ARTICLES

CORPORATIONS AND SOCIAL COSTS: THE WAL-MART CASE STUDY

Benedict Sheehy* **
Lecturer, School of Law, University of Newcastle, Australia

ABSTRACT

This article examines the role of the corporate vehicle in the creation of social costs. The article identifies some of the political commitments and philosophies behind the differing notions of corporations. Social costs are those problems that result from business activity and cause uncompensated harm to society. The founding contribution to the Law and Economics discussion by Ronald Coase is given a thorough treatment. Next, this article turns to the dominant explanation of corporate structure, namely the Law and Economics model developed and expounded by Easterbrook and Fischel. It then applies the theoretical discussion in a case study of the world’s largest corporation, WAL-MART, Inc. It next examines the relation of social costs and corporate legal structure. It concludes with some recommendations for corporate reform.

* B.Th., M.A., LL.B., M.A., LL.M. Lecturer, School of Law, University of New Castle, NSW, Australia. The author practiced law in Canada, and has taught law in Canada, Mexico, and Australia.
** The Author would like to thank Dr. L. Chappele and Dr. K. Sadiq of the University of Queensland, Australia, as well as Michele Zerr for her assistance with this article.
Table of Contents

I. Introduction ........................................................................................................... 2
II. How to Read this Paper: Dimensions of the Discussion ................................. 5
   A. Ten Dimensions and the Law and Economics Discussion ............................ 7
III. Corporations ......................................................................................................... 8
   A. Concession Theories ...................................................................................... 9
      1. Political Entity ......................................................................................... 10
      2. Communitarian ......................................................................................... 11
   B. Contractarian Theories ................................................................................. 11
   C. Criticisms of the Models ............................................................................. 13
   D. The Ideological Divide ................................................................................... 15
   E. Shareholder Primacy ..................................................................................... 16
IV. Costs ..................................................................................................................... 17
   A. Coase's Theory on Social Costs .................................................................... 20
   B. Coase's Recommendations: Private vs. Public ........................................... 23
   C. Coase's Assumptions .................................................................................... 23
   D. Criticisms of Coase ....................................................................................... 24
V. Law and Economics ............................................................................................... 27
   A. The L&E Model of the Corporation .............................................................. 27
   B. Assumptions of the L&E Theory of Corporate Law ..................................... 28
   C. Criticisms of the L&E Model ....................................................................... 30
VI. Case Study ............................................................................................................. 33
   A. Community Impact ...................................................................................... 35
   B. Supplier Social Costs .................................................................................... 36
   C. Labour Social Costs ..................................................................................... 37
   D. Democracy .................................................................................................... 40
   E. Cultural Control .............................................................................................. 42
   F. Foreign, “Outsourced” Social Costs .............................................................. 43
   G. Consumerism .................................................................................................. 45
   H. Environmental Costs .................................................................................... 46
   I. Wal-Mart’s Position ........................................................................................ 48
VII. Corporate Vehicle and Social Costs ................................................................. 49
VIII. Conclusion .......................................................................................................... 53

I. INTRODUCTION

Social costs of business activity have been a concern of economists, politicians, lawyers, business people and society at large for decades. With the passage of time, our awareness of the nature, extent, dimensions, and
incremental and accumulating impact of social costs has increased dramatically. Various approaches to the problem have been suggested, ranging from governmental regulation, to cessation of activities, to free markets.

Regardless of one's underlying commitments, it cannot be denied that with respect to the most significant social cost—the threatened habitability of the planet—the current approaches are failing. Yet despite our knowledge of the impending disaster and its causes, to date there has been very limited success in coordinating efforts to address it. From this failure it may be argued that indeed there are other social costs which have yet to be clearly identified that are, nevertheless, accumulating, possibly with significant consequences.

This study considers some of these social costs which at present are only poorly identified and not much studied. Social costs are the negative by-products of commercial activity not compensated for by the beneficiaries of the activity. Instead, these negative by-products or "costs" are borne by the rest of society—hence, "social costs." They are the costs to others or society at large for the conduct of business. As will be discussed, social costs often involve coordination problems—problems that can only be solved by people's coordinating their efforts rather than simply acting as individuals seeking the furtherance of their own interests. Obviously, the previously mentioned matter of climate change is one such matter. Another less obvious one arises from business activity, particularly through the corporate vehicle.

In considering corporations in society, one must have an understanding of the nature of the corporation, ideas about the nature of society, and the role of law, business, people and corporations in the composition and functioning of society. From a corporate law perspective, one needs to consider who counts as a member of the corporation; whether it be shareholders, directors,

---

1. UNEP Climate change, at http://climatechange.unep.net (last visited Nov. 6, 2004). The website suggests that there is indeed a climate change problem caused by human activities and that the consequences could be drastic.

2. The most recent failure of coordination has been the failure of the United States of America and Australia to sign the Convention and Kyoto Protocol. For recent information on this matter, see The Convention and Kyoto Protocol, at http://unfccc.int/resource/convkp.html (last visited Nov. 6, 2004). For a discussion of the problem as a coordination problem, see Katharina Holzinger, Aggregation Technology of Common Goods and Its Strategic Consequences: Global Warming, Biodiversity and Siting Conflicts, 40 EUR. J. POL. RES. 117 (2001). Ecological economists have been making an effort to address environmental problems resulting from perspectives promoted by their discipline. For a helpful introduction to ecological economics and its relation to law, see Douglas A. Kysar, Sustainability, Distribution, and the Macroeconomic Analysis of Law, 43 B.C. L. REV. 1 (2001).
managers, employees and other suppliers, or possibly even including society at large. Corporate law must consider the coordination of all of these elements of society and the costs imposed on society. The focus of this article is on the social cost—i.e., the cost to the people who make up society—of the activities of large corporations. In order to create an informed context for the discussion, all of these issues will have to be addressed.

To avoid creating an argument based on mere speculation about social costs and corporations, the second part of this study will be a case study of Wal-Mart. The study will attempt to answer the question: Are there significant social costs that are poorly identified and not well studied associated with large corporations? This question is becoming increasingly important as a consequence of globalization, which is driven largely by corporations and which has significantly increased corporate power. Multinational corporations and their investors have been implicated in the inhumane and devastating policies known as “Structural Adjustment Programs” promoted by the World Bank and the International Monetary Fund, and the manifestly unfair trade policies of the World Trade Organization. The great power of these corporations is not being used for the betterment of society, and so it is incumbent upon scholars to study and consider carefully the activities of these members of society.

This study will examine critically theories of the corporation, then the views and theories of Ronald Coase, a leading economist and thinker on social costs. Next, it will turn to a critical review of the Law and Economics analysis of corporate law. This Law and Economics perspective will be used since its descriptive power, particularly in corporate law, is widely accepted.

3. See Joseph E. Stiglitz, Globalization and Its Discontents 128-30 (2002) (a thoroughgoing and stinging indictment of the IMF and, to a lesser degree, of the World Bank, for which Stiglitz himself served as chief economist). Stiglitz’s comments are mostly restricted to the investors. The investors, however, are those who invest on behalf of corporations in hedge funds, futures and options to limit the exposure of their corporate sponsors. See also Noam Chomsky, Profit Over People: Neoliberalism and Global Order 19-20 (1999) (discussing the collusion, if not control, exercised by international financial interests and multinational corporations over the IMF and World Bank, as part of the Washington Consensus). Chomsky further discusses the WTO as charged with the task of exporting American values. Id. at 63-72.

4. Much of Chomsky’s work is a sweeping review and analysis of the involvement of corporations in the political system of the United States of America. Chomsky shows how corporations have corrupted government and subverted democratic processes to serve their own interests. See, e.g., id. at 38-39, 61. Chomsky refers to the trend as the “corporatization of America.” Id. at 132. See, e.g., Tan Yock Lin, Legal Change and Commercial Law in Singapore, in East Asia—Human Rights, Nation—Building, Trade 27, 29 (Alice Tay ed., 1999) (describing the role of Multination companies in thwarting private enterprise in Singapore).

In order to understand the Law and Economics perspective, it will be necessary to analyse its presuppositions, and then see how these approaches produce outcomes consistent with their presuppositions. Finally, it will apply this critical analysis to the activities of the specific business that serves as the case study, Wal-Mart, by identifying the social costs, and determine what, if any, relation there is between these social costs and the corporate vehicle-corporate law.

The study has identified a number of poorly considered social costs created by Wal-Mart. Furthermore, for various reasons, it will be shown that these social costs tend to fall outside of the traditional Law and Economics paradigm, and so fail to be considered as matters of corporate law. Finally, the study will conclude with some suggestions for further law reform and directions for future study.

The study is limited to the discussion of a single case. Because of the innovative nature of the study, there is limited data available for broader study. In addition, at this stage in the research, it is the author’s opinion that a deeper study, identifying more specifically and identifying a higher quantity of social costs is more important or helpful than a broader, more general discussion. Accordingly, the generalizations which can be made from this study are limited. It does not purport to be suitable to all jurisdictions, nor to all corporate models, nor to all industries. It is the study of a specific multinational retail sales corporation, which happens to be the largest corporation in the world.6

II. HOW TO READ THIS ARTICLE: DIMENSIONS OF THE DISCUSSION

At the outset, I believe it is necessary to identify the main belief sets forming the backdrop for this discussion. In his fascinating and comprehensive analysis of academic legal debate, Professor Gerald Wetlaufer observes that, “conversations and arguments are less easily understood, less easily learned, less productive, less conclusive, and sometimes less civil than we might think it reasonable to expect.”7 He comments: “We hear a great many arguments in which it seems that people ought to be convincing one another but, in fact, are not. We see arguments that fail to persuade, disagreements that never end, and, all too often, partisans who neither

understand nor respect their adversary’s positions. Few of those engaged in
the dialogue would disagree with this comment; hence, his analysis of the
underlying philosophical commitments that are the cause of this inability to
communicate within the academic legal community are worth identifying for
improving an understanding of the intractability of the advocates of the
various positions presented in this article.

Wetlaufer identifies a “Master Paradigm” in which most legal dialogue
is conducted. That paradigm is liberalism—views of individualism,
autonomy, and freedom, and the belief that the role of the state is protector of
the individual and those freedoms. This view includes commitments to
rights discourse, a particular version of rule of law, notion that public and
private spheres are distinguishable realities, and that state action is appropriate
only in the public sphere. Any discussion that does not bow to these primary
commitments is simply dismissed. Within this larger paradigm, there are two
main schools of thought that have relevance to this discussion. They are the
Legal Realists and their most important successors, the Law and Economics
scholars, and the Legal Positivists. Whereas the Legal Realists see law as
nothing more than the conventions of a society (i.e., changeable, measurable,
instrumental in achieving specified objectives, having no particular
commitment to method), the Legal Positivists see law as an objective,
independent first principle. More contentiously, at least in the strong version,
the Legal Realist and Law and Economics scholars see all value and morals
as nothing more than the cash amount a person is willing and able to pay.
Furthermore, Law and Economics adherents, at least the neo-classicist
scholars, view justice as the mere maximization of aggregate wealth. Any
notion of redistribution or movement of costs, other than as placed by the
market, is inefficient diminution of wealth maximization.

Legal Positivists, by way of contrast, view law as an independent
deavour, an independent discipline with its own set of norms, methods of
analysis and values. Legal Positivism carries with it commitments to
philosophical positivism, utilitarianism, and classical liberalism.

8. Id.
9. Id. at 9.
10. Id.
12. Id. at 41 n.144 (citing Posner). For criticism of Posner’s views on this matter, see Whitney
13. Wetlaufer, supra note 7, at 38.
14. Id. at 42 n.148.
15. Id. at 44-45.
Additionally, it holds to notions of justice as fairness, Aristotelian notions of corrective and distributive justice, and practical reason. It sees moral knowledge as both possible and objective.

The Law and Economics scholars clearly belong to the Legal Realist tradition and clash with the Legal Postivists. Before coming to any conclusion concerning the matters discussed in this article, it is important to consider the validities of each frame of reference, regardless of which set of a priori commitments one finds oneself drawn to. As is most often the case in such debates, neither has a corner on the truth and so it behoves all disputants to consider the contribution of the other.

Wetlaufer proceeds to identify ten dimensions of prior commitments that set the legal debate into different directions. These dimensions are:

1. the fairness and legitimacy of the existing order;
2. prime values and projects;
3. focus and center of attention;
4. human nature and social existence;
5. the nature and consequences of language;
6. the nature of knowledge and the possibilities of reason and objectivity;
7. the relationship between law and other disciplines;
8. interpretive strategies and forms of argument;
9. the possibility of the rule of law; and
10. the consequences of speaking against either of the above.

One’s various commitments along the above ten dimensions primarily determines what one finds, and what one finds acceptable among various possible outcomes.

A. Ten Dimensions and the Law and Economics Discussion

Among the commitments Wetlaufer discusses, we can identify the following dimensions as critical to this discussion: (1) the fairness and legitimacy of the existing order; (2) prime values and projects; (3) focus and center of attention; and (4) human nature and social existence. As will be discussed in more depth later in this article—concerning the value assumptions of the Law and Economics movement—the Law and Economics

16. Id. at 47.
17. Id.
18. For example, law is to facilitate wealth making maximization, creation of a just society, or ensure order.
19. Wetlaufer, supra note 7, at 60.
discussion is decidedly in favour of the status quo, sees efficiency and wealth maximization as the prime value and project, is focused on individual wealth and rights, and denies the existence of any such thing as society. As a discipline, Law and Economics' commitment to neo-classical economics incorporates by default the assumptions of neo-classical economics. One of the hallmarks of neo-classical economics is its commitment to radical individualism. Individuals are the only legitimate subject of study as society is nothing more than a collection of individuals.

III. CORPORATIONS

To understand the corporation, its role in society and the problem associated with controlling its social costs, there needs to be a brief discussion of the nature of the corporation and corporate theory. The nature of the corporation can be explained by a review of some of its historical developments and a brief examination of some of its models.

In its early form, the joint-stockholder corporation would have passed liability for social costs onto the shareholders. This potential passing of liability to shareholders may have had a significant impact on corporate behaviour and subsequent corporate development if tort law had been more mature and social costs more clearly identified. Interestingly, it should not be supposed that social costs were invisible. Indeed, there were high rates of worker injury and death; the courts, however, placed no liability on the corporate owners for such injury. Society had to bear these costs for the benefit of industrialization, the benefit of which primarily accrued to the entitled classes. As a theory popular in the late 19th and early to mid-20th century, the main social costs identified were smoke and other visible


industrial atmospheric discharges, which the law deals with as a matter of mere nuisances between neighbours.24

A. Concession Theories

Concession theorists note that the corporation owes its existence to a governmental concession. In the beginning, governments delegated and granted trading rights to corporations.25 Corporations were permitted to carry on only those activities authorized in the concession granted by the government. The limits of the concession were set out in the articles of incorporation or the constitution of the corporation. Given this concessionary nature of the corporation, the government retained certain rights concerning the governance and operation of the corporation.26

The roots of this view are in the corporation’s history. In the concessionaire view, the corporation is an entity different and separate from the shareholder/ investors. It is often referred to as the legal fiction or corporate personality theory. In its essence, this model focuses on such characteristics as the corporation’s legal identity, which remains independent of the parties involved in maintaining the corporation’s daily activities, like managers, investors, or employees. It also highlights the corporation’s legal rights and responsibilities as a legal person who can sue in its own right and be sued, pay taxes, and otherwise subject, independently of its members, to the


26. An interesting, peculiarly Australian view, that may be viewed as an offshoot of the concessionaire theory is “constitutionalism.” As argued by Australian corporate law scholar, Stephen Bottomley, “[corporations] themselves are systems in which power and authority, rights and obligations, duties and expectations, benefits and disadvantages, are allocated and exercised. . . . Each company is a body politic . . . .” Stephen Bottomley, From Contractualism to Constitutionalism: A Framework for Corporate Governance, 19 SYDNEY L. REV. 277, 291 (1997). Dine observes that the concessionaire view is susceptible to the criticism that the corporation is no more than a mere fiction. If it is not made up of the solid, physical shareholders, acting in concert to create a common enterprise, the corporation has no more substance than a mere idea. Further, while it may explain the foundation of the corporation, concession theory fails as an operational theory. It does not explain by whom or how the corporation is to be run. Nor yet does it set any limits on state involvement. Indeed a pure concession view allows the corporation to be a mere instrument of the state. Dine, supra note 25, at 22-24.
laws of society. In this view, the corporation is a concession granted by the government to a group of would-be investors. As a concession from the government, the corporation continues to be subject to the government's will. If one accepts a concessionaire view of the corporation, it is easier to see the argument for stakeholder involvement or at least for government regulation that limits social costs, such as greenhouse gas emissions permitted to a particular corporate entity. As a governmental concession, the corporation owes duties back to the government. This obligation, however, does not extend automatically beyond a duty to the government into a general duty to society. The concessionaire model of the corporation in the historical context allows social costs as unfortunate consequences, to be borne by society for the benefit of the investor.

1. Political Entity

In a variation of the concession theory, some corporate theorists focus on the corporation’s political character. Its political characteristics are its constitutional foundation setting up internal control structures similar to governments, its power, its decision making processes, its need for managers to balance competing interests, and such broader concerns as implied by the Corporate Governance movement. Some scholars draw in further political implications from this model such as the democratic principle that those affected by decisions should have a voice.

Social costs in this model are viewed much as social costs in all political decision making. They are part of the society. The issue in corporate law, of course, is who makes this “corporation’s society”? Is it investors and directors only, or does it include employees and other suppliers, or society at large? Perhaps the most important benefit of the model is the acknowledgement of the corporation as a powerful, political entity. Although currently out of fashion because of its connection to the concession theory, it may yet have some life.

27. See David Millon, Frontiers of Legal Thought I: Theories of the Corporation, 1990 DUKE L.J. 201.
29. See DINE, supra note 25, at 21.
2. Communitarian

These views—concessionaire and political views—are subsumed in the communitarian model of the corporation. Communitarians argue that the corporation is a community, a political entity, granted a separate identity by the government, participating in society at large with its own independent rights, privileges, duties and obligations. Accordingly, it should be responsible for its social costs, just as every other rights bearer in society.

B. Contractarian Theories

Contractarians view the corporation as a form of contract between its members. This theory posits the corporation as a private matter between individuals and accordingly places no additional duty on the corporation than that which exists on each separate individual involved in the corporation. The corporation, as nothing more than a collection of individuals, is a private matter and as such should be subject to the least possible government interference.

The roots of this theory go back historically to an era when the characteristics of the modern corporation—particularly, limited liability—had not yet existed. This model of the corporation comes from corporate origins of the joint-stockholder company. In that model, the corporation is simply another partnership-like arrangement in which the shareholders are essentially owners and are liable for the debts of the company. The corporate vehicle is a convenient private financial arrangement, which allows entrepreneurs to invest jointly in enterprises too large or too risky to undertake on a single investor basis. This model is often called the aggregate model and in it the directors are the agents of their principals, the shareholders. It is discussed primarily as the aggregate model, meaning that the corporation is nothing more than the aggregate of the individual members.

32. See PROGRESSIVE, supra note 28.

33. There are other approaches to the analysis of corporations as voluntary collectives. See, e.g., Paula J. Dalley, To Whom It May Concern: Fiduciary Duties and Business Associations, 26 DEL. J. CORP. L. 515 (2001).

34. See, e.g., Max Radin, The Endless Problem of Corporate Personality, 32 COLUM. L. REV. 643 (1932).

The economic contractarian model, as distinguished from the legal contractarian model traces its origins at least as far back as the economist Ronald Coase. Coase first proposed that the corporation is a type of firm. By describing the corporation as a firm, Coase means that this type of organization operates as a more efficient means of production than the market, and it does this, he claims, by grouping people and inputs together, combining tasks in one enterprise and thereby lowering transaction costs. In this model, there is a direct connection and related accountability between the contracting parties, the capital provider-shareholders and the managers. As economist Milton Friedman has famously put it “He [an executive] has direct responsibility to his employers. That responsibility is to conduct the business in accordance with their desires . . . to make as much money as possible.”

Contractarians reject the notion of the corporation being a body independent of the shareholders and in fact reject the very idea of corporation. Rather, a corporation is merely a nexus of contracts. Logically, it cannot have obligations distinct from the obligations of its individual members. Therefore, the notion of corporate social responsibility—as distinct from the responsibilities of the individual shareholders—is a non sequitur. It is simply a logical contradiction.

In the contractarian view, as Millon explains it:

State corporate law provides the terms of the contract by which shareholders purchase management’s undivided loyalty to their welfare . . . to the extent that management’s pursuit of shareholder welfare threatens nonshareholder interests, workers, creditors, and other affected nonshareholders are free to bargain with shareholders (through their agents) for whatever protections they are willing to pay for. This view assumes that feasible (that is, not excessively costly) contracting strategies exist for correction of the
corporate contract have failed to bargain for. Many advocates of this view fail to recognize that markets are inevitably incomplete, do not exist for many social costs, and accordingly, cannot be considered an appropriate or sufficient solution to social costs.  

Social costs in this model are part and parcel of this group’s business activities, and as such, those who complain about them should be subject to the same constraints and bargaining positions as any other member of society, including those contracting together forming the corporate contract. The core contractors are the shareholders and thus their interests should be the focus of corporate concern. This focus leads to the related contractarian model known as the shareholder primacy model.

C. Criticisms of the Models

The contractarian model has a number of shortcomings. Critically, it fails to explain the most significant feature of the corporation—that is to say it does not account for limited liability. Nor do contractarian models adequately address other corporate rights such as the right to hold property and the right to freedom of expression. These rights are held by the corporation independently of its members.

An important aspect of some social costs, as we shall see, is that they arise precisely because of inabilities to contract. Markets will always be incomplete, and accordingly, to suggest that social costs are a mere problem of contracting suggests a failure to understand the nature of the problem (to address social costs in the market would require new types of property to be

42. Dine notes the state involvement in creating the limited liability aspect of corporations. This grant of limited liability is what made corporations such an attractive option for conducting business (Eley v. Positive Government Life Assurance (1876) 1 Ex D 88) and essentially what gave rise to their dominance in commerce. DINE, supra note 25, at 4. The explanation that this would eventually have been contracted for, according to Dine, is not supported by the facts. See proposed solution in Michael Whincup, Inequitable Incorporation—The Abuse of a Privilege, 2 COMPANY L. 158, 158-60 (1981). The English law still rests on the decision of the House of Lords in Salomon v. A. Salomon & Co., 75 L.T.R. 426 (1897).
created and distributed) and the nature of markets as incomplete along with other market failures.

The univocal focus on efficiency supported by contractarian models brings the question of why efficiency should be set as the prime value. As Millon observes: "References to efficiency simply beg the underlying question of why efficiency should provide the sole normative criterion. As a society, we have not embraced the market as a totalizing model for the definition of rights and responsibilities." Furthermore, this focus on the bottom line always creates a strong incentive to externalize costs, increase production, and thereby increase profit. As Horrigan observes: "[F]inancially-based shareholder focus . . . 'allows the corporation to externalise the costs of maximising stock prices onto everyone except the stockholders; that includes employees, the environment, consumers, suppliers and the community at large.'" Contractarians are focused on internal corporate activity and apply a cost-benefit analysis to a relatively narrow range of items that are more susceptible to numeric measurement.

Critics of the concessionaire model, such as Easterbrook and Fischel, note that people will choose to associate in manners suitable to their interests, regardless of government recognition. Accordingly, they claim that such things as limited liability would have been contracted for had the government not granted it through legislation. Further, concessionaire critics point to the non-existence or fictional nature of the "body" of the corporation. Where is the “concession” or “community” apart from the freely contracting members? To have anything more or other than the individuals is nonsense, in the most literal sense of the term.

Ultimately, we are left with Hart's observation: "a survey of competing theories of ‘the corporation’ leaves one to conclude that none has survived intact."

---

43. Contractarians’ efficiency focus follows closely on the economists’ view that creating wealth is the sole objective of corporate activity. Any increase in wealth is a social benefit, and permits turning a blind eye to the distribution of that wealth or the costs of producing that wealth.

44. Millon, supra note 40, at 1386.


D. The Ideological Divide

Underlying this war of models is a much deeper ideological conflict. Contractarian advocates start from the idea that people are isolated autonomous rights bearers. Included among their sui generis rights is the right to decide how to dispose of their property rights and in the case of the corporation, their property rights as shareholders. They view the corporation as a nexus of contracts between private individuals in which the government has no business.

Communitarian advocates, by way of contrast, view the individual as set in a context, and that context is a social context. They view liberty as having positive duties. From their perspective: “Liberty is empty without taking into account those primary needs upon which adequate conceptions of individual dignity and human flourishing depend.”48 They view the corporation as a social body—as a member of society, and a significant member at that. They emphasize the power and effects of corporations in society. In addition, communitarians are, in Millon’s words, “skeptical about the practical efficacy of contract as a mechanism by which nonshareholders can protect themselves ex ante from . . . harmful effects.”49

As Millon frames the debate: “what does set communitarians apart from contractarians is the communitarians’ strong skepticism toward the baseline presumption that contract alone should specify the terms of corporate governance relationships.”50 At a fundamental ideological level, contractarians and communitarians are divided. Contractarians believe that justice is manifest in the status quo and the only legitimate interests are those bargained for: “For communitarians,” as Millon puts it, “justice does not require endorsement of the existing distribution of wealth and bargaining capability. They seek instead to reform corporate law so as to foster individual dignity and promote societal welfare.”51 Such deep ideological debates are not about to be settled on the basis of superiority of models.52

49. Id. at 1379.
50. Id. at 1381.
51. Id. at 1386. In Millon’s review of Chayes’s theories, he summarizes the issue at a personal level: “Having induced nonshareholders to rely on legitimate expectations of fair dealing, shareholders therefore may forfeit the right to insist on contract terms guaranteeing profits at the expense of others.” David Millon, The Ambiguous Significance of Corporate Personhood, WASH. & LEE PUB. L. & LEGAL THEORY RES. PAPER SERIES 23 (Working Paper No. 01-6, 2001).
52. See Wetlaufer, supra note 7.
The importance of how one understands the corporation should not be underestimated. If one views it as a government franchise, the government has a right to control it, and society has a right to demand certain behaviours of it, including internalizing social costs. If, however, one views the corporation as a mere official recognition of a spontaneously occurring organization of individuals, there is no justification for governmental interference. The simple fact that some individuals have decided to come together to conduct business does not suddenly or automatically give the government the right to interfere in the private affairs of its citizens, and certainly not to place additional obligations on the individuals who form the corporate contract.

Perhaps most significantly, regardless of the model one accepts or what view one takes of the corporation, any political positivist analysis makes obvious the observation that corporations have grown in terms of their power. Their economic might and control over resources is astounding. No less than fifty of the world’s largest one hundred economies are corporate bodies, and studies indicate that the control of these bodies tends to be concentrated in the hands of a very small number of people.

E. Shareholder Primacy

The model of the corporation in vogue at the present is a variant of the contractarian model, known to business scholars as the shareholder primacy or profit maximization model. This view is that the corporation’s objective

53. See Corporate Models, supra note 22.
or *raison d'etre* is to produce the greatest profit. Although various reasons are advanced as to why shareholders of all the corporation’s suppliers should be privileged above all others, none is particularly convincing, at least in larger corporations. In order to do so, it must have high revenues and low costs. In other words, it must be efficient. This use of the term “efficiency” is important and should be distinguished from the similar, but different, use of the term “efficiency” as used by economists. To economists, efficiency means making the most effective use of resources thus creating the maximum product possible from those resources. Business scholars mean creating the maximum profit from the resources.

While both scholars deal with money as the main resource, the difference is in the means to, or view of, the end product. The economist is concerned with both internalities and externalities, and so, how these things are accounted for, whether public or private, is irrelevant. The business scholar, however, sees a great distinction between internalities and externalities. For the business scholar, the greater the negative externalities, the greater the positive internalities or “profit” and hence the more attractive the enterprise appears to be. The more one is able to externalize the negatives the more profitable, or desirable (i.e., get the costs outside of the corporation) the remainder. Hence it is only logical to observe that increased activity of business corporations and increased negative externalities are correlated phenomena.

**IV. Costs**

The next important discussion concerns the notion of costs. At its most basic level, the existence of a thing precludes the non-existence of that same thing. This mutually exclusive existence/non-existence condition creates what economists refer to as an externality. That is, each condition creates an inevitable anti-condition or “externality.” Externalities are either positive (beneficial) or negative (harmful). When the externality is negative, it is called a cost. Costs are the negative impact or loss of any activity or thing.


57. Interestingly, some calculations indicate that the total economic production of activity on the planet results in a net loss once all “externalities” are factored in. Accordingly, the terminology of “externality” has been questioned. Kysar, *supra* note 2, at 35. Kysar attributes original identification of the problem of externalities to A.C. Pigou, *The Economics of Welfare* 149-79 (1920). *Id.* at 9 n.29.
Externalities are explained by Cooter and Ulen as a problem that occurs "when the utility or production functions of different people are interdependent, . . . [imposing] benefits or costs upon each other, regardless of whether or not they have agreed" and are externalities "because the costs or benefits are conveyed outside of a market." As noted in the introduction to this article the topic is social cost—i.e., the cost to the people who make up society.

There have been a number of approaches to the problem of social costs. One approach has been to increase private property. Hardin’s famous article “The Tragedy of the Commons” is often cited as proof positive of the impossibility of preserving the environment without private property rights. In his startling article, Hardin observed that when people had unlimited access to communal property or “commons,” their overuse of the commons led to its demise. By way of contrast, Hardin observed that private property is maintained at sustainable levels. From this observation, Hardin concluded that the best way to preserve things held in common is to break up the commons, destroying public property rights, and creating private property.

Hardin’s argument has been adopted as a model for much economic thought and subsequent policy; however, as we have seen, social costs are mounting in both quantity and seriousness of consequence. This conclusion, too, should cause us to re-examine Hardin’s approach. Hardin’s analysis is based on the usefulness of common property rights, or more accurately, the results of holding property in common. The general analysis, however, fails to acknowledge that the destructive impact of common use only occurred once the profit motive was introduced. In other words, as long as people are using

58. ROBERT COOTER & THOMAS ULEN, LAW AND ECONOMICS 139 (2d ed. 1997).
60. Id. at 1244.
61. Id. at 1245.
62. Id. at 1247. The discussion which ensues ignores that property is a social construction, meaning that property is whatever a society decides to recognize and value. Examples of property can include honours, offices, and humans. See MICHAEL WALZER, SPHERES OF JUSTICE: A DEFENSE OF PLURALISM AND EQUALITY 7-9 (1983). See also ARISTOTLE, NICHEOMACHEAN ETHICS 109-14 (David Ross trans., 1998).
63. Hardin was an internationally recognized authority on population control and policy. It is worthwhile to note that he was not blind to the coordination problem in pollution control matters and indeed it was one of his concerns in writing his piece. See, e.g., Hardin, supra note 59, at 1245.
64. David Feeny et al., The Tragedy of the Commons: Twenty-Two Years Later, 18 HUM. ECOLOGY 1 (1990). See Ortega Santos, Commons: Past and Present in Mediterranean Societies: Property Rights and Modes of Use, available at http://dlc.dlib.indiana.edu/archivei0000320/00/santosa040800.pdf(2000). This discussion was presented at "Constituting the Commons: Crafting Sustainable Commons in the New
goods in common for their own sustenance needs, they are able and willing to manage property communally. Once, however, the ability to profit is introduced, the over-exploitation of the resource occurs and some form of control over the exploitation of the resource appears necessary. Still, whether that control is best done by means of privatization or some other regulatory regime, remains unclear.

Other criticisms of Hardin's view have been developed. For example, scholars have noted that Hardin's assumption that the only rational behaviour is to increase material consumption without regard for leisure, cultural or intellectual activities. Further, Hardin equates self-interest with certain ideas about private property, individual freedom, and the utility of maximizing wealth in the free market system. In essence, Hardin's thesis is "that people cannot work out sustainable ways to utilize common-property resources on their own" and therefore all property must be given over to private control. Hardin's thesis has been a critical in supporting corporate domination of more and more of the commons, for if individuals cannot organize the commons as common property, more private property must be created, and those with the capital to accumulate the property have the social obligation, one could argue, to do so. It is a basic justification for corporate domination of the world.

Another approach to costs has been legal. Traditionally, law has been the way of dealing with problematic costs between people. Either through legislation or by common law, law has been able to resolve property rights...
disputes through its various principles and doctrines. These principles include notions of justice and rights, and the doctrines include the doctrines of nuisance, causation, and rights in rem and in personam. More recently, Law and Economics have been combined to develop an economic analysis of traditional legal problems. A leader in this new discipline of Law and Economics is the University of Chicago economist, Ronald Coase, to whose analysis we now turn.

A. Coase’s Theory on Social Costs

Coase’s landmark article “The Problem of Social Costs” is an elegant argument, concerning cattle herdersmen and farmers, doctors and confectioners, and neighbours of adjoining properties. His article is an effort to demonstrate that people will resolve their disputes smoothly regardless of what the law says. Essentially, Coase argues that where people can bargain, they will bargain for the rights that will bring them the best return on their investment, and further, that where they can do so in a costless environment without legally imposed liability structure, they will do so creating from an economic perspective, the most efficient use of resources and maximum level of production.

Coase correctly identifies the issue as “should A be allowed to harm B or should B be allowed to harm A?” Coase is also correct in his analysis: From an economic perspective, who gets the right to harm is irrelevant.

To make his point, Coase examines the case of Bryant v. Lefever, where the court had to decide the rights as between neighbours. Should a neighbour who had been using his chimney for several years without problems have the right to continue to do so? Or should the other neighbour be permitted to stack wood on top of his house for his own benefit although causing the neighbour’s chimney to smoke? Coase said the issue should be resolved by the economics of the situation.

70. Minda, supra note 5, at 604.
71. Coase, supra note 24, at 1.
72. Id.
73. Id. at 6-8.
74. Id. at 2. This perspective is what is so foreign to lawyers and most people. Both legal and traditional thinking is that it does matter who does what to whom. The issue from this perspective is: Who caused the harm. That is the person who should pay for damage. Cooter & Ulen, supra note 58.
75. Bryant v. Lefever, 4. C.P.D. 172 (1878-1879) (cited in Coase, supra note 24, at 11). Coase’s assumption is that all activity is to be measured against or valued by its relation to production.
76. Coase, supra note 24, at 15.
From Coase’s economic perspective, the problem is caused in part by each party—the one party by lighting his chimney and the other party by stacking wood.\textsuperscript{77} He suggests that the case should be resolved by looking at the economic costs and economic benefits generated by the activities, and then engaging in transacting so as to produce the most efficient outcome.\textsuperscript{78} Causation is not the issue; the issue is permitting activities that make the most of the resources.\textsuperscript{79}

Coase points out that:

The reasoning employed by the courts in determining legal rights will often seem strange to an economist because many of the factors on which the decision turns are, to an economist, irrelevant. Because of this, situations which are, from an economic point of view, identical will be treated quite differently by the courts. The economic problem in all cases of harmful effects is how to maximise the value of production.\textsuperscript{80}

The court’s analysis of \textit{Bryant v. Lefever} was based on the doctrine of lost grant.\textsuperscript{81} Lord Cotton identified the legal issue as identifying rights in order to trace causation and to identify in turn whose right preceded whose.\textsuperscript{82} This, Coase recognized, is ultimately a fruitless exercise. From the legal perspective then, the issue becomes a matter of pragmatics.\textsuperscript{83} The law solves the problem by drawing an arbitrary line, calling it the “doctrine of lost grant” and finishing the case.\textsuperscript{84}

Coase’s comment about this legal solution is humourous. He writes: “the ‘doctrine of lost grant’ is about as relevant as the colour of the judge’s eyes.”\textsuperscript{85} But the legal doctrine embodies old solutions to problems only relatively recently recognized by economists. To explain this legal result in terms meaningful to an economist, one would say that to follow the line of causation all the way back in history to the right associated with the original owners and then trace them forward through title is to increase information costs exponentially and fail to appreciate bounded rationality of the human condition. Coase has failed to address the reasoning for legal rules, and in this case, limited information and information costs, undetected externalities, the

\begin{itemize}
\item \textsuperscript{77} \textit{Id.} at 11.
\item \textsuperscript{78} \textit{Id.} at 13.
\item \textsuperscript{79} \textit{Id.}
\item \textsuperscript{80} \textit{Id.} at 15.
\item \textsuperscript{81} \textit{Id.} at 11-12.
\item \textsuperscript{82} Coase, \textit{supra} note 24, at 12.
\item \textsuperscript{83} \textit{Id.} at 15.
\item \textsuperscript{84} \textit{Id.}
\item \textsuperscript{85} \textit{Id.}
\end{itemize}
incremental nature of some externalities, and the fundamental fairness required for a society to continue peacefully. For the economist, the role of law is solely to define legal rights and provide predictability. These legal rights and institutions permit people to act in self-interested ways without regard for the non-legally enforceable (property) rights of others. Economics fails to appreciate much about law and the society it promotes.

In Coase's hypothetical world, property rights law is irrelevant because it does not add to efficiency and hence does not add to overall social product. People resolve their disputes on the basis of the dollar value of an activity. Which activities should be undertaken are determined on the basis of the total social value of potential production. This calculative exercise, argues Coase, should include total social costs. Imposition of liability by law makers should be avoided as creating legal liabilities increases transaction costs. Reallocation in a society with legally imposed liability schemes impairs achieving increased social production because the parties are forced to expend greater effort to reallocate the resources.

Given the importance of his insight and the remarkably broad application his theory has found, it is unfortunate that Coase has identified only one of the assumptions of his model: that it works only in a zero-transaction cost environment. Had he considered other assumptions, his theorem may have contributed to a much deeper, more broadly socially beneficial outcome and included more forcefully the social costs he considered. Having limited his discussion of the phenomena of social costs in private transactions and his explanation of assumptions to the zero-transaction costs environment, he draws the economic conclusion that the initial allocation of rights is unimportant. His argument, however, is meaningless in the real world—and interestingly, this criticism is not a criticism with which he would disagree. As he explains, economic analysis has a different objective, to which we turn next.

86. Id. at 18.
87. Id. at 31. Cooter and Ulen note this as the costs of non-cooperative legal rules in their example where instead of relying on competitive legal rules, by coincidence, a cattle rancher and corn farmer get married. COOTER & ULEN, supra note 58, at 80.
88. See MALLOY, supra note 45 (author attempts to address this problem by discussing semiotics, although his success in doing so may be questioned).
89. Despite the acclaim his article received, subsequent studies have put his views into doubt. More recent studies suggest he may not be correct. See, e.g., Dan Usher, The Coase Theorem is Tautological, Incoherent or Wrong, 61 ECON. LETTERS 3 (1998); Cooter, infra note 100; Andrew Halpin, Disproving the Coase Theorem? (Working Paper), available at http://ssrn.com/abstract=424820 (last visited Nov. 6, 2004).
90. Coase argues that economic argument needs to be more focused on reality.
B. Coase’s Recommendations: Private vs. Public

For Coase, the public-private distinction is irrelevant. The issue is maximizing overall social product. Coase suggests that the appropriate level of analysis in nuisance is total social product and rights, not things such as factories, smoke and homes.\(^9\) The issue for Coase is “one of choosing the appropriate social arrangement for dealing with the harmful effects. All solutions have costs . . . .”\(^9\)

Coase identifies three alternative social arrangements or orderings of production: government, the private firm, and do nothing. He allows that at times government may more efficiently deliver services, but to him, the central distinction is that government has the power to seize private property.\(^9\)

Coase’s analysis has broad implications for law. In matters of nuisance or social costs, traditional legal analysis gets it wrong. As he puts it, “[t]he belief that it is desirable that the business which causes harmful effects should be forced to compensate those who suffer damage is undoubtedly the result of not comparing the total product obtainable with alternative social arrangements.”\(^9\)

As he observes, “the proper procedure is to compare the total social product yielded by these different arrangements. The comparison of private and social products is neither here nor there.”\(^9\) But there are a number of highly problematic assumptions inherent in his approach in which all is merely a matter of the transaction of property rights. We turn to discuss these assumptions next.

C. Coase’s Assumptions

Consider, for example, that Coase’s transaction of property rights approach fails to address adequately the problem of non-identified commons, and people without resources to pay for things or rights they value. All of Coase’s examples deal with individuals who have property—i.e., wealth. Coase does not deal with those who do not have sufficient resources.

Furthermore, Coase does not seem to consider that private firms do the equivalent of government seizure when they utilize the commons by their

\(^{91}\) Coase, supra note 24, at 41-42.

\(^{92}\) Id. at 18.

\(^{93}\) Id. at 17.

\(^{94}\) Id. at 40.

\(^{95}\) Id. at 34.
externalities. Such activity is equivalent to seizure of the commons. Additionally, the only value is the economic value, or more accurately, the revenue generating possibilities of the property. There is no discussion of fairness or things, such as happiness that make life worthwhile, known to economists as "psychic income."96

Further, Coase does not look at the non-monetized costs. What are the costs to the comfort of the family without a chimney? Put differently, what is the value of the individual and individual rights in a society. Consider, for example, that perhaps the family will be more susceptible to illness, or if it is forced to move, the members may suffer from increased insecurity and not be able to make an adjustment socially, at school or at work. He does not discuss the fact that a person with more assets has more mobility, and so has more alternatives, and ultimately a stronger bargaining position than someone who is poor.97 He does not seem to identify the problem faced by people without the alternative of moving, or not having cash to buy the right to have a chimney extended to stave off the cold of winter, nor yet the unfairness some economic outcomes may impose on the parties.

D. Criticisms of Coase98

97. Coase alludes to the further problem of unequal parties bargaining with each other when he states: "What payment would in fact be made would depend on the shrewdness of the farmer and the cattle raiser as bargainers." Coase, supra note 24, at 5.
98. There are many criticisms of Coase that could be included. Perhaps the most penetrating criticism, particularly of Coase's view that private property rights are the best solution to social costs is in V.V. Chari & Larry E. Jones, A Reconsideration of the Problem Social Cost: Free Riders and Monopolists, 16 ECON. THEORY 1 (2000).

For purposes of brevity and focus the criticisms discussed in the body of the paper are only those with the most direct bearing on the matter. In thinking about Coase, however, one must consider the broader issues which Coase's hypothetical world fails to address, such as: Who values and transacts public goods and how? A dollar value on public goods does not address the actual value received by the public from the public good. Take for example, Coase's rancher and farmer. What is the value to the public of a herd of cattle as opposed to a field of corn? The considerations are not what Coase has identified: again, his analysis is far too limited in its perspective. In his example there are also the problems of methane gas produced by cattle, as well as the pollution to streams from their wastes. Further, the production of cattle increases the demands on the land for producing cattle feed and reduces the land available for other uses. Nor yet does it take account of the fact that cattle grazing accounts for 35% of the erosion of the planet's arable land.

Similarly, corn production requires consideration of the costs and benefits of monoculture agricultural production. The inputs of energy to create fertilizer, pesticides, herbicides, as well as the destruction of the soil by compaction of the soil and monoculture itself need to be considered. Furthermore, each of these
As noted, Coase's work has received wide acclaim. Indeed, he has been awarded the Nobel Prize in Economics for his work. Due to its pervasive use and citation, it merits a careful and thorough criticism. Despite its general acceptance, Coase's work has not been received with equanimity in the legal, economics, or Law and Economics communities. Among the most trenchant of the criticism are those raised by Cooter in his article "The Costs of Coase." Cooter notes, among other criticisms, that Coase's examination is limited exclusively to one-on-one strategic game situations. This limitation facets of corn production have long term, environmental effects such as algae blooms in significant areas of the ocean, dying rivers and the exhaustion of soil, requiring the removal of land from agricultural use. The marginal utility of land is a more difficult calculation as it includes not only the above mentioned factors but also because change will be forced in production as a result of depletion of the world's petroleum resources, loss of productive land due to global warming and increased demand for food production resulting from the world's population doubling over the next fifty years. Society needs to make hard decisions about whether more cattle feed, for the inefficiencies of wealthy, beef eating consumers or more efficiently for food for the rest of the world, needs to be produced. Such concerns are, of course, the complexities that concerned Keynes. See Anna Carabelli & Nicolò De Vecchi, Individuals, Public Institutions and Knowledge: Hayek and Keynes, in KNOWLEDGE, SOCIAL INSTITUTIONS AND THE DIVISION OF LABOUR 229, 232 (Pier Luigi Porta et al. eds., 2001).

Given the immense amount of information needed to be collected, processed and analyzed (not to mention matters of probability and uncertainty), economic analysis alone may not be a sufficient enough basis on which to rely. The costs of error in such calculations are too great to imagine, and accordingly, it may be appropriate to look to some other tools or values in preserving the planet. Thus, the inability to calculate these goods suggests that Coase's view of the matter while interesting and helpful at a micro-level, is of next to no use at a macro-level. Coase does address some of these objections, such as the direct overall damage of activities and such non-economic concerns as poor people needing food, the value of social peace by preventing nuisance through using reasonable care and not waiting until there is complaint—quoting with approval from the case of Andreae v. Selfridge and Company Ltd; however, the "Coasean" tradition, like the Pigovian tradition he complains about, has been taken to mean something else.

Coase, supra, note 24, at 21-23, 39. See Ronald H. Coase, Lecture to the Memory of Alfred Nobel, available at http://www.nobel.se/economics laureates/1991/coase-lecture.html (Dec. 9, 1991). In fact, Coase does not claim that his paper is about the irrelevance of liability in a situation which is free from transaction costs. Nor is his paper about irrelevance of the initial allocations of rights. Rather he identifies the point of his paper clearly and quite contrary to these various interpretations. He suggests that the goal of his article is to "indicate what the economic approach to the problem should be." Coase, supra note 24, at 19. It is not prescriptive of the total approach. In his own words, the point of his paper is that while "[i]t would clearly be desirable if the only actions performed were those in which what was gained was worth more than what was lost. But in choosing between social arrangements ... we should have regard for the total effect. This, above all, is the change in approach which I am advocating." Id. at 44.

99. There is empirical evidence that the Coase theorem is incorrect. See supra note 89. How counterfactual evidence is dealt with is a particular problem for economics and challenges its claims to be a science. See Hausman, supra note 20.

is critical for a number of reasons.\textsuperscript{101} First, and perhaps most importantly, such strategic games are zero sum. In such games, no rational player is willing to give up more in order to resolve the solution and so the problems posed are in fact, intractable.\textsuperscript{102} Accordingly, there is no rational solution.

Coordination problems are those types of problems that require coordination of differing and conflicting interests among parties who together form a united whole. Coordination problems make up the vast majority of society's problems including social costs—yet Coase's solution does not address these either. Finally, Cooter notes that Coase operates on a very optimistic assumption, that despite the aforementioned intractability caused by the rationality assumption, people will cooperate. As Cooter puts it, the opposite and more realistic assumption is a pessimistic one, one which he calls the "Hobbes Theorem."\textsuperscript{103} In Hobbes' view of society, people will fight rather than share. Where such is the case, Coase's theory is useless beyond its value as an intellectual exercise.

If one accepts Cooter's criticism, it leads to Coase's second ordering of production, namely, a dominant role for government. It is government's job to coordinate diverse interests, not private individuals who have their own means—money, power and violence—to impose their "solutions" on the rest of society.\textsuperscript{104} In other words, social costs are no longer a mere concern of bargaining as between two individuals, nor yet as among a smaller group of easily identifiable individuals. It is a matter to be dealt with exactly by such mechanisms as liability created by law. This conclusion is controversial because Coase's thought and neo-classicism in Law and Economics, discussed next, is usually used to support the opposite conclusion—namely, that private orderings are preferable to any and all government orderings.

\textsuperscript{101} Id.
\textsuperscript{102} Id. at 16-17.
\textsuperscript{103} Id. at 18. Cooter develops a valuable normative theorem concerning the role of law from his Hobbes Theorem. He writes: "[T]he normative Hobbes theorem: Structure the law so as to minimize the harm caused by failures in private agreements." Cooter & Ulen, supra note 58, at 90 (emphasis omitted). This theorem's importance to the matter will be discussed below as structuring law to minimize social costs, and hence, reform corporate law along these lines.
\textsuperscript{104} See, e.g., matters raised in Harold Demsetz, Ownership, Control and the Firm: The Organization of Economic Activity 261-81 (1988) (in particular, Demsetz's criticism of Block). This point of large scale coordination problems being particularly intractable with respect to externalities, is the topic of Chari, supra note 98. They observe: "In large economies with decentralized systems, problems caused by externalities lead to outcomes far from the efficient level." Id. at 19. Although somewhat technical in parts, it is clear from the issue of incomplete markets for externalities discussed by Coase, that the market solution is simply not viable.
V. LAW AND ECONOMICS

A. The L&E Model of the Corporation

In the last decades of the twentieth century Corporate law has been dominated by Law and Economics.105 Easterbrook and Fischel's "The Economic Structure of Corporate Law"106 is a monumental work in the intellectual landscape of both Law and Economics (L&E) and corporate law. It quite clearly sets out the agenda of the corporation and makes a coherent normative argument for rationalizing, selecting and developing corporate law along a single path.

As they state in the preface: "We conclude that corporate law has an economic structure, that it increases the wealth of all by supplying the rules that investors would select if it were easy to contract more fully."107 They spend the balance of their work examining the general principles of corporate law and the specific rules that support that conclusion. Generally, they argue that corporate law is what investors would select if they were given the opportunity to contract, namely, efficiency leading to wealth maximization. Their attention is drawn to and focused upon the economic explanations of corporate law's principles and rules. The crux of the dilemma from their perspective is finding a balance between the ability to raise funds and the ability to control management.108

Easterbrook and Fischel start their explication of corporate law with a few short answers for their would-be critics. They state that large corporations, including multinationals, are the products of success in satisfying investors and customers.109 In other words, the corporations that exist, exist because they are the best. It is a robust view of survival of the fittest, the most worthy survive and grow, the weaker, inferior ones die. It suggests that the large corporation deserves its place and power because it is the best at what it does, or possibly, that it is most suited to the environment in which it exists.

They explain their approach as positive (i.e., descriptive) rather than normative (i.e., prescriptive), although they admit to straying into the

105. Minda, supra note 5.
108. This is a contemporary version of the A. Berle and G. Means concern resulting from the separation of "ownership" and management. ADOLPH BERLE & GARDINER C. MEANS, THE MODERN CORPORATION AND PRIVATE PROPERTY (rev. ed. 1968).
109. EASTERBROOK, supra note 106, at 4-8.
normative realm on occasion. This approach is reasonable within their assumptions: where the corporate structure is supposed to reflect the investors' wishes, and where the investors' wishes produce the greatest efficiency and hence the greatest good for society, the laws should reflect those assumptions. Indeed, as argued here, the idea that law "should reflect those assumptions" demonstrates that, at times, economics cannot but be normative. Where it has identified the goals, and, within its own limited framework, the best way to achieve those goals, to pursue other means is simply perverse.

B. Assumptions of the L&E Theory of Corporate Law

Easterbrook and Fischel state that they accept only one assumption—the assumption of implied investor consent. Therefore, they argue that they are engaging in a strictly positive exercise. They are merely describing the corporation as they find it, and they reject any theoretical starting point. Interestingly, before one can make sense of their argument, one needs to understand their theory. Both their economic theory (as they subscribe to neo-classical economic theory) and their theory of the corporation are quite developed and wide ranging.

Fellow law and economics scholar, Robin Malloy, identifies the following six assumptions as forming the basis of neo-classical law and economics:

i) People are rational and therefore act in their own self-interest. This position suggests that the appropriate role of central planners is minimal, and that the aggregate of these individual self-interested choices is the best for society.

ii) People have complete and perfect information, and that the current distribution of education is appropriate.

iii) Free movement to follow economic opportunity is available and appropriate to all people and that the effects of dislocation are not relevant.

iv) Free market and competition are desirable and the outcome of competition is desirable, and

v) The current distribution of wealth is accepted because it came about by just means and furthermore, any re-distribution would be unfair or inequitable.

110. Id. at vii-viii.

111. Pouney, supra note 20.

112. Easterbrook, supra note 106.

113. Id.

114. Id.

These neo-classical economic assumptions are fundamental to Easterbrook and Fischel’s work. As applied to law, corporate law, and legal theory, the main tenets of their theory are that:

- efficiency is the primary objective of law;
- the market is the most efficient method of resource allocation, not government imposed distributions;
- corporations are the best vehicle for coordinating resources;
- utility can be equated with wealth, not social justice, happiness or civil peace;
- only those with wealth sufficient to be investors need be concerned or consulted about resource allocation in production;
- increasing the wealth of those with wealth is the fundamental principle of economic activity;
- all other forms of wealth, such as environmental wealth (e.g., biodiversity and clean environment) or social wealth (e.g., psychic income, cultural heritage and knowledge), are unimportant;
- concerns of distributive justice are irrelevant; and
- the future of the planet and interests of future generations should be subjected to the appropriate discounting for present value calculations.

Once one accepts all of these tenets underlying their theory, one is free to move on with the authors, “free of theory,” to examine corporate law as it is. As they have it, investor choice is optimal “because the choices do not impose cost on strangers to the contracts, [and so] what is optimal for the firms and investors is optimal for society.” As they put it, having dealt with the preliminaries—the corporate contract, limited liability and voting in the introductory chapters of their work—they “arrive at the relation between shareholders and managers which holds center stage in the rest of this book.”

Easterbrook and Fischel define a firm as an “extra-market, team method of production with certain benefits and costs. Corporations are a subset of firms. The corporation is a financing device and is not otherwise distinctive.” As it is the investors who bear the risk of loss, so too, they should have the benefit of the reward.

116. See Easterbrook, supra note 106.  
117. Id. at 6-7.  
118. Reading Joo’s work, examining “economic contract” and “legal contract” (supra note 38) alongside Easterbrook and Fischel’s work is an invaluable exercise which sheds considerable light on the confusion and consequent complexities and conundrums created by confounding economic and legal understandings of the term “contract.”  
119. Easterbrook, supra note 106, at 90.  
120. Id. at 10.  
121. Id. at 11.
Further concerning this nexus of contracts model, they observe, that corporate law is designed to support "the complex arrangements of many sorts that those who associate voluntarily in the corporation will work out among themselves. The form of reference is a reminder that the corporation is a voluntary adventure, and that we must always examine the terms on which real people have agreed to participate." Accordingly, "[t]he role of corporate law at any instant is to establish rights among participants . . . ." The corporation is a wonderful finance tool in which every individual has complete bargaining freedom to buy and sell what he or she likes at prices that reflect the value of those things to each party. Working within their model, they are certainly correct.

C. Criticisms of the L&E Model

Given this nature of the corporation and the value to many people of the freedom of contract, it is undoubtedly true from a normative perspective that corporate law should reflect what the parties would contract, and that corporate law should be guided by the parties and not by the regulators. This particular view of the corporation and the interested parties leads them to the interesting conclusion that the goal of the corporation is a matter of complete indifference. As they put it: "what is the goal of the corporation? . . . who cares?" Since all are free participants, all should be free to do as they choose. Risk bearers get residual claims, non-risk bearers get fixed returns. Should those who have fixed returns prefer the residual claim, it is a rather simple matter for any one of them to simply withdraw their fixed return investment and invest in the residual claim.

Their justification for an economic analysis of corporate law is correct as far as it goes. As they observe, the same pressures affecting the shape of

122. Id. at 12.
123. Id. at 14.
124. Id. at 15.
125. Id. at 35-36. Although they do not spell it out in their text, Easterbrook and Fischel are following Coase's ideas on liability and allocation of rights. Who has what rights and liabilities is irrelevant in the quest to increase overall social wealth. Whatever arrangement has the greatest level of production is best, and Coase argues that, left to themselves without transaction costs, market players will find that arrangement on their own.
126. Assuming of course that the only investment one has is financial, or alternatively that a "contractor," such as a telemarketing employee, has sufficient funds on hand to permit him/her the simple switch to investing in dividend bearing shares where the dividends would replace his or her income.
markets are the same pressures that affect the structure of corporate law.\textsuperscript{127} Although not identified by the authors, one assumes they are referring to competitive pressures arising from efficiencies. It is unfortunate that they fail to identify the pressures as surely the market's pressures include such things as strategic behaviour, desire for power and dominance, defensive behaviours, inefficiencies caused such behaviours, and efforts to maximize profits by externalizing as many costs as possible. Had they done so, their analysis of corporate law would have been significantly more valuable, their analysis of the corporate law and normative conclusions would have been much more nuanced, and they would have had to address at least some of the social costs which are of concern to this article.

Easterbrook and Fischel acknowledge social costs but find they are best dismissed from an analysis of corporate law. They write:

\begin{quote}
We do not address optimal ways to deal with pollution, bribery, plant closings, and other decisions that have effects on people who may not participate in the corporate contract. Society must choose whether to conscript the firm's strength (its tendency to maximize wealth) by changing the prices it confronts or by changing its structure so that it is less apt to maximize wealth. The latter choice will yield less of both good ends than the former.\textsuperscript{128}
\end{quote}

They may be correct about their conclusion—although they provide neither evidence nor argument—if there is no middle ground and if, as they suppose, the soviet experience is the only alternative and it has indeed failed.\textsuperscript{129} Their suppositions about wealthy firms in light of experience are questionable. Wealthy firms provide more jobs, "better working conditions and clean up their outfalls . . . ."\textsuperscript{130} One of the banes of the increasingly dominant multinational corporations is their failure in each of these areas as they increasingly look to lower costs by moving to poor countries where they do none of the supposed wealthy firm activities.\textsuperscript{131}

\textsuperscript{127} See id. at 8.
\textsuperscript{128} Id. at 38. Again, like most law and economics scholars, Easterbrook and Fischel fail to explain why the particular goods they focus on should dominate the discussion and society as a whole. See Walzer, supra note 62.
\textsuperscript{129} See Janos Komai, What the Change of System from Socialism to Capitalism Does and Does Not Mean, 14 J. ECON. PERSP. 27 (2000). One also must remember that the soviet government accomplished a level of industrialization in 70 years that the west required more than 200 years to accomplish. While some may see this as an argument in favour of communism, it is intended as cautionary and a source for a bit of humility in the capitalist societies. See Chomsky's discussion of this error with respect to SE Asia and Latin America, in Chomsky supra note 3, at 32-35, 92-93.
\textsuperscript{130} Easterbrook, supra note 106, at 38.
\textsuperscript{131} See Stiglitz, supra note 3.
Although they claim that they are not panglossian, one is hard pressed to find a better term to describe them.\textsuperscript{132} As they view it, corporate governance is really only a matter of better-defined property rights. They make the assertion, without argument,

\textit{No reagrrangement of corporate governance structures can change this [social costs]. The task is to establish property rights so that the firm treats the social costs as private ones, and so that its reactions, as managers try to maximize profits given these new costs . . . to view pollution . . . or other difficult moral and social questions as governance matters is to miss the point.}\textsuperscript{133}

But these social costs are precisely the point and the current model is a significant cause of the problem.

Finally, they ignore a number of important issues. In their analysis, the big corporation is big because it is fittest for survival, but they ignore: 1) merger and acquisitions which often simply absorb the success of others’ ability to innovate, produce and market, 2) undervaluing the actual contribution of a business to the community—corporate raiders look for corporations with sufficient capital to meet potential corporate liabilities which are often simply sustainable practices, 3) stealth, deceptive, strategic behaviour and efforts to create monopolies, 4) luck in timing: right place, right time, 5) the role of right connections, and 6) the anti-social, un-ethical behaviour of many corporate founders and successors.\textsuperscript{134}

So far, we have developed an understanding of social costs as those costs that are borne by non-parties to activities, and particularly, income generating activities. Further, we have seen that the traditional Social Cost analysis as developed by Coase has viewed the problem as solved by individual participants in a market setting rather than through law. We have noted that Coase’s analysis of Social Costs fails to address coordination problems, being those problems that involve solving conflicting interests in using goods. Further, we have seen that because of its commitment to neo-classical economics, Law and Economics tends to view the objective of law narrowly as maximizing wealth, and tend to disregard public good. In this context corporations and corporate law are about fulfilling the interests of the parties

\textsuperscript{132} Indeed a book review of their work in the Harvard Law Review is titled: \textit{Dr. Pangloss Meets the Coase Theorem}, 105 \textsc{Harv. L. Rev.} 1408 (1992).

\textsuperscript{133} EASTERBROOK, supra note 106, at 39.

\textsuperscript{134} The history of such behaviour is well documented from J.P. Morgan’s kidnapping of couriers of competitors, to Microsoft’s continual legal battles concerning its anti-trust activities. Some of these antics are noted in MAURY KLEIN, THE LIFE AND LEGEND OF JAY GOULD 80-86 (1986).
privy to the corporate contract. It is generally assumed that there is but one interest: increasing the efficiency of the corporation, and in particular, in the business sense of efficiency, increasing internal profits—that is, by increasing externalities, the social costs. This analysis allows the author to suggest that corporations increase social cost. To test this hypothesis, we will now examine a particular case.

VI. CASE STUDY

Perhaps the best way to understand the nature of the problem of uncontrolled social costs created by the Law and Economics supported nexus of contracts model of the corporation, is by way of a case study. The world’s largest corporation is Wal-Mart. Its corporate structure is made up of six retail divisions and six specialty divisions. It is a publicly traded corporation listed on the NYSE and two other exchanges. Majority shareholders include three family members and a number of institutional investors.

Wal-Mart was started in the 1950’s by Sam Walton, apparently a small time store owner, in Bentonville, Arkansas, U.S.A. It started as a small department store, growing into a small regional chain, and then growing and spreading first through the southern United States of America, and then throughout the rest of the country. It has now moved beyond its national focus and operates internationally.

In 2002, sales were $245 billion. There are over 3,200 stores in the U.S. and over 1,500 in Mexico, Puerto Rico, Canada, Argentina, Brazil, China, South Korea, Germany and the U.K., and plans to expand to every market which could sustain it and protect its profits. Wal-Mart employs 1.5 million people worldwide as “associates” (i.e., sales clerks). At least 30%...
of Wal-Mart employees are part-time.\footnote{143} Full-time at Wal-Mart means 28 hours or more per week.\footnote{144} Nearly 10\% of all imports from China to the U.S. were imported by Wal-Mart in 2002, at a value of approximately $12 billion.\footnote{145} Twelve percent of the American economy’s productivity gains in the period 1995-2000 are believed to have resulted from Wal-Mart.\footnote{146}

The effects of Wal-Mart and other big-box stores is not well researched nor well documented. Although a recent spate of articles has started to draw attention to the issue,\footnote{147} perhaps the only thorough study was done in 1997 by the leading expert on big-box stores, Edward Shils, Director Emeritus of the Wharton Entrepreneurial Centre, at the University of Pennsylvania.\footnote{148} The Shils Report is a landmark study of the social costs of this form of retailing. In his study, entitled: “Measuring the Economic and Sociological Impact of the Mega-Retail Discount Chains on Small Enterprise in Urban, Suburban and Rural Communities,” Shils examined the impact of these big-box stores on the communities in which they are located.\footnote{149} Shils’ study focused on two big-box stores: Wal-Mart and K-mart.\footnote{150} The main dynamics that drew Shils’ attention were the effects on the traditional structure of the labour market in the communities, and how it worked before and after the location of a big-box retail outlet within a 10-15 mile radius.\footnote{151} Our examination of the social costs of corporations will begin with those identified by Shils. After considering

143. Edward B. Shils, Measuring the Economic and Sociological Impact of the Mega-Retail Discount Chains on Small Enterprise in Urban, Suburban and Rural Communities, SHILS REP., Feb. 7, 1997, at ch. ix. Shils observes that as full-time is considered 28 hours per week or more, the 30\% part-time is an “exceedingly conservative figure.” Id.

144. Id.

145. Fishman, supra note 135.

146. Id. (citing a McKinsey & Co. study).


148. See Shils, supra note 143. Another expert on Wal-Mart is Kenneth E. Stone of Iowa University; however, his focus is on how to stay in business if Wal-Mart moves into the area. For a full listing of his work, see http://www.econ.iastate.edu/faculty/stone/VITA-KES.pdf (last visited Nov. 6, 2004).

149. Shils, supra note 143.

150. Id.

151. Id.
Shils' comments, the article will turn to examine a broader group of social costs. Given the innovative nature of the study it was not possible to utilize previously compiled lists. Social costs include breakdown of functioning communities, undermining of markets, impoverishment of workers, harm to democratic institutions of government, damage to culture, damage to efforts promoting cooperation and conservation, and environmental pollution. The list was compiled on the basis of observations concerning activities and hypothesis of costs of those activities by corporations in general and in certain instances, as will be clear in the discussion of Wal-Mart.

A. Community Impact

Traditional western communities have thriving commercial centers. These centers are composed of a mix of retail, commercial and office space. The majority of the commerce in these centers is transacted through small businesses. These businesses tend to be highly involved in the community, create employment which pays sufficiently to sustain a reasonable standard of living, pays taxes, and are innovative, community building in the sense of promoting ideas of individual ability, responsibility and an entrepreneurial spirit. Indeed, small business is often described as the “backbone” of an economy and a community—at least in a market economy.

Shils draws attention to the effects of shifting labour opportunities from the downtown urban areas to suburban big-box retailers. When labour opportunities disappear communities fall apart. When people do not employ their time with productive activities such as working in a commercial center, they turn to other unproductive activities. Effected malls and commercial areas tend to display levels of vacancy from 30%-40% after a superstore moves into the radius. These vacancies represent significant losses of small businesses and mid-level incomes. Further, when vacancies increase and employment decreases, vandalism, petty crime, and drug use increase.

152. Id. at ch. x.
154. Shils, supra note 143, at ch. x.
155. Id. This vacancy and downward spiral in a center is a phenomena that first occurred in the 1960's and 70's as suburbs were created in greater numbers. The socio-economic problems of gutted city centres has yet to be resolved.
Thus, when Wal-Mart establishes a retail outlet, detrimental community effects can be expected. These effects include decreased community involvement, decreased community building efforts, decreased small business, decreased labour opportunities, and increased commercial vacancies.

B. Supplier Social Costs

Another social cost imposed by big-box stores results from the demands such stores place on suppliers. Having Wal-Mart as a customer has both advantages and disadvantages. On the one hand, the supplier’s sales increase dramatically. On the other hand, the stress on the business increases exponentially as profit margins dip dramatically.

The pressure Wal-Mart place on suppliers is enormous. Wal-Mart requires its suppliers to drop prices annually by as much as 5%. There are different responses to this type of pressure. In some instances, Wal-Mart has driven its suppliers out of business. In other instances whole industries, such as the orange industry in the U.S., have suffered severely adverse effects.

Another common response is for a business to cannibalize itself. This cannibalization occurs when a business is forced to undercut its own products in other markets (often much more profitable markets) or give up markets in order to supply Wal-Mart. In other words, it is a zero-sum situation in which the change in business from a profitable market to Wal-Mart has no net gain to the supplier: it is pure loss. And the cost involved is borne solely by the business supplying Wal-Mart, not only through the cannibalization, but also in the cost of shifting production resources from one product to another. Businesses contract with Wal-Mart for different reasons, including being unable to compete, and not having sufficient or complete information as to how Wal-Mart deals with its suppliers.

Interestingly, Wal-Mart’s suppliers are not free to talk to the press about their experiences for fear of retaliation, or in their terms, “being in the penalty-

---

156. Fishman, supra note 135 (reporting information from Bain & Co., one of the top management consulting firms in the world).
157. Id. Given the particular nature of these problems, it is exceedingly difficult to get information. Usually when businesses go bankrupt or even just go out of business the information concerning causes is lost along with the other information management may have had. Stiglitz notes this with respect to restructuring in various countries and the resultant need to work with officials of governments not previously in favour with IMF administration. Stiglitz, supra note 3.
158. Fishman, supra note 135.
159. As one supplier put it, “When you speak to God in Bentonville, you speak in hushed tones.” See Bianco, supra note 147.
The relationship between executives of Wal-Mart has been colorfully analogized to "getting into the company version of basic training with an implacable Army drill sergeant." The stresses of these pressures applied to the business are borne by management and employees. Every person involved in the business from top management on down to the part-time floor workers are required to meet much more exacting standards—computer driven standards. Humans are driven particularly hard to meet inflexible, to the second, machine driven standards. Given the cost cutting, the exacting standards, and the huge value of the contracts, a business simply cannot afford to fail its contractual obligations—regardless of how unreasonably and stringently enforced. To fulfill the demands of the low profit margins, workers at all levels are forced to take on more responsibility and are given less resources. This process combined with the environment of low tolerance increases the level of stress and stress-related problems dramatically.

C. Labour Social Costs

A May 2004 study released by the University of California, Berkeley entitled "The Hidden Public Costs of Low-Wage Jobs in California" identifies low pay in retail as a serious cost to the public. Interviews with one of the study's authors identified Wal-Mart as costing California's taxpayers $86 million annually as a result of under-paying its employees. They are

160. Fishman, supra note 135.
161. Id.
163. This difficulty of humans working to machine driven rates and rhythms has been recognized as a problem in assembly line labour but appears not to be recognized when it comes to working with computers. The exception is among fighter plane pilots whose human cognitive ability is at times insufficient to deal with the complexities of computer flown aircraft resulting in air crashes. See, e.g., David Bookstaber, Optimized Visual Interfaces for Combat Pilots, available at http://bookstaber.com/david/opinion/PilotInterfaces.pdf (last visited Nov. 6, 2004). Bookstaber is a former USAF pilot and Electronic Systems Center Scientist.
164. See id.
paid over minimum wage, but then they are limited, potentially to 28 work hours per week.\textsuperscript{167} This cap on hours worked permits Wal-Mart to avoid costs such as health insurance it may otherwise be forced to incur. Obviously, the employees are not earning sufficient wages to live.\textsuperscript{168} Under-paying employees has a number of consequences. Whereas prior to the arrival of the big box store, competing employers used to pay a living-wage, once big-box stores arrive, smaller employers can no longer do so as they are driven to cut costs or go out of business altogether.\textsuperscript{169} Wal-Mart’s size and correlated impact on the labour market wages are driven down throughout the area, as small businesses close and their better paying jobs are lost.\textsuperscript{170}

Further, because of low wages, Wal-Mart employees must look elsewhere for supplemental income. Such supplemental income can come from the
state, other part-time jobs, the underground economy, or illegal activities. These activities in turn have the further consequences of additional stress, and less time to spend engaging in other non-income generating activities ("psychic income") that reduce stress and make life enjoyable and worthwhile. This situation is exacerbated by Wal-Mart’s refusal to pay for certain over-time activities, as this refusal has formed the basis for a class-action against it by some 65,000 employees.\footnote{Wal-Mart’s equity decisions also seem suspect. For example, while 72% of its workforce is female, only 33% of its management is female.\footnote{Currently, it is subject to a class-action lawsuit on behalf of 1.5 million female former employees for sex discrimination.\footnote{Wal-Mart has taken a defiantly anti-union stance. It maintains an active anti-union response team of 70 people ready to descend on any Wal-Mart where employees are considering unionizing.\footnote{It attempts to inoculate employees against unions by threats rather than by providing competitive benefits. By way of contrast, a successful anti-union strategy which worked for various Japanese auto manufacturers has been to provide competitive pay and compensation packages. The result for these employers has been to make them the employer of choice for many workers.}}\footnote{Wal-Mart employee dissatisfaction is high. This fact is evidenced by an employee turnover estimated at 44\% per year.}}\footnote{Some Wal-Mart stores encourage employees to seek state assistance to subsidize the low incomes Wal-Mart pays. Barbara Ehrenreich, Wal-Marts Invades Earth, N.Y. TIMES, July 25, 2004.}

Wal-Mart’s equity decisions also seem suspect. For example, while 72\% of its workforce is female, only 33\% of its management is female.\footnote{Currently, it is subject to a class-action lawsuit on behalf of 1.5 million female former employees for sex discrimination.\footnote{Wal-Mart Faces Class-Action over Off-the-Clock Work, USA TODAY, Nov. 6, 2003. Wal-Mart employees are required to participate in some activities before the stores open, without pay. Wal-Mart is currently subject to several lawsuits in the U.S. on the issue of unpaid over-time work. Rausch, supra note 147. Details are available on one of the attorney’s websites. Wal-Mart Employment Practices, at http://www.lieffcabra.com/walmart%20lawsuit.htm (last visited Nov. 6, 2004).}}\footnote{Rausch, supra note 147.}

Furthermore, Wal-Mart has taken a defiantly anti-union stance. It maintains an active anti-union response team of 70 people ready to descend on any Wal-Mart where employees are considering unionizing.\footnote{It attempts to inoculate employees against unions by threats rather than by providing competitive benefits. By way of contrast, a successful anti-union strategy which worked for various Japanese auto manufacturers has been to provide competitive pay and compensation packages. The result for these employers has been to make them the employer of choice for many workers.}}\footnote{Wal-Mart employee dissatisfaction is high. This fact is evidenced by an employee turnover estimated at 44\% per year.\footnote{Such dislocations have a high social cost.\footnote{When people lose employment, even when it is low}}\footnote{Rausch, supra note 147.}

\footnote{The certification of the class was a significant step in class-action lawsuits, and was made by Judge Jenkins on June 21, 2004. For a copy of the certification order, see http://walmartclass.com/staticdata/walmartclass/classcert.pdf (last visited Nov. 6, 2004). For information on the case, see the class-action web site dedicated to the case at http://www.walmartclass.com/walmartclass94.pl?wsid=0\&websys_screen=walmartclass_casedevelopments (last visited Nov. 6, 2004).}

\footnote{Rausch, supra note 147.}

\footnote{Holhut observes: "Wal-Mart is resolutely anti-union and has perhaps the most aggressive union-busting operation of any major U.S. corporation. . . ." Holhut, supra note 139.}

\footnote{Id.}

paying, they lose a sense of security and stability.\textsuperscript{179} The loss of a job undermines one’s sense of well being and dramatically increases stress, depression and related socially damaging behaviors, including excessive alcohol consumption and gambling as people attempt to deal with stress. These costs are passed on into their close communities of friends and family.\textsuperscript{180}

In summary, Wal-Mart’s low wage policy drives down prices in the labour market. It off-loads its operating costs onto the state and other businesses. It damages the well-being of employees by eliminating opportunity to access psychic income generating activities, and increasing stress resulting from employee turn-over. Further, its equity and overtime policies, and anti-unionism are manifestly opposed to the well-being of its labour force.

\section*{D. Democracy}

Wal-Mart harms democracy by unduly influencing the political process needed to get development permissions, by funding promotional school materials, by controlling which reading materials and products get supplied to consumers,\textsuperscript{181} by anti-competitive pricing,\textsuperscript{182} by its anti-unionism (discussed above) and by misusing tax-payer largess intended to assist local communities stay alive and keep their economies thriving.\textsuperscript{183} A major research study

\begin{itemize}
\item 181. Holhut notes Wal-Mart controls 15\% of the market for magazines and books. Holhut, \textit{supra} note 139.
\item 182. Anti-competitive pricing is selling goods for less than competitors at prices that may cause a loss for the purpose of driving a competitor out of business. After the competitor is gone, the prices are usually raised to even higher levels. Wal-Mart has engaged in these activities. See litigation under the Robinson-Patman Act and discussion at \url{www.lawmall.com} (last visited Nov. 6, 2004).
\end{itemize}
released in May 2004 was able to document receipt by Wal-Mart “[of] more than $1 billion in such subsidies from state and local governments to Wal-Mart; the actual total is certainly far higher. . . .”184 These subsidies were designed to promote new businesses in communities for the purposes of benefiting the community. The main subsidies the researchers were able to document are: free or reduced-price land, infrastructure assistance, tax increment financing, property tax breaks, state corporate income tax credits, sales tax rebates, enterprise zone (and other zone) status, job training and worker recruitment funds, tax-exempt bond financing, and general grants.185

Together these activities undermine a community’s ability to organize itself to pursue its best interest. This set of activities is particularly pernicious as the community’s opponent is a powerful organization quite able to organize itself and keep its consumers’ community in the dark without good information for the purposes of its own, self interested profit motive.

Despite all its ubiquitous statements to the contrary, consumer interests are not the ultimate concern. Clearly, corporate profit is. Where an entity absorbs such wealth and power, it works not only to maintain, but to increase, its position. This tendency is a phenomenon identified by economists in the economic realm as an effort to control a market by means of monopoly. Wal-Mart is open about its intentions to continue its growth (noted above).

Further, Wal-Mart reduces expression by its dominance of the market. Consumers are free to choose whatever they like, provided Wal-Mart has agreed to provide it. This restriction of consumer options harkens back to Henry Ford’s comment: “They can have any colour they like so long as it is black.”

Wal-Mart has launched an attack on diversity of opinions—which form the basis of democracy—by the restrictions it places on authors and artists who wish their goods to be distributed as widely as possible, and given Wal-Mart’s dominance as a distributor, such wide distribution would include being sold in Wal-Mart stores. This aspect of the problem of democracy is dealt with in greater detail in the next subsection.

184. Id. at 7. Mattera et al., claim that their research “documents more than $1 billion in such subsidies from state and local governments to Wal-Mart; the actual total is certainly far higher, but the records are scattered in thousands of places and many subsidies are undisclosed.” Id. at 8. The same $1 billion figure is offered in Ehrenreich, supra note 171.
185. Mattera, supra note 183.
E. Cultural Control

Wal-Mart, because of its buying power, and buying practices as demonstrated above, can and does dictate to its suppliers. It does so as well with respect to its consumers—it seeks only those products which it can sell in vast quantities—literature without depth, but with much popular appeal, and movies and other entertainment with the same qualities. Based in Bentonville, Arkansas, a conservative backwater of the Southern U.S., Wal-Mart is a product of a conservative world-view. This background continues to inform its buying decisions and what it will permit consumers to purchase at its outlets. It has refused products which have a particular level of sexuality. For example, Wal-Mart has refused to print photos taken by consumers where the subject of the photo has been nude, and further, refuses to stock certain contraceptives. Further, it has insisted music lyrics be changed or simply refused to place the product. It refuses to stock magazines such as Maxim and insists on editing others such as In Style and Sports Illustrated Swimsuit and hides the magazine covers of Glamour, Cosmopolitan and Redbook. Essentially, this is the fear in all democracies: that the tyranny of the majority will suppress the views of the minority—in this case, it is the fear of the minority who control Wal-Mart that the majority may oppose the political agenda they wish to advance through Wal-Mart.

186. Randall, supra note 138.
187. Bianco et al., note Wal-Mart’s refusal to stock Preven, a morning after pill, on the basis that it does not want to subject its pharmacists to the moral dilemma of dispensing abortion pills. Bianco, supra note 147.
190. Bianco, supra note 147, notes this, quoting Wal-Mart general merchandise manager, Gary Stevens, “There’s a line between provocative and pornographic. I don’t know exactly where it is.” The statement is reminiscent of Supreme Court Justice Potter Stewart, who famously stated: “I shall not today attempt further to define [pornography]. . . . [b]ut I know it when I see it. . . .” Jacobellis v. Ohio, 378 U.S. 184, 197 (1964). Clearly the justice was struggling to define the issue for the good of the American public in the early 1960’s with the information provided by a bevy of lawyers and specialists. It seems odd that a merchandiser seems to think it his role to define pornography, presumably with nothing more than his parochial wisdom informing him as to what the public should be exposed to.
191. No research was conducted to determine whether Wal-Mart’s cultural control has extended to restrict the literature accepted for sale at Wal-Mart stores to reflect a particular political party.
F. Foreign, "Outsourced" Social Costs

A broader perspective includes the activities of manufacturers who supply Wal-Mart with the goods it desires to sell. In order to produce cheap goods, manufacturers must use the cheapest methods. Basic economic theory suggests that one can substitute inputs and still obtain the same outputs or goods desired. So, for example, if a manufacturer wishes to produce good A, it can pay X amount of capital plus Y amount of labour to produce n quantity of goods. Alternatively, it can manufacture n amount of good A with X+1 in capital and a corresponding decrease in labour of Y-1.

In China, where Wal-Mart purchased $12 billion of its goods for the U.S. market, the cost of labour at its factory suppliers is $0.13 per hour. Workers must work 13-16 hours per day, seven days per week. The working conditions are described as "sweatshops" and those working to provide Wal-Mart with its low cost goods are forced to work in conditions that are consistently rated among the worst. The argument that these conditions are an improvement over unemployment is ingenuous as it is not clear that unemployment is the only alternative, nor that local businesses and the local economy and environment would not be better off investing in itself and providing products for local consumption.

Further, in order to keep production costs low, a manager must look for every means possible for externalizing costs. One way of doing so is by not treating wastes properly before discharge or simply dumping them directly without any treatment whatsoever. While these costs are passed on to the

192. Fishman, supra note 135.
193. Rausch, supra note 147.
194. Id.
195. Id. (quoting Charles Kernaghan, director of the National Labor Committee, an NGO that monitors sweatshops). But see a different perspective on the value of such jobs in third world economies is offered by Eugene B. Mihaly, Multinational Companies and Wages in Low-Income Countries, 3 J. SMALL & EMERGING BUS. L. 1 (1999).
196. Mihaly's position in favour of trickle down economics in developing economies is well argued. Id. Stiglitz indicates that the argument for trickle down economics has lost credibility. Stiglitz, supra note 3. The failure of trickle down economics to work even in the country most friendly to the notion, the U.S., has formed the basis for a proposition that every American should be given $80,000. BRUCE ACKERMAN & ANNE ALSTOTT, THE STAKEHOLDER SOCIETY 3-5 (1999).
197. See Stiglitz, supra note 3.
local and national communities in developing countries where the manufacturing is done, the benefit is passed on to the American consumer who receives under-priced goods. These factories are using the oldest technologies in order to take advantage of the cheaper labour inputs in producing low cost goods that they must produce in order to keep Wal-Mart as a customer.

It is truly a no-win situation. To not produce is to not have money in the economy necessary to live, but to have a habitable, clean environment. To produce, however, requires incurring great social costs. Further, because of market power, the vast majority of the economic benefits of trade are passed on to the U.S. while the majority of the costs stay with the people and the environment of the developing nation.

A secondary set of externalities arises from this trade. While at one time, economists insisted that trade benefited all of society, the rising tide theory—a rising tide raises all ships and hence, all people in a growing economy will benefit—is no longer the received wisdom. As Professor George Kent put it: "The rising tide of trade supposedly will lift all ships. But it may be that instead, as the critics suggest, it lifts only yachts, and swamps vessels that are leaky and decrepit." This consideration is important in two respects. First, by diverting resources to production for export, local markets are disrupted and new pressures are put on participants (including local villagers and local vendors) in that market. These pressures are largely uncompensated as the participants in those markets are not benefited much by trade. By way of contrast, those controlling production for export may be benefiting dramatically. This fact leads to the second consideration. Trade for export may increase significantly inequities in a local economy, exacerbating existing tensions and further upsetting community orderings. While the discussion here is not a defence of the status quo, where such changes occur, at times a gradual approach may be less disruptive as communities have time to adapt.

Another social cost downloaded on foreigners results not from the production impacts, but from the demand side, the retailing model. The social costs identified as U.S. bound in this article will likely occur, but as amplified by the conditions found in the foreign context. For example, Wal-Mart’s damage will hit countries like Japan hard. Japan’s commercial sector is

predominantly made up of small retailers. Where Wal-Mart enters a market like Japan, severe dislocations of small retailers and the related social disruption should be anticipated. Again, the benefit of the foreign subsidiaries is directed to the U.S. parent, leaving the disruption outward in the foreign context and the benefit inward in to the U.S. investors.

It should not be considered that Wal-Mart will alter its business strategy as a result of these social costs to foreigners. Wal-Mart’s market saturation in the U.S. has led it to plan to continue its strategy in other markets. Thus it should be anticipated that these social costs will continue to be imposed on countries outside the U.S.

In sum, the production of goods demanded by Wal-Mart forces overproduction (with maximum social costs) in poorer countries. This overproduction causes considerable environmental harm, social dislocation, sweatshops, and disruption in local market conditions. Further, the greater part of the benefit goes to the few wealthy in control of the production process and the U.S. consumer. The cost goes to the foreign country and the majority of its people.

G. Consumerism

Wal-Mart’s approach of increasing by supplying goods in large or bulk size creates its own special set of problems. For example, Wal-Mart decided to use pickles to create an impression of incredibly cheap prices. It pressured a supplier of high quality pickles (with threats to discontinue business with them) to produce gallon jars of pickles for less than $3. The net result was a dramatic increase in sales at very low margins, increased demand on farmers and all pickle producers, undermining its high quality pickle market it had built up over the years, and eventually contributing to the supplier’s bankruptcy. Perhaps worst of all, as an executive at the former

---

203. That the parent/subsidiary relation is established to benefit the parent corporation should be uncontroversial.  
204. This comment is not that non-U.S. investors are not benefitting from the profits of Wal-Mart. Rather, that the majority of investors are U.S. institutional investors, whose clients are largely U.S. based corporations and other citizens.  
207. *Id.*
pickle supplier observed: "They'd eat a quarter of a jar and throw the thing away when they got moldy. A family can't eat them fast enough."\footnote{208}

This problem—promoting over-consumption in a world of limited resources, currently reeling under the environmental costs of its consumption habits—is nothing short of moronic. Americans are the most over-weight people on the planet, spend more money per capita on diets, consume more goods per capita than anyone else on the planet, and Wal-Mart's strategy, effectively, is to promote further over-consumption by under-pricing more goods. Basic economic theory indicates that when goods are under priced they are over consumed. We need look no further than Wal-Mart to see the truth of this principle. While Wal-Mart is not the creator of consumerism,\footnote{209} its dominance creates a large responsibility to inform consumers about the real costs. By under-pricing, Wal-Mart is misinforming the consumer encouraging over-consumption, and to do so in the planet's current state is nothing less than perverse.\footnote{210} Because of its market dominance, a strong argument can be made for its bearing considerable corporate responsibility to inform consumers about costs by pricing correctly.

\textbf{H. Environmental Costs}

The environmental costs imposed by Wal-Mart's model, alluded to above with respect to developing nations, are vast both abroad and in the U.S.\footnote{211}

\footnote{208. \textit{Id.}}

\footnote{209. Thinking about this can be traced at least as far back as economist Thorstein Veblen who noted the efforts of the poor to imitate the consumption patterns of the rich. See \textsc{David C. Korten, When Corporations Rule the World} (2d ed. 2001) (discussing the creation of consumerism in Western culture). See also \textsc{Steven Miles, Consumerism—As a Way of Life} (1998); \textsc{Matthew Hilton, Consumerism in Twentieth-Century Britain: The Search for a Historical Movement} (2003). The idea that equates consumption with happiness comes from economic theory. For a discussion of the principle of unlimited growth being desirable from an economic perspective, see Kysar, supra note 2, at 29-32. See discussion in \textsc{John A. Wolfenden, Homo Economicus: Fantastic Fact or Factual Fantasy?}, 1 ETHOS J. GLOBAL ETHICS (1998). The dominance of economic discourse in public policy is becoming a common complaint. See, e.g., Kysar, supra note 2, at 66, and references therein.}

\footnote{210. See discussion of ecological economics, which is an effort to integrate the seemingly obvious fact of limited planetary resources with economic theory, and the challenges faced in both that project and law and economics, in Kysar, supra note 2.}

\footnote{211. Consider, for example, the recently settled lawsuit, \textit{United States v. Wal-Mart Stores Inc.}, filed in the Western District of Arkansas Fayetteville Division. While this externality has been caught by the Environmental Protection Agency and settled by a payment of a $1.0 million fine as is accepted in regulatory law, there are certainly many others not being caught. In this instance, the infraction resulted from Wal-Mart's failure to monitor its contractors in the construction of new stores. It is interesting to note that Plaintiff alleges in paragraph 8 of the complaint that Wal-Mart is opening between 100 and 200 new stores annually. Of the 17 infractions in the complaint, 9 give approximate sizes of the development. The}
Indeed they are certainly so extensive as to beyond the scope of this particular study. Therefore, only a single example will be examined. Consider, for example, the matters of packaging and transport. Wal-Mart requires extensive packaging of goods. Each individual item must be packaged and wrapped, placed in boxes, placed on pallets each of which in turn are wrapped, shipped locally first and then often from overseas. Almost all packaging is discarded immediately by the consumer as it is largely without benefit, and it is often made of plastics which are in turn made of limited and highly polluting petrochemicals which require the use of other toxic chemicals which have their own environmental and human health costs. The costs of the manufacturing of packaging is openly acknowledged not to include the true costs.212

Further, it can hardly be argued that the actual environmental costs of burning fossil fuels—creating greenhouse gases—for the transport over land is factored into the transportation costs of goods to market. Greenhouse gases are already costing hundreds of billions of dollars and are increasing exponentially.213 Further, sea-going cargo is shipped on container vessels that burn the dirtiest fuel produced by refineries. An average vessel produces emissions that are equivalent to 350,000 automobiles.214 These environmental costs are not factored into the costs simply because they are not charged to the vessel operators. The world’s container fleet has increased five fold over the last twenty years with no world body effectively addressing these issues.215 Of course, because the analysis in this study has been focused on Wal-Mart


213. These costs are the reason that the insurance industry has begun lobbying for action against global warming. Sharon Beder notes that Reinsurers Association of America claims “[i]nsurers paid $57 billion for weather-related losses in the first half of the 1990s compared with $17 billion for the whole of the previous decade.” Sharon Beder, Insurers Sweat over Global Warming, ENGINEERS AUSTL. 41 (Aug. 2001).


215. The International Maritime Organization, the UN’s body for marine environmental pollution has yet to consider emissions as a treaty item. Its problems in creating treaties that are effective in controlling marine environment pollution are great. See discussion in Benedict Sheehy, International Marine Environment Law: A Case Study in the Wider Caribbean Region, 16 GEO. INT’L ENVTL. L. REV. 441 (2004).
Stores, Inc. as a retail sales corporation, the vast majority of issues related to the manufacture, over-consumption, and disposal of consumed goods has not been addressed.

I. Wal-Mart's Position

Wal-Mart is not blind to criticism of social costs or the idea of the good corporate citizen. As it states on its website: "Wal-Mart Stores, Inc. believes each Wal-Mart store, SAM'S CLUB and distribution center has a responsibility to contribute to the well being of the local community. Our more than 3,400 locations contributed more than $150 million to support communities and local non-profit organizations."\(^{216}\) It goes on to describe how the funds are allocated and the various recognitions it has received for its contributions. Do these contributions fulfill its social responsibility, or compensate fully the community for social costs? Lee Scott, the President and CEO offers "Wal-Mart paid $4 billion in U.S. federal income taxes in fiscal year 2004," which he sees as another measure of the corporation's contribution to society.\(^{217}\) But it is difficult to see why avoiding criminal sanctions for not paying taxes should be seen as contributing to society. Further, it must be remembered that the tax bill is the absolute minimum that the corporation could be forced to pay, having been prepared by the most competent and aggressive tax specialists Wal-Mart could buy.

Business ethicists, who see corporate activity as falling into their domain, note six areas which can be considered as corporate social costs. They note the effect on the community, representation of minorities and women, how corporations treat their employees, environmental protection, foreign stakeholders, and customers.\(^{218}\) Interestingly, in the last five years that Business Ethics Magazine has been auditing and compiling lists, Wal-Mart, despite being the number one corporation in the world in terms of size, has not been listed among the 100 most ethical corporations since 2000. In other words, it has not matched its size achievement in terms of internalizing its correlative social costs.\(^{219}\)

\(^{216}\) Wal-Mart, supra note 136, "Our Commitment to Communities."
All of the forgoing leads to the question of the causes or nature of the problem. Clearly, one cause is the information asymmetry. As noted above, in the pickle sales example, the goods were being sold at a price that was "incredible." Literally it is not credible to sell goods at that price, because as we have seen, the actual price is considerably higher. Quite simply, the price did not factor in all the costs. The information was not passed on to the people. Where people have the information, there is evidence to suggest that people prefer not to have those consequences.220

Another aspect to the problem is the focus on wealth creation and, in particular, profit making. Where profit is the sole objective, other abilities, such as broader community cooperation, are diminished or lost.

VII. CORPORATE VEHICLE AND SOCIAL COSTS

Wal-Mart is culpable neither in business terms, nor, except as identified in the actual, pending and potential lawsuits, in legal terms.221 Further, it is a darling of the stock market.222 The question is whether this matter of social costs is a problem resulting from the corporate form or merely a matter unique to the mega-retail discount giants? If it is the latter, then it is simply matter of regulation concerning the size of retailers. If it is the former, it requires further consideration and analysis.

The corporation's role in this situation is not self-evident. If one accepts the corporation as a mere nexus-of-contracts, one can escape from the reality of Wal-Mart's damage around the world, simply claiming as Easterbrook and Fischel would have it, that it was all voluntary and therefore not in need of any regulation.223 If one chooses, however, to acknowledge the reality of the widely disseminated detriment caused to the socio-economic landscapes in the

220. There is a considerable consumer and social lobby against Wal-Mart because of the damage it causes to society. This consumer reaction and the damage caused to communities by Wal-Mart is noted by Stiglitz, supra, note 3, at 68. See, e.g., anti-trust lawyer, Carl E. Person's website, infra note 220, and Al Norman's work. Further work is being done in Australia as the damage of big-boxes is becoming known. A search of google.com produced 1,690 hits for "stop Wal-Mart." No activist groups attempting to bring Wal-Mart to localities were found but many opposing it. For the law and economics perspective of the consumer-merchant information asymmetry and views of regulatory intervention, see Bailey Kuklin, Self-Paternalism in the Marketplace, 60 U. CIN. L. REV. 649 (1992).

221. Concerns about the legality of its monopolist business strategies and anti-union activities are noted by U.S. lawyer, Carl E. Person on his website, at http://www.lawmall.com (last visited Nov. 6, 2004).

222. On a scale of 1-5, with 1 being a strong buy recommendation, a sampling of analysts give it a 2. Yahoo, supra note 137.

223. Society does not condone, or law permit, all voluntary transactions. This is the concept of inalienability in Calabresi & Melamed's theory of property.
developed nations and in the third world, which additionally bears the social costs—namely, the harsh reality faced by the workers in the sweatshops and the environmental damage created, one can see a very significant role caused by corporations.

The corporate structure serves as a vehicle for raising funds and coordinating production. By shielding its participants, investors, directors and other controllers alike from the consequences of their actions—in this case, their social costs—the corporation makes it much easier to engage in activities that, on a personal level, one would find unacceptable.224

The corporate form permits and encourages the concentration of wealth and power—in Easterbrook and Fischel's terms: "[it is] the firm’s strength (its tendency to maximize wealth) . . ."225 It enables corporate controllers and investors to exploit the weaknesses of the market for their own advantage, as Easterbrook and Fischel implicitly acknowledge in their statement: "The task is to establish property rights so that the firm treats the social costs as private ones, and so that its reactions, as managers try to maximize profits given these new costs."226 The weaknesses of the market susceptible to exploitation are those market failures, noted above, information asymmetry and externalities, which permit the corporation to benefit without being able to force the corporation to bear the costs. By creating an entity that is focused exclusively on finance and wealth generation without concern for the other consequences of its activities, the law has created an entity that will maximize its use of externalities for which it has no liability, in order to maximize its internal profits and wealth creation. In the Wal-Mart case study, the strategy of employing the greatest number of part-time employees without benefits, anti-unionism, and imposition of social costs on China all work to increase profits. These strategies are implementations of the incentive scheme facilitated by the corporate form.

The corporation facilitates this minimization or externalizing of costs by offering a legal shield to insiders—the beneficiaries of the corporate form—from the true costs of the activities from which they intend to profit. In a worst case scenario from the perspective of insiders, a corporate bankruptcy, neither directors nor officers, nor shareholders, nor creditors, nor employees will be liable for all the costs created by the corporation where the corporation has acted in accordance with the law, regardless of the quantity

224. This is the problem of role specific ethics and is discussed in the ethics literature surrounding corporate failures and white collar crime.
225. EASTERBROOK, supra note 106, at 38.
226. Id. at 39.
or severity of those costs. In such a worst-case scenario, the corporation acts as a shield and all that is lost are its assets and share value.

A worst case scenario from the perspective of outsiders, those bearing the social costs, is not by any means a corporate collapse.\(^\text{227}\) A corporation which continues to operate, destroying the environment, poisoning employees, and undermining societies is certainly the worst. In other words, the worst case scenario for society is the opposite of a corporate collapse, it is corporate survival.

Furthermore, given the incentive structure in the market, being tied exclusively to profits, there is no incentive to internalize any costs. In what can only be described as a perversion of social good, corporate incentives are the exact opposite. To the extent that a director, officer or manager can externalize a cost and so increase profits, there is a reward for doing so. Thus with the combination of a structure providing a shield from consequences and an incentive structure for externalizing negative consequences, it cannot but be supposed that corporations will act in exactly the manner of Wal-Mart.

Further, with its power over the market and control of information, the corporation will exploit the information asymmetry between it and other market participants. The corporation is not required to disclose much about the majority of its activities, and as seen in the case of Wal-Mart, will tend to be intensely secretive about many of its activities.\(^\text{228}\) It does not want competitors to utilize the information to its disadvantage. More importantly, the corporate form will continue to facilitate profit making when people do not understand the consequences of its activities. Again, the corporate structure and the incentives discussed above are designed to support this approach. This strategy has been employed by big tobacco, automobile manufacturers, and oil companies. It is as if these latter lessons have not been learned by society; instead society has accepted continued corporate harm by merely instituting a non-smoking campaign while corporations increase the toxicity of tobacco, by accepting automobiles as status symbols instead of transportation while automobile corporations manufacture more dangerous and environmentally damaging vehicles (such as SUVs), and by accepting increased greenhouse emissions as petroleum corporations join in the

\(^{227}\) The media attention to corporate collapse causes many to infer that such an event is a worst case scenario. While a large corporate collapse causes disruption to the economy and to the lives of employees and suppliers, certainly some of the externalities discussed in this paper are greater concerns.

\(^{228}\) See Fishman, supra note 135.
promotion of increased burning of fossil fuels, by supporting vehicle manufacturers campaigns for larger vehicles.229

To address the information asymmetry, some scholars have begun advocating triple bottom line accounting. Whereas the corporate focus on economic results has led to exclusive focus on financial reporting, this approach to accounting requires corporations to provide information on social costs, not just monetary profits. While this may well be a step in the right direction, unless there is a dramatic reform in the economic structure of the corporation tying such measures to profit they are unlikely to have much effect.230 Furthermore, given the incomplete nature of markets, it will never be possible to account for all costs in a market regime. Accordingly, for those committed to both a market economy and accounting for social costs, another mechanism needs to be developed for attaching cost to benefit and deducting the former from the latter for purposes of accurately stating the position of the corporation. As Coase would say, “choosing . . . arrangements we should have regards for the total effect.”231 Where such an accounting has been done, it has led to the conclusion that current economic activity, contrary to the supposed benefit indicated by ever increasing GDP figures, is in fact a net loss to life on the planet.232

Another effort to address corporate social costs has been reflected through the Corporate Social Responsibility movement. This movement’s advocates promote triple-bottom line accounting, corporate governance and higher levels of personal responsibility. This recommendation of increased liability where property rights are inappropriate or ineffective, is in accord with the recommendations of Law and Economics scholars.233 One example of this increased liability, it may be argued, is the recent Sarbanes-Oxley legislation, which places the onus on corporate insiders to support the figures presented to the public. The problem with this approach is one not unique to the problem of social costs or corporate law: it is a problem with law in general. Law tends to be post facto, fixing things after they have gone wrong. So, where a corporate insider chooses to support a false statement, such falsehood may not be discovered until it is too late (as in the case of Enron)

230. Efforts of ethical investment funds or socially responsible investing are an exception, but the size, coordination and influence of these institutional investors is not known.
231. Coase, supra note 24, at 44.
232. See Kysar, supra note 2.
and the insider has disappeared with the profits, or destroyed some aspect of
the environment, or created some other social cost.

While the benevolent view of the market advocated by Adam Smith may
have been appropriate for his day of small entrepreneurs and minimal obvious
social costs, the environmental and social carnage caused by a single
corporation like Wal-Mart is beyond anything he could have imagined, let
alone advocated. With our increased understanding of the ecology of the
planet and the forces in society, it is inappropriate to continue to permit
corporations with their current structural immunities and perverse incentive
structures to destroy the very thing we humans value most: a thriving society
in a clean environment.

VIII. CONCLUSION

Sociologist Sharon Zukin has identified the broad-based negative effect
of big-box stores. She opines:

I think stores like Wal-Mart are bad for the world . . . and bad for the local communities,
because they suck up the buying power without creating the dynamism for local
economies to grow. Local economies grow on the basis of new products, growth in
production, growth in jobs and lots of local merchants. But with one store you just don't
get that.

Her view, which summarizes much of the argument in this article, would lead
to the conclusion that the social costs are overtaking the utility of the neo-
classical law and economics model of the corporation.

To a certain extent, the issue is a coordination problem—the particular
type of problem that faces parties when more than a single value is involved.
This type of situation, as demonstrated above, is not susceptible to a Coasean
analysis. It requires collective action, governmental intervention, and where
governments have been co-opted by corporations, some type of change in
corporate legislation to address the issue.

One aspect or cause of coordination problems are the concerns that
parties bring to their everyday concerns and work. As Stiglitz, the former
chief economist for the World Bank, observes: “The typical central bank
governor begins his day worrying about inflation statistics, not poverty
statistics; the trade minister worries about export numbers, not pollution

234. As Stiglitz observes, Smith himself was aware of market failures. Stiglitz, supra note 3, at 219.
com/mld/dfw/news/opinion/7420967.htm?lc. See also Zukin, supra note 147.
indices." In other words, humans tend to focus on the matters under their immediate control without worrying or making efforts to coordinate their efforts with others. This natural tendency is particularly worrisome where it affects people at the centres of power, such as the governors of central banks failing to coordinate with others in similarly located centres of power (let alone ignoring the ecology which sustains human life and the economy in the first place). Yet if social costs are not successfully addressed because of a failure to resolve the coordination problem, the world will become a much more difficult place to inhabit, at least for the human species. Ironically, the corporate structure, that is such a significant creator of social costs, facilitates coordination within itself. It is able to do so because of its single focus on profits and it so suffers to a much lesser degree, the coordination problem. The corporation's strength in this regard may yet be helpful in solving the problem of social costs where it could be turned to that end.

Regardless, given these problems of coordination and dramatically increasing social costs, it may make sense to look at corporate law reform. Such reform should follow on our experience with business, where corporate directors have been granted power on the basis of financial performance, perhaps directorships of the other important social costs should be developed. An empowered, informed, incentivized, and accountable director of ecology, for example, sitting on the board of directors, or a similarly created directorship of labour could potentially reduce significantly the related social costs resulting from a corporation's profit making activities.

A Law and Economics approach provides two directives: normatively, that the social costs of the corporate vehicle must be internalized and positively: that rational self-interested actors will act only according to their knowledge. Where that knowledge includes social costs, and where the incentive structure is appropriate, a more effective means of internalizing externalities and hence minimizing these social costs will lead to appropriate pricing. Appropriate pricing permits the market to appreciate the costs associated with actions and preferences, and so to make better choices concerning the allocation and use of the planet's resources. This approach to addressing the market failure caused by information asymmetry and the corporation's concerted effort to exploit consumer ignorance is certainly not

236. Stiglitz, supra note 3, at 216.
237. Such as is found in the GmBH in Germany.
238. Some suggestions are canvassed in Corporate Models, supra note 22.
an easy agenda; however, given the consequences of failure to address the issues, continuing current practices is simply not an option.

The larger question of this article has been: How well does the Law and Economics contractarian model describe the corporate activity and deal with social costs? Our answer is clearly, not well at all. This suggests further research and the possibility that working with a concessionaire model may yet be a more successful manner for addressing the increasingly grave social costs created by corporate activity.