 714. G Alexander, “Property as a Fundamental Constitutional Rights? The German Example” (2003) 88 Cornell Law Review 733, 734 notes the same phenomenon.

107 The problems with this view of property are thoroughly critiqued in Penner, supra n 93. Penner observes (714): “this ‘dominant paradigm’ [bundle of rights] is really no explanatory model at all, but represents the absence of one. ‘Property is a bundle of rights’ is little more than a slogan.”

108 W Hohfeld, quoted in Penner, supra n 93.

109 Cook, supra n 62, 13.

110 Penner, supra n 93, 731.


112 Ibid, 732.
Fundamentally, property is a concept created by law, and as such, is subject to the law and thus not independent or absolute. It can be defended by a call to a police officer, litigated in a court or taxed by a government. It cannot be used in any manner the owner may wish, as owners are not permitted generally to use their property to harm indiscriminately. Its use is subject to law as well. Each of these activities recognises that, in some form or manner, property does not exist outside of the law and hence is not absolute. Blackstone’s bald assertion is evidently unfounded as demonstrated that the notion of property is a weak contender for election to the category of absolutes. In no sense is property properly absolute.

2. Is Property a Thing?

Blackstone’s second element of property is that it deals with “the external things of this world”. Kevin Grey’s aptly titled article “Property in Thin Air” clarifies whatever misconceptions concerning the physical nature of property that may have remained. He argues eloquently and convincingly that property is not a thing, using as his illustration empty space. Gray indicates that property can exist where there is nothing, literally no thing.

Another approach to property in a similar vein is the brilliant discussion concerning the social construction of property in Michael Walzer’s work, Spheres of Justice. Walzer’s analysis makes it clear that property does not exist prior to its creation by humans, who, through the acts of perception, delimitation, identification, valuation and ascription of certain rights, create it. The whole notion of property depends on each of the previously listed intangibles and notably, as distinct from other human creations, the processes of delimitation, value ascription and rights.

Among recent law and economics thinking about property rights, the theories of Guido Calabresi and Douglas Melamed have come into prominence. Their study is focused on “entitlements”, and in particular the preferences between property, liability and the role of inalienability in such...
determinations. Their studies indicate that property rights are a type of right granted when transaction costs are low; when transaction costs are high, the law prefers liability. In their analysis property rights and liability duties are merely opposite sides of the same entitlement coin, interchangeable on the basis of efficiency. The difference between property—a permission right—and liability—a coercion duty—is the question of efficiency in terms of transaction costs. A further distinction is that property rights transactions are voluntary, whereas liability rules address involuntary transactions of property. The final part of their analysis addresses the question of which, and under what conditions, property entitlements and liability entitlements are alienable or, more importantly, inalienable.

Inalienability rules, say Calabresi and Melamed, apply when the government does not permit property or liability entitlements to be traded between parties. They claim that inalienability rules come into play when two conditions are met: (1) when a transaction would create significant externality costs; and (2) when these costs are not susceptible to objective valuation or monetisation, which situation they refer to as “moralisms.” Where entitlements are on questionable or undecided moral grounds, inalienability rules, regardless of the wishes of the parties, are usually enacted or judicially determined. Inalienability is essentially a denial of property, from a law and economics perspective for being able to freely transact rights, i.e., alienability is generally considered to be a hallmark of property.

From the foregoing arguments of Grey, Walzer and Calabresi and Melamed, it is clear that property is not a thing but an idea, flexible and malleable, and dependent on circumstance and perspective.

119 As will be discussed later, shareholders have a property right as between themselves and other securities market participants; however, it seems that they have an unrecognised liability vis-à-vis other parties both in the corporation and in the community. Corporations have a liability to the non-property participants of society that is not recognised. Some may argue that the liabilities—such as clean environment and non-concentration of wealth—are or ought to be inalienable.
120 In addition, they note that property rights are transferred more or less at the time of payment, whereas liability rights are paid for post facto. This distinction is not significant for shareholders’ rights discussion.
121 Calabresi, supra n 117, 1111–12.
122 Various other law and economics scholars have contributed to the debate; however, space does not allow a thorough review and analysis. In selecting Calabresi and Melamed, I hope to be able to provide some analysis of shareholder rights that is more meaningful to the reader. Other relatively recent law and economics book length works include J Christman, The Myth Of Property: Toward An Egalitarian Theory Of Ownership (Oxford University Press, 1994); S Munzer, A Theory Of Property (Cambridge University Press, 1990); J Waldron, The Right To Private Property (Oxford University Press, 1988); Epstein, supra n 102.
3. Is Property Exclusive?

More recently, JE Penner has picked up on the third of Blackstone’s elements of property—namely, that it operates “in total exclusion of the right of any other individual in the universe”. Penner has argued that the ultimate or uniquely characterising feature of property is the right to exclude other parties from a thing. Penner attacks the bundle of rights theory of property proposed by Hohfeld and Honore, suggesting that it is a weak descriptor rather than either a theory or a useful analytical tool. He argues that property, like other areas of law, can and indeed does have a unified conceptual core. Through his careful analysis with particular attention to the concepts of rights in rem, Penner argues that property, rather than being a right to exclude, is more a universal duty on the world in general not to interfere. The “thinghood” is the object of property mediating between the owner and the world, the universal duty of non-interference.

Penner draws from Moore v Regents of University of California, in which the courts denied the plaintiff, Moore, the right to profit from cells taken from his body in a medical procedure and subsequently commercialised, that property cannot be delimited by stating that property is limited to things that have value. The court declared that Moore had no property in his body, but that the Regents of the University of California had property in the commercialised, modified cells. Penner demolishes the “magical” view that by some action, some thing suddenly becomes property. Penner observes that property occurs or is created in socially determined contexts and temporally determined contexts such that a particular object may at one time be the object of property and at another time not. He describes this as the contingency aspect of property. Property, therefore, says Penner, is a legal concept of things in a particular contingent circumstance in which we stand in the privileged position in which the world in general owes us the duty to abstain from interference. It seems that if Penner’s view is correct, property is nearly whimsical, at one moment existing, at another not. In other words, whether one can be excluded depends, at least in part, on the timing. Certainly, this capricious nature of property may suggest a more conservative approach to exercising exclusivity rights as time’s passage may well change the situation.

123 Penner, supra n 93. This position is explicitly attacked by Mossoff, supra n 15.
125 Summarised succinctly, ibid, 817–18.
126 793 2d 479 (Cal. 1990), discussed in Penner, ibid, 718–22.
127 Penner, ibid, 716–17.
3. Property in Contemporary Legal Thought—Vaporisation of the Concept

Blackstone’s orthodox, traditional view of property, supported in recent years by scholars such as Penner, has come under considerable attack. For, despite the seeming clarity of property rights as set out in the discussion to this point, a deeper investigation into the nature of property itself has led many legal scholars to a sceptical position. From an economic and political perspective, Thomas Grey, for example, whose opinion may be taken to be representative of a number of these scholars, holds that property at its foundation is simply another legal rule, and that essentially property has “disintegrated . . . [and] ceased to be an important category in legal and political philosophy”.

Grey is arguing that property rights have no special or distinctive character but are merely another way of describing what is left or assigned after a dispute about resource use is resolved. As Joseph Sax has it: “property is the end result of a process of competition among inconsistent and contending economic values . . . The value which each owner has left after the inconsistencies between the two competing owners has been resolved.” In other words, property rights are simply legal rights to which the word “property” adds nothing.

Perhaps the most thoroughgoing and rigorous critique in contemporary legal scholarship of the whole notion of property is found in the work of the Cambridge scholar Kevin Gray. Gray agrees that excludability is among property’s traditional three indicia and an important feature of property. He argues, among other things, that excludability is severely limited by the limits imposed by moral and social concerns, and that it is subject to change over time. He points out the ideological premises separate property arguments from other legal arguments, and particularly on the

“premises that relate to fundamentally divergent opinions about the proper relation between self-reliance, self-determination and community regulation; about the social and economic balance between individualism and paternalism; about the tension between individual and collective responsibility for actions which, in truth, are never quite free-willed but which are never quite deterministic either.”


130 Sax, supra n 129, 61.

131 Gray, supra n 114.

132 Gray points to assignability, enforceability, and excludability. Ibid, 292.

133 Ibid, 301.

Property, however, is not a mere exclusion of others from property, or a duty not to interfere as Penner would have it, but a means to “concretize individual needs and aspirations and to protect a shared base of constructive human interactions”. In other words, it is purposive, advancing social good. It is “but a shadow of the individual and collective human response to a world of limited resources and attenuated altruism”. As to its fundamental nature, Gray talks of “deep scepticism” and states “beyond the irreducible constraints imposed by the idea of excludability, ‘property’ terminology is merely talk without substance—a filling of empty space with empty words”. He holds that “‘Property’ remains ultimately an emotive phrase in search of a meaning”.

The significant conclusion from this debate for the purpose of this article is to note that property has undergone a radical metamorphosis since Blackstone’s definition. Even if one is not prepared to go as far as Gray, it must be conceded that at least property is malleable, abstract and broadly assignable. Property is a group of rules allocating power over a resource at a particular time according to the prevailing consensus in the law. Property is not something inherent or fixed in the thing itself.

In terms of rights, property rights may be viewed as both permissive and coercive rights. That is, property permits parties to act or not act in certain ways, as well as coercing other parties to act or not act in certain ways. Furthermore, property rights can be characterised as being “choice or will” rights in that they permit property rights holders to control how parties act. Equally, property rights demonstrate aspects of “interest and benefit” in that they serve to protect interests and benefits of property rights holders. Property rights can be categorised as power and liability because a property right may grant one power to change jural relationships of another, such as by posting a “No Trespassing” sign on real estate interests, and so create or change a liability for a third party who may wish to pass across the real estate. From the foregoing, it is evident that a general rights analysis, although illuminating, is not conclusive when applied to property rights. Perhaps the best analysis is that of Sumner, who places property rights as a type of liberty right where “its periphery consists of further elements (especially claims, but also powers and immunities) whose function is to enhance and protect the core liberty”. Of course, this is merely another way of expressing property as a type of Hohfeldian claim right, which, as applied by Penner to property, is simply the right to claim the duty as against the rest of the world to leave one in peace.

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135 Ibid, 305.
136 Ibid, 297.
139 Sumner, supra n 3, 77.
Property rights, in summary, concern relations between persons, determining a general duty not to interfere, and may include a limited alienability right as pertaining to a thing. Property rights tend to be limited to entitlements which have low transaction costs—ie where a market exists—and, furthermore, to those transactions not limited by moralisms. Most importantly, property, if one chooses to accept it at a meaningful legal category, is a malleable, arbitrary assignment of power ostensibly assigned on economic or fairness grounds. Regardless of the view one takes, in considering the moral claim shareholders’ rights advocates attempt to invoke, one would do well to heed Gray’s words: “The value-laden mystique generated by appeals to the ‘property’ exerts a powerful and yet wholly spurious moral leverage.” In other words, property is empty of legal content and wholly void of moral imperative.

F. SHAREHOLDERS RIGHTS

Against this background of rights theory and property law, we turn now to our discussion of shareholder rights. The question concerning shareholders’ rights is another approach to the larger question: whom should the corporation serve? This question has had several, sharply debated answers. How one answers the question of whom the corporation should serve determines in turn who should control the corporation. Corporate control has its own set of objectives which include investor protection, functioning of the economy, social development, public good, wealth creation and technological advancement.

140 Gray, supra n 114, 305. Gray and other property critics have drawn replies from various writers, including Penner whose work has been discussed above. The reply, in essence, acknowledges that property has come a long way from Blackstone’s absolutist proposition, but that it remains a significant but flexible concept. Property, the defenders reply, is a valid and valuable legal concept dealing with objects, conditions of ownership, and incidents of ownership in some for or other. See, eg E Sherwin, “Two and Three-dimensional Property Rights” (1997) 29 Arizona State Law Journal 1075, and Mossoff, supra n 15.

141 This question frames the classic and ongoing shareholder-stakeholder debate, initiated by Professors Berle and Dodd in the 1930s. See A Sommer, “Whom Should the Corporation Serve? The Berle-Dodd Debate Revisited Sixty Years Later” (1991) 16 Delaware Journal of Corporate Law 33.

142 The meaning of the term “corporate control” is not easy to determine. Farrar observes: “Corporate control . . . is another of those concepts that start from a legal base but ultimately transcend law.” J Farrar, Corporate Governance in Australia and New Zealand (Melbourne, Oxford University Press, 2001), 42. But its importance is beyond question. Again Farrar, “Indeed one could argue that, together with the possibility of diffused ownership, corporate control is the essence of the modern corporation” (ibid, 42). Farrar identifies five candidates as determining “corporate control” within the corporation and four external market elements of corporate control all exerting pressure on the corporation (ibid, 42–53).

143 Generally, the broad version of the corporate governance debate. See S Turnbull, “Corporate Governance: Its Scope, Concerns and Theories” (1997) 5 Corporate Governance 180, 181.
Approaches to answering the question of corporate control are made from various angles. Some scholars approach it from the angle of founding investors,144 others from the perspective of the objects of the corporation (for the public good or for private ends),145 others from its legal nature (whether a separate entity or a concession from the government).146 Still others consider the corporation from a nexus of contracts perspective,147 while others emphasise external market pressures and the efficiency perspective.148 Some scholars argue from the corporation’s role in society as a powerful economic entity controlling limited resources in a democratic society,149 and yet others argue from the perspective of the corporation as a means of owning production and separating it from workers,150 among any number of analyses.

The shareholder rights approach, which argues that the corporation should be controlled by and for the benefit of the shareholders, requires particular attention because of its dominance as the particularised version of the shareholder primacy model of the corporation promoted particularly by the law and economics and management scholars.151 Concisely, shareholders’ rights advocates argue that shareholders should control the corporation and they develop a series of arguments to support their view from various ideas on rights, legal rights, property and history. Of particular interest to shareholders’ rights advocates are the rights that give shareholders the maximum control: the “core rights”,152 namely the absolute right to all profits of the corporation—save taxes153—the absolute right to vote for all the directors of the corporation and

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146 Discussed in Farrar, supra n 142, 23.
147 This is Berle and Means, “The Nature of the Firm” (1937) 4 Economia (NS) 386, and NS Buchanan, The Economics of Corporate Enterprise (New York, Henry Holt, 1940).
150 This, of course, is the Marxist critique of corporations.
153 There is constant pressure on governments to reduce taxes and the current administration in the US seems to be falling into step with these demands more than previous governments.
the absolute right to the entire residue on the winding-up of the corporation. These rights, they argue, are property rights and thus inviolable, protected from any and all encroachment or diminution. While certainly there are numerous rights available to shareholders,154 these three form the core rights of all shares and are the foundation on which shareholder advocates stand and base their claim.

To help develop an appropriate perspective from which to analyse shareholder property rights arguments, certain aspects of corporate legal history will be briefly reviewed, and general comments and observations concerning shareholder rights will be made. This review will be followed by a review of the legal nature of shares which will lead into a specific analysis of the rights shareholders have and to a limited extent, their justifications.155

1. Early Corporations, Shareholders, and Control

Historically, corporate enterprises were established for the public “good”.156 Such “good” included supporting the European invasions of other continents,157 establishing colonies and extracting wealth for the Crown and investors, and for developing urban settlements and mercantilist/capitalist economies—which again produced more wealth for the Crown and investors.158 These corporations, such as the joint stockholder corporation, today would be considered partnerships and not business corporations.159 At law, the directors of these corporations were viewed as agents for the shareholders.160 These corporations

155 It is beyond the scope of this article to analyse these claims critically in depth. A well-thought-out piece doing exactly such an analysis on the three rights is L Stout, Bad and Not-so-bad Arguments for Shareholder Primacy, UCLA School of Law, Research Article No 25, Law and Economics Research Article No 02-24.
156 See Hill, Public Beginnings, supra n 145, 1, and Farrar, supra n 142, 23. Smith, although arguing for the opposite outcome, observes that the judgement in the famous Dartmouth College case of 1819 reads in part: “The objects for which a corporation is created are universally such as the government wishes to promote.” G Smith, “The Shareholder Primacy Norm” (1998) 23 The Journal of Corporation Law 277, 293 (hereinafter “Smith, Primacy”).
157 For an interesting recent critical reading of this history, see J Diamond, Germs, Guns and Steel (New York, WW Norton, 1997), 67–82.
158 See discussion of W Johnson, “Overview of Corporate Law: Past, Present and Future”, in K McGuinness, The Law and Practice of Canadian Business Corporations (Toronto, Butterworths, 1999), lxiii. Smith, Primacy, supra n 156, 296 quotes the preamble of the 1795 North Carolina statute creating a canal cutting corporation which identified the public purpose of the corporation as: “cutting canals has been productive of great wealth and convenience . . . contribute[s] to the wealth and revenue of this state... promote[s] health, reclaim[s] immense quantities of our most fertile lands, and in a peculiar manner tend[s] to the wealth and welfare of this state.”
159 Johnson observes that many of the joint-stocks companies were in fact partnerships. Ibid, lxiii, noted also in Hill, Visions, supra n 149, 42.
did not have the benefits of limited liability and had illiquid markets for their shares. In fact, prior to 1825 there was no particular market for stock.161

The main method of control over the activities of these early corporations was the authority granted to the corporation in its charter.162 Early corporate charters were not easily come by and required an act of the legislature or concession directly from the Crown.163 Early corporations were permitted to act only within the strict limitations set out in their charters and any actions reaching beyond those authorised in the charter were ultra vires.164 Corporate charters were public records, and any party wishing to deal with the corporation was deemed to have notice of the nature of the permissions and restrictions found in the charter.165 Ultra vires acts were not binding on the corporation: they were a nullity and as such did not create a liability on the shareholders.166 This ultra vires doctrine was of considerable significance because in the early corporation the shareholders were personally liable for the debts of the corporation.

The public nature of charters served not only as notice to the public at large but also to protect shareholders.167 Potential investors knew what the limits of the corporation’s authority were to be. They had assurance that their investment would be controlled or limited to the particular set of risks they were willing to accept as set out in the corporate charter.168 It could be argued that these charter limits put the shareholders in control of the corporation—if only by default—in that they would not invest in an uninteresting or overly risky corporation.169
Shareholders had the right or the security that their investment would be used for these purposes and for nothing more.

Further, early corporate law viewed the corporation as being composed of its members. Share capital represented merely the capital invested by the founders of the corporation at its formation.170 There was no company apart from the member/investor/stockholders. For example, an early New York charter reads in part: “That immediately from and after the filing and recording in manner aforesaid the list of subscribers . . . the persons therein named . . . shall be and hereby created and made a corporation and body politic and in name . . .”171 Likewise in English law a body corporate was made up of “several individuals, united in such a manner that they and their successor constitute but one person in law, a person distinct from that of any of the members, though made up of them all”.172 Without the members, the corporation ceased to exist.

Where members of a “company” in a joint stockholder company bear all the liabilities of a partnership and form nothing further than a group assembled for business, and each member carries the incidents of ownership, including liability, “ownership” rights are at least to some degree justified.173 Shareholders had direct property rights in the assets of the corporation, not just in the shares.174 At this point in the development of corporate law, the argument for shareholder control based on ownership easily follows from the Lockean view of property where one accepts property justification based on creating something by one’s own activity—in the case of a corporation joining a group and investing funds together.175 In Lockean thought, where one has formed the group, one ought to have the right to own it in an Honorean sense. One can argue that shareholders’ property should include a complete Hohfeldian bundle and a significant portion of Honore’s incidents.176 Thus, where one views the

170 Smith, Primacy, supra n 156, 297. Smith quotes from a 1792 New York corporate charter which reads: “stockholders . . . shall be and are hereby created and made a corporation and body politic in fact and in name”. Early American corporate law can be found in the first complete treatment of the subject by K Angell and S Ames, Treatise on the Law of Private Corporations Aggregate 7 (1832) and in Joseph Davis, Essays in the Earlier History of American Corporations 18–19 (1917), both cited in Smith, Primacy, ibid, nn 79 and 89 respectively.

171 From An Act for establishing the Western Inland Lock Navigation in the State of New York (30 March 1792), ch 40, quoted in Smith, Primacy, ibid, 297.

172 JW Smith, Mercantile Law (London, Maxwell, 3rd edn, 1843) quoted Company, supra n 161, 39 fn 47.

173 Discussed in Ireland, Company, supra n 161, 38–41.

174 In the 1837 case of Bligh v Brent (2 Y & C Ex. 260), for example, counsel argued that shares were realty because “the shareholders has an estate of the same nature as the company” and as the company owned real estate, so the shares must be considered realty. Cited in Grigg-Spall, supra n 161.

175 Bird argues that Locke’s view is contra this corporate body as the investors are severed from the activities. H Bird, “A Critique of the Proprietary Nation of Share Rights in Australian Publicly Listed Corporations” (1998) 22 Melbourne University Law Review 131, 148–9.

corporation as an entity not separate from the shareholders but rather resulting from the effort and coordination of the shareholders, all rights related to, concerning and arising out of the corporation are properly property rights of the shareholders. Equally, however, one can argue that the Lockean justification undermines any claim for shareholder property rights in that most shareholders are trading on the secondary market and so add nothing to the equation of nature and labour that underpins the Lockean justification.177

In this view of “company”—ie a collective of individual humans—the government is doing nothing more than acknowledging the “natural formation” of the corporation.178 Accordingly, a Benthamite view of property rights here is apropos as well. The government is bestowing rights on a group of individual subjects. It is interesting to note, by way of contrast, that a Benthamite view of property rights could just as easily place the corporation in a very different light. As Bentham viewed all rights, including property rights, as a grant or concession from the government, again contrary to Locke, there are no special or inherent rights given to founders of any entity including a corporate entity. Any property rights a shareholder may have would be those granted by the government, and accordingly, any Hohfeldian relations and Honorean incidents are those granted or permitted on the whim of the government to serve its own ends by distributing political and economic power as it sees fit.

Still, following from the investor-founders paradigm, the people who make up the corporate body, the shareholders, have the right to claim control in the joint stock companies. It is this view, more than any other, which gives power to the claim for the primacy of shareholders’ rights. And it is completely consistent with this perspective, that one views shareholders as “owners of the corporation”.

The historic view of shareholders as being the company, however, does not fit the contemporary legal reality.179 Law severed the shareholder’s connection with the assets of the corporation in the nineteenth century,180 and in a type of trade-off limited the liability or risk of the shareholder for the debts of the corporation. The corporation was given an independent identity and legal status wholly apart from the member/shareholders, and accordingly, ever since, the corporation has owned its assets separate and apart from the shareholders. The shareholder is a distinct and separate person from the corporation.181 It follows

177 This argument is made by Bird, supra n 175.
179 See Grantham’s powerful analysis of the development of corporate law, supra n 154.
180 In the case of Bligh v Brent, supra n 174, the court severed the connection between the share and the assets of the corporation. It held, for the first time in legal history, that shares were a form of personality.
181 Salomon v Salomon & Co Ltd. [1897] AC 22; 66 LJCh 35.
that, at this point, shareholders no longer have property rights in the assets of
the corporation. Instead they hold a type of personal property, a right to income
or “title to revenue”, a discussion of which follows. Law did not stop at that
point; indeed, it has continued to take rights away from shareholders, including,
among others, the right to manage.182

2. The Legal Nature of Shares

In this section, the legal nature of the share will be examined, namely, how the
law treats it as a whole, before turning in the next section to consider individual
rights attached to shares. From the most general perspective, shares form the
equity of a body corporate. They are the store of capital of a corporation. From
a property law perspective, a share is identified as a legal chose in action.183 As
McGuinness writes: “it is clear that a share is a type of chose in action in the
nature of intangible personal property”.184 He continues, it is “a property interest
in the capital of the corporation itself”.185 In more tangible terms, as Penner
observes: “A share in a company is, roughly, a right to a proportionate share of
dividends if declared, when declared, and to a proportionate share of the
company’s assets if wound up, when wound up.”186

From a corporate law perspective, a share is a number of things: it is a right
to participate in the body corporate,187 a liability of mutuality to other
covenanters, and a representation of a monetary value which may be higher or
lower than the amount originally paid to acquire it.188 As discussed above, a
share was originally a direct ownership interest in the assets of the corporation,
which rights were later redrawn to be a right limited to certain aspects of
income.

The nature of the share is neither fully nor well determined. Not only is legal
history inconsistent, the current consensus, if it existed, would be that there is no
consensus. An interesting starting point could be the view of Oxford legal
scholar, F Lawson, who wrote 50 years ago, in his tome *Property Law*:

“a share may best be defined as a hope, often rising to an expectation, of receiving
dividends from a company, though not of any definite amount, together with a right
not to be differentiated against in respect of any dividend which may be declared by
the directors and an ultimate right to a share in the capital of the company if it is
wound up.”189

182 Automatic Self-Cleansing Filers Syndicate Co. v Cuninghame [1906] 2 Ch 34; 75 LJCh 185, and generally
see discussion in Grantham, supra n 154.
183 McGuinness, supra n 158, 284.
184 Ibid.
185 Ibid., 285.
186 Penner, supra n 93, 810.
187 See Lowry and Watson, supra n 165, 132–33, and McGuinness, supra n 158, 836.
188 Taken from McGuinness’s excellent discussion of the nature of the share, supra n 145, 282–85.
Lawson's view of the share as “hope” is certainly less than comforting to many investors. Consider the contemporary English scholar Pennington, who writes:

“The most that may be said . . . [is that] shares in a registered company . . . are a species of intangible movable property which comprise a collection of rights and obligations relating to an interest in a company of an economic and proprietary character, but not constituting debt.”

Pennington sees both property “proprietary character” and contract “economic . . . character” in shares, but seems unable to place his finger on what exactly they are. Penner provides a revealing and important insight for our discussion. A shareholder, Penner notes, “has no legal right to any existing share of an operating company’s wealth.”

Leading case law in the UK, USA and Australia has defined the share, not without contest, as follows. In the UK:

“A share is the interest of a shareholder in the company measure by a sum of money, for the purpose of liability in the first place, and of interest in the second, but also consisting of a series of mutual covenants entered into by all the shareholders inter se in accordance with [section 14]. The contract contained in the articles of association is one of the original incidents of the share. A share is not a sum of money . . . but is an interest measured by a sum of money and made up of various rights contained in the contract including the right to a sum of money of a more or less amount.”

Here, a share is property with incidents one of which is a contract, and a peculiar type of property subject to measurement by money. A leading US case on shares in banks offers: “They are made so [ie personal property] in express terms by the act of Congress under which such banks are organised. They are a species of personal property which is, in one sense, intangible and incorporeal . . .”

More fully, the court in *Burrall v Bushwick R. Co.* opined:

“A share of the capital stock gives the right to partake, according to the amount put into the fund, of the surplus profits of the corporation, and ultimately, on the dissolution of it, of so much of the fund thus created as remains unimpaired and is not liable for debts of the corporation, but not to withdraw their amount from the corporate funds.”

In Australia, the leading case has it: “A share in a company is property consisting of proprietary rights as defined by the articles of association.” The High Court continued: “but [a share] is more than a ‘capitalized dividend stream’ . . . it is a

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190 R Pennington, “Can Shares in Companies be Defined?” (1989) 10 Company Lawyer 144.
191 Ibid.
192 *Boland’s Trustee v Steel* [1901] 1 ch 279, 288. See criticisms of this view in Gower, *supra* n 152, 359.
194 *Burrall v Bushwick R. Co.* 30 Sickels 211, NY 1878.
form of investment that confers proprietary rights on the investor”.196 All of these explanations are explications of the governing legislation in each of the three jurisdictions.

This problem of share definition arises from a number of factors. First, it is not clear whether shareholders are inside or outside the corporation. In other words, it is not clear whether shareholders have rights against or in the corporation. As a party having rights against the corporation, they are like debenture holders and any other creditor.197 Shareholders as mere contractors with the corporation, and have the relationship of creditor and debtor.198 More troubling, if shareholders are outside the corporation, what claim can they have to control its operations? The obvious answer is “none”. Shareholders, however, are also insiders to the corporation. They are the “members” of the corporation.199 They have rights to elect the directors of the corporation. This right to elect an organisation’s directors is clearly a right one would give only to a party who is a member of an organisation. Further, profit rights seem to be more appropriate to members. Finally, it may be that shareholders are both inside and outside the corporation. This combination of insider–outsider rights, however, leads to the potential conundrum of suing oneself encapsulated in the maxim prohibiting such: nemo agit in se ipsam.

Scholarly debate on an important Australian case illustrates the problem nicely. The 1996 High Court decision in Gambotto v WCP Limited200 concerned WCP’s legislated right to expropriate Gambotto’s shares. WCP wished to become the sole shareholder of a publicly traded company in which Gambotto held about 0.3% of the outstanding shares. Gambotto argued that he had a long-term expectation of holding the shares and did not wish to part with them. Two groups of scholars have taken opposing stances on the case. In their analysis of the High Court’s decision, which went in favour of Gambotto, one group of scholars, taking a property view of shares, argued that the proprietary nature of shares is inconsistent with a private right of expropriation.201 Property owners, they argued, have the justified expectation that their property will not be interfered with except by governments acting within tightly circumscribed rights of expropriation. The second group of scholars, taking a contractual view, argued that shares are but evidence of a contract for an income stream and have lost all their proprietary characteristics.202 Accordingly, a breach of contract is

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196 Gambotto v WCP Limited (1995) 182 CLR 432.446. See the debate by Spender and Bird, supra nn 176 and 177.
197 See, eg the discussion in Gower, supra n 152, 357–59.
198 Analysis based on Ireland, Company, supra n 161, 46.
199 Grantham, supra n 154, 563–4.
201 Spender, supra n 176.
202 Bird, supra n 175.
not as serious as an infringement of property rights and so should be subject to the normal contractual remedy of damages.203

The scholars in this debate have offered careful analysis of the property in shares. Spender, who favours a property analysis, argues that shares, with some minor qualification, carry all of the Honorean incidents of ownership.204 She identifies and discusses each of the 11 incidents and finds evidence of each in shares. Bird, who favours the contractual version, in her reply to Spender argues that the incidents have been radically diminished. Further, she points to Honore’s four cardinal incidents of property—“the rights to unrestricted use, to exclude, to alienate and to immunity from expropriation”205—and observes that the right to immunity from expropriation has been abolished in Australian law.206 Without this cardinal right, certainly shares are not property.

This debate between scholars concerning the nature of shares as property versus contract is a reflection of the larger debate on the correct understanding of the corporation as either a thing in itself, a legal person, or a mere nexus of contracts, referred to earlier and nowhere near resolution.207 Where shares at this fundamental level cannot fit neatly into the property paradigm, the property basis for shareholders’ rights advocates claiming their right to control the corporation is much weaker than the rhetoric would first appear.

All of this information helps to clarify the various conceptions of the share and of shareholders in their role in the corporation, and provides a starting point and a background for examining their role and rights in the corporation, and hence arguments justifying shareholder’s rights to control.

3. Entrepreneurs and Institutional Investors: Contributions and Positions

Regardless of how one views the Locke–Bentham debate and considers its impact on the issue of shareholder rights, and regardless of the problematic nature of shares, the view of shareholders as creators/owners of the corporate entity has a long history and a strong appeal as a justification for the shareholder’s right to dominate the corporation, at least in part, because of its simplicity.208

As we have seen, this view arises from the partnership nature of the early corporation. The historical accuracy of the intimate connection between shareholders and the corporation is questionable, and indeed has been described
by various scholars as “another myth of corporate law”. In fact, even as early as the eighteenth century, Adam Smith worried about the disregard shareholders had for the activities of the corporation. Smith wrote:

“the greater part of these proprietors seldom pretend to understand any thing of the business of the company; . . . [but] give themselves no trouble about it, . . . [and] receive contentedly such half yearly or yearly dividend, as the directors think proper to make them.”

This historical concern should sound a note of caution or at least cause a bit of consternation among shareholders’ rights advocates. The divide between investor and entrepreneurial activity was already a considerable gully several hundred years ago.

A contemporary analogous argument is drawn from the business perspective and based on the private, closely held or “entrepreneurial-founder model” of the corporation. In this model, the entrepreneur-shareholders or investors are intimately involved with the management of the production they financed. As such, they know the business as well as anyone else and, indeed, in addition to being the source of original start-up capital for the business, have the initial conception of the business and develop its basic strategy. Where this is the case, it is a strong argument, or at least a strong business case, for keeping those parties in control of the corporation where the ongoing operations of the business corporation are seen as a desirable objective. This view, however, conflates two radically different types of shareholders: the entrepreneur/business person and the investor/financial analyst.

As many scholars have noted, a new class of investors has sprung up whose strength has nothing to do with the business acumen needed to create and operate a successful corporation. This new class, the institutional investor, is a financial analyst rather than a business manager. The financial analyst is concerned with the valuation of shares and other financial interests irrespective
of the underlying commercial activities of the issue. Disclosure documents reflect this concern reporting on financial matters and only referring to operational matters to the extent necessary for purposes of explaining or supporting financial information.

At least with respect to publicly traded corporations, therefore, shareholders’ rights advocates lack a sound basis for their argument for control where they wish to base the control argument on the “entrepreneur-founder model”. In essence, the corporation has evolved such a great distance from its origins a few centuries ago when there was plausibly a valid argument for the shareholder as owner, to the point that it has lost all power—a point recognised at law by the diminution of shareholder rights discussed above. Further, as previously noted, since most shareholders are trading on the secondary market they add nothing to the equation, and so their claims for a privileged position inside the corporation ring hollow.

The argument for shareholder control can still be supported from two further positions: first, from the central role of share capital in corporate finance, and secondly, from the unique position of the shareholder as the provider of the equity–non-debt portion of the corporation’s capital. From a corporate finance perspective one finds that share capital is a minor, less important and less preferred means of financing the enterprise. Hill notes that as a result of the long-term involvement of some corporate finance suppliers they end up having much more at stake than the shareholders, who, in contrast, are able to exit easily from a corporation in a precarious financial situation. She notes that as a result of some of the controlling positions these lenders take, not only in securing their funds but also in the operations of the corporations, they become more like insiders than the traditional outsider role they hold as creditors. This situation, which she argues is the common corporate reality, does not jibe with the shareholder/owner model advocated by shareholders’ rights advocates. The point is pressed further in that even in a closely held corporation, once the corporation has assumed debt, the creditor has a greater right of “ownership” to the cash flow of the corporation than the shareholder. The point is advanced further still when one recalls Penner’s observation that shareholders have no claim on an operating corporation’s static wealth “working capital”. It is fair to say, therefore, that shareholders are merely one group of financiers to the corporation whose characteristics are not remarkable.

The second aspect of the shareholder as owner argument is premised on a clear distinction between debt and equity. Hill argues that this distinction in

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217 Section 6(a) supra and, generally, Grantham, supra n 154.
218 Hill, Public Beginnings, supra n 145, 5.
219 Ibid, 5.
220 She notes that shareholders have a first claim on profits. They only have a claim on profits when the corporation is (a) profitable and (b) the directors declare a dividend. Stout, supra n 155, 1192.
contemporary corporations is very hard to maintain. She writes: “with the rise of more complex funding instruments the traditional distinction between debt and equity fails to accord with economic reality and looks artificial, arbitrary and increasingly passé”.

She notes that the disaggregation of equity investments—dividing the risk and control components—makes the notion of shareholder as risk bearer and residual claimant much less compelling. The securities industry recognises this mixing of debt and equity in a single instrument such as a convertible bond by referring to such securities as “hybrid securities.” The courts have taken note of this reality in judgments which place the interests of other financiers ahead of shareholders. This situation may be a start to addressing some of the problems arising from earlier legal decisions creating a separate corporate entity.

In sum, the reality of the contemporary publicity traded corporation is that shareholders’ rights advocates cannot base their claims for primacy on the entrepreneurial significance nor peculiar risks of their contributions, nor their special position as shareholders.

4. Shareholder Core Rights

In contemporary corporate law, among the various rights shareholders have, the fundamental incidents of share property are the core rights. These are: the right to dividends as declared, the right to vote directors and the right to the residue on the winding-up of the corporation. As a group, these rights form

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221 Hill, Public Beginnings, supra n 145, 4.
222 McGuinness, supra n 138, 434–5.
225 See Grantham, supra n 154, 563.
226 Gower, supra n 152, 361. Spender mounts a strong argument for the property nature of shares on the basis of voting rights, supra n 176, 115–17.
227 In the US: “shares . . . are the interest or right which the owner has in the management, profits and assets of a corporation” (Commissioner of Internal Revenue v Scatena 85 F.2d 729 (C.A. 9 1936.)) 732). In Australian corporate law the right to vote directors is limited to publicly traded companies. Identified and discussed in Stout, supra n 155. McGuinness supra n 158, 836 add the additional right of alienability. This later position, however, does not appear as significant historically in view of the illiquidity of the markets and the communal nature of share property.
the essence of control of the modern corporation. Interestingly, none of these rights fall among the four cardinal rights identified by Honore as the hallmarks of ownership—"the rights to unrestricted use, to exclude, to alienate and to immunity from expropriation".228

Shareholder primacy advocates take as fact that the shareholder votes for the director, who in turn returns money to the shareholder either by declaring a dividend, restructuring or winding-up the corporation. They argue that through this mythical cycle229 they can, will and deserve to control the corporation to increase shareholder wealth and exclusively shareholder wealth. We will now turn to examine each of the rights involved in the process.

(a) Right to Dividends

Historically, profit from owning shares came only by way of dividends.230 Investors became shareholders for the purpose of the potential return on investment.231 For an investment of a given amount, a predetermined number of shares were issued from the corporation's treasury. Shares traditionally were issued with a par value. That is, each share had a set monetary value imprinted on its face. Ownership of the share gave the owner a single, definite and central right: the right to the profit of the corporate enterprise in proportion to the share. This right to profit is the reason the investor purchased the share.232 Accordingly, shareholders have the absolute right to all the profits of the corporation.233

The main argument for shareholder's right to the profits is that as providers of the corporation's most critical resource—capital—they deserve the return. That is to say, they bought the shares and in so doing they provided the capital which forms the corporation's foundation and basis for the operation of its enterprise. In this way, by some form of logic, they bought the right to the

See discussion in Holderness, supra n. 88, 94. Also, the issue of growth of alienability is discussed from an economic historian's perspective in R. Ekelund and R. Tollison, “Mercantilist Origins of the Corporation” (1980) 11 Bell Journal of Economics 715. Finally, note Penner’s view that although alienability is an essential property right, the only true alienability right in property law is by way of gift, Penner specifically excluding transfers for value, supra n 93, 730–52.

228 Bird, supra n 175, 150.


230 Noted by Smith, Primacy, supra n 156, 298.

231 On the first shipload of spices from India, traders earned a profit of over 700%.232 A contrary view is held by Smith, who observes that the early American corporate historian Davis wrote: "it is doubtful if the companies were, strictly speaking, organized for profit". Smith, Primacy, supra n 156, 295, n 89. Nevertheless, it is difficult to imagine what other motives would drive these investor-capitalists in corporations to stake all of their worldly possession—these corporations did not have limited liability for shareholders—on a venture if it were not for profit.

233 Subject, of course, to the obligation of the corporation to pay taxes to the government.
profits. This position can be challenged if one considers that without human labour there would be no profit, or equally if one considers the related broader social capital arguments, or other resources from tax-supported infrastructures to environmental inputs necessary to run a business. This argument is obviously circular and the only clear way out is predicated on whether one accepts the assumption that capital is the paramount input. The debate between Marxism and capitalism is in one sense simply a debate concerning whether it is the input of capital or of labour that is primary, each having a different champion.

Another argument for granting the right to all profits comes from the risk accepted by the investor. The argument is that since investors bear the risk of loss, they have the corollary risk of gain. In essence, the argument is an argument based on the debt-equity distinction. As Hill has demonstrated, however, this distinction has faded to the point that it no longer holds. It is not at all clear that this view is anything more than the vestiges of Christian Protestantism (the notion that investment requires return) or an apology for the status quo, and indeed fails to address the more basic assumption that there are many people who would and in fact do accept the risk, such as employees, but are prevented from receiving the benefits.

An argument for granting investor-shareholders all the profits can be made from the Calabresi and Melamed analysis. Shareholders, one would argue, are entitled to the profits as a property right rather than a liability because participation by way of capital in the stock market carries a lower transaction cost. This application, however, is more a description than a justification, and is in any event indeterminate.

Another important argument for the shareholder’s right to profit is based on the argument of ownership of the corporation. As owners of the corporation, they have the right to Honore’s incidents of property, which rights include the right to income and, in this case, the income of the corporation. We have previously noted Bird’s criticism of attempts to apply Honorian categories and

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236 Hill, Public Beginnings, section “Corporate Finance—The Blurring of the Boundary Between Debt and Equity”; also treated to a more extensive discussion in McGuinness, supra n 138, 273–81 and noted by Berle and Means, supra n 117, 245, who as early as the 1930s observed that shareholders were more like bond holders.
238 Schweickart, supra n 235, 33–39.
239 See Spender’s discussion in Spender, supra n 176, 117–18.
240 See the challenge to this view in Ireland, supra n 148, 32.
discussed how ownership of the corporation came about and is both justified in
Lockean terms and undermined by Bentham, and accordingly will not revisit
that argument. It will suffice to say that one must conceive of shareholders as
owners of the corporation, conceive of the corporation in terms of Lockean
property and ignore the fact of secondary trading if one wishes to support the
shareholder-owner’s absolute right to all the profits of the corporation. As
demonstrated above, however, the “shareholder-equals-owner” equation is
incorrect at law.

This right to profit is derived at least in part from the capitalist right to profit
from the value differential between the value of the labourer’s labour and the
value of the good or service produced by that labour.\(^\text{241}\) By accepting this
capitalist right, as the west has done for the last several hundred years, one has at
least excluded one claim on the profits of the corporation—namely the rights of
the labourer to the profit. It leaves, however, claims by employees, directors,
government and other suppliers unanswered. Again, one is forced to accept a
Lockean view of property and other corollaries if one is to exclude these further
claims on the profits, but again, the above criticisms apply and undermine the
claim.

(b) Right to Vote

Whether the right to vote is a property right is unclear. Some argue that the right
to vote shares is probably not a property right per se.\(^\text{242}\) Spender argues that this
right is analogous to Honore’s “right to manage” with the divorce of ownership
and management being a “reduction in the liberties of the owner”.\(^\text{243}\)

On the contrary, Bird argues that the reality of the publicly traded
corporation (legislated in Australia) is that there is no right to manage.\(^\text{244}\)
Shareholders have the absolute right to elect all the directors of the corporation.
There may be no director not voted in by the shareholders. It would appear that
the right to vote is based on the right of original appointment of agent/directors

\(^\text{241}\) Capitalism is a preliminary and fundamental assumption at this point. This assumption is
mentioned in various writings. See, eg the discussions of cited in Williams, supra n 25, fn 264, and
Reich in Williams, supra n 25, 295–304 et passim, and her discussion of republicanism using
examples of F Michelman, “Political Markets and Community Self-Determination: Competing
Judicial Models of Local Government Legitimacy” (1977–78) 53 Indiana Law Journal 145 and
“Law’s Republic” (1988) 97 Yale Law Journal 1493; and Sunstein’s early view “Interest Groups in

\(^\text{242}\) See Lawson, supra n 149, 29. This is interesting, for if this right is not a property right, depriving
shareholders of this right is not a government taking and need not be compensated. It could be
reallocated on policy, economic or other grounds.

\(^\text{243}\) Spender, supra n 176, 113.

\(^\text{244}\) Bird, supra n 175, 152.
by principal/investors, going back to original partnership law in the joint stock companies. As a general principle of agency law, principals are responsible for the actions of their agents where the agents are acting within the bounds of their authority. It follows logically, therefore, that principals have the right to select who to appoint as their agents.

The argument for voting rights can be made on the basis of the initial organisation of the corporation. While clearly there is a responsibility and a need to appoint managers of the corporation if the initial investors themselves are not disposed to manage the corporation, once the corporation has been founded, the dynamic nature of shareholding in the stock market undermines those ongoing responsibilities and hence the correlative rights. In Hohfeldian terms the shareholders’ power as principals to vote directors should be dissolved along with the correlative liability of the directors as agents to shareholder interests.

The problem, of course, is that as company law developed, courts took the position that directors are directors of corporations and not agents of principals, ie shareholders. Until recent corporate law amendments in the US, directors have had very little liability to the shareholders, and indeed this lack of liability formed the basis for Berle and Means famous analysis of the managerial corporation in their 1932 work The Modern Corporation and Private Property. At law, they are not agents of the shareholder/principals, and accordingly law provides shareholders with very few and weak remedies against directors. It was because of this lack of control and directors’ arbitrary decision-making power on whether to declare dividends that shareholders may have originally had the right to vote for them.

While shareholders’ rights advocates would like to increase this liability of directors to shareholders, presumably to be able to exert pressure on directors to increase shareholder wealth, the market reality undermines the argument. Institutional investors who comprise the majority of the shareholdings, who in turn do the majority of their trading via sophisticated computer-programmed trading, as a group are not particularly interested in individual directors or

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246 Grantham, supra n 154, 557–59.
248 Argued forcefully by Bottomley, supra n 224, 277.
249 Automatic Self-Cleansing, supra n 183.
250 Sarbanes-Oxley Act.
251 See supra n 117.
252 The recent case of Disney shareholders against directors concerning Michael Orvitz severance package may be a move in the direction of increasing director liability to shareholders. In Australia see the recent decision in Thomas v D’Arcy & Ors [2005] QCA 68 (18 March 2005).
253 Smith, Primacy, supra n 156, 299.
specific companies: they prefer exit to voice. They are portfolio managers seeking to maintain appropriate levels of diversity on an efficient frontier. Management of companies is neither their interest nor their forte. Directors respond to the pressure of stock markets in terms of reacting to share prices rather than specified shareholder interests, and their pay is limited only by the shock factor, not negotiation with shareholders.

Another approach to the right to vote appears to go back to the issue of control for the purposes of protecting one’s interest in the capital invested. Where one has the power to appoint a director to guide the corporation in a direction the attendant risks of which one agrees to accept, one will be disposed to make an investment. While this perspective may be more accurate in a small, privately held corporation, current public corporate practice does not appear to follow this strategy. Given the choice of “voice” or “exit”, investors tend to prefer “The Wall Street Walk”. Quite simply, for various reasons, including free-rider issues and transaction costs, most shareholders are not interested in running the firm, even if they have the right. Furthermore, given the blurred line between debt and equity, the decision to give one capital supplier a vote which is denied to another, particularly a rather uninterested one, seems arbitrary at best.

A second argument can be advanced by way of analogy. A principle supporting a government’s legitimacy is “no taxation without representation”. Analogously, one could argue that voting to choose who manages one’s financial investment is just and creates legitimacy for the actions of the directors and hence the corporation. What it fails to justify, however, is why one voter/shareholder gets more votes than another. For example, a larger investment by a very wealthy shareholder may be a smaller portion of that shareholder’s capital than a less well off shareholder who has invested all her


256 The idea of a unified shareholder interest is undone by the study of H Hu, “Risk, Time and Fiduciary Principles in Corporate Investment” (1994) 38 UCLA Law Review 277. The effort to align management and shareholder interests by granting substantial part of the executive compensation by way of share options has had questionable success. As Peter Drucker puts it, one of the lessons of the 1990s is that “bribing” the executive to do their job does not work. The Economist also available online Drucker Archives, available at http://drucker.cgu.edu/DruckerArchives/data/index.htm. Note Booth’s comments, however, infra n 268.

257 See Behchuck, n 1.

258 Noted in Hill, Visions, supra n 149, 58 and Farrar, supra n 142, 13.

259 See discussion in Farrar, supra n 142, 318–30 and S Turnbull, supra n 143, 194.

260 This slogan was the American response to the 1765 British Stamp Act and declared to be a principle by the Massachusetts General Court in its 1766 condemnation of the Townshend Acts. Related texts available at available at http://www.constitution.org/bcp/vir_res1765.htm, accessed 20 November 2004.
capital in the corporation. If it is a matter of representation according to proportion funds available for investment, then the system would require another form of allocating the interest in voting rights. Further, it does not justify the exclusion from representation of employee interests in the activity carried on by the corporation while including the representation of those investing the capital.

Furthermore, the granting of all the voting rights to the shareholders fails to distinguish and address the different nature of the investment invested by different parties. In particular, it fails to justify or explain why other parties, such as employees, who arguably have a greater investment in the corporation, are excluded from this right to vote. When one thinks of this right in Hohfeld’s relational terms, and particularly in terms of rights in personam—which is arguably what a vote creates—it would seem that the third parties most effected by the decisions of those elected to the board ought to have the greatest power and overriding right to vote. Furthermore, from a practical viewpoint, directors, managers and employees need to be able to work together and get along. It is imperative that they do so for the purposes of coordinating effectively the objectives and strategy of the corporation. In fact, it is acknowledge in “whistle-blower” legislation that employees may well have a much great understanding, ability and opportunity to identify and monitor potentially inappropriate activity by directors and managers than investors or other parties interested in monitoring and controlling corporate behaviour. Accordingly, where the objective is to limit executive rent extraction or offer other economic efficiencies, certainly employee votes would make sense. If the average citizen can be trusted to vote for a prime minister, why not for a CEO? From this perspective, it seems only logical to grant these parties the vote.

Three further aspects of the contemporary corporation should be considered in this discussion of voting rights: the separation between investors and management, the phenomenon of widely dispersed shareholdings, and the
fact of the emergence of a class of professional managers.\footnote{On the rise of professional management, see Berle, supra n 160. The growth of this professional class of managers creates a view of shareholders identified by Hill as the “Shareholder as Bystander” model of shareholders in Hill, Visions, supra n 149, 47–51.} First, the separation of shareholders and management is significant because without a close proximity neither party truly has the attention of the other.\footnote{Richard Booth notes that management shareholdings have increased substantially in the recent past and predicts this to be an ongoing trend in the future. He observes that only 14% of the compensation of the top 200 companies’ executives is in the form of salary. R Booth, “The Direction Of Corporate Law: The Scholars’ Perspective” (2000) 25 Delaware Journal of Corporate Law 79, 81.} Shareholders’ attention is focused on the share value whereas management attention is focused on the corporate enterprise. Furthermore, efforts to coordinate their interests have been less than successful.\footnote{Richard Booth notes that management shareholdings have increased substantially in the recent past and predicts this to be an ongoing trend in the future.}

The lack of proximity of the shareholder to the enterprise sets up a different group of problems. The enterprise is not close enough physically nor accessible enough to the shareholder for the shareholder to take a real interest in the enterprise. This distance is what Adam Smith complained of in the quote offered above. Indeed, corporate law scholar Stephen Bainbridge has recently opined: “corporate stock evidences . . . a commodity little different from pork bellies”.\footnote{S Bainbridge, “Community and Statism: A Conservative Contractarian Critique of Progressive Corporate Law Scholarship” (1997) 82 Cornell Law Review 856, 873.} Furthermore, as previously noted, shareholders do not have the power to make changes in how a corporation is run on a day-to-day basis, not to mention the problem of consensus among them as to how it should be run in the first place were they given that power directly. Given the fact of this separation both in physical terms, in terms of attention, and by law in terms of management control, it can hardly be surprising that shareholders focus on shares rather than the actual operations of the enterprise—assuming, of course, that there were shareholders interested in doing so in the first place.

Secondly, the dispersal of power weakens the ability of individual shareholders as well as diminishes their interest in controlling (or at least attempting to control) the decisions and actions of the directors.\footnote{Stake, supra n 117, 32–4.} Law and economics scholars note that spreading property rights too thinly devalues the right to near zero.\footnote{Stake, supra n 117, 32–4.} Tying voting rights to shares has effected a dispersal of
power among a greater number of people not involved in the operations and management of the corporation and not in a position to oversee the management. Further, it undermines the accountability of the directors to the corporate community most affected by their decisions, namely, employees, suppliers and customers. The importance of these other constituents has been increasingly recognised through legislative and common-law developments.273

Berle and Means offer an interesting critique of the matter. They argue:

“having surrendered control and responsibility . . . [shareholders have] surrendered the right that the corporation should be operated in their sole interest . . . [and in doing so] released the community from the obligation to protect them to the full extent implied in the strict doctrine of property rights.”274

Thirdly, the reality of corporate practice is that managers in most cases control the voting through the mechanisms of proxies and control of the corporate agenda.275 In fact, it is questionable whether shareholders even value the right to vote.276 With “exit” as the preferred alternative of shareholders and the reality of managerial power in terms of controlling corporate voting and the deeper investment of other constituents, it seems difficult to make a case for keeping the right to vote among the exclusive rights of shareholders.

(c) Right to Residue277

The third of the core rights is the right to the residue. Shareholders have the absolute right to all the residue of the corporation, qualified by the duty to pay to the government any taxes and other creditors left outstanding. The right to the residue can hardly be thought of as novel. When an enterprise is wound up the residue either must go somewhere or be abandoned, escheating to the government. The shareholders’ right to the residue would appear to come from the rights of its historical predecessor the partnership. Partners have partnership interest—i.e., property—in the property of the firm, and as such, when the partnership is dissolved, the property is divided among the partners according to their interest. Assuming one accepts as legitimate the property distribution of a capitalist system,278 when a corporation is likewise wound up, the excess or

273 Grantham, supra n 154, 569–73.
274 Berle, supra n 117 (revised edn, 1967), 312.
275 Hill, Visions, supra n 149, 44–46.
276 Big shareholders in the United States have not lobbied to have any changes to corporate law which would allow them to nominate their own directors and break management power. See “Triumph of the Pygmy State”, The Economist, 25 October 2003, 55–56. Promoters have taken no steps to modify shareholder rights in charters being prepared for IPOs. Noted in Stout, supra n 155, 1207.
277 Stout argues that this right is in fact limited to bankruptcy of the corporation.
278 One must accept the capitalist model or else the excess produced by labour would go to the labourers, not the capitalists. Further, it seems unlikely to be abandoned in the west in the foreseeable future.
remaining capital should be distributed among the capitalists/investors/shareholders. To accept this right, one must accept the shareholder as owner model of the corporation.

Others suggest that the residual claim forms part of the right to vote. The argument is that as the shareholders will be left with whatever is left in residue, they should have the right to protect those interests by having the right to vote. This argument seems to be less than compelling. In a winding-up, shareholders are not given a vote on the disposition of the assets. Those are directors’ duties which will be among their final duties—hardly a point leaving them vulnerable to shareholder power. In any event, the vast majority of shareholders, other than corporate raiders, do not wish the corporation to be wound up and see winding-up only as a last resort. As such, winding-up is a rare and seldom sought or granted remedy. Accordingly, to grant immediate voting power on the basis of this remote possibility is arguably an unjust, unreasonable, and inefficient allocation of rights.

In Honorean terms, identifying the right to the residue as an incident of ownership does little more than confirm Penner’s view that the “bundle of rights” paradigm is little more than a slogan. As mentioned previously, Honore himself does not identify this right as one of the cardinal four. Turning to Hohfeld, a voting right is in the privilege no-right category. Unfortunately, neither of these analyses goes beyond stating the relation: they fail to justify its existence. Finally, given the proxy system in which management solicits proxies for its own agenda and the gratis grant by many shareholders of voting rights, it would seem that shareholders de facto place little value on voting rights. In summary, there appears little to justify the core rights of shareholders, particularly in their absolute forms.

G. SHARES AND PROPERTY LAW

At a first level of analysis in which property is rejected as a meaningful legal category, the share as a type of property becomes meaningless. It survives as an income stream or dividend stream in contractual form. From a practical perspective shares are not really an income stream so much as a hope: a hope of a return in terms of dividend or capital appreciation. In a legal sense, in this contractual form, a share devoid of property is not much of anything. It is certainly not an item carrying the strong moral imperative that the shareholders’ rights advocates intend in their use of the language of rights. It is hard to imagine how holders of shares could begin to sustain the distribution of political

279 Farrar suggests this residual claim is the basis of their right to vote. Farrar, supra n 142, 158, and citation in n 6.
280 Penner, supra n 93, 714.
and economic rights they demand as the controllers of the corporation and its economic focus without the purported moral imperative that goes along with property rights, or at least rights in general.

At a second level, if property is accepted as a meaningful legal category, what information does it provide about the share? We see that it does not fit Blackstone's, Hohfeld's or Honore's paradigm. In terms of Blackstone, it is not a thing as it fails the first criteria, being an intangible—if one reads Blackstone's rhetoric as implying that property is tangible. The share's amorphous nature being any one or a number of rights does not sit comfortably or wholly in any of Hohfeld's categories, and fails to address convincingly the basic requirement of jural relations—relations between whom, why and how. As noted previously, scholars vary considerably in their views as to whether shares meet Honore's criteria. Indeed, a recent Honorean analysis of shareholders' ownership found that they fully satisfy just two of the 11 criteria and only three more incidents partially. Since shares fail to meet these generally accepted criteria for property, they lack the justificatory force property may carry. In the most basic analyses of property, regardless of whether one prefers that of Penner's duty to be left alone or that of Gray's right to exclude others from the benefit, shares seem to only weakly meet the criteria, in part because of their very flexible nature as instruments of control, finance or mere monitoring. As Gray observes, property at this level is little more than "an emotive phrase in search of a meaning" which "exerts a powerful ad yet wholly spurious moral leverage".

From the perspective of property as an institution, we see that there are fundamental problems with respect to the Lockean paradigm of private property. Private property is but a choice among alternative social orderings for the distribution of power and economic resources. Where a Lockean justification is invoked, shares offer no creative contribution or mixing of labour, particularly when one focuses on trading in the secondary market, and so they fail to command the moral force such a justification would offer and, as demonstrated, the entrepreneur-shareholder model fails as an accurate model of much investing activity. What this failure in institutional terms suggests is that shares as property is perhaps one of the most specious bases for the moral claim for the justificatory strength of property rights.

If, for argument's sake, we accept the position that there is significance in the notion of property and apply it to share core rights, what do we have? Penner has argued that the hallmark of property is the right to exclude the general

281 See discussion between Bird and Spender, supra nn 175 and 176.
283 Gray, supra n 114, 306.
284 Ibid, 305.
public or its corollary, to be left alone. Traditionally, this hallmark of property has been viewed in corporate law as being between the corporation and the general public, and not as between the members of the corporation. Nevertheless, as demonstrated in the argument above, perhaps it makes more sense to think about this hallmark of corporate and share property in terms of distribution of rights among members of the corporation.

Calabresi and Malamed would also agree that shares are a type of property in that for the most part they are transferred voluntarily, in a low-transaction-cost market and without inalienability or moralism problems. The reality is, however, that shareholders’ property rights are not absolute even in terms of maintaining ownership of their shares. Shareholders do not have absolute control of their shares even within the corporation as members of the corporation itself. The considerable regulation of mergers and acquisitions, including mandatory acquisitions and going private transactions, make it clear that shares can be taken on an involuntary basis from shareholders. Further, alienability rights are not absolute, even in publicly traded corporations, where, for example, shares can be subjected to lock-ups.

In light of this legal reality and what we have seen about the malleability of property rights, the importance of these rights to various parties in the corporation and the nature of the various interests and commitments of parties to the corporation, we may well ask whether or not the current assignment of property rights in shares are being appropriately or efficiently allocated. Indeed, the deeper our examination, the more tenuous the absolutist position of shareholders’ rights advocates has become. As we have seen, the exclusion of other capital providers such as lenders from greater control over the corporation is not justified when the breakdown between equity and debt is acknowledged. This exclusion of creditors becomes even more difficult to justify when the level of involvement and risk assumed by lenders is acknowledged to be greater than that of shareholders, whose easy exit option is nearly always available. Even more difficult to justify is the exclusion of other parties whose very livelihoods depend on the ongoing operation of the enterprise controlled by the corporation from seeing to its ongoing financial health. Finally, the issue of understanding, monitoring and controlling corporate behaviour suggest that these rights should be vested in other parties.


286 For a comprehensive and very readable discussion of the general principles and mechanisms, see McGuinness, supra n 138, 1134–62.
H. Conclusion

Historically shareholders have had the power to impose their will on the corporation by setting it up, appointing the original directors, and investing the initial capital. Why these rights, particularly in their absolutist expressions, continue in the chain of successive shareholders is much more puzzling. To say shareholders have bought these rights is simply to beg the question of this article: why are these particular rights of interest to shareholders in the first place and what is the justification for permitting these rights to be allocated to, bought by, controlled by and passed on to successive shareholders?²⁸⁷

Shareholders are interested in one thing: their own personal wealth. Their calls for power or control over a corporation are not a reflection of a fundamental interest in the means, methods or strategies of the corporation in the conduct of its business.²⁸⁷ Nor do they wish to control the corporation for the corporation’s own profit, benefit or survival, or for the good of the community of consumers, workers or related industries. Rather, their argument is that shareholder power as embodied in the property of core rights creates the most efficient management corporate of assets, thereby maximising shareholder wealth and, ultimately, social wealth. While the first part of their argument concerning efficiency may carry some weight,²⁸⁸ there is serious doubt about whether shareholders’ wealth maximisation has translated into overall social wealth.²⁸⁹

Further, as argued above, at least in publicly traded corporations, shareholders appear to have little interest in controlling the business of the corporation or taking on the responsibility for its management. Such being the case, it is difficult to see why this group of people should be given control over a corporation. Indeed, as previously noted, most trading on the securities markets is done by computers programmed on trends and movements, not on corporate fundamentals.

The argument for control of the corporation based on the need for shareholder protection is weak, particularly in justification of voting rights. The fact is that nearly every scandal and bankruptcy of publicly traded corporations

²⁸⁷ For a current discussion of the questionable interest and ability of shareholder interest in corporate management, see “Triumph of the Pygmy State”, supra n 276. See J Kay, “The Stakeholder Corporation”, in G Kelly, supra n 144.
²⁸⁹ See, eg DC Johnston, who reports “The 400 wealthiest taxpayers accounted for more than 1% of all the income in the United States in the year 2000, more than double their share just eight years earlier” in “Very Richest’s Share of Income Grew Even Bigger, Data Show” New York Times, 26 June 2003.
has been caused by the directors voted in and supposedly controlled by the shareholders. Apparently, shareholder voting and control of directors leaves something to be desired. The common perspective is that shareholder protection is best based on understanding the operations of the corporation, particularly through financial disclosure. If that is the case, increased, ongoing, independently monitored information disclosure would seem to be all that is necessary for a shareholder in a liquid market to make decisions about which corporations to invest in and which to avoid. Of the currently available alternatives, disclosure appears to be the most effective means of shareholder protection absent fraud.290

As previously argued, there appears to be a stronger argument for the three core rights in an illiquid market. In an illiquid market, such as the market for privately controlled corporations and in early corporate history, the argument is stronger on the basis of limited ability of shareholders to protect their investment by exit. When there is liquidity, however, as there is in publicly traded corporations, there is no reason to give control to shareholders. Indeed, as indicated above, shareholders prefer to protect themselves by exiting from troubled companies rather than getting further involved in management.

We have seen Honore’s claim that ownership is what persons with the greatest interest in a thing have.291 A strong argument could be made that those more interested in the corporation would be those whose livelihoods depend on it, namely, the employees. Germany successfully transferred some management supervisory rights to employees in 1976 without harm to investors.292 On this type of analysis shareholders’ rights advocates fail to have a strong ownership claim, particularly when that claim is weighed against the claim of employees.

Changing property rights associated with shares is not new, dangerous or foreign.293 Shares originally denoted the share of the assets of the joint stock company, whether realty or personalty, regardless of whether the joint stock company was incorporated. It represented that portion to which the shareholder was entitled.294 As a result of a judgement in 1837, the nature of shares was changed from an interest in the assets to an interest equal to that of the

290 Eg analysts who carefully monitored Enron’s financial disclosure were concerned about its activities for more than a year before it collapsed.
291 Qualified, of course, by his comment “in a mature legal system”, whatever that is. One assumes he means a legal system that he accepts, as some legal systems will have been extant for thousands of years and deal with incidents of ownership in ways he could not have imagined.
292 For an interesting discussion and analysis of the property rights of German shareholders see G Alexander, supra n 106, 751–53. The results have been discussed as a “competitive advantage” in S Turnbull, “Stakeholder Governance: A Cybernetic and Property Rights Analysis” (1997) 5 Corporate Governance 11, 16. Note, for example, Siemens’s performance, which is significantly better than GE if one removes the profits generated by GE Capital, noted in “Who Is in Charge? The Ins and Outs of Corporate Governance” The Economist, 26 October 2003, 15–16.
293 See generally Grantham, supra n 154.
294 Grigg-Spall, supra n 161, citing as an example Scott’s Company Law (1912), vol 1, 45.
corporation\textsuperscript{295} and later determined in 1854 to be exclusively an interest in the profits of the corporation.\textsuperscript{296} There is no reason a further reform transferring some of these rights cannot be done.

Finally, law fails to make an appropriate distinction between privately held and publicly traded corporations.\textsuperscript{297} Privately held corporations have a much stronger argument for granting their shareholders the three basic rights than publicly traded ones. In terms of risk, it is common that shareholders (usually families) be required to guarantee corporate loans.\textsuperscript{298} Also, the lack of liquidity, which increases vulnerability by denying the easy exit option (the market for private securities is notoriously hard and exorbitantly costly), and the involvement and responsibility of investors in the management and operations of the corporation provide a reasonably solid basis for the corollary rights traditionally granted to shareholders. As noted in \textit{The Economist}, these private corporations tended to be “well-run because those who sat on the board not only knew them intimately, but also had an interest in their continued prosperity that went beyond that of the shareholder”.\textsuperscript{299} The article continues: “In family owned firms, there is generally a profound sense of stewardship—often to the irritation of the firm’s professional managers.”\textsuperscript{300} The views of people responsible for private firms tend to be more far reaching than quarterly earnings reports and include the overall welfare of the corporation.

By way of contract, in publicly traded corporations the core rights seem considerably more difficult to justify. As B Cheffins notes:

“Shareholders who own equity in a company with publicly traded shares tend not to be tied to the business in the same way as their counterparts in closely held firms . . . individuals who buy equity in a public company rarely develop any links to the business by participating in management. As well, when investors decide to terminate the relationship and sell their shares they can usually do so readily.”\textsuperscript{301}

As there are many approaches to property rights,\textsuperscript{302} so too there are many approaches to dividing up the monopoly power currently granted to shareholders. Not only would a broader redistribution of power among members of the corporation more accurately reflect the reality of corporate involvement

\textsuperscript{295} Bligh v Brent, supra n 175, cited in Grigg-Spall, supra n 161.

\textsuperscript{296} Watson v Spratley [1854] (10 Ex 222), cited in Grigg-Spall, supra n 161.

\textsuperscript{297} See, eg the problems of the court in dealing with the case of privately held company attempting to rid itself of an overbearing shareholder who was also a director and general manager, in Krynen v Bugg (2003) 64 O.R. (3d) (Ont. S.C.) 393.

\textsuperscript{298} See, eg the sexually transmitted debt debate.

\textsuperscript{299} “Who Is in Charge?”, supra n 292, 15.

\textsuperscript{300} Ibid., 17.


\textsuperscript{302} Eg property prior to the European invasion of North America was not generally spatially defined. For an interesting discussion see S Banner, “The Evolution of Property Rights” (2002) 31 \textit{Journal of Legal Studies} 359.
in society, but it could also open doors to new ways of governing corporations and, accordingly, the efficient allocation of resources.

From a property law perspective, shares represent an exclusive monopoly on certain elements of corporate control in addition to their ownership incident of income. What a property law analysis does is help us realise the nature of that monopoly and the potential divisibility and reassignment of some those rights. It further highlights those rights that are of true interest to the shareholders, and those which are of peripheral interest and mere vestiges of corporate history. It also suggests where some of those vestigial rights may more effectively or efficiently allocated among parties to whom such rights would be of especial interest.

While shareholders’ rights can be analysed as legal property rights, as we have seen, it is much more difficult to make sense of them in any broader sense of rights. The absolutist position taken by shareholders’ rights advocates demanding complete non-interference requires a moral rights foundation that is clearly lacking. At an intuitive level the call for shareholders’ rights fails to strike something deeper, more fundamental, Dworkin’s “trump” card. In Sumner’s words, shareholders’ rights demands fail as a “normative ... form ... of urgent or insistent demand”. They are not the first-order rights that demand attention and remedy. Indeed, shareholders’ rights appear to be some type of ordinary thing like ketchup or contracts—claims created by a small but wealthy segment of society and supported by the government through the legal system. In other words, if one accepts that position, one finds oneself close to Bentham’s famous conclusion: “rights are nonsense on stilts”. Perhaps shareholders’ rights advocates are walking a bit taller than a careful analysis of the situation suggests is justified.