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Are Corporate Super PAC Contributions Waste or Self-Dealing? A Closer Look

Joseph K. Leahy

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Are Corporate Super PAC Contributions Waste or Self-Dealing? A Closer Look

*Joseph K. Leahy**

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“[N]othing need be added to the present legal rights of the stockholder, a single stockholder having already a complete right of action in case of expenditure of any portion of corporate funds for political purposes.”¹

I. INTRODUCTION

Four years ago, in *Citizens United v. FEC*,² the United States Supreme Court famously held that corporations may spend unlimited sums of money on behalf of candidates for federal political office.³ This decision paved the way for the rise of “Super PACs,”⁴ which spent billions of dollars in the 2010 and 2012 elections.⁵ Today, *Citizens United* remains deeply unpopular among progressives who decry the growing influence of corporate money in politics.⁶

Yet, opposition to *Citizens United* is not simply a matter of politics. Proponents of increased shareholder power also have criticized the *Citizens United* decision because it permits a corporation’s management to spend the corporation’s money to support political candidates whom most shareholders oppose.⁷ From a shareholder perspective, corporate political spending is wrong not due to fears of the excessive power and influence of big business, but rather because it could possibly constitute a misuse of corporate funds. That is, company executives could essentially misappropriate the corpora-

1. Perry Belmont, *Publicity of Election Expenditures*, 180 N. AM. REV. 166, 167 (1905).

2. 558 U.S. 310 (2010).

3. See *infra* Part II. A corporation may not coordinate its spending with a candidate, however. See *infra* Part II. Further, direct contributions from corporations to federal political campaigns remain strictly prohibited, as they have been for over 100 years. See Tillman Act, ch. 420, 34 Stat. 864, 864-65 (1907) (current version at 2 U.S.C. § 441b(a) (2006)) (bars contributions of money from corporations to candidates for federal political office); see also Adam Winkler, “*Other People’s Money*”: *Corporations, Agency Costs, and Campaign Finance Law*, 92 GEO. L.J. 871, 918 (2004).

4. See *infra* Part II.B.2.

5. See Lucian A. Bebchuk & Robert J. Jackson, Jr., *Shining Light on Corporate Political Spending*, 101 GEO. L.J. 923, 937 (2013).

6. See, e.g., Paul Blumenthal, *Citizens United Third Anniversary Marked by Reformers with Push for Constitutional Amendment*, HUFFINGTON POST (Jan. 19, 2013, 12:15 PM), http://www.huffingtonpost.com/2013/01/19/citizens-united-third-anniversary_n_2511103.html (describing rallies marking the third anniversary of *Citizens United*).

7. See Lucian A. Bebchuk & Robert J. Jackson, Jr., *Corporate Political Speech: Who Decides?*, 124 HARV. L. REV. 83, 90 (2010) (“[P]olitical spending decisions may be a product not merely of a business judgment regarding the firm’s strategy, but also of the directors’ and executives’ own political preferences and beliefs.”).

tion's funds to serve their own political agendas, rather than the corporation's best interest.⁸

To allay concerns about management making donations to serve its own political ends, leading scholars have proposed revising the federal securities laws to require that large, publicly traded corporations disclose certain political contributions⁹ and consult shareholders before making such contributions.¹⁰ If both proposals were adopted into law, they might (in theory¹¹) prevent management from making some campaign contributions that are wildly unpopular with shareholders.¹² However, there are conflicting reports in the media about whether the Securities and Exchange Commission (SEC) is even considering adoption of the former proposal,¹³ and there has been no indication whatsoever that the SEC plans to take up the second proposal.¹⁴

Even if the SEC promulgates rules requiring greater disclosure of political spending by publicly traded corporations, shareholders of such corporations who oppose political spending still will have no way of preventing it. A corporation's management – the board of directors and its executive officers – have exclusive domain over the corporation's day-to-day affairs.¹⁵ Just as

8. *See id.*; *see also* Winkler, *supra* note 3, at 873 (explaining that corporate political contributions were first banned to prevent “company executives . . . misappropriating” the corporation's funds “to purchase legislation benefiting the executives themselves” and to “immunize executives from the oversight of owners,” rather than to “help companies’ bottom lines”).

9. *See generally* Bebchuk & Jackson, *supra* note 5.

10. *See generally* Bebchuk & Jackson, *supra* note 7.

11. However, in practice it is unlikely that shareholders of a publicly traded corporation would organize to reject any corporate political contribution. *See infra* note 19 and accompanying text (describing the “collective action problem”).

12. Indeed, research showing that higher political contributions correlate with lower revenues suggests that shareholders might broadly oppose political contributions. *See* Rajesh K. Aggarwal et al., *Corporate Political Donations: Investment or Agency?* 4-5 (2008 WFA Meeting Paper, AFA 2012 Chicago Meetings Paper), *available at* <http://ssrn.com/abstract=972670>.

13. *Compare* Lucian A. Bebchuk & Robert J. Jackson, Jr., *SEC to Propose Rules on Corporate Political Spending by April 2013*, HARV. L. SCH. F. ON CORP. GOVERNANCE & FIN. REG. (Jan. 9, 2013), <http://blogs.law.harvard.edu/corpgov/2013/01/09/sec-to-propose-rules-on-corporate-political-spending-by-april-2013/>, *with* Sarah N. Lynch, *White Says SEC Not Now Writing Political Spending Rule*, REUTERS.COM (May 16, 2013, 10:01 PM), <http://www.reuters.com/article/2013/05/16/us-congress-sec-political-spending-idUSBRE94F0PC20130516>.

14. A similar disclosure proposal has been introduced into Congress. *See* Press Release, Menendez, Capuano Reintroduce Shareholder Protection Act (Apr. 25, 2013), *available at* <http://www.menendez.senate.gov/newsroom/press/menendez-capuano-reintroduce-shareholder-protection-act->. However, this bill would seem to have little chance of passing the Republican-controlled House of Representatives.

15. *See, e.g.*, D.G.C.L. § 141(a) (“The business and affairs of every corporation . . . shall be managed by or under the direction of a board of directors.”).

with other ordinary¹⁶ business decisions, corporation law provides no mechanism for shareholders to play a direct role in deciding whether or not a corporation makes political contributions.¹⁷ A shareholder who disagrees with any management decision generally has three options: elect a different board at the next annual shareholder meeting, sell her shares in the market, or sue the board for a violation of its fiduciary duties to the corporation – *i.e.*, “vote, sell or sue.”¹⁸

16. By contrast, only a few, extraordinary transactions – like a merger of the corporation into another corporation – require shareholder approval. *See, e.g.*, D.G.C.L. § 251.

17. *See* Thomas W. Joo, *Corporate Governance and the Constitutionality of Campaign Finance Reform*, 1 ELECTION L.J. 361, 368-69 (2002) [hereinafter Joo, *Corporate Governance*] (explaining that a corporation’s board of directors may contribute corporate money to the party of its choice “without consulting shareholders”); Bebchuk & Jackson, *supra* note 7, at 87 (explaining that “political speech decisions” are “governed by the same rules as ordinary business decisions” – meaning that “there is . . . no role for shareholders”); *see also* Reza Dibadj, *Citizens United as Corporate Law Narrative*, 16 NEXUS 39, 51 (2011); Adam Winkler, *Beyond Bellotti*, 32 LOY. L.A. L. REV. 133, 165 (1998) (“Management, not shareholders, makes the determination of what to say, where to say it and how much to spend. [C]orporate speech is really corporate management’s speech.”).

18. *See* ROBERT CHARLES CLARK, CORPORATE LAW 93-105 (1986); Dibadj, *supra* note 17, at 49. Selling one’s own shares does not “discipline” management directly. However, if enough shareholders sell their shares, in theory the market price for the corporation’s stock will decline, thereby increasing the chance that a corporate raider will (1) make a tender offer for the corporation’s “undervalued” stock, (2) take over the company and (3) fire management. *See generally* Frank H. Easterbrook & Daniel R. Fischel, *The Proper Role of a Target’s Management in Responding to a Tender Offer*, 94 HARV. L. REV. 1161 (1981) (explaining how a robust market for corporate control can discipline a corporation’s management).

“Vote,” “sell” and “sue” are state law remedies. In addition, federal law permits certain shareholders of publicly traded companies to submit proposals on management’s proxy form for an up-or-down vote by all voting shareholders. *See* 17 C.F.R. § 240.14a-8 (2013). However, such proposals generally must be precatory rather than mandatory in nature. *See* THOMAS LEE HAZEN, 3 LAW SEC. REG. § 10.8 (2013) (citing SEC no-action letters); *see also* Joo, *Corporate Governance*, *supra* note 17, at 368. Further, such proposals rarely win sufficient shareholder support to be taken seriously by the board. *See, e.g.*, Bebchuk & Jackson, *supra* note 5, at 962 & n.133 (explaining that proposals regarding corporate political spending are generally defeated, often by large margins); Reuters, *Starbucks Shareholders Reject Political Contribution Ban*, CHICAGO TRIB., Mar. 30, 2013, http://articles.chicagotribune.com/2013-03-20/business/chi-starbucks-shareholders-reject-political-contribution-ban-20130320_1_chief-executive-howard-schultz-starbucks-political-contribution-ban. As a result, shareholder proposals are not an effective way to obtain redress for objectionable corporate political contributions.

Yet, since the SEC does not specifically require disclosure of corporate political spending, shareholders can attempt use such proposals to encourage corporations to disclose their political spending. *See* Home Depot, Inc., SEC No-Action Letter, 2011 SEC No-Act. LEXIS 333, at *1 (Mar. 25, 2011) (allowing such a proposal); *see,*

Voting out the existing board of a publicly traded corporation is a practical impossibility for all but the largest of shareholders. Most shareholders face a “collective action problem” that prevents them from acting in their own interest: they are rationally apathetic and do not engage in costly proxy battles because the cost of taking action outweighs any financial gains they may achieve via electing their own slate.¹⁹ As a result, the hand-selected boards of most publicly traded corporations run for re-election unopposed,²⁰ which means that shareholders cannot simply give their proxy votes to the opposition candidate. Moreover, simply withholding one’s vote often is no solution, because incumbent directors generally only need a plurality of votes to be re-elected.²¹ Even for corporations that require a majority of shareholders to elect directors,²² management is permitted to spend corporate funds “in an

e.g., Carey L. Biron, *Chevron Rejects Shareholder Demands to Explain Record Political Spending*, IPS NEWS.NET, May 29, 2013, <http://www.ipsnews.net/2013/05/chevron-rejects-shareholder-demands-to-explain-record-political-spending/>.

In theory, shareholder proposals also could be used to enact a bylaw prohibiting or limiting political contributions. However, even if such a bylaw were permitted under Delaware law (a question that is beyond the scope of this Article), such proposals are unlikely to pass due to the collective action problem. See Paul S. Miller, *Shareholder Rights: Citizens United and Delaware Corporate Governance Law*, 28 J. L. & POL. 51, 78-85 (2012).

19. See WILLIAM T. ALLEN ET AL., COMMENTARIES & CASES ON THE LAW OF BUSINESS ORGANIZATION 154 (4th ed. 2012); Claire A. Hill & Brett H. McDonnell, *Disney, Good Faith, and Structural Bias*, 32 J. CORP. L. 833, 854 (2007); see also Thomas W. Joo, *The Modern Corporation and Campaign Finance: Incorporating Corporate Governance Analysis into First Amendment Jurisprudence*, 79 WASH. U.L.Q. 1, 44-45 (2001) [hereinafter Joo, *The Modern Corporation*] (describing this issue in the context of political activity).

20. See Lucian A. Bebchuk, *The Case for Shareholder Access: A Response to the Business Roundtable*, 55 CASE W. RES. L. REV. 557, 559 (2005); Joo, *The Modern Corporation*, *supra* note 19, at 44; Dashka Slater, *Resolved: Publicly Traded Corporations Shall Take Us Seriously*, N.Y. TIMES MAG., Aug. 12, 2007, <http://www.nytimes.com/2007/08/12/magazine/12exxon-t.html?pagewanted=all>.

21. See D.G.C.L. § 216(3) (plurality voting is default rule for electing directors); Jennifer S. Taub, *Money Managers in the Middle: Seeing and Sanctioning Political Spending After Citizens United*, 15 N.Y.U. J. LEGIS. & PUB. POL’Y 443, 468 (2012). Even under majority voting, incumbent directors who fail to receive a majority are not generally required to resign until a new director is elected. See *id.* As such, some have described majority voting as “smoke and mirrors.” William K. Sjostrom, Jr. & Young Sang Kim, *Majority Voting for the Election of Directors*, 40 CONN. L. REV. 459, 486-89 (2007).

22. Most Fortune 500 corporations have recently switched to majority voting. See Robert Yates & Bimal Patel, *ISS Releases 2012 U.S. Board Practices Study*, ISS GOVERNANCE BLOG, Mar. 2, 2012, <http://blog.issgovernance.com/gov/2012/03/iss-releases-2012-board-practices-study.html>.

almost unlimited way” in order to drum up support for its slate of directors.²³ As a result, the corporate election process is largely “an irrelevancy.”²⁴

Selling one’s shares also is an unappealing solution. Since it is unlikely that a small shareholder of a publicly traded corporation has access to non-public information, once such a shareholder learns of a political contribution, that information also presumably will be available to the market.²⁵ If other market participants agree that the contribution is bad for the corporation, that news will be reflected in the price at which the existing shareholder can sell her stock.²⁶ As such, selling merely allows a shareholder to “avoid future misuse” of corporate funds “after it has occurred. It does not prevent misuse, or provide any remedy for past misuse.”²⁷

A derivative lawsuit against management, alleging a breach of the duty of loyalty to the corporation,²⁸ is a third way that a shareholder might potentially obtain redress for (or avert future) corporate political contributions. However, the scholarly consensus rejects this option out of hand. Myriad scholars have opined – almost always in passing – that a derivative lawsuit against the board would fail because the decision to make a political contribution is an ordinary business decision protected by the potent business judgment rule.²⁹ Yet, until recently, no commentator has undertaken more than a cursory inquiry into the issue.³⁰

23. William B. Chandler III & Leo E. Strine, Jr., *The New Federalism of the American Corporate Governance System: Preliminary Reflections from Two Residents of One Small State*, 152 U. PA. L. REV. 953, 999 (2013).

24. *Id.*; see also Joo, *The Modern Corporation*, *supra* note 19, at 44.

25. See Michael Molitor, *The Crucial Role of the Nominating Committee: Reinventing Nominating Committees in the Aftermath of Shareholder Access to the Proxy*, 11 U.C. DAVIS BUS. L.J. 97, 143 (2010).

26. See ALLEN ET AL., *supra* note 19, at 673 (describing the Efficient Capital Market Hypothesis).

27. Joo, *Corporate Governance*, *supra* note 17, at 368-69; accord Taub, *supra* note 21, at 468; Winkler, *supra* note 17, at 168; Joo, *The Modern Corporation*, *supra* note 19, at 57-59 (explaining that the “Wall Street Rule” of shareholders “voting with their feet” “allows the shareholder only to escape continued unauthorized use of corporate resources” but does “not put a stop to the activity . . . or provide any remedy”).

28. A suit alleging a breach of the board’s other key fiduciary duty – the duty of care – is not really an option. In theory, the duty of care requires that directors manage the corporation with the care of an “ordinarily careful and prudent [person] . . . in similar circumstances.” *Graham v. Allis-Chalmers Mfg. Co.*, 188 A.2d 125, 130 (Del. 1963). However, the duty of care is largely unenforceable due to the business judgment rule, damage waiver provisions in corporate charters and corporate indemnification of directors who breach of the duty of care. See ALLEN ET AL., *supra* note 19, ch. 6; Claire A. Hill & Brett H. McDonnell, *Stone v. Ritter and The Expanding Duty Of Loyalty*, 76 FORDHAM L. REV. 1769, 1770 (2007) (“Care . . . essentially translates into ‘plaintiff loses’ (and even if . . . not . . . , there would be exculpation).”).

29. See *infra* Part III.A.

30. Indeed, the most thorough treatment of this issue to date appears in a blog post. See Stephen M. Bainbridge, *Citizens United, Corporate Political Expenditures*,

Bucking this trend, in 2012 two separate authors published papers urging that a shareholder could use a derivative lawsuit to successfully challenge a corporate political contribution.³¹ Yet, as described below, these authors' analysis is founded largely on assertion.³² Perhaps as a result, these articles have been almost completely ignored by the law reviews; one was summarily panned in a single blog post.³³

Although these two authors' analysis may be superficial, the idea of using derivative suits to challenge political contributions nonetheless warrants careful study before being discarded. As such, this Article undertakes a detailed inquiry into the theories – waste and self-dealing – that these authors propose that shareholders could use to successfully challenge a corporate political contribution.

After a careful review, the first theory – waste – is a loser. Despite the Delaware Court of Chancery's³⁴ seemingly generous treatment of waste suits in recent years,³⁵ there is simply no plausible argument that a typical corporate political contribution satisfies the extremely onerous waste standard.³⁶ Only a contribution to a deeply offensive candidate with zero chance of winning would qualify.³⁷

However, the second theory – self-dealing – could be viable in some instances.³⁸ In particular, a corporate contribution in support of a candidate

and the Business Judgment Rule, PROFESSORBAINBRIDGE.COM (May 24, 2012), <http://www.professorbainbridge.com/professorbainbridgecom/2012/05/citizens-untied-corporate-political-expenditures-and-the-business-judgment-rule.html>.

31. William A. Nelson II, *Post-Citizens United: Using Shareholder Derivative Claims of Corporate Waste to Challenge Corporate Independent Political Expenditures*, 13 NEV. L.J. 134, 135 (2012) (urging that the corporate waste doctrine could be used to challenge political contributions); Jonathan Romiti, *Playing Politics With Shareholder Value: The Case for Applying Fiduciary Law to Corporate Political Donations Post-Citizens United*, 53 B.C. L. REV. 737, 737 (2012) (arguing that political contributions might be challenged as self-dealing or waste).

32. *See infra* Part III.

33. To date, the only substantive discussion of the arguments advanced in either article is a brief blog critique of Nelson's article by Professor Bainbridge. *See* Bainbridge, *supra* note 30.

34. This Article focuses principally on Delaware law and decisions of the Delaware Court of Chancery because they are by far the most important sources of state corporate law in the United States. *See* LEWIS S. BLACK, JR., *WHY CORPORATIONS CHOOSE DELAWARE* (2007), available at http://corp.delaware.gov/pdfs/whycorporations_english.pdf (nearly sixty percent of all publicly traded corporations in the United States are incorporated in Delaware); *see also* Omari Scott Simmons, *Branding the Small Wonder: Delaware's Dominance and the Market for Corporate Law*, 42 U. RICH. L. REV. 1129, 1163 (2008) (discussing the Court of Chancery's "national reputation for its sophistication and expertise in handling corporate cases").

35. *See infra* notes 150-151 and accompanying text.

36. *See infra* Part IV.

37. *See infra* Part IV.

38. *See infra* Part V.

who advocates policies that favor the personal financial interests of directors (or officers³⁹) over the interests of most Americans might plausibly be deemed self-dealing.⁴⁰ However, this argument is tenuous at best for most ordinary political contributions because of the attenuated causal connection between a political contribution and any personal financial benefit that directors might stand to gain from such a contribution.⁴¹

Ultimately, this Article concludes that the scholarly consensus probably is correct: a shareholder lawsuit to challenge a typical Super PAC contribution is unlikely to succeed on either a theory of waste or self-dealing.⁴² If shareholder plaintiffs are going to succeed in challenging corporate Super PAC contributions, they will need to come up with different theories.⁴³

* * * * *

The remainder of this Article is organized into four parts and a brief conclusion. Part II provides a brief background on the *Citizens United* decision. Part III describes derivative lawsuits, the business judgment rule, and what little leading scholars have said about shareholders' ability to challenge corporate political contributions using derivative suits. Parts IV and V, respectively, summarize and critique arguments advanced by two recent authors, that shareholders could challenge political contributions as a breach of the duty of loyalty. Part IV deals with the theory of corporate waste and Part V deals with the theory of self-dealing.

II. BRIEF BACKGROUND ON *CITIZENS UNITED*

A. *The Decision and the Experts' Reaction*

In early 2008, Citizens United, a nonprofit corporation, produced a documentary video entitled *Hillary: The Movie*.⁴⁴ The documentary was highly critical of then-Senator Hillary Clinton, a candidate for the Democratic Party's nomination for President.⁴⁵ Citizens United released *Hillary: The Movie* in theaters and on DVD, and arranged to make the documentary available as an "on demand" feature on DirectTV and cable television shortly before the

39. This Article will use the term "director" (or sometimes, "management") to refer to both directors and officers.

40. See *infra* Part V.

41. See *infra* Part V.

42. See *infra* Part VI.

43. One such theory might be bad faith, which is more flexible than self-dealing and a lower standard than corporate waste. See Joseph K. Leahy, *Corporate Political Contributions as Bad Faith*, 86 U. COLO. L. REV. (forthcoming 2015), *current draft available at* <http://ssrn.com/abstract=2328991>.

44. *Citizens United v. FEC*, 558 U.S. 310, 319-20 (2010).

45. See *id.* at 322.

2008 primary elections.⁴⁶ To promote the documentary, Citizens United produced various television advertisements.⁴⁷

At the time, section 441b of the Bipartisan Campaign Reform Act of 2002 (BCRA), as amended by BCRA section 203, prohibited corporations from spending general treasury funds on “electioneering communications” or on speech that expressly advocated the election or defeat of a candidate.⁴⁸ In December 2007, Citizens United filed suit in district court seeking a declaratory judgment that, *inter alia*, BCRA section 441b was unconstitutional as applied to *Hillary: The Movie*.⁴⁹ The district court granted summary judgment for the Federal Election Commission (FEC), holding that the television ads for the documentary violated BCRA’s ban on electioneering communications within thirty days of a primary for federal election.⁵⁰ The district court also rejected Citizens United’s First Amendment challenge to section 441b, holding that the section was constitutional both on its face and as applied to the documentary because it was “susceptible of no other interpretation than to” attack Clinton’s candidacy for office.⁵¹ After losing its appeal to a three-judge panel of the district court, Citizens United appealed directly to the Supreme Court (as permitted by statute).⁵²

The Supreme Court, by a 5-4 decision, reversed the district court. It held that BCRA section 441b was unconstitutional on its face, thereby striking down the section’s ban on corporate independent expenditures.⁵³ In support of its holding, the Court reasoned that the “[g]overnment may not suppress political speech on the basis of the speaker’s corporate identity.”⁵⁴ Applying strict scrutiny, the Court considered whether section 441b was narrowly tailored to serve a compelling interest.⁵⁵ The Court held that “[n]o sufficient governmental interest justifies limits on the political speech of nonprofit or for-profit corporations.”⁵⁶ Further, the Court rejected the respondents’

46. *See id.* at 319-21.

47. *Id.* at 320.

48. An “electioneering communication” is any broadcast, cable, or satellite communication that (1) refers to a clearly identified candidate for federal office, (2) is made within thirty days of a primary or sixty days of a general election, and (3) is “publicly distributed.” *Id.* at 321 (citing 11 C.F.R. §§ 100.29(a)(2), (b)(3) (2009)).

49. *See id.* at 321.

50. *See Citizens United v. FEC*, 530 F. Supp. 2d 274, 281-82 (D.D.C. 2008) (per curiam).

51. *Id.* at 279.

52. *See* 558 U.S. at 319; 28 U.S.C. § 1253 (2012).

53. *See* 558 U.S. at 364-65. In so doing, the Court overturned *McConnell v. FEC*, in which the Court had recently upheld BCRA section 203’s extension of section 441b. *See id.* at 365-66 (overruling *McConnell*, 540 U.S. 93 (2003)).

54. *Id.* at 365.

55. *See id.* at 362.

56. *Id.* at 365. In so doing, the *Citizens United* Court also overruled another recent case, *Austin v. Michigan Chamber of Commerce*, which had held that

argument that protection of individual shareholders' speech rights was itself a compelling governmental interest.⁵⁷ The Court reasoned that "[t]here is . . . little evidence of abuse that cannot be corrected by shareholders 'through the procedures of corporate democracy.'"⁵⁸

However, the Court did uphold certain disclosure and disclaimer provisions in the BCRA,⁵⁹ reasoning that these were merely incidental burdens on speech.⁶⁰ The Court reasoned that disclosure plays an important role in helping shareholders to protect themselves:

Shareholder objections raised through the procedures of corporate democracy, can be more effective today With the advent of the Internet, prompt disclosure of expenditures can provide shareholders . . . with the information needed to hold corporations . . . accountable for their positions Shareholders can determine whether their corporation's political speech advances the corporation's interest in making profits.⁶¹

In dissent, Justice John Paul Stevens criticized the majority's reasoning that shareholders could protect themselves using "the procedures of corporate democracy."⁶² Justice Stevens reasoned that shareholders' ability to use the franchise to protect their own speech interests is limited due to the boards' wide-ranging authority.⁶³ Further, he reasoned that derivative suits for breach

political speech may be banned on the speaker's corporate identity. 494 U.S. 652, 668-69 (1990).

57. See 558 U.S. at 361-62.

58. *Id.* at 361-62 (quoting *First Nat'l Bank of Boston v. Bellotti*, 435 U.S. 765, 794 (1978)). Justice Kennedy's reasoning here echoed the *Bellotti* Court's assumptions about shareholder power: "Acting through their power to elect the board of directors . . . shareholders normally are presumed competent to protect their own interests." *Bellotti*, 435 U.S. at 794-95.

59. See 558 U.S. at 366-67. For example, BCRA section 201 requires that persons who spend more than \$10,000 making electioneering communications in any calendar year – which would include Super PACs – must disclose the "names and addresses of all contributors who contributed . . . \$1,000 or more" during a specified period. 2 U.S.C. § 434(f)(2)(f) (2012). See also Douglas M. Spencer & Abby K. Wood, *Citizens United, States Divided: An Empirical Analysis of Independent Political Spending*, 89 IND. L.J. 315, 330 (2014) (discussing the emergence of "Super PACs" following the Court's decision in *Citizens United*).

60. See 558 U.S. at 366-67.

61. *Id.* at 370 (internal citations omitted).

62. *Id.* at 476 (Stevens, J., concurring in part and dissenting in part).

63. See *id.* at 477 (Stevens, J., concurring in part and dissenting in part) ("In practice, . . . many corporate lawyers will tell you that these rights [i.e., shareholder voting and derivative suits] are so limited as to be almost non-existent, given the internal authority wielded by boards and managers and the expansive protections afforded by the business judgment rule.") (internal quotation marks omitted).

of fiduciary duty would be ineffective due to “the expansive protections afforded by the business judgment rule.”⁶⁴

Numerous corporate law experts have echoed Justice Stevens’ remarks.⁶⁵ Indeed, some leading corporate law scholars have lamented that the *Citizens United* opinion evinces a poor understanding of corporate law.⁶⁶

B. The Result: CEOs Can Cause Corporations to Contribute to Super PACs

1. *Citizens United* Leads to Unlimited Independent Expenditures

As a result of the *Citizens United* decision, corporations can engage in unlimited independent expenditures on behalf of a candidate for election to state⁶⁷ or federal office. As Professor Ciara Torres-Spelliscy explained at a recent symposium:

Before *Citizens United* if a CEO of a publicly traded company wanted to buy a political ad in a federal election, [she] had to reach into [her] pocket and pull out [her] personal checkbook. . . . But after *Citizens United* [she] can . . . reach into [her] other pocket . . . and pull out the corporate checkbook . . . where the bill does not go to [her] house [Thus,] corporate managers can spend what Justice Brandeis used to call “other people’s money” in politics.⁶⁸

Of course, money in the corporate treasury does not really belong to other *people* (i.e., the corporation’s shareholders). Rather, it belongs to one

64. *Id.*

65. See *infra* Part III.B and note 101.

66. See, e.g., Symposium: Accountability After *Citizens United* – Panel One Transcript, Panel One: Can Shareholders Save Democracy?, BRENNAN CENTER FOR JUST. 15 (Apr. 29, 2011), <http://www.brennancenter.org/sites/default/files/events/Accountability%20After%20Citizens%20United%20panel%20one.pdf> [hereinafter Symposium] (remarks of Prof. John R. Coates; incorrectly labeled as remarks of Prof. Robert Jackson) (“[O]ne thing we can agree on is that the Supreme Court was not well informed about corporate law.”); video available at http://www.youtube.com/watch?feature=player_embedded&v=-1AA61leLN4 (remark appears at 58:50 mark).

67. Although *Citizens United* struck down a federal statute, it also effectively invalidated state statutes prohibiting independent expenditures. See Spencer & Wood, *supra* note 59 at 336, n.108 (citing *Citizens United*, 558 U.S. at 399 (Stevens, J., concurring in part and dissenting in part)). The Court confirmed this in a later decision involving Montana law. See *id.* at 339 (analyzing *Am. Tradition P’ship v. Bullock*, 132 S. Ct. 2490, 2491 (2012) (per curiam)).

68. Symposium, *supra* note 66, at 1 (introductory remarks of Ciara Torres-Spelliscy).

other *person*: the corporation.⁶⁹ However, management's expenditure of funds from the corporate treasury is nonetheless somewhat akin to spending "other people's money" due to two well established corporate law norms: First, management has a fiduciary duty of loyalty to make decisions in the best interest of the corporation.⁷⁰ Second, the dominant paradigm in corporate law (from which there is, admittedly, frequent and fervent dissent⁷¹) holds that "the best interest of the corporation" is largely synonymous with "shareholder wealth maximization."⁷²

2. The Rise of Super PACs

Although corporations may now make unlimited independent expenditures in support of candidates for state or federal political office, they rarely spend money directly to influence elections. Instead, they generally spend through intermediaries, such as Super PACs. Or, to avoid disclosure, they contribute to section 501(c)(4) non-profits that are affiliated with Super PACs.⁷³ Super PACs are "independent expenditure-only" entities, meaning that they can spend unlimited money in support of a candidate for federal

69. See 11 WILLIAM MEADE FLETCHER ET AL., FLETCHER CYCLOPEDIA OF THE LAW OF CORPORATIONS § 5096 (2013); see, e.g., DEL. CODE ANN. tit. 8, § 122(4) (parenthetical needed).

70. See *Cede & Co. v. Technicolor, Inc.*, 634 A.2d 345, 361 (Del. 1993) ("Essentially, the duty of loyalty mandates that the best interest of the corporation and its shareholders takes precedence over any interest possessed by a director, officer or controlling shareholder and not shared by the stockholders generally."). See also *T.V.I. Corp. v. Gallagher*, No. 7798-VCP, 2013 WL 5809271, at *11 (Del. Ch. Oct. 28, 2013) ("An officer or director's duty of loyalty requires them scrupulously to place the interests of the corporation and shareholders that they serve before their own.").

71. See, e.g., Lynn A. Stout, *Why We Should Stop Teaching Dodge v. Ford*, 3 VA. L. & BUS. REV. 163, 169 (2008) (urging that the answer to the question of whether state corporation law codes "limit the corporate purpose to shareholder wealth maximization" is "not just 'no' but 'hell no'").

72. See STEPHEN M. BAINBRIDGE, CORPORATE LAW & ECONOMICS 306 (2d ed. 2009) ("It is well-settled that directors have a duty to maximize shareholder wealth.") (citing *Dodge v. Ford Motor Co.*, 170 N.W. 668 (Mich. 1919)). Cf., e.g., *eBay Domestic Holdings, Inc. v. Newmark*, 16 A.3d 1, 34 (Del. Ch. 2010) (reasoning that directors of a for-profit corporation "are bound . . . to promote the value of the corporation for the benefit of its stockholders.").

73. See Sean Sullivan, *What Is a 501(c)(4), Anyway?*, WASH. POST (May 13, 2013, 1:51 PM), <http://www.washingtonpost.com/blogs/the-fix/wp/2013/05/13/what-is-a-501c4-anyway/>; Taub, *supra* note 21, at 465. See also, e.g., Dylan Matthews, *Crossroads GPS and Priorities USA Were Created for the Purpose of Hiding Donors*, WASH. POST (May 15, 2013, 9:00 AM), <http://www.washingtonpost.com/blogs/wonkblog/wp/2013/05/15/crossroads-gps-and-priorities-usa-were-created-for-the-purpose-of-hiding-donors/> (interview with campaign finance reform advocate Fred Wertheimer).

political office so long as they do not expressly coordinate their spending with any candidate or campaign.⁷⁴

The Super PAC is a new player in electoral politics, made possible by *Citizens United* and a subsequent appellate court case.⁷⁵ In that case, *SpeechNOW.org v. FEC*,⁷⁶ the U.S. Court of Appeals for the D.C. Circuit held that a PAC that promised not to make contributions to candidates, parties, or other PACs could accept unlimited contributions for the purpose of making independent expenditures.⁷⁷ The media promptly dubbed these deep-pocketed spending machines “Super PACs.”⁷⁸ Once unleashed by *Citizens United* and *SpeechNOW.org*, Super PACs immediately became major players in the 2010 and 2012 federal election cycles⁷⁹ (and in states’ 2010 election cycle⁸⁰).

III. DERIVATIVE LAWSUITS TO CHALLENGE CORPORATE POLITICAL CONTRIBUTIONS: THE SCHOLARLY CONSENSUS

A. Shareholder Derivative Lawsuits and the Business Judgment Rule

In a derivative lawsuit, a shareholder sues in the name of the corporation to address an injury to or vindicate a right of the corporation.⁸¹ These suits are dubbed “derivative” because the shareholder’s right to sue is derivative of the corporation’s right to sue.⁸² Shareholder derivative lawsuits face high standing hurdles, including most notably the requirement that the shareholder

74. See Matthews, *supra* note 73.

75. See Gregory J. Krieg, *What Is a Super PAC? A Short History*, ABCNEWS.COM (Aug. 9, 2012), <http://abcnews.go.com/Politics/OTUS/super-pac-short-history/story?id=16960267>.

76. 599 F.3d 686 (D.C. Cir. 2010).

77. See *id.* at 695. See also Spencer & Wood, *supra* note 59, at 330, 333 n.101.

78. See Dave Levinthal, *How Super PACs Got Their Name*, POLITICO.COM (Jan. 10, 2012, 1:41 PM), <http://www.politico.com/news/stories/0112/71285.html>.

79. See Michael Beckel, *Led by Karl Rove-Linked Groups, ‘Super PACs’ and Nonprofits Significantly Aid GOP in Election 2010*, Nov. 5, 2010, OPENSECRETS.COM (Nov. 5, 2010), <https://www.opensecrets.org/news/2010/11/led-by-karl-rove-linked-groups-nonp.html>; *Election 2012: Independent Spending Totals*, N.Y. TIMES, <http://elections.nytimes.com/2012/campaign-finance/independent-expenditures/totals> (last visited June 11, 2014). See generally Richard L. Hasen, *The Numbers Don’t Lie*, SLATE (Mar. 9, 2012), http://www.slate.com/articles/news_and_politics/politics/2012/03/the_supreme_court_s_citizens_united_decision_has_led_to_an_explosion_of_campaign_spending_.html.

80. See Spencer & Wood, *supra* note 59, at 361 (concluding that, after *Citizens United*, “independent spending increased at twice the rate” in states that had previously banned independent expenditures compared to states that had not).

81. See ALLEN ET AL., *supra* note 19, at 367.

82. See *id.*

first make “demand” on the corporation’s board of directors.⁸³ Demand is required because the decision whether to file suit on behalf of the corporation, like any other business decision, actually belongs to the board.⁸⁴ While demand is always required in some jurisdictions, in other jurisdictions (such as Delaware) it can be excused if a court concludes that making demand would have been “futile.”⁸⁵

Even if shareholder derivative plaintiff has standing to sue – that is, if a court concludes that the shareholder may sue because demand is futile (or, in jurisdictions where demand is essentially always required, if the shareholder makes demand and the court concludes that the suit may proceed) – every shareholder lawsuit faces another major hurdle: the business judgment rule. This judge-made rule reflects several policy rationales, including: (1) skepticism that judges are qualified to make business judgments; and (2) the view that shareholders have voluntarily hired the directors, not the courts, to make business decisions for the corporation.⁸⁶

The business judgment rule is often described as a “presumption”⁸⁷ (but is perhaps better described as an “assumption”⁸⁸) that, in making a business decision,⁸⁹ management “acted on an informed basis, in good faith and in honest belief that the action taken was in the best interests” of the

83. See, e.g., DEL. CH. CT. R. 23.1(a) (“In a derivative action . . . to enforce a right of a corporation . . . , the complaint shall allege . . . with particularity the efforts, if any, made by the plaintiff to obtain the action the plaintiff desires from the directors . . . and the reasons for the plaintiff’s failure to obtain the action or for not making the effort.”).

84. See *White v. Panic*, 783 A.2d 543, 546-47 (Del. 2001).

85. See *Aronson v. Lewis*, 473 A.2d 805, 811-12 (Del. 1984), *overruled on other grounds* by *Brehm v. Eisner*, 746 A.2d 244 (Del. 2000).

86. *Auerbach v. Bennett*, 393 N.E.2d 994, 1000 (1979) (“[T]he business judgment doctrine . . . is grounded in the prudent recognition that courts are ill equipped . . . to evaluate . . . business judgments [I]nescapably there can be no available objective standard by which the correctness of every corporate decision may be measured . . . [and] by definition the responsibility for business judgments must rest with the corporate directors Thus, absent evidence of bad faith or fraud . . . the courts must and properly should respect their determinations.”).

87. Unfortunately, courts do not agree on how the business judgment rule works. Some courts view the rule as a substantive rule of law; others describe it as an abstention doctrine; others treat it as a hybrid. See FRANKLIN A. GEVURTZ, *CORPORATION LAW* 289-90 (2d ed. 2010); BAINBRIDGE, *supra* note 72, at 243.

88. See GEVURTZ, *supra* note 87, at 243; BAINBRIDGE, *supra* note 72, at 110. Or, perhaps it is most accurately described as “simply a policy of judicial *non-review*.” Lyman Johnson, *The Modest Business Judgment Rule*, 55 BUS. LAW. 625, 631 (2000) (*italics in original*). This Article will nonetheless use the language of presumption.

89. Absent an exercise of judgment – i.e., a business decision – the business judgment rule does not apply. See BAINBRIDGE, *supra* note 72, at 110. This could, however, include a *decision to refrain* from acting. See *id.* That is to say, only *unconsidered* inaction is excluded from the ambit of the business judgment rule.

corporation.⁹⁰ Unless a shareholder plaintiff can meet her affirmative obligation to rebut the business judgment rule presumption, management's conduct is not subject to challenge as a breach of fiduciary duty under any circumstances.⁹¹ The effect of this rule is to refocus a court's inquiry into management's conduct:

When courts invoke the business judgment rule, they are . . . converting the question "Was the standard of care breached?" into the related, but different questions of whether the directors were truly disinterested and independent and whether their actions were not so extreme, unconsidered, or inexplicable as not to be an exercise of good-faith judgment.⁹²

That is to say, the business judgment rule instructs courts that, rather than look at the *quality* of the board's *decision* (i.e., was the decision negligent?⁹³), the court should look to *integrity* of the board's *decision-making process* (i.e., was the decision made in good faith, uninterested, independent, minimally informed, and not made in a grossly negligent manner?).⁹⁴ As a

90. *Aronson*, 473 A.2d at 812.

91. *See id.*; *accord*, e.g., *Kamin v. Am. Express Co.*, 383 N.Y.S.2d 807, 810 (N.Y. App. Div. 1976) ("In actions by stockholders, which assail the acts of their directors . . . , courts will not interfere unless the powers have been illegally or unconscientiously executed; or unless . . . the acts were fraudulent or collusive, and destructive of the rights of the stockholders.") (quoting *Leslie v. Lorillard*, 18 N.E. 363, 365 (N.Y. 1888)).

92. ALLEN ET AL., *supra* note 19, at 231; *see also* BAINBRIDGE, *supra* note 72, at 109 (explaining that the business judgment rule requires a court to "review the facts to determine not the quality of the decision, but rather whether the decision-making was tainted by self-dealing and the like . . . the merits of the board's decision are irrelevant"); Stephen M. Bainbridge, *The Business Judgment Rule as Abstention Doctrine*, 57 VAND. L. REV. 83, 95 (2004) ("[T]he whole point of the business judgment rule is to prevent courts from even asking the question: did the board breach its duty of care?"); Johnson, *supra* note 88, at 631 (describing the business judgment rule as "a judicial policy of not reviewing the substantive merits of a . . . business decision for the purpose of determining whether directors breached or fulfilled their duty of care.").

93. In the absence of a business judgment – i.e., when the board faces liability for being inattentive to corporate affairs – the duty of care essentially embodies a negligence standard. JAMES D. COX & THOMAS L. HAZEN, *BUSINESS ORGANIZATION LAW* 202-03 (2011); *see, e.g.*, *Francis v. United Jersey Bank*, 432 A.2d 814 (N.J. 1981).

94. *See* RICHARD D. FREER & DOUGLAS K. MOLL, *PRINCIPALS OF BUSINESS ORGANIZATIONS* 263 (2013) ("Under the business judgment rule, courts do not address whether a decision was dumb or smart; they do not second-guess business decisions."); *see, e.g.*, *Kamin*, 383 N.Y.S.2d at 810 ("Mere errors of judgment are not sufficient as grounds for equity interference[.]"); *Auerbach v. Bennett*, 393 N.E.2d 994, 1000 (N.Y. 1979) ("[T]he business judgment doctrine . . . bars judicial inquiry into actions of corporate directors taken in good faith and in the exercise

result, judges are effectively prohibited from evaluating the merits of rational, good faith business decisions.⁹⁵

B. Most Scholars Reject Derivative Suits Challenging Political Contributions

A shareholder lawsuit challenging a corporate political contribution as a breach of management's duty of loyalty would, in all likelihood, be derivative in nature. That is to say, the lawsuit presumably would allege that the contribution harmed the corporation and/or violated a right that belonged to the corporation.⁹⁶

Relatively few scholars have written at length about shareholder challenges to corporate political contributions. Most scholars who have written on the topic have rejected such challenges out of hand – much like Justice Stevens did – in brief commentaries focused upon the all-encompassing power of the business judgment rule.

For example, in his blog, Professor Stephen Bainbridge analogized political contributions to charitable donations by posing the following hypothetical:

Suppose a powerful CEO caused the corporation to make massive contributions to her alma mater. Is that a waste of corporate assets? Maybe. But the plaintiff has a serious problem; namely, that “When director decisions are reviewed under the business judgment rule, this Court will not question rational judgments about how promoting non-

of honest judgment in the lawful and legitimate furtherance of corporate purposes. Questions of . . . management . . . are left solely to their honest and unselfish decision . . . [and] may not be questioned, although the results show that what they did was unwise or inexpedient.” (internal quotation marks omitted); *Shlensky v. Wrigley*, 237 N.E.2d 776 (Ill. App. Ct. 1968) (“[W]e do not mean to say that we have decided that the decision of the directors was a correct one. That is beyond our jurisdiction and ability. We are merely saying that the decision is one properly before directors and the motives alleged in the amended complaint showed no fraud, illegality or conflict of interest[.]”).

95. Joo, *Corporate Governance*, *supra* note 17, at 368 (“Under the ‘business judgment rule,’ . . . shareholders [cannot] sue management for any act that can be characterized as a good-faith business decision, even if shareholders can show that it did not benefit the corporation. Courts presume that managers’ acts are good-faith business decisions, and make it very difficult for shareholders to prove otherwise. Thus courts will defer to all but the most egregiously negligent or obviously self-interested management decisions.”).

96. A shareholder could in theory challenge a corporate political contribution as a breach of management's duty of loyalty on the grounds that it violated her own *individual* rights (e.g., the right against compelled speech under the First Amendment). Such a lawsuit would *not* be derivative in nature because it does not assert to address a harm to and/or vindicate a right of the corporation. The ability of a shareholder to bring such a lawsuit is beyond the scope of this Article.

stockholder interests – be it through making a charitable contribution [or otherwise] – ultimately promote stockholder value.”⁹⁷

According to Professor Bainbridge, it will be “damned difficult” for a plaintiff challenging this hypothetical charitable donation – or the analogous political contribution – to survive a motion to dismiss because “courts will require considerable evidence of self-dealing before the business judgment rule will be rebutted.”⁹⁸ In short, Professor Bainbridge argues:

The basic problem [with shareholder challenges to corporate political contributions] is that corporate decisions about political expenditures differ neither in kind nor degree from any other decision to expend corporate funds. As such, there is no reason to think courts will – or should – treat the former class differently than they treat the latter.⁹⁹

The same is true, Professor Bainbridge has urged elsewhere, with regard to other corporate political activity, such as taking stances on political issues.¹⁰⁰

Numerous other scholars have made this same point (though never in too much detail).¹⁰¹ Indeed, even one of the authors who recently wrote to

97. Bainbridge, *supra* note 30 (quoting *eBay Domestic Holdings, Inc. v. Newmark*, 16 A.3d 1 (Del. Ch. 2010)).

98. *Id.* Professor Bainbridge presumably concluded that it would be atypical for a court to find “considerable evidence” of self-dealing under the circumstances of a normal political contribution, since he did not expand on his “damned difficult” comment. Indeed, Professor Bainbridge has opined elsewhere that charitable contributions – which he likens to political contributions – probably do not often constitute self-dealing. See Bainbridge, *supra* note 72, at 438 (“[I]t seems doubtful that corporate philanthropy poses the sort of conflict of interest necessary to justify limiting board discretion.”).

99. Bainbridge, *supra* note 30 (emphasis added); accord Robert H. Sitkoff, *Corporate Political Speech, Political Extortion, and the Competition for Corporate Charters*, 69 U. CHI. L. REV. 1103, 1105 (2002) (“There is nothing special about the agency problem associated with managerial control over corporate political speech that distinguishes it from any other area of managerial discretion.”).

100. Stephen M. Bainbridge, *Is Starbucks [sic] Support of Marriage Equality a Breach of Fiduciary Duty to Its Shareholders?*, PROFESSORBAINBRIDGE.COM (Mar. 21, 2013), <http://www.professorbainbridge.com/professorbainbridge.com/2013/03/is-starbucks-support-of-marriage-equality-a-breach-of-fiduciary-duty-to-its-shareholders.html>.

101. A few authors have devoted paragraphs or even pages to this topic. See Sabina Bunt Thaler, *Citizens United And Forced Speech: Why Protecting The Dissenting Shareholder Necessitates Disclosure Of Corporate Political Expenditures After Citizens United v. FEC*, 17 WASH. & LEE J. CIVIL RTS. & SOC. JUST. 591, 639-40 (2011) (describing the business judgment rule and the waste standard, and promptly concluding that, “[g]iven these director-friendly standards, a claim for waste, premised on a corporation’s political spending, is . . . unlikely to succeed”); Joo, *Corporate Governance*, *supra* note 17, at 368 (explaining that a shareholder “would probably be

unable to mount a successful shareholder lawsuit challenging” a contribution to one political party or another because “[c]orporate law gives the directors’ decision . . . a presumption of propriety and a great deal of judicial deference.”); Joo, *The Modern Corporation*, *supra* note 19, at 70 (“The limited case law . . . suggests that managerial decisions regarding election-related spending fall within the business judgment rule. In other words, courts presume that election-related spending is intended in good faith to serve shareholder interests.”).

However, most scholars who have addressed the issue have done so only in passing. *See, e.g.*, Jay Kesten, *Democratizing Corporate Political Activity* 21 (FSU Coll. of Law, Law, Bus. & Econs. Paper, 2013), available at <http://ssrn.com/abstract=2242107> (noting that, if corporate political spending “were subject only to business judgment rule review, the likelihood of liability is virtually nil.”); Ciara Torres-Spelliscy, *Corporate Political Spending & Shareholders’ Rights: Why the U.S. Should Adopt the British Approach*, in RISK MANAGEMENT AND CORPORATE GOVERNANCE 392 (Abol Jalilvand & Tassos Malliaris eds., 2011) (“The idea that . . . derivative suits might be successful when so far no modern court has punished a manager for political spending, is completely divorced from reality . . . [C]ourts are very deferential to managers under the business judgment rule.”); Dibadj, *supra* note 17, at 52 (quoting Torres-Spelliscy); Ciara Torres-Spelliscy & Kathy Fogel, *Shareholder-Authorized Corporate Political Spending in the United Kingdom*, 46 U.S.F. L. REV. 525, 532-33 (2011) (“[C]ourts historically have denied relief to shareholders who have sued companies to protest corporate political spending after the fact.”); Anne Tucker, *Flawed Assumptions: A Corporate Law Analysis of Free Speech and Corporate Personhood in Citizens United*, 61 CASE W. RES. L. REV. 497, 533 (2011) (arguing that derivative suits “do not present a reasonable remedy” for dissenting shareholders who oppose corporate political expenditures due to the “high costs of such suits and their low success rate . . . , even for claims that could survive the business judgment rule and the accompanying procedural roadblocks”); Stephen A. Yoder, *Legislative Intervention In Corporate Governance Is Not A Necessary Response To Citizens United v. Federal Election Commission*, 29 J.L. & COM. 1, 20-21 (2010) (“Qualitatively, political expenditures are no different from the many other decisions that managers must make every day without direct shareholder involvement.”); Taub, *supra* note 21, at 468 (explaining that, “in most circumstances” suits against directors for breach of fiduciary duty “would be fruitless” because of the demand rule and because “directors are still shielded by the business judgment rule”); Elizabeth Pollman, *Citizens Not United: The Lack of Stockholder Voluntariness in Corporate Political Speech*, 119 YALE L.J. ONLINE 53, 56-57 (2009) (urging that derivative suits “based on corporate political spending” are “unlikely to provide relief” due to the “hurdles” like the “highly deferential business judgment rule,” which would allow directors to “rationalize their conduct of making . . . political contributions as being in the interest of the corporation”); Adam Winkler, *The Corporation In Election Law*, 32 LOY. L.A. L. REV. 1243, 1264-65 (1998) (“Due to the unbridled discretion embodied in the business judgment rule, derivative suits by dissenting shareholders . . . are destined to fail.”) (discussing *Stern v. Gen. Elec. Co.*, 924 F.2d 472 (2d Cir. 1991)); Winkler, *supra* note 17, at 206 (“[S]o long as the expenditures can reasonably be characterized as in the shareholders’ best interests, such expenditures are protected from judicial oversight by the business judgment rule.”). *Cf.* Mallory E. Mendrala, *Citizens Divided By Citizens United: How The Recent Supreme Court Decision Affects Small Business In Politics*, 7 OHIO ST. ENTREPRENEURIAL BUS. L.J. 253, 271-72 (2012) (explaining that shareholders can sue derivatively to challenge political contri-

urge that shareholders could use derivative lawsuits to challenge corporate political contributions also has admitted in passing that the business judgment rule is likely to be the downfall for most such suits.¹⁰²

C. *The Sparse Case Law on Point*

Only two cases in the past century have addressed shareholder derivative suits challenging corporate political contributions.¹⁰³ The cases, *Marsili v. Pacific Gas and Electric Co.*¹⁰⁴ and *Stern v. General Electric Co.*,¹⁰⁵ largely support Professor Bainbridge's contention that such suits are likely to fail due to the business judgment rule.

In *Marsili*, a California appellate court upheld a contribution made by an electric utility to an organization advocating the defeat of a ballot measure that would have required advance voter approval of the construction of any buildings above a certain height.¹⁰⁶ Some shareholders challenged the contribution on the ground that it served no corporate purpose.¹⁰⁷ The *Marsili* court disagreed. Invoking the business judgment rule (under California law¹⁰⁸), the court reasoned "[t]he law is clear that . . . management . . . [is] primarily responsible for judging whether a particular act or transaction is . . . expedient for the attainment of corporate purposes."¹⁰⁹ Accordingly, the court held that "[n]either the court nor . . . shareholders can substitute their

butions, but pointing out that "most courts . . . apply the business judgment rule" and that pleading would be a high hurdle – and then, not opining whether or not such suits might succeed).

102. See Romiti, *supra* note 31, at 757-58 ("Although political donations may not appear related to a corporation's day-to-day operations, the reach of the business judgment rule is extremely broad; for this reason, rebutting the rule is the most significant obstacle to a shareholder suit [I]n most cases, the business judgment rule will shield these decisions as matters of business discretion.").

103. Presumably, this dearth of caselaw is attributable at least in part to the longstanding ban on corporate contributions to candidates for federal political office. See *supra* note 3.

104. 124 Cal. Rptr. 313, 319-21 (Cal. Ct. App. 1975).

105. 924 F.2d 472, 476 (2d Cir. 1991).

106. See 124 Cal. Rptr. at 322.

107. See *id.* at 319.

108. See CAL. CORP. CODE §§ 309(a), (c) (1987) ("A director shall perform the duties of a director . . . in good faith, in a manner such director believes to be in the best interests of the corporation and its shareholders and with such care, including reasonable inquiry, as an ordinarily prudent person in a like position would use under similar circumstances A person who [satisfies this standard] shall have no liability based upon any alleged failure to discharge the person's obligations as a director.").

109. *Id.* at 319.

judgment” for the board’s judgment so long as the “board has acted in good faith and used its best business judgment.”¹¹⁰

Similarly, in *Stern*, a General Electric Company (GE) shareholder challenged GE’s contributions to its PAC on the ground that the contributions were made “to support congressional incumbents without regard to their past position on business issues.”¹¹¹ As in *Marsili*, the court in *Stern* invoked the business judgment rule (this time, under New York law).¹¹² The court described the rule as prohibiting judicial review of board decisions “only upon a showing of fraud or bad faith.”¹¹³ Finding that plaintiffs’ allegations of fraud were not stated with sufficient particularity and that no attempt was made to plead bad faith even generally, the *Stern* court upheld the trial court’s dismissal of the complaint (albeit without prejudice to amend).¹¹⁴

IV. CHALLENGING CORPORATE POLITICAL CONTRIBUTIONS AS WASTE

A. *What is Corporate Waste?*

Corporate waste is a “transfer . . . [that] amounts to a . . . waste of corporate assets.”¹¹⁵ A director’s fiduciary duties obligate her not to waste the corporation’s assets.¹¹⁶ There appear to be two ways to establish waste: a subjective method and an objective method.¹¹⁷ Either way, whether waste

110. *Id.* at 320 (quoting *Olson v. Basin Oil Co.*, 136 Cal. App.2d 543, 559-60 (1955)).

111. *Stern v. Gen. Elec. Co.*, 924 F.2d 472, 473 (2d Cir. 1991).

112. *See id.* at 476 (“[U]nder the New York business judgment rule, the actions of corporate directors are subject to judicial review only upon a showing of fraud or bad faith.”).

113. *Id.* In *Stern*, the shareholder also urged that the contributions in question resulted in “no benefit” to the corporation and, as such, amounted to corporate waste. *Id.* However, the *Stern* court did not address these allegations because under New York law, “allegations of ‘waste,’ standing alone” are not sufficient to overcome the business judgment rule. *Id.*

114. *See id.* at 477-78.

115. *Michelson v. Duncan*, 407 A.2d 211, 217 (Del. 1979).

116. *Spirit v. Bechtel*, 232 F.2d 241, 246 (2d Cir. 1956) (“As directors the defendants did owe the corporation fiduciary duties not to waste or give away its assets.”).

117. Thanks to my colleague Gary Rosin, who first described waste to me in this manner. *See also* John W. Murrey, III, *Excessive Compensation in Publicly Held Corporations: Is the Doctrine of Waste Still Applicable?*, 108 W. VA. L. REV. 433, 456-57 (2005) (urging that transfers can constitute waste even when directors made payment in good faith).

Some courts and commentators appear to disagree that there are two types of waste. To them, objective waste appears to be a way of proving bad faith. That is to say, objective waste raises a rebuttable presumption of bad faith, which then requires the court to inquire into the board’s motives. *See, e.g.*, Peter C. Kostant, *Meaningful Good Faith: Managerial Motives and the Duty to Obey the Law*, 55 N.Y.L. SCH. L.

occurred is a fact-specific question¹¹⁸ upon which the plaintiff bears the burden of proof.¹¹⁹

The remainder of this Part is divided into four sub-Parts. Sub-Part A briefly explains the doctrine of corporate waste. Sub-Part B critiques – and finds seriously lacking – William A. Nelson II’s argument that shareholders could use the corporate waste doctrine to challenge corporate political contributions. Sub-Part C attempts to rehabilitate Nelson’s proposal by focusing on a key point that he fails to develop: that corporate political contributions differ substantially from corporate donations to charity. Finally, sub-Part D briefly reviews the Delaware case law concerning the corporate waste doctrine.

1. The Objective Approach to Waste¹²⁰

When applying the objective approach to waste, a court focuses on the actual benefit to the corporation received from the transaction being chal-

REV. 421, 427 (2011) (criticizing *Sinclair Oil Corp. v. Levien*, 280 A.2d 717 (Del. 1971), and noting that under *Sinclair*, “a finding of waste is a necessary precondition for an examination of motive”); *Gagliardi v. TriFoods Int’l, Inc.*, 683 A.2d 1049, 1051-52 (Del. Ch. 1996) (describing waste as “a theoretical exception” under which “some decisions may be so ‘egregious’” as to lead to liability – but then concluding that “to allege that a corporation has suffered a loss as a result of a lawful transaction, within the corporation’s powers, authorized by a corporate fiduciary acting in a good faith pursuit of corporate purposes, does not state a claim for relief against that fiduciary no matter how foolish the investment may appear in retrospect.”) (emphasis omitted).

Ultimately, whether there are two types of waste turns on one’s understanding of the business judgment rule. Some view the business judgment rule as having no hard floor, so that good faith business judgments by the board, no matter how *substantively* egregious, are *absolutely* protected. See GEVURTZ, *supra* note 87, at 289-90; BAINBRIDGE, *supra* note 72, at 115 (“inquiry into the rationality of a decision is a proxy for an inquiry into whether the decision was tainted by self-interest”). On this view, objective waste is mere evidence of what is *actually* actionable – bad faith. Others recognize that, in rare instances, courts do review the substance of directors’ business decisions. See, e.g., David Rosenberg, *Galactic Stupidity and the Business Judgment Rule*, 32 J. CORP. L. 301, 301-02 (2007); BAINBRIDGE, *supra* note 72, at 115.

118. *Michelson*, 407 A.2d at 243-44 (quoting *Gottlieb v. McKee*, 107 A.2d 240, 243 (Del. Ch. 1954)).

119. *In re Walt Disney Co. Derivative Litig. (Disney I)*, 906 A.2d 27, 74 (Del. 2006).

120. The Delaware courts have regularly stated the standard for waste in objective terms. See *infra* Part IV.A.1. However, in other states, such as New York, courts appear to hold that waste requires a finding of fraud or bad faith. See Romiti, *supra* note 31, at 758 n.137 (citing *Stern v. Gen. Elec. Co.*, 924 F.2d 472, 476 (2d Cir. 1991)). Such jurisdictions therefore seem to adopt a subjective-only approach to waste.

lenged.¹²¹ Under this objective approach, waste occurs when “no consideration” is received for the transfer in question.¹²² Of course, if “no consideration” were the extent of the test, the legal standard for waste would be so easy to circumvent as to be useless.¹²³ Therefore, even if the corporation receives *some* infinitesimal benefit from the challenged transaction, courts nonetheless deem the deal to be waste if it was “so one sided that no business person of ordinary, sound judgment could conclude that the corporation has received adequate consideration.”¹²⁴ However, if “there is *any substantial* consideration received by the corporation,”¹²⁵ the transaction is not waste.

Under this objective approach, waste is a claim that the transaction in question essentially *destroyed* corporate resources, because no person “in his right mind” would conclude that the transaction benefitted the corporation.¹²⁶

121. See *Brehm v. Eisner*, 745 A.2d 244, 263 (Del. 2000) (quoting *Lewis v. Vogelstein*, 699 A.2d 327, 336 (Del. Ch. 1997)).

122. *Id.*

123. E.g., a gift of \$1 billion in cash in return for no tangible or intangible benefit would be rendered permissible if some nearly worthless item – say, an eraser-less nub of a sharpened-to-the-quick pencil – was exchanged for the cash. See *infra* note 129 (distinguishing the test for objective waste from the “peppercorn standard” in contract law).

124. 746 A.2d at 263 (quoting *In re Walt Disney Co. Derivative Litig.*, 731 A.2d 342, 362 (Del. Ch. 1998)). In an alternative formulation, waste occurs when assets are exchanged for “consideration so disproportionately small as to lie beyond the range at which any reasonable person might be willing to trade.” *Lewis v. Vogelstein*, 699 A.2d 327, 336 (Del. Ch. 1997). But “[i]f reasonable, informed minds might disagree” about whether the corporation received adequate consideration for the transaction, then the transaction is not waste. *Glazer v. Zapata Corp.*, 658 A.2d 176, 183 (Del. Ch. 1993).

125. *Brehm*, 746 A.2d at 263 (quoting *Lewis*, 699 A.2d at 336). The full quote from *Brehm* underscores that there are two standards for waste, one objective and one subjective: “[A] corporate waste claim must fail if there is *any substantial* consideration received by the corporation, and . . . there is a *good faith judgment* that in the circumstances the transaction is worthwhile.” *Id.* (internal quotation marks omitted). Use of the word “and” here seems to imply that *either* a lack of “any substantial consideration” *or* the board’s lack of a subjective belief that the transaction was in the best interest of the corporation would result in the transaction being deemed waste. See also *id.* at 264 (“Irrationality may be the functional equivalent of the waste test *or* it may tend to show that the decision is not made in good faith, which is a key ingredient of the business judgment rule.”) (emphasis added).

126. EDWARD BRODSKY & M. PATRICIA ADAMSKI, *LAW OF CORPORATE OFFICERS AND DIRECTORS: RIGHTS, DUTIES AND LIABILITIES* § 2:17 n.17 (2012) (“[T]he fundamental basis for a waste claim must rest on the pleading of facts that show that the economics of the transaction were so flawed that no disinterested person of right mind and ordinary business judgment could think the transaction beneficial to the corporation.”) (citing *Harbor Fin. Partners v. Huizenga*, 751 A.2d 879, 893 (Del. Ch. 1999)).

It is akin to a claim that the corporation simply burned its money.¹²⁷ Viewed this way, waste is a transaction that is irrationally one-sided.¹²⁸ For this reason, although “waste” is sometimes described as being akin to a “gift,” only a limited class of gifts meet the standard for waste: Only those gifts made for which there is no plausible reciprocal benefit to the corporation (no matter how uncertain or intangible), other than perhaps a mere token, truly constitute “waste.”¹²⁹

Of course, most business transactions involve at least some uncertainty. As a result, business decisions that appear to be net present value positive¹³⁰ when they are made can turn out to be big losers, costing the company millions but resulting in little or no income to the firm.¹³¹ Such disasters are not necessarily waste, though. When deciding whether management has committed waste, courts look to facts at the time that management decided to enter the transaction.¹³² Hence, only bets that are irrational *when made* constitute objective waste.

127. It seems safe to assume that any heat or light that the corporation gained from burning cash would not approximate the market value of that money if it were spent rather than burned.

128. See Phillip I. Blumberg, *The Corporate Entity in an Era of Multinational Corporations*, 15 DEL. J. CORP. L. 283, 319 (1990) (“Under the doctrine of waste, corporate expenditures are invalid unless supported by some rational basis for concluding that the challenged corporate expenditure will in some way benefit the corporation.”).

129. As such, waste is a more stringent standard than the contract law doctrine of consideration, which deems valid any vanishingly small consideration so long as the parties exchanged *something* of value. See *Haft v. Dart Grp. Corp.*, No. 13736, 1994 WL 643185, at *2 (Del. Ch. Nov. 14, 1994) (“The legal test of corporate waste is more demanding than a peppercorn standard; it asks whether any reasonable person could conclude, in the particular circumstances, that the exchange represented a fair exchange.”).

130. A “net present value” (NPV) analysis compares “the value of a dollar today to the value of that same dollar in the future, taking [projected] inflation and [expected] returns into account.” *Net Present Value – NPV*, INVESTOPEDIA.COM, <http://www.investopedia.com/terms/n/npv.asp> (last visited June 11, 2014). If the NPV of a potential investment is projected to be positive “it should be accepted”; if the NPV is projected to be negative, the investment “should probably be rejected.” *Id.*

131. E.g., a big-budget movie that costs \$100 million to make and brings in \$10 million at the box office.

132. See *Lewis v. Vogelstein*, 699 A.2d 327, 336 (Del. Ch. 1997) (“If . . . there is *any substantial* consideration received by the corporation . . . there should be no finding of waste, even if the fact finder would conclude *ex post* that the transaction was unreasonably risky.”); *Leung v. Schuler*, No. 17089, 2000 WL 264328, at *10 (Del. Ch. Feb. 29, 2000) (“[E]ven if the . . . facts . . . show that in hindsight the consideration was inadequate, that alone will not satisfy the waste standard.”).

Objective waste is therefore an *extremely* difficult standard for a derivative plaintiff to satisfy.¹³³ It will only be proved “in the rare, ‘unconscionable case where directors irrationally squander or give away corporate assets.’”¹³⁴ Indeed, one prominent jurist has compared the successful waste case to the oft-discussed but probably non-existent beast of Scottish legend: the Loch Ness Monster.¹³⁵

That said, the objective approach to waste provides (at least in theory¹³⁶) a lower limit to the protections of the business judgment rule.¹³⁷ In applying the rule, courts will uphold the board’s good faith business judgments only so

133. See *Kates v. Beard Research, Inc.*, No. 1480-VCP, 2010 WL 1644176, *5 (Del. Ch. 2010) (“the standard for corporate waste [is] onerous, stringent, extremely high, and very rarely satisfied”); Julian Velasco, *How Many Fiduciary Duties Are There In Corporate Law?*, 83 S. CAL. L. REV. 1231, 1235 (2010) (describing the “irrationality or waste” standard as the “most deferential standard of all” in corporate law); Hill & McDonnell, *supra* note 19, at 837 (describing the waste standard as “extremely hard for . . . plaintiffs to meet”).

134. *Disney I*, 906 A.2d 27, 74 (Del. 2006) (quoting *Brehm v. Eisner*, 746 A.2d 244, 263 (Del. 2000)).

135. *Steiner v. Meyerson*, No. 13139, 1995 WL 441999, at *5 (Del. Ch. July 19, 1995) (Allen, Chancellor) (“[T]he waste theory represents a theoretical exception . . . very rarely encountered in the world of real transactions. There surely are cases of fraud; of unfair self-dealing and, much more rarely negligence. But rarest of all – and indeed, like Nessie, possibly non-existent – would be the case of disinterested business people making non-fraudulent deals (non-negligently) that meet the legal standard of waste!”); see also Steven C. Caywood, Note, *Wasting the Corporate Waste Doctrine: How the Doctrine Can Provide a Viable Solution in Controlling Excessive Executive Compensation*, 109 MICH. L. REV. 111, 115 (2010) (describing the corporate waste standard as “impossibly high”).

136. The Delaware Supreme Court has “not foreclose[d] the possibility” that a plaintiff could successfully make out a claim for waste. *Brehm*, 746 A.2d at 263. However, the Delaware courts have rarely if ever held any directors liable for waste, absent a conflict of interest. See *Gagliardi v. TriFoods Int’l, Inc.*, 683 A.2d 1049, 1051-52 (Del. Ch. 1996) (observing that the “theoretical exception” of waste “has resulted in no awards of money judgments against corporate officers or directors” in Delaware). Many years ago, a Delaware court might reject retirement benefits for a retiring CEO as waste because such benefits constituted additional compensation for services already rendered and paid. See, e.g., *Fidanque v. Am. Maracaibo Co.*, 92 A.2d 311, 320-21 (Del. Ch. 1952) (voiding “consulting” contract with former president intended as compensation for “services previously rendered” as waste). However, such retirement packages are now upheld if not unreasonable. See *Seinfeld v. Slager*, No. 6462-VCG, 2012 WL 2501105, at *4 (Del. Ch. June 29, 2012) (citing *Fidanque*, 92 A.2d at 320-21).

137. See *Brehm*, 746 A.2d at 264 (“Irrationality is the outer limit of the business judgment rule.”); *Sample v. Morgan*, 914 A.2d 647, 669 (Del. Ch. 2007) (“[T]he doctrine of waste is a residual protection . . . that polices the outer boundaries of the broad . . . discretion afforded directors by the business judgment rule.”).

long as they are rational.¹³⁸ Utterly irrational board decisions, even if subjectively intended to benefit the corporation, are not protected by the business judgment rule.¹³⁹

2. The Subjective Approach to Waste

The subjective approach to waste focuses on the directors' motivations for engaging in the transaction in question, rather than the actual benefit received from the transaction. To use the subjective approach, a derivative plaintiff must show that the transaction "cannot be 'attributed to any rational business purpose,'"¹⁴⁰ or was "a transfer of corporate assets that serves no corporate purpose"¹⁴¹ or "the diversion of corporate assets for improper or unnecessary purposes."¹⁴² On this view, waste is a "vestige" of the traditional doctrine of *ultra vires* (i.e., "beyond the powers"), which prevents a corporation from acts that deviate from the purpose stated in its charter.¹⁴³ Like objective waste, subjective waste is nearly impossible to prove.¹⁴⁴

3. Waste is a Breach of the Duty of Loyalty

Under both the objective and subjective approaches, it seems, waste is an act of bad faith.¹⁴⁵ Subjective waste constitutes bad faith because it in-

138. See *In re Citigroup Inc. S'holder Derivative Litig.*, 964 A.2d 106, 122 (Del. 2006).

139. See BAINBRIDGE, *supra* note 72, at 115 (describing the "supposed[] . . . incredible stupidity" exception to the business judgment rule) (discussing *Litwin v. Allen*, 25 N.Y.S.2d 667, 685 (N.Y. Sup Ct. 1940)). *But see id.* (criticizing this view of *Litwin*, doubting that some decisions are "so dumb" as to not be protected by the business judgment rule). See also *Gottlieb v. Heyden Chem. Corp.*, 90 A.2d 660, 663-64 (Del. 1952) (gift of corporate assets can be challenged as waste even when directors honestly believed that gift was made in the best interests of the corporation).

140. *Disney I*, 906 A.2d at 74 ("This onerous standard for waste is a corollary of the proposition that where business judgment presumptions are applicable, the board's decision will be upheld unless it cannot be 'attributed to any rational business purpose.'") (quoting *Sinclair Oil Corp. v. Levien*, 280 A.2d 717, 720 (Del. 1971)).

141. *Lewis v. Vogelstein*, 699 A.2d 327, 336 (Del. Ch. 1997).

142. *Michelson v. Duncan*, 407 A.2d 211, 217 (Del. 1979).

143. See *Harbor Fin. Partners v. Huizenga*, 751 A.2d 879, 896 n.62 (Del. Ch. 1999).

144. See *supra* note 135.

145. See *In re Walt Disney Co. Derivative Litig. (Disney II)*, 907 A.2d 693, 749 (Del. Ch. 2005) ("The Delaware Supreme Court has implicitly held that committing waste is an act of bad faith.") (citing *White v. Panic*, 783 A.2d 543, 553-55 (Del. 2001)), *aff'd*, 906 A.2d 27 (Del. 2006). However, it has been persuasively argued that the issue of whether waste constitutes bad faith is "still not definitively settled." Jamie L. Kastler, Note, *The Problem with Waste: Delaware's Lenient Treatment of Waste Claims at the Demand Stage of Derivative Litigation*, 95 MINN. L. REV. 1899, 1913 (2011).

volves acting without regard to or contrary to the best interests of the corporation.¹⁴⁶ By contrast, objective waste raises an inference of bad faith due to the utter irrationality of the transaction at issue.¹⁴⁷ Either way, since acts in bad faith constitute a breach of the duty of loyalty,¹⁴⁸ waste apparently constitutes a breach of a director's duty of loyalty.¹⁴⁹

4. When Does a Waste Claim “Succeed”?

Waste, under the standards set forth above, seems nearly impossible to prove. But this does not mean all waste claims fail at the motion to dismiss stage. To the contrary: Even under this exacting standard, it appears that twenty-nine percent of waste claims brought in Delaware during the twentieth century survived an initial legal challenge such as a motion to dismiss.¹⁵⁰

146. See *Disney I*, 907 A.2d at 67 (explaining that bad faith exists when a “fiduciary intentionally acts *with a purpose other than* that of advancing the best interests of the corporation”) (emphasis added).

147. See *White*, 783 A.2d at 554 n.36 (“The standards for corporate waste and bad faith . . . are similar. To prevail on a waste claim or a bad faith claim, the plaintiff must overcome the general presumption of good faith by showing that the board’s decision was so . . . irrational that it could not have been based on a valid assessment of the corporation’s best interests.”). It therefore seems that the Delaware courts view waste as a proxy for bad faith. See Robert B. Thompson, *The Short, But Interesting Life of Good Faith As An Independent Liability Rule*, 55 N.Y.L. SCH. L. REV. 543, 545 (2010/11) (describing waste as an example of a “fail-safe mechanism” by which courts can intervene if a challenged substantive decision is “sufficiently beyond the pale” – allowing courts to find directors liable “where direct proof of disloyalty . . . is absent, but the substantive decision seems explainable only as a product of the directors’ failure to carry out their fiduciary responsibilities”). But see Stephen M. Bainbridge, *Does Irrationality = Bad Faith?*, PROFESSORBAINBRIDGE.COM (Apr. 27, 2009), <http://www.professorbainbridge.com/professorbainbridgecom/2009/04/does-irrationality-bad-faith.html> (urging that irrationality is a proxy for self-interest).

148. *Stone v. Ritter*, 911 A.2d 362, 369-70 (Del. 2006) (“[T]he requirement to act in good faith is a subsidiary element, i.e., a condition, of the fundamental duty of loyalty [Upon a] showing of bad faith conduct, . . . the fiduciary duty violated by that conduct is the duty of loyalty.”) (internal quotation marks omitted).

149. If objective waste constitutes bad faith, then good faith is not an entirely subjective standard, contrary to the views of an eminent Delaware jurist and his co-authors, and must have a subjective component as other scholars have contended. Compare Leo E. Strine, Jr. et al., *Loyalty’s Core Demand: The Defining Role of Good Faith in Corporation Law*, 98 GEO. L.J. 629 (2010) (arguing that good faith is purely subjective in nature), with Melvin A. Eisenberg, *The Duty of Good Faith in Corporate Law*, 31 DEL. J. CORP. L. 1 (2006) (arguing that good faith must have an objective component). The nature of good faith is beyond the scope of this Article and is addressed elsewhere. See Leahy, *supra* note 43, at ___.

150. See Nelson, *supra* note 31, at 141 (summarizing empirical study that examined Delaware shareholder derivative suits filed between 1912 and 2000, and concluded that, in twenty-nine percent of cases, the claim survived a motion to dismiss for failure to make demand or for failure to state a claim, or survived a summary

Indeed, a recent student note expresses concern that the Delaware Court of Chancery is too lenient in waste cases, allowing them to regularly survive beyond the motion to dismiss phase.¹⁵¹

But even if the Chancery Court has gone soft on waste, is surviving a motion to dismiss “victory”? Perhaps in cases where the complaint alleges massive damages, because the defendant board might settle just to avoid even the remote possibility of a large judgment. However, such settlement seems unlikely in suits challenging political contributions because of the small stakes involved. A single contribution might only cost the company tens or hundreds of thousands of dollars, or perhaps a million dollars at most. This is chump change for the directors of a public company, who are paid around \$200,000 per year for each board on which they sit.¹⁵² Even if a board were required to pay a non-indemnified million-dollar verdict, splitting it would mean that each director would probably pay less than a typical yearly country club fee. Moreover, it is essentially impossible to win a waste claim on the merits after trial.¹⁵³

Accordingly, the key question to be asked by a shareholder and her attorney in evaluating whether to challenge a corporate political contribution under the waste standard is: Can we actually *win*? In a lawsuit where the actual recovery by the corporation might be limited, surviving a motion to dismiss will be a largely symbolic victory, even if the lawsuit results in a small settlement. Plaintiffs’ lawyers are unlikely to expend substantial time and effort on a lawsuit for minimal compensation.

B. Nelson’s Arguments for Waste and a Critique Thereof

The first derivative suit advocate, William A. Nelson II, urges that “shareholders can use derivative claims of corporate waste to challenge independent political expenditures that they believe are detrimental to the corpo-

judgment motion, or prevailed at trial or on appeal) (discussing Randall S. Thomas & Kenneth J. Martin, *Litigating Challenges to Executive Pay: An Exercise in Futility*, 79 WASH. U. L. REV. 569, 608 (2001)).

151. See Kastler, *supra* note 145, at 1914.

152. See SERDAR SIKCA, FREDERIC W. COOK & Co., INC., 2012 DIRECTOR COMPENSATION REPORT: NON-EMPLOYEE DIRECTOR COMPENSATION ACROSS INDUSTRIES AND SIZE 1 (2012), available at http://www.fwcook.com/alert_letters/2012_Directors_Compensation_Report_NonEmployee_Director_Compensation_Across_Industries_and_Size.pdf (median 2012 director compensation was \$178,000 at mid-cap public companies and \$229,000 at large-cap public companies).

153. Apparently, no pure waste claim has ever resulted in a money judgment in the Delaware courts. See *Gagliardi v. TriFoods Int’l, Inc.*, 683 A.2d 1049, 1051-52 (Del. Ch. 1996) (contending that waste claims which include no serious allegation of a conflict of interest have “resulted in no awards of money judgments” and only one “dubious” order for equitable relief in Delaware). That is to say, the only successful claims of waste have been levied at conflicted directors. See, e.g., *Fidanque v. Am. Maracaibo Co.*, 92 A.2d 311, 321 (Del. Ch. 1952).

ration.”¹⁵⁴ In so doing, Nelson addresses both the subjective and objective theories of waste.¹⁵⁵ He contends that shareholders should argue that corporate political contributions constitute waste because they (1) “are in effect corporate gifts,” but “are not charitable”; (2) “damage the corporation and decrease shareholder return”; and (3) “serve no corporate purpose.”¹⁵⁶ Let us explore each argument in turn.

1. Corporate Gifts, but Not Charitable?

Certainly a political contribution is a “gift” in common parlance. After all, political contributions cannot be a specific bargained-for exchange – i.e., a quid pro quo – because that would constitute an illegal bribe.¹⁵⁷ As such, there is no “consideration,” in the contractual sense of the word,¹⁵⁸ for a political contribution. Thus, Nelson, advancing the objective theory, urges that courts might strike down corporate political contributions as “gift[s] . . . completely unsupported by consideration” – in other words, payments that are “so

154. Nelson, *supra* note 31, at 137. The second author, law student Jonathan Romiti, also briefly argues that political contributions might constitute waste, in that they are unjustified risks. *See* Romiti, *supra* note 31, at 770 (asserting that “the possibility of favorable business policies” flowing from contributions are “an illusory return” that “would almost never justify” spending corporate funds in “any other business setting”); *id.* at 771 (describing a corporate political contribution as “a lottery ticket” that “carries extremely remote chances of paying out a tangible return” and “a significant risk of inflicting damage to that company’s reputation”). Although it is certainly possible that the costs of corporate political contributions greatly outweigh the benefits, Romiti offers no empirical support for such a conclusion. More importantly, a business decision does not constitute waste simply because it fails a cost/benefit analysis. Rather, the transaction must be objectively irrational or subjectively without any corporate purpose. *See supra* Part IV.A.1 & 2 (describing objective and subjective waste standards).

155. *See* Nelson, *supra* note 31, at 155, 164.

156. *Id.* at 155.

157. *See* 18 U.S.C. § 201 (2012); *United States v. Jennings*, 160 F.3d 1006, 1013 (4th Cir. 1998) (“A bribe requires that the payment be made . . . with . . . the intent to receive a specific benefit in return for the payment. In other words, the payor of a bribe must intend to engage in some more or less specific quid pro quo with the official who receives the payment.”) (internal citations and quotation marks omitted); *see, e.g.*, Andrew Harris, *Rod Blagojevich, on Stand, Denies Charges in Chicago Trial*, BLOOMBERG (May 26, 2011, 7:22 PM), <http://www.bloomberg.com/news/2011-05-26/rod-bлагоjevich-takes-witness-stand-in-second-chicago-corruption-trial.html> (describing man who was solicited to make a \$100,000 campaign contribution to Rod Blagojevich, Governor of Illinois, in exchange for Blagojevich signing a 2008 law “to divert casino revenues to the horse racing industry”).

158. A valid contract requires consideration – that is, “a bargained-for exchange of promises or performance.” *In re Vargas Realty Enterprises, Inc.* 440 B.R. 224, 236-37 (S.D.N.Y. 2010) (quoting *Ferguson v. Lion Holdings, Inc.*, 312 F. Supp. 2d 484, 494 (S.D.N.Y. 2004)).

unreasonably disproportionate to the benefits created by the exchange that a reasonable person would think the corporation did not receive any benefit.”¹⁵⁹

But not *all* corporate “gifts” constitute waste. As Nelson recognizes, corporate donations to charity are authorized by statute in every state.¹⁶⁰ Courts typically uphold such donations if they are “within reasonable limits both as to amount and purpose”¹⁶¹ and “designed to assure a present or foreseeable future benefit to the corporation.”¹⁶² Further, as Nelson acknowledges, the expected benefit to the corporation need not be direct.¹⁶³ Moreover, while many charitable donations may result in an indirect benefit to the corporate donor, some donations do not.¹⁶⁴ Many states nonetheless permit corporations to make such donations, irrespective of any benefit to the corporation.¹⁶⁵ Thus, in many jurisdictions it is perfectly legal for a corporation to literally give away property to charity without receiving *anything* in return – a rare departure from the profit maximization norm.¹⁶⁶

Hence, Nelson’s real problem with political contributions seems not to be that they are “gifts” in common parlance, but rather that they are different from gifts *to charity*, which courts have upheld. He maintains that political contributions are not like charitable donations because they “are not made for the purpose of benefitting the community” and “do not generate good will” (as charitable donations do).¹⁶⁷ Nelson offers three basic reasons in support of these contentions.

159. Nelson, *supra* note 31, at 159 (citing *Int’l Ins. Co. v. Johns*, 874 F.2d 1447, 1461 (11th Cir. 1989)).

160. *See id.* at 141 (including, as an example, Del. Code Ann. tit. 8, § 122(9) (2010)).

161. *Id.* at 144 (quoting *Theodora Holding Corp. v. Henderson*, 257 A.2d 398, 404 (Del. Ch. 1969)); *see also infra* notes 430-435 and accompanying text (discussing Henderson).

162. Nelson, *supra* note 31, at 159 (quoting *Union Pac. R.R. Co. v. Trs., Inc.*, 329 P.2d 398, 402 (Utah 1958)).

163. *See id.* at 144 (quoting *Henderson*, 257 A.2d at 405 (reasoning that lost income due to a charitable donation was “far out-weighed by the overall benefits” of such gift, which, “by benefit[ing] those in need,” providing “justification for large private holdings, thereby benefiting plaintiff in the long run.”)).

164. *See* R. Franklin Balotti & James J. Hanks, Jr., *Giving at the Office: A Reappraisal of Charitable Contributions by Corporations*, 54 BUS. LAW. 965, 967-68 (1999) (describing three different types of charitable donations).

165. *See* Jill E. Fisch, *Teaching Corporate Governance Through Shareholder Litigation*, 34 GA. L. REV. 745, 765 (2000); Faith Stevelman Kahn, *Pandora’s Box: Managerial Discretion and the Problem of Corporate Philanthropy*, 44 UCLA L. REV. 579, 603 (1997). *But see* STEPHEN M. BAINBRIDGE, *CORPORATION LAW AND ECONOMICS* 436 (2d ed. 2002) (explaining that “the principles of [Dodge] arguably require that corporate philanthropy redound to the corporation’s benefit”).

166. *See* Kahn, *supra* note 165, at 604-05.

167. Nelson, *supra* note 31, at 160.

a. Goodwill: The Disclosure Straw Man

First, Nelson argues that corporations cannot justify corporate political contributions as generating goodwill because they often are not reported to shareholders or the public.¹⁶⁸ This argument is a “straw man,” because under the current regulatory regime corporations *could* easily disclose any or all political contributions. Better yet (from a public relations perspective), corporations could cherry pick and disclose only the contributions that seem most likely to generate goodwill among the corporation’s customers and in its community and decline to disclose contributions that would destroy (or at least fail to enhance) goodwill. In any event, this argument could soon be mooted, at least for publicly traded corporations, if the SEC promulgates regulations that require that reporting companies disclose some or all political contributions.¹⁶⁹

b. Goodwill: The Target Corporation/MN Forward Debacle

Second, Nelson posits that (assuming disclosure) charitable donations arguably generate goodwill while corporate political contributions do not.¹⁷⁰ Nelson offers no factual support for this argument. Rather, he argues that there are no cases stating that the failure of a corporation to make corporate political contributions will result in a loss of goodwill.¹⁷¹

This argument fails both as a matter of logic and as a matter of history. Logically, the absence of affirmative evidence of a fact is not conclusive evidence of the absence of the fact, unless there is good reason to believe that the

168. *Id.* at 162.

169. *See supra* notes 9-14 and accompanying text.

170. Romiti makes a similar argument. *See Romiti, supra* note 31, at 770 n.221 (arguing that “corporate political contributions are easily distinguishable from corporate donations to charity” because, if Target Corporation had contributed “to the American Red Cross rather than MN Forward, it is highly unlikely that its customers would have boycotted Target’s stores”). But Romiti’s argument compares apples and oranges: a *non-controversial* charitable organization (the Red Cross) and a *controversial* political action committee (MN Forward). Comparing apples to apples would require substituting a *controversial* non-profit organization, such the National Organization for Marriage Education Fund (NOMEF), which that opposes gay marriage, for the Red Cross. If Target Corporation contributed a huge sum to NOMEF in 2010, and the contribution was disclosed, there is little doubt that customers would have boycotted Target stores just as they did after Target contributed to MN Forward. Thus, it the Target/MN Forward debacle clearly counsels against making *any* controversial contribution, whether to a charity or to a political action committee.

171. Nelson, *supra* note 31, at 162 (arguing that one court has recognized that “a refusal to make charitable donations ‘might bring on the loss of the good will of the community . . . [if] other businesses make donations for worthy causes,’” while “no case” stating that a lack of corporate political contributions will cause a corporation to lose goodwill) (quoting *Bd. of Supervisors v. Va. Elec. & Power Co.*, 87 S.E.2d 139, 149 (Va. 1955)).

fact would necessarily have revealed itself if it existed.¹⁷² This is known as the “absence of evidence is not evidence of absence” or “argument from ignorance” logical fallacy.¹⁷³

Further, there is good reason to believe that courts simply have had no occasion to address whether corporate political contributions generate goodwill in the community. Corporations have been prohibited from making direct political contributions to candidates for over 100 years,¹⁷⁴ and for a decade before the Supreme Court decided *Citizens United* corporations were prohibited from making independent expenditures. As a result, the flood of corporate money in political campaigns to which progressives object apparently post-dates *Citizens United*.¹⁷⁵ Hence, modern courts simply have not had many opportunities to pass on the validity of corporate political contributions.

In addition, Nelson’s argument seems to be based on a worst-case scenario, where a corporation makes an absolutely dunderheaded political contribution. The key example that Nelson proffers in support of his argument that corporate political contributions do not generate goodwill – Target Corporation’s 2010 donation of \$150,000 to a Super PAC called MN Forward¹⁷⁶ – might actually be, in retrospect, the most shortsighted corporate political contribution in recent history. The Target contribution to MN Forward – which, in turn, ran TV ads in support of Republican candidate Tom Emmer, a conservative legislator running for governor of Minnesota¹⁷⁷ – generated enormous controversy among supporters of same-sex marriage due to Emmer’s staunch opposition to same-sex marriage.¹⁷⁸ (Minnesota-based Target was required to disclose the contribution under the

172. E.g., one cannot logically conclude that “none of my friends eat oatmeal for breakfast” simply based on the mere fact that none of one’s friends have said that they eat oatmeal for breakfast, unless one regularly discusses breakfast choices with one’s friends. *See also, e.g.*, J.P. MORELAND & W.L. CRAIG, PHILOSOPHICAL FOUNDATIONS FOR A CHRISTIAN WORLDVIEW 157 (2003) (explaining that “the failure to observe” an elephant nearby is a “good reason to think that there is no elephant” present, but the failure to observe a flea nearby is not good evidence that there is no flea present, because we would expect to see an elephant but not a flea).

173. *See id.* at 156-57.

174. *See supra* note 3.

175. *See* Michael Beckel & Megan R. Wilson, *BREAKING: Election 2010 Outside Political Spending Officially Eclipses Such Expenditures from 2004 Cycle*, CENTER FOR RESPONSIVE POL. (Oct. 28, 2010), <https://www.opensecrets.org/news/2010/10/breaking-outside-spending-this-seas.html>.

176. *Cf.* Romiti, *supra* note 31, at 744-45 (describing Target contribution generously as a “gamble”).

177. Nelson, *supra* note 31, at 156.

178. *See id.*; *see also* Romiti, *supra* note 31, at 742-43 (discussing the Target contribution).

state's "nation-leading" disclosure law.¹⁷⁹) The fallout from the MN Forward donation included calls for boycotts of Target stores nationwide.¹⁸⁰ The value of Target's stock also plummeted.¹⁸¹

But Nelson fails to point out that Emmer (specifically) and opposition to same-sex marriage (generally) turned out to be *particularly* bad bets for Target to make in Minnesota at that time. Although Emmer only lost the 2010 Minnesota governor's election to Democrat Mark Dayton¹⁸² by 8,700 votes,¹⁸³ each man garnered less than forty-four percent of the vote due to a third-party candidate, Tom Horner, who won nearly twelve percent of the votes that year.¹⁸⁴ Horner, a well-known former moderate Republican, was a serious candidate from the outset, with endorsements from prominent Republicans, Democrats and major newspapers.¹⁸⁵ This was largely because Emmer – a "bombastic, ultraconservative"¹⁸⁶ – was far too conservative for many Minnesota Republicans and independents, while Dayton was extremely liberal even by Minnesota's standards.¹⁸⁷ In short, Emmer was *such* a bad candi-

179. See Taren Kingser & Patrick Schmidt, *Business in the Bulls-Eye? Target Corp. and the Limits of Campaign Finance Disclosure*, 11 ELECTION L.J. 21, 24-25 (2012).

180. See *id.* at 28; Nelson, *supra* note 31, at 156; Romiti, *supra* note 31, at 742-43, n.35.

181. See Romiti, *supra* note 31, at 744 (Target lost \$1.3 billion in market capitalization shortly after the debacle).

182. Ironically, Target, originally named Dayton Dry Goods Company (and later the Dayton Hudson Corporation) was founded George Nelson Dayton, Mark Dayton's great-grandfather. The financial success of Target and its sister department store, Neiman Marcus (formerly Dayton's) is the source of Mark Dayton's own fortune.

183. Elizabeth Dunbar & Tom Scheck, *Mark Dayton Declared Winner, Finally*, MPRNEWS.COM (Dec. 8, 2010), <http://minnesota.publicradio.org/display/web/2010/12/08/emmer-recount-concession>.

184. See *Statewide Results for Governor*, MINN. SECRETARY OF ST., <http://minnesotaelectionresults.sos.state.mn.us/20101102/ElecRslts.asp?M=S&Races=0331> (last visited June 13, 2014).

185. Horner was endorsed by three of Minnesota's five living ex-governors, including two moderate Republicans; the Democratic party's U.S. Senate candidate from 2008; and several major newspapers, including the *Minneapolis Star-Tribune*, the state's most widely-subscribed (and probably its most influential) daily paper. See *Tom Horner*, WIKIPEDIA, http://en.wikipedia.org/wiki/Tom_Horner (last visited June 13, 2014) (explaining that Horner, the Independence Party candidate, was endorsed by "two former Republican Governors, Arne Carlson and Al Quie . . . DFL U.S. Senate candidate Mike Ciresi . . . , the Star Tribune, and the Duluth News Tribune.").

186. *Editorial: Tom Horner for Governor*, MINNEAPOLIS STAR TRIBUNE (Oct. 20, 2010, 2:10 PM), <http://www.startribune.com/opinion/editorials/105067929.html?refer=y>.

187. See, e.g., Bill Salisbury, *Dayton, Emmer, Horner Give Minnesota Voters 3 Distinct Choices for Governor*, ST. PAUL PIONEER PRESS (Aug. 12, 2010, 12:01 AM), http://www.twincities.com/ci_15748757.

date that thousands of Minnesotans who identified as Republican voted for a third-party candidate (which was by no means unprecedented in a Minnesota gubernatorial race¹⁸⁸), and he lost to a Democrat who might not have won state-wide office if the Republicans had offered a palatable alternative. Indeed, Emmer lost despite that 2010 was otherwise a historically *good* year for Republicans in Minnesota: the party gained control of *both* houses of the Minnesota Legislature for the first time since 1972!¹⁸⁹

Supporting Emmer was not the real problem for Target, however. Even worse was Target's apparent failure to read the prevailing winds – both in Minnesota and nationally – concerning same-sex marriage. In 2011 – just months after Target's donation to MN Forward – the Republican-led Minnesota legislature adopted a constitutional amendment that would have banned recognition of same-sex marriage in the state if subsequently approved by voters.¹⁹⁰ However, when the matter was put to a vote in November 2012, Minnesotans rejected the amendment, 52.6 percent to 47.4 percent.¹⁹¹ At the same time, Minnesota voters swept the unpopular Republican majorities out of the state legislature after just one term, giving Democrats full control of state government – both houses and the governor's office – for the first time in twenty-two years.¹⁹² Then, in May 2013, Governor Dayton signed a bill, passed by the majority-Democrat legislature, making Minnesota only the twelfth state to legalize gay marriage.¹⁹³ These changes in Minnesota were part of a wave of legislation and ballot initiatives legalizing same-sex marriage that swept across the country starting in 2009 (when Vermont became

188. Just twelve years earlier, in 1998, Jesse Ventura, a former professional wrestler, the Reform Party candidate, “narrowly and unexpectedly” defeated both the Democratic and Republican candidates for governor. See Pam Belluck, *The 1998 Elections: The States – The Maverick; A “Bad Boy” Wrestler’s Unscripted Upset*, N.Y. TIMES (Nov. 5, 1998), <http://www.nytimes.com/1998/11/05/us/the-1998-elections-the-states-the-maverick-a-bad-boy-wrestler-s-unscripted-upset.html?page-wanted=1>; see also *Election 98 Ex-Wrestler Elected Governor*, ASSOCIATED PRESS, Nov. 4, 1998, available at 1998 WLNR 2859558.

189. See Martiga Lohn, *GOP Takes Over Minn. Legislature After 38 Years*, MPRNEWS.COM (Nov. 3, 2010), <http://minnesota.publicradio.org/display/web/2010/11/03/minnesota-legislature>.

190. See Tom Scheck, *Minn. Senate OKs Same-Sex Marriage Ban Amendment*, MPRNEWS.COM (May 11, 2011), <http://minnesota.publicradio.org/display/web/2011/05/11/same-sex-marriage-senate>.

191. *2012 Minnesota Ballot Measures Results*, POLITICO, <http://www.politico.com/2012-election/results/ballot-measures/minnesota/> (last visited Mar. 15, 2014).

192. See Jennifer Brooks, *DFLers End GOP Control in Legislature After Two Years*, MINNEAPOLIS STAR TRIBUNE (Nov. 7, 2012, 3:03 PM), <http://www.startribune.com/politics/statelocal/177543791.html?refer=y>; Bill Salisbury, *Minnesota Legislature: Democrats Regain Control*, ST. PAUL PIONEER PRESS (Nov. 7, 2012, 12:01 AM), http://www.twincities.com/ci_21946122/.

193. See Baird Helgeson, *Minnesota Ushers in Gay Marriage*, MINNEAPOLIS STAR TRIBUNE (May 15, 2013, 10:01 AM), <http://www.startribune.com/politics/statelocal/207479871.html?refer=y>.

the first state to enact same-sex marriage into law without a prior judicial decision),¹⁹⁴ and accelerating in November 2012 (when three states enacted same-sex marriage into law in a single month).¹⁹⁵ Popular support for gay marriage also swelled: By May 2013, for the first time, more than half of the country supported legalization of gay marriage.¹⁹⁶ In 2013 courts became caught up in the tidal wave: In June 2013 the Supreme Court issued two “major victories” for advocates of same-sex marriage.¹⁹⁷ After (and based upon) the Supreme Court’s decision, state and federal courts began to strike down bans on same-sex marriage with increasing regularity.¹⁹⁸ As a result, alt-

194. Vermont enacted a law providing for gay marriage in 2009. See Abby Goudnough, *Gay Rights Groups Celebrate Victories in Marriage Push*, N.Y. TIMES (Apr. 7, 2009), http://www.nytimes.com/2009/04/08/us/08vermont.html?_r=0.

195. In November 2012, voters in Maine, Maryland, and Washington approved same-sex marriage via ballot initiatives. See Ashley Fetters, *Same-Sex Marriage Wins on the Ballot for the First Time in American History*, THE ATLANTIC (Nov. 7, 2012, 8:37 AM), <http://www.theatlantic.com/sexes/archive/2012/11/same-sex-marriage-wins-on-the-ballot-for-the-first-time-in-american-history/264704/>. Rhode Island and Delaware enacted laws providing for same-sex marriage in May 2013. See Doug Denison, *Delaware Becomes 11th State with Gay Marriage*, USA TODAY (May 7, 2013, 9:33 PM) <http://www.usatoday.com/story/news/nation/2013/05/07/delaware-gay-marriage/2142703/>. The New Jersey legislature also passed a bill to legalize gay marriage in 2012, but Governor Chris Christie vetoed that bill. See Kate Zernike, *Christie Keeps His Promise to Veto Gay Marriage Bill*, N.Y. TIMES (Feb. 17, 2012), http://www.nytimes.com/2012/02/18/nyregion/christie-vetoes-gay-marriage-bill.html?_r=0.

196. See Drew DeSilver, *Supreme Court’s DOMA Ruling Comes as Majority Now Supports Same-Sex Marriage*, PEW RES. CTR. (June 26, 2013), <http://www.pewresearch.org/fact-tank/2013/06/26/supreme-courts-doma-ruling-comes-as-majority-now-supports-same-sex-marriage/> (“A Pew Research Center survey in May found that for the first time, more than half (51%) of Americans favored allowing gay men and lesbians to marry.”). This sort of wide-spread political support for gay marriage seemed unthinkable just five years earlier when the case against the California ban was filed. At that time, only three states had legalized same-sex marriage and “public support of marriage equality was in the high 30s or low 40s.” Adam Nagourney, *Court Follows Nation’s Lead*, N.Y. TIMES (June 26, 2013), <http://www.nytimes.com/2013/06/27/us/politics/with-gay-marriage-a-tide-of-public-opinion-that-swept-past-the-court.html?pagewanted=all> (quoting Chad H. Griffin).

197. First, the Court struck down as unconstitutional the parts of the Defense of Marriage Act of 1996 that prohibited married same-sex couples from receiving the same benefits as married opposite-sex couples. See Adam Liptak, *Supreme Court Bolsters Gay Marriage with Two Major Rulings*, N.Y. TIMES (June 26, 2013), <http://www.nytimes.com/2013/06/27/us/politics/supreme-court-gay-marriage.html?ref=politics>. Second, the Court declined to decide an appeal from a lower court decision that struck down California’s ban on same-sex marriage, thereby effectively allowing same-sex marriages in California. See *id.*

198. Prior to 2013, courts in four states – Massachusetts, California, Iowa and Connecticut – had held that prohibiting gay marriage was unconstitutional. See *States that Allow Same-Sex Marriage*, NAT’L CONF. OF ST. LEGISLATURES (Mar. 6, 2014), <http://www.ncsl.org/research/human-services/same-sex-marriage-laws.aspx>. Califor-

though opposition to gay marriage remains high among social conservatives – and (as of this writing) it is still outlawed in thirty-one states¹⁹⁹ – if the aforementioned bans are all upheld, more than half of the nation’s population will live in states where gay marriage is legal.²⁰⁰

Hence, Nelson’s use of the Target example, while a good cautionary tale for boards of directors, probably says little about whether political contributions are *inherently* unable to generate goodwill, for several reasons. First, since the backlash against Target occurred because the company made the *wrong* donation at the wrong time in Minnesota politics, there is no reason to believe that a well-considered donation would result in the same negative publicity. For example, if Target were headquartered in Utah and made a donation to Republican Mitt Romney, a Mormon, in the 2012 presidential election, Target presumably would have suffered little or no bad publicity in Utah – despite that Romney lost the election – because Romney won Utah by a wide margin and Utah is approximately sixty-percent Mormon.²⁰¹ What’s more, if a hypothetical Utah-based Target had donated to the 2012 campaign for incumbent Republican governor Gary Herbert – who crushed his Demo-

nia’s decision was overturned by a constitutional amendment that was struck down by the U.S. Supreme Court in 2013. See Liptak, *supra* note 197. Then, in September 2013, a New Jersey state court struck down that state’s ban on gay marriage. See Kate Zernike & Marc Santora, *Judge Orders New Jersey to Allow Gay Marriage*, N.Y. TIMES (Sept. 27, 2013), <http://www.nytimes.com/2013/09/28/nyregion/new-jersey-judge-rules-state-must-allow-gay-marriage.html>. Since that time, judges in eight other states – New Mexico, Utah, Oklahoma, Idaho, Virginia, Texas, Pennsylvania and Oregon – have struck down state prohibitions on gay marriage as unconstitutional. See Manny Fernandez, *U.S. Judge Strikes Down Texas Ban on Same-Sex Marriage*, N.Y. TIMES (Feb. 26, 2014), <http://www.nytimes.com/2014/02/27/us/texas-judge-strikes-down-state-ban-on-same-sex-marriage.html?hpw&rref=us>; Kirk Johnson, *Federal Judge Strikes Down Oregon’s Ban on Same-Sex Marriage*, N.Y. TIMES (May 19, 2014), <http://www.nytimes.com/2014/05/20/us/federal-judge-strikes-down-oregons-ban-on-same-sex-marriage.html>. The rulings in several states were stayed pending appeal. The attorney generals of some states, including Pennsylvania and Oregon, did not appeal, allowing the rulings to take immediate effect. See Trip Gabriel, *Pennsylvania Governor Won’t Fight Ruling That Allows Gay Marriage*, N.Y. TIMES (May 21, 2014), http://www.nytimes.com/2014/05/22/us/pennsylvania-governor-will-not-appeal-same-sex-marriage-ruling.html?hpw&rref=us&_r=0.

199. See Gabriel, *supra* note 198; Sophia Pearson & Erik Larson, *Pennsylvania Gay Marriage Ban Thrown Out as Divide Evens*, BLOOMBERG (May 20, 2014, 11:01 PM), <http://www.bloomberg.com/news/2014-05-20/pennsylvania-gay-marriage-ban-tossed-as-states-now-evenly-split.html>.

200. Phillip Bump, *If Texas’s Ban Falls, Over 49 Percent of Gay Americans Will Be Able to Legally Marry*, WIRE.COM (Feb. 26, 2014, 5:04 PM), <http://www.thewire.com/politics/2014/02/if-texas-ban-falls-over-49-percent-gay-americans-will-be-able-legally-marry/358572/>.

201. See Matt Canham, *Census: Share of Utah’s Mormon residents holds steady*, SALT LAKE TRIBUNE (Apr. 17, 2012, 2:25 PM), <http://www.sltrib.com/sltrib/home3/53909710-200/population-lds-county-utah.html.csp>.

cratic Party opponent Peter Cooke 68% to 28% in the 2012 election²⁰² – then it seems plausible that the company might have even gained some goodwill. In short, Target’s donation in support of a controversial loser (Emmer) teaches little about the wisdom of contributing to an uncontroversial loser (Romney) or a big winner (Herbert). In both of the latter situations, a gain in goodwill is plausible.

Second, because the fallout of Target’s decision to support MN Forward was national in scope, the situation might have turned out differently – and less negatively for Target – if the company ran a different type of store, catering to a different type of clientele. As the nation’s second-largest general merchandise retailer or discount retailer (after Wal-Mart)²⁰³ with a large media presence, Target presumably appeals to customers from all walks of life. People who shop at Target presumably vote for both major parties, Republican and Democrat, and hold a wide range of political views. As a retailer catering to a diverse group of people, Target would be wise not to take public positions that would offend perhaps half of its customers.²⁰⁴ However, if Target were instead a different type of corporation that catered to a narrower band of people – most or all of whom tended to be conservative or at least vote Republican – then there is no reason to believe that donating to Emmer would have caused Target to lose any goodwill among the people who matter most: its customers.²⁰⁵ What’s more, even among retailers, Target was particularly vulnerable to boycotts due to Minnesota’s “civically engaged public”; the fact that “Target had positioned itself as a progressive company” in the past and because “[c]ompared to its more down-market competitor, Wal-

202. See *Utah Election Results: Governor*, UTAH.GOV, <http://www.electionresults.utah.gov/xmlData/300300.html> (last visited June 14, 2014).

203. Abram Brown, *Wal-Mart: A Business Slump at the World’s Largest Retailer*, FORBES (May 16, 2013, 8:39 AM), <http://www.forbes.com/sites/abrambrown/2013/05/16/wal-mart-a-business-slump-at-the-worlds-largest-retailer/>.

204. See Edward Lotterman, *Target’s Politics May Sink to the Bottom Line*, ST. PAUL PIONEER PRESS (Aug. 8, 2010), http://www.twincities.com/business/ci_15642678 (Economist Lotterman notes “[n]ot offending the public is more critical for retailers than for any other business If [customers’] first reaction to the word ‘Target’ is ‘anti-gay’ . . . it is easy to buy one’s toilet paper somewhere else. Avoiding unnecessary public controversy and not taking actions that might compromise one’s brand identity are basic principles in marketing. Public relations experts know and teach that consumer reactions to political stances are asymmetric. They tend to repel those who disagree with the stance much more than they attract those who agree.”).

205. See Tom Hamburger & Jennifer Martinez, *Target Feels Backlash from Shareholders*, L.A. TIMES (Aug. 19, 2010), <http://articles.latimes.com/2010/aug/19/nation/la-na-target-share-holders-20100820> (summarizing opinion of Tara Malloy of the Campaign Legal Center that the Target debacle will not necessarily reduce corporate campaign contributions by “[e]nergy companies and defense contractors” who “have less interaction with the public [and] won’t be subject to the same kind of pressure as retailers”).

Mart, Target's market segment has long been higher income customers who tend to be more socially aware in their shopping decisions.²⁰⁶

Third, the negative publicity and boycotts that Target faced may simply have been a matter of bad timing, as Target was the first major Minnesota company to disclose its contributions after the state's new disclosure law went into effect in 2010. In fact, several other prominent Minnesota corporations – including well-known consumer products companies like 3M and Best Buy – gave large sums to MN Forward in 2010, but did not face any of the same backlash that Target faced.²⁰⁷

Ironically, Target's conduct since 2010 shows precisely why Nelson is wrong to argue that corporate political contributions are *inherently* bad for corporations. Nelson's argument that political contributions are inherently bad for corporations is, at bottom, an argument that corporations should never take public stances on political issues. Yet, since 2010, Target has publicly *promoted* same-sex marriage. In 2012 alone, the company created a media stir by running an ad for its online marriage registry featuring a same-sex couple, sold t-shirts on its website to benefit an organization that publicly opposed the constitutional amendment that would have banned gay marriage in Minnesota, and sold same-sex marriage themed greeting cards in its stores.²⁰⁸ While these activities were not corporate political contributions, they were clearly intended to show that "Target is not anti-gay"²⁰⁹ and overcome the negative publicity generated by the 2010 MN Forward debacle – despite raising the ire of organizations that oppose same-sex marriage. Further, Target refused to stop making political contributions after the MN Forward debacle.²¹⁰

Thus, the clear lesson that Target itself took from its 2010 MN Forward debacle is *not* to avoid supporting *any* overtly political causes, but rather, to support the "right" causes in the right ways (i.e., with glossy ads rather than political donations). As a result, although Target was criticized for not going far enough to support gay marriage in 2012,²¹¹ the company's public image

206. Kingser & Schmidt, *supra* note 179, at 33.

207. *See id.* at 31.

208. *See* Curtis M. Wong, *Target Selling Gay Marriage Greeting Cards for Couples*, HUFFINGTON POST (July 16, 2012, 11:23 AM), http://www.huffingtonpost.com/2012/07/16/target-gay-marriage-greeting-cards-sale_n_1676356.html.

209. *Id.*

210. Kingser & Schmidt, *supra* note 179, at 31. Instead, Target convened a panel of executives to screen contributions for concerns that may be "important" to employees, customers and other stakeholders. *Id.*

211. Proponents of gay marriage criticized Target for failing to officially oppose Minnesota's failed constitutional amendment banning same-sex marriage and for failing to officially support the state's subsequent legislation legalizing same-sex marriage. *See, e.g.,* Abe Sauer, *Target's Stance on Gay Rights Takes Ironic Turn as Home State Passes Equality Bill*, BRAND CHANNEL (May 15, 2013, 10:54 AM), <http://www.brandchannel.com/home/post/2013/05/15/Target-Gay-Rights-051513.aspx>.

has gone from anti-gay to gay-friendly in less than three years due to its gay-friendly advertising. Moreover, other prominent Minnesota-based corporations have taken the next step that Target has not and continued to advocate on the subject of marriage equality.²¹² Apparently believing that they are now on the *correct* side of history (or, more cynically, their customers), Minnesota-based companies such as General Mills actively opposed the failed 2012 same-sex marriage constitutional amendment and supported the successful 2013 legislation.²¹³

In sum, one lesson from the Target/MN Forward fiasco could be that companies should avoid politics altogether. But another, just-as-plausible lesson is that, if a company involves itself in politics, it better not “get it wrong” by making controversial or unpopular political contributions.²¹⁴

c. Tax Deductibility

Nelson’s third argument about why corporate political contributions differ from corporate charitable donations concerns tax deductibility. As he correctly explains, political expenditures differ from charitable gifts because the latter are tax-deductible under the Internal Revenue Code while the former are not.²¹⁵ Further, as Nelson correctly urges, courts that have upheld corporate charitable donations have often done so in part due to the tax deduction generated by such gifts.²¹⁶ Nelson therefore argues that, absent the tax deduction, corporate political contributions are on far weaker ground than charitable donations.²¹⁷

This argument fails in part because it is overbroad. The argument would encompass *all* non-tax-deductible corporate political spending – not just corporate political contributions, but any lobbying as well. Yet, it would be laughable to suggest that lobbying never benefits corporations. There must

212. See, e.g., Mike Hughlett & Baird Helgeson, *General Mills against Gay Marriage Ban*, MINNEAPOLIS STAR TRIBUNE (June 14, 2012), <http://www.startribune.com/business/159143335.html?refer=y>.

213. See *id.*; Mike Hughlett, *General Mills Defends Gay Marriage Stance*, MINNEAPOLIS STAR TRIBUNE (Sept. 24, 2012), <http://www.startribune.com/business/171022151.html?refer=y>.

214. Hamburger & Martinez, *supra* note 205 (quoting Tara Malloy of the Campaign Legal Center) (“The Target case may just be an example of a corporation doing it wrong.”); see also Samuel Issacharoff, *On Political Corruption*, 124 HARV. L. REV. 118, 131 (2010) (referencing the Target example and noting “[m]ost publicly traded corporations do not want to be associated with controversial positions on hot-button social issues that dominate elections.”).

215. Nelson, *supra* note 31, at 161 (citing I.R.C. § 162 (2006) and IRS, DEP’T OF THE TREASURY, MISCELLANEOUS DEDUCTIONS 16 (2011), available at <http://www.irs.gov/pub/irs-pdf/p529.pdf> (Corporations cannot “deduct contributions made to a political candidate [or] campaign committee.”)).

216. *Id.* at 161-62; see *infra* Part V.E.

217. Nelson, *supra* note 31, at 161-62.

be hundreds of instances where lobbying legislators or regulators have improved a corporation's bottom line. For example, large global banks have engaged in a massive lobbying effort to water down protections for consumers in the Dodd-Frank Act of 2010 (Dodd-Frank).²¹⁸ Presumably, the millions of dollars banks spent lobbying and the resulting changes in the implementation of Dodd-Frank were well worth the banks' investments.

What's more, Nelson's argument about tax deductibility fails to grasp how tax deductions work. A tax deduction effectively reduces the *amount* of the gift from the corporation because the government subsidizes part of the donation.²¹⁹ For example, if a corporation donates \$1000 to charity and the corporation's marginal tax rate is thirty-five percent, deducting that \$1000 from the corporation's net income will reduce the corporation's overall tax burden by \$350.²²⁰ Thus, the effect of tax deductibility is that a gift of \$1000 from a corporation to a charity only "costs" the corporation \$650, because of the offsetting \$350 reduction in the corporation's tax liability due to that donation. As a result, the tax deduction that the corporation receives in return for a charitable gift is not properly viewed as a "benefit" to the corporation, but rather as a reduction in the amount of the gift.

Hence, while Nelson describes the "non-tax deductible status of political expenditures" as "a critical" difference between charitable gifts and political expenditures,²²¹ this is simply not true. Tax deductibility simply means that a \$1000 donation to charity (again assuming a thirty-five percent tax rate) costs the corporation the same amount as a \$650 corporate political contribution. When comparing the two gifts, there must nonetheless be some *plausible* benefit to the corporation or else each donation would be waste (assuming that charitable contributions require a corporate purpose).²²²

For this reason, although Nelson is correct to note that two important charitable donation cases, *Kahn v. Sullivan*²²³ and *Theodora Holding Corp. v. Henderson*,²²⁴ turned in part on the tax benefits to the corporation resulting from the gift, Nelson misunderstands *why* tax benefits were important to ren-

218. See Gary Rivlin, *How Wall Street Defanged Dodd-Frank*, THE NATION (Apr. 30, 2013), <http://www.thenation.com/article/174113/how-wall-street-defanged-dodd-frank>.

219. See Brian D. Galle, *Charities in Politics: A Reappraisal*, 54 WM. & MARY L. REV. 1561, 1568 (2013) ("In effect, [a tax] deduction is a matching grant from the government to the charity: for every dollar the donor contributes, the government gives back, say . . . 35 cents, which the donor can then also contribute.").

220. See Brian D. Galle, *The Role of Charity in a Federal System*, 53 WM. & MARY L. REV. 777, 786 n.27 (2012) ("[I]f [my marginal tax rate is] \$0.35[,] . . . a \$1,000 donation . . . [to charity] reduces the amount of tax I pay by \$350.").

221. Nelson, *supra* note 31, at 161-62.

222. *But see infra* Part IV.C.1.g (explaining that charitable contributions may require no business purpose).

223. See *Kahn v. Sullivan (Hammer II)*, 594 A.2d 48 (Del. 1991); *Sullivan v. Hammer (Hammer I)*, No. 10823, 1990 WL 114223 (Del. Ch. Aug. 7, 1990).

224. 257 A.2d 398 (Del. Ch. 1969).

der the donations reasonable in those two cases. In each case, the deduction simply went to the reasonableness of the amount of the donation; it did not create a separate benefit.²²⁵ Although this same standard is not available to measure the reasonableness of the amount of political contributions (as they are not tax deductible), the approach could be applied by analogy.²²⁶

2. Damage to Corporation and Reduced Shareholder Value

Nelson's second argument also pertains to the objective theory of corporate waste. He argues that "[i]ndependent political expenditures may damage corporations, both socially and economically" because "[t]aking controversial and highly visible political stands *can potentially cost clients* and therefore lead to financial costs."²²⁷ Moreover, "overt, direct political action by most corporations carries with it risks far exceeding the political gains" and the corporation's "image could be tarnished if these contributions or political activities go awry."²²⁸

In addition to offering the possible worst-case scenario example, Target's donation to MN Forward (discussed above), Nelson cites other companies that engaged in political spending that led to shareholder proposals targeting such spending. Tesoro Corporation, for example, spent money to support Proposition 23, a "ballot initiative to suspend California's global warming law" that ultimately failed.²²⁹ Nelson hypothesizes that a shareholder might successfully argue that Tesoro's political expenditures were waste because the company "derived no net benefit from" the spending, since the proposition failed to pass.²³⁰ However, money spent in support of a losing political cause is not necessarily waste simply because the cause failed, so long as the decision to engage in the cause was not irrational at the time it was made.²³¹

Nelson argues further that "empirical studies have shown that corporate independent political expenditures correlate with lower shareholder re-

225. *See id.* at 405 (concluding that "[t]he contribution . . . can be said to have 'cost' . . . some fifteen cents per dollar of contribution, taking into consideration" the federal tax deductions, and concluding that this "relatively small loss of immediate income" was "far out-weighted by the overall benefits" of the contribution); *Hammer I*, 1990 WL 114223, at *1 (considering the "after-tax cost of" the gift to the corporation). *Cf. Cox Enters. v. News-Journal Corp.*, 469 F. Supp. 2d 1094, 1098, 1111 (M.D. Fla. 2006) (holding that shareholder had probable cause to conclude that newspaper committed waste, in part because its charitable spending "exceed[ed] the maximum allowed for charitable deductions."), *aff'd* 510 F.3d 1350 (11th Cir. 2007).

226. *See Nelson, supra* note 31, at 165.

227. *Id.* at 155 (emphasis added).

228. *Id.*

229. *Id.* at 156-57.

230. *Id.* at 157.

231. *See supra* notes 131-132 and accompanying text.

turns.”²³² Perhaps if the scholarly consensus in support of this proposition were as well accepted as the scholarly consensus that Tesoro Corporation apparently opposed (i.e., that the Earth is warming and mankind is the likely cause²³³), then this argument of Nelson’s would be a winner. However, other scholarly studies *not* cited by Nelson reach the *opposite* conclusion – that corporate political spending in fact *increases* shareholder returns.²³⁴ Absent overwhelming evidence that the studies reaching one conclusion were written by crackpot theorists using universally-debunked methodologies, it would be imprudent for a layperson to argue that *no reasonable person* could conclude that corporate political contributions could increase shareholder returns *under any* circumstances. It is *by definition* reasonable for a layperson to come down on either side of a question upon which experts are truly divided.

3. No Corporate Purpose

Finally, Nelson raises the subjective theory of waste by arguing that “independent political expenditures have no corporate purpose” and are “examples of corporate . . . directors using corporate treasury funds to further their own personal political goals.”²³⁵ Nelson himself offers no factual basis whatsoever for this assertion, other than the unsupported assertions of others.²³⁶ However, other authors have argued persuasively in support of his point. Indeed, one of the strongest objections to corporate political contributions in the scholarly literature, at least to those advancing a shareholder perspective, is an “agency cost”²³⁷ problem: Corporate political contributions

232. Nelson, *supra* note 31, at 158 (citing finance research); *see also* Romiti, *supra* note 31, at 764-65 n.179.

Nelson argues further, without citation, that independent expenditures “are generally made without any due diligence” about potential effect on the corporation. Nelson, *supra* note 31, at 158-59. In the unlikely event that this unsupported assertion is true, it certainly could lead management to lose the protection of the business judgment rule.

233. *See Is There A Scientific Consensus on Global Warming?*, SKEPTICAL SCI., <http://www.skepticalscience.com/global-warming-scientific-consensus-basic.htm> (last visited Mar. 19, 2014) (“97% of climate experts agree humans are causing global warming.”).

234. *See, e.g.*, Michael J. Cooper et al, *Corporate Political Contributions and Stock Returns*, 65 J. FIN. 687 (2010); ROBERT J. SHAPIRO & DOUGLAS DOWSON, CORPORATE POLITICAL SPENDING: WHY THE NEW CRITICS ARE WRONG (2012), *available at* http://www.manhattan-institute.org/pdf/lpr_15.pdf. However, these authors’ conclusions are “hotly debated.” Bebchuk & Jackson, *supra* note 7, at 958.

235. Nelson, *supra* note 31, at 162.

236. *Id.* at 155 (“Managers may have personal preferences over candidates and parties they wish to support that are simply unrelated to the firm’s activities.”) (quoting Aggarwal et al., *supra* note 12).

237. The agency problem is that corporate managers, who control the corporation’s purse strings, can use corporate funds to further their personal goals rather than the best interest of the corporation (i.e., profit maximization). *See* ADOLF A.

could constitute a misuse of corporate funds – that is, executives essentially misappropriating the corporation’s funds to serve *their own* political agendas.²³⁸ In fact, surveys indicate that shareholders widely suspect this is management’s true motivation.²³⁹

The problem with this agency cost-based argument is that, under the subjective standard, waste must have *no* corporate purpose. As such, it is not sufficient to show that corporate executives make corporate political contributions to serve their own political objectives, if the contributions *also* serve corporate purposes. A political contribution that the board believes will serve its own political agenda and also advance the corporation’s interest does not constitute waste.

Unfortunately, Nelson’s own example – Target’s donation to MN Forward – reveals the flaws in any argument that corporate political contributions have *no* corporate purpose. In describing MN Forward and Target’s donation thereto, Nelson leaves out some critical facts. First, MN Forward is not on its face an anti-same sex marriage organization. Rather the organization describes itself as a “pro-business” organization and “an effort by Minnesota job providers to elect a governor and state legislators who understand the importance of creating private-sector jobs and economic opportunity in our state.”²⁴⁰ The organization’s three main platforms, according to its website are: “tax reform,” “spending reform,” and “education reform.”²⁴¹ Searches of the website indicate that it says *nothing whatsoever* about gay marriage.

In fact, according to MN Forward’s Executive Director Brian McClung, the group supported Emmer for governor “because of his position on job growth and the state’s economy.”²⁴² Although this statement obviously could

BERLE, JR. & GARDINER C. MEANS, *THE MODERN CORPORATION & PRIVATE PROPERTY* 68 (1932).

238. See Winkler, *supra* note 3, at 873 (explaining that corporate political corruption was historically viewed “as a problem of agency costs”); see also Bebchuk & Jackson, *supra* note 7, at 941-42 (urging that the political interests of directors and shareholders “often diverge” because directors may be influenced by factors that are exogenous to the firm’s performance and because “shareholders do not sort themselves [based on their] . . . political preferences.”).

239. See Romiti, *supra* note 31, at 766 (discussing CTR. FOR POLITICAL ACCOUNTABILITY, *CORPORATE POLITICAL SPENDING: A SURVEY OF AMERICAN SHAREHOLDERS* 19 (2006), available at <http://www.politicalaccountability.net/index.php?ht=a/GetDocumentAction/i/918>).

240. See *Who We Are*, MN FORWARD, <http://www.mnforward.com/who-we-are/> (last visited Mar. 19, 2014).

241. See *Issues*, MN FORWARD, <http://www.mnforward.com/issues/> (last visited Mar. 19, 2014). The website does not appear to have been updated since the 2012 election.

242. Emily Friedman, *Target, Best Buy Angers Gay Customers by Making Contribution to GOP Candidate*, ABCNEWS (July 28, 2010), <http://abcnews.go.com/Business/target-best-buy-fire-campaign-contributions-minnesota-candidate/story?id=11270194>.

have been a self-serving attempt to protect its donors from political harm, this is not necessarily or even likely so. Some anti-gay rights organizations have no qualms about publicly stating their goals and beliefs.²⁴³

Further, there is some objective reason to believe McClung's statement. Although MN Forward spent most of its money supporting Emmer for governor, not all of the candidates that it supported in 2010 were Republicans – or even opposed to gay marriage. For example, Jim Metzen, a long-time incumbent Democratic-Farmer-Labor senator, is listed among the pro-jobs candidates supported by MN Forward in 2010.²⁴⁴ Metzen was among the minority of senators who voted *against* Minnesota's constitutional ban on gay marriage in 2011²⁴⁵ and among the majority who voted *for* the legislation legalizing gay marriage in May 2013.²⁴⁶ Clearly MN Forward did not make anti-gay marriage a litmus test for its support in 2010.

More importantly, Target never suggested that its support for MN Forward, which in turn supported Emmer, had anything to do with opposition to rights of gay individuals. To the contrary, when the controversy first started, Target CEO Greg Steinhafel explained in a letter to the company's employees:

Target has a history of supporting organizations and candidates, on both sides of the aisle, who seek to advance policies aligned with our business objectives, such as job creation and economic growth. It is also important to note that we rarely endorse all advocated positions of organizations or candidates we support, and we do not have a political or social agenda.

Let me be very clear, Target's support for the GLBT community is unwavering, and inclusiveness remains a core value of our company.²⁴⁷

Further, even when Steinhafel subsequently apologized to the company's employees after the bad publicity and boycotts began in earnest, he nonetheless steadfastly explained that the contribution was about economics, not social issues:

243. *E.g.*, the Westboro Baptist Church.

244. *See Candidates*, MN FORWARD, <http://www.mnforward.com/candidates/> (last visited Mar. 19, 2014).

245. *See* Danielle Cabot, *Mendota Heights-Area Legislators Oppose Gay Marriage Ban Amendment*, MENDOTA HEIGHTS PATCH (May 23, 2011, 5:11 PM), <http://mendotaheights.patch.com/articles/mendota-heights-area-legislators-oppose-gay-marriage-ban-amendment>.

246. *See* Micheal Foley, *Sen. Metzen Votes 'Yes' on Same-Sex Marriage Bill*, MENDOTA HEIGHTS PATCH (May 22, 2013, 10:02 AM), <http://mendotaheights.patch.com/articles/sen-metzen-votes-yes-on-same-sex-marriage-bill>.

247. Friedman, *supra* note 242.

The intent of our political contribution to MN Forward was to support economic growth and job creation. . . . While I firmly believe that a business climate conducive to growth is critical to our future, I realize our decision affected many of you in a way I did not anticipate, and for that I am genuinely sorry.²⁴⁸

Obviously, Steinhafel had good reason to lie about why Target's board (or its executive officers) decided to contribute to MN Forward. Perhaps opposition to gay marriage was, in fact, the board's primary reason for supporting MN Forward and Emmer. Yet, the board's *primary* motivation is not particularly relevant to the subjective waste inquiry – even assuming that opposition to rights for gay individuals, including same-sex marriage, serves no corporate purpose whatsoever.²⁴⁹ Rather, since the relevant legal question is whether the donation served “no corporate purpose,” it simply does not matter whether the board had the purpose of opposing gay marriage in mind when making the donation. The proper question is whether the board also supported MN Forward for the purpose of promoting “economic growth and job creation” – and whether promoting “economic growth and job creation” serves *any possible* corporate purpose.

It surely does. If the post-2008 recession teaches anything, it is that retail chains depend on customers. In a down economy – where potential customers are out of work, and have less disposable income – the retail chain will sell fewer products, probably at lower prices.²⁵⁰ Customers who have less pocket money will buy fewer luxuries – and perhaps even fewer “necessities.” And government intervention in the way of unemployment insurance only partly covers workers' lost salaries, and only lasts for so long. Therefore, while a depressed economy that creates few jobs may benefit a corporation in some ways (by lowering labor costs, for example), it certainly is reasonable to argue that an economy that creates jobs helps retail chains overall.

248. Tom Scheck, *Target CEO Apologizes for Donation to MN Forward*, MPRNEWS.COM (Aug. 5, 2010, 12:58 PM), http://minnesota.publicradio.org/collections/special/columns/polinaut/archive/2010/08/target_ceo_apol.shtml; see also Romiti, *supra* note 31, at 742 n.31.

249. This author cannot fathom any reasonable argument that opposition to gay rights served any corporate purpose for Target Corporation, and subsequent events seem to show it was not.

250. See *Retail Sales Decline in July as Jobless Claims Edge Higher*, WASH. TIMES (Aug. 14, 2009), <http://www.washingtontimes.com/news/2009/aug/14/retail-sales-decline-in-july-as-jobless-claims-edg/>; see also Andria Cheng, *Another Downturn Seen at the Mall for the Holidays: Determined and Cautious Shoppers are Expected to Reduce Window Shopping*, MARKETWATCH (Oct. 20, 2009, 8:00 AM), <http://www.marketwatch.com/story/holiday-shopping-faces-another-drop-off-2009-10-20>.

4. Cost-Benefit Analysis and Other Arguments

Perhaps realizing that he has failed to show that corporate political contributions have no corporate purpose, Nelson ultimately drops this argument. Instead, he suggests that courts could “apply a cost-benefit analysis” to evaluate corporate independent expenditures.²⁵¹ Alternatively, he asserts that courts could use “a net loss test” to assess “damage to the corporation” from such contributions.²⁵²

The problem with these arguments is that they return to the objective standard of waste – but cannot meet that difficult threshold. Engaging in a cost-benefit analysis or a net loss test is precisely the sort of close judicial analysis of business decisions that the business judgment rule prohibits. The objective waste standard only allows courts to analyze transactions where there is no plausible argument that the corporation received adequate consideration. The objective waste standard is not a vehicle for judicial consideration of whether, on balance, a corporation received enough benefit to justify an expenditure.

Ultimately, Nelson essentially admits this. In concluding, he states that his goal is not to show that corporate political contributions necessarily *are* waste, but rather to simply suggest arguments that will give shareholder plaintiffs a “much greater chance of success.”²⁵³ Unfortunately, few of his arguments offer shareholders much promise of success in bringing a waste claim.

* * * * *

In sum, Nelson’s objective waste argument is simply an argument that *some* corporate political contributions *can* be bad for *some* corporations (especially when the board makes a bad bet, like Target’s board did) – *not* an argument that *all* (or even most) corporate political contributions are *inherently* bad for *all* corporations.²⁵⁴ Further, Nelson’s subjective waste argument is simply that *some* directors *may* make corporate political contributions to further their own political goals *some* of the time – not that *all* directors necessarily do this *all* of the time. Shareholder derivative plaintiffs need better arguments than this in order to survive a motion to dismiss.

251. Nelson, *supra* note 31, at 165.

252. *Id.*

253. *Id.* at 172-73.

254. Nelson admits this: He states that he has provided “ample evidence that even though corporations have the ability to make independent political expenditures, it is *not always in their best interest* to do so.” *Id.* at 172 (emphasis added). But the waste standard does not permit courts to second-guess management in this way. *See supra* Part IV.A.1-2 (describing objective and subjective waste standards).

C. A Better Argument for Waste?

1. How Charitable Donations Differ from Political Contributions

Nelson's only promising argument seems to be that corporate political contributions constitute waste because they differ from charitable contributions (which are upheld if reasonable). Yet, he offers no compelling basis for concluding that political contributions in fact differ from charitable contributions. He fails to articulate any material or inherent differences between the two.

In contrast to Nelson, Professor Bainbridge posits (in criticizing Nelson), that corporate campaign contributions are no different than corporate charitable donations.²⁵⁵ Yet, in his brief blog post²⁵⁶ Professor Bainbridge offers little factual support for his position.²⁵⁷ As a result, we ought to inquire: Are corporate political contributions *inherently* different from charitable contributions in a material way, such that political contributions damage shareholder value (thereby constituting objective waste) or fail to advance any legitimate corporate purpose (thereby constituting subjective waste)? The remainder of this sub-Part explores seven ways in which political contributions differ from charitable donations and assesses whether these differences render political contributions corporate waste.

a. Binary, Winner-Take-All Nature of Elections

While Nelson's Target example is a poor one, his Tesoro example actually hints at a good argument. Nelson urges shareholders to file a derivative lawsuit against Tesoro, on the grounds that it "spent \$1.5 million" opposing California's Proposition 23 and "received nothing in return"²⁵⁸ because the proposition failed to pass. This is not unusual. Indeed, it is the way of politics! On average, more than half of all candidates for political office presumably lose their election bids.²⁵⁹ As a result, after each election, some contributors are arguably left with "nothing to show for" their support of a candidate.

In this way, corporate political contributions in support of a candidate for elected office or a ballot initiative (and, to some extent, funds spent lobby-

255. Bainbridge, *supra* note 30. Other scholars have made this same point. *Cf.* Bebchuk & Jackson, *supra* note 7, at 117 n.97 (positing that political speech and corporate charitable contributions "are, under current law, governed by the rules that govern companies' ordinary business decisions").

256. Bainbridge, *supra* note 30.

257. Extensive research has unearthed no other scholar who has treated this subject in any depth.

258. Nelson, *supra* note 31, at 159.

259. Presumably in our largely two-party system, candidates rarely run for office unopposed. Further, to the limited extent that candidates run opposed, others at least occasionally face a third-party opponent.

ing for a certain result) differ starkly from the typical charitable contribution: political elections are an *all-or-nothing* proposition. After each election for public office, one candidate wins the election and gains the power of that office; the other candidates lose and go home, with no power whatsoever. As a result, in each election, only one candidate's supporters have a realistic chance that their candidate will be able to keep her campaign promises by enacting legislation or making policy in some way. All of the other candidates' supporters must either await the next election or hope that the candidate who they opposed will reach across the aisle when governing.

Civic, social and educational organizations do not necessarily work this way. They can serve a charitable, social, or educational mandate without "defeating" competing organizations, either by besting like-minded organizations in the battle for scarce resources or by defeating the policy goals of organizations that oppose their charitable, social or educational goals. Although charities undoubtedly set goals that are uncertain to come to fruition, such benefits do not inherently present the same sort of all-or-nothing choices that political elections do.²⁶⁰

As a result, even if some corporations make charitable donations in support of contingent benefits, those contingencies will rarely be (or at least, are not inherently) all-or-nothing propositions. What's more, even in those instances where a donation to a charitable organization supports a win-or-lose proposition – like class action litigation – the gains from funding that proposition may not be so starkly all-or-nothing as in the context of politics. All litigation does not end in victory for one party and defeat for the other.²⁶¹

260. For example, a donation to the medical school still can improve the educational opportunities for students at the medical school even if the medical school does not build the new wing for which the donation was intended; an opera company can still use a donation to fund its upcoming production even if the company is unable to land the famous tenor it wanted to sing the lead role; an organization that feeds and clothes homeless citizens can always use money for some other purpose even if it cannot raise sufficient funds to build a brand new shelter; an organization that distributes a free malaria vaccination in Africa may be able to immunize some children even if it cannot obtain the money for a program to vaccinate every child in a particular country as planned.

261. For example, is a donation to Natural Resources Defense Council (NRDC) to support a lawsuit against the Environmental Protection Agency to raise air quality standards in a particular city wasted if the suit is dismissed? Or was a donation to fund litigation to challenge the constitutionality of the Patient Protection and Affordable Care Act (ACA) wasted simply because the Supreme Court upheld the ACA? Perhaps not. In modern litigation, lawsuits are rarely complete victories or defeats – especially when administrative agencies are involved. (Shareholder derivative suits are entirely different matter.) Rather, whether or not the lawsuit settles or ultimately results in a judgment, even when both sides view one side as the "winner" and the other side as the "loser," it is rare that the winner gains *everything* it sought in the litigation and the loser loses *everything* that it sought to defend. So, in the hypothetical NRDC v. EPA lawsuit, while the NRDC may not get the EPA to enforce the applicable regulation in exactly the desired way, it may "move the ball" somewhat.

Although this “winner take all” argument may seem compelling at first glance, it nonetheless has flaws. First, political campaigns are not always solely about the election of a particular candidate. Advertisements in support of a candidate may fail to get that candidate elected but may nonetheless inform voters’ opinions for future elections. Indeed, sometimes elections are more about raising awareness or laying the groundwork for future elections than about winning office. Politicians may run for the same office again, or for different offices.²⁶² It is certainly possible that expenditures made in support of a politician in one election cycle will help that same politician win in a later election. Or, the expenditures to support one candidate may lead voters to vote for a different, like-minded candidate in a future election. This is particularly true with primary elections, where the candidate who loses the primary is from the same party and may end up supporting the candidate who wins the primary in the general election.

Second, losing candidates do not necessarily disappear after the election. If they already hold a lower elective office, they may remain in that office and continue to wield power for many years after failing to win higher office.²⁶³ Or, even if the losing candidate never runs for higher office again, she may later be appointed to higher office.²⁶⁴ As a result, a corporate political contribution that results in influence over or goodwill from a losing candidate or her supporters may benefit the corporation down the road, despite that the candidate was defeated.

Third, this “winner take all” argument proves too much. Although charities are not typically win-or-lose endeavors, businesses often are. Businesses compete with each other for customers – sometimes winning and sometimes losing. As a result, business decisions, like political contributions, regularly result in zero or negative returns to a company.²⁶⁵ Although business out-

Further, those who oppose the ACA may view the Supreme Court’s decision to uphold the law as a temporary setback rather than a definitive loss, since the holding allowed states to opt out of Medicaid expansion. *See, e.g.,* Sabrina Tavernise & Robert Gebeloff, *Millions of Poor Are Left Uncovered by Health Law*, N.Y. TIMES (Oct. 2, 2013), <http://www.nytimes.com/2013/10/03/health/millions-of-poor-are-left-uncovered-by-health-law.html>.

262. For example, Mark Dayton ran for U.S. Senator from Minnesota and lost in 1982, then ran again in 2006 and won. *See Mark Dayton’s Career*, Minneapolis Star Tribune (Dec. 27, 2009, 9:36 PM), <http://www.startribune.com/politics/statelocal/80179727.html>.

263. For example, John McCain remains in the U.S. Senate after failing to win the Presidency in 2008.

264. For example, John Kerry remained in the U.S. Senate for nearly a decade after failing to win the Presidency in 2004, and was appointed U.S. Secretary of State in 2013.

265. Thus, Romiti’s expression of doubt that “donating to political campaigns is . . . a rational business judgment because the likelihood of getting tangible returns . . . is inherently speculative” completely fails to understand the nature of business decisions. Romiti, *supra* note 31, at 758 n.135. Most if not all business decisions are “inherently speculative”; there are few if any “sure bets.”

comes are not necessarily binary, win-or-lose propositions, businesses nonetheless regularly spend large sums of money with little or no financial return. This is the nature of business. Yet, a board does not waste the corporation's assets simply by betting on a project that does not pay off. Such a standard would eviscerate the business judgment rule. Rather, the waste inquiry is whether, in light of the facts known *at the time* of the board's decision, it made an irrational gamble with the corporation's money.²⁶⁶ The same question could easily be asked for political contributions.

b. Zero-Sum Nature of Politics in the Two-Party System

Donations to one charitable organization do not necessarily harm the interests of a different charitable organization that does not receive the donation.²⁶⁷ Although there are certainly some divisive political issues – for example, abortion or religion in public schools – where social welfare organizations advocate on both sides of an issue, the vast bulk of charities are not in direct competition with each other (other than in the hunt to raise funds). Thus, if a corporation donates money to Charity A, while that may disappoint Charity B because of the loss of potential funds to “move the ball forward” on that charity's own issue of choice, the funds going to Charity A rarely will result in a *loss* to Charity B's issue of choice. Even charitable organizations that are competing for scarce resources that have similar missions are not actually harmed by a donation to their rival organization.²⁶⁸ For example, it would seem that a \$1 million gift to education is a benefit to education everywhere, whether it goes to Princeton or Harvard.²⁶⁹

Corporate political contributions differ, especially in the United States. In our largely two-party system, money given to Republicans is not simply unavailable to Democrats; it is money that probably will be used to advance an agenda that is squarely at odds with the Democrats' agenda. That is to say, money spent for the purpose of *electing* Republican candidates is money spent either directly or indirectly for the purpose of *defeating* Democratic candidates and the ideas they espouse. Accordingly, corporate political contributions in support of a Democratic candidate in a particular election will in

266. See *supra* notes 131-132 and accompanying text.

267. For example, none of the charities mentioned above (the hospital, the vaccination organization), including the charities engaged in litigation (the NRDC and groups litigating against the ACA), would have their interests directly harmed if one of the other organizations above received a donation.

268. Presumably the NRDC, which engages in litigation in support of environmental causes, is not harmed by a donation to Earthjustice, which engages in litigation in support of similar causes.

269. Obviously, it depends on how the organization's goals are defined. If Medical School A's goal is to be the number one ranked medical school in the country, then certainly a donation to Medical School B will harm Medical School A's pursuit of this goal. But hopefully most educational organizations define their goals more broadly than this.

theory cancel out corporate political contributions in support of the Republican candidate in that same election.

c. Political Spending is an Arms Race

Because a dollar spent to elect a Democrat essentially cancels out a dollar spent to elect the opposing Republican, more spending on political elections does not necessarily result in greater societal welfare (even assuming the money is spent on the “best” candidates). This is another key difference from spending on charitable, social or educational institutions. In theory, there is no limit to the amount of societal welfare that can be created by giving to these types of organizations. Thus, each dollar spent on charity (if used efficiently by the charity) expands societal welfare. There is every reason to believe that \$1 million in donations to a charity increases societal welfare more than \$1 donated to charity.²⁷⁰

By contrast, spending on political elections is an arms race. In each election, *only one* candidate will win office regardless of the overall amount of money that is spent on that election. As a result, in an election between Candidate X and Candidate Y, each additional dollar spent to support Candidate X does not increase societal welfare. At best, that dollar simply increases the chances that Candidate X will be elected rather than Candidate Y. Hence, unless spending to educate the electorate on the candidates inherently promotes societal welfare,²⁷¹ the societal welfare resulting from either candidate’s victory is necessarily the same whether the candidate spends \$1 or \$1 million. No matter how much money is spent, either Candidate X or Candidate Y will be elected, with the benefits that result from that candidate taking office. Allowing deep-pocketed corporations to participate in elections will only exacerbate this problem.²⁷²

d. Elections Are About People, Not Policies

Another difference between donations to charity and spending on political campaigns is that candidates for elective office, by their very nature, hold a variety of views. A corporation that donates to a particular candidate may

270. For example, every dollar received by the charity that provides immunizations to poor children (less administrative and fund-raising costs) provides more vaccines to poor children. Presumably the need for such vaccines is sufficiently large that every dollar increases the number of vaccinations, and therefore, increases social welfare. The same is true for gifts to medical schools or organizations that feed the homeless. Until every child is vaccinated, until the shortage of medical doctors has been met, and until all the homeless are fed, every single dollar increases social welfare incrementally.

271. In a world where the *same* political ads run *hundreds* of times in battleground states just shortly before a major election, it would seem that we are well past the point where each incremental ad expands political awareness.

272. See Dibadj, *supra* note 17, at 56.

do so because that candidate's policies on many different issues, if enacted, would benefit the corporation. But except in the (hopefully rare) case where a politician is elected to office with the sole purpose of serving all of the interests of a particular corporation (e.g., "the Senator from Boeing"²⁷³), it seems likely that the corporation's interest and the politician's interests will diverge *somewhere*.²⁷⁴ The corporation that supports that candidate must, if the candidate is elected, take the good with the bad.²⁷⁵ This is not necessarily true with donations to charity. Corporations can promote particular narrow goals by donating to single-issue organizations, if necessary, or to organizations that more closely align with the corporation's policy goals.

Target's support of Tom Emmer is a fine example of this. If Target's management truly supported Emmer solely because they believed that he would institute "tax reform," "spending reform," and "education reform" – and if Target was "not anti-gay" – then Target could have donated to three different single-issue charitable organizations that focused on promoting those goals.

By contrast, the benefit from donating to single-issue organizations instead of to Super PACs that advocate on behalf of political candidates comes at a cost: elected officials, not charitable organizations, enact legislation and make policy. No matter how much influence a charitable organization has over an elected official, it is still one step removed from office. What's more, charitable organizations to which donations are tax deductible – section 501(c)(3) organizations – cannot lobby broadly²⁷⁶ for political change, and therefore can only promote societal good in other ways.²⁷⁷ Hence, from a perspective of "bang for the buck," it is rational for a corporation's management to decide that spending money to elect a political candidate that sup-

273. See ANN R. MARKUSEN, *THE RISE OF THE GUNBELT: THE MILITARY REMAPPING OF INDUSTRIAL AMERICA* 163 (1st ed. 1991) (referring to Henry M. "Scoop" Jackson's derisive nickname).

274. For example, if a corporation supports a candidate because the candidate supports policies that benefit the corporation, a shareholder might still oppose the contribution if the shareholder disagrees with the candidate on a different issue and feels more strongly about that issue. See, e.g., Russell Mangas, *Citizens United Against Dissenting Shareholders*, 46 TULSA L. REV. 409, 412-14 (2011) (describing an example of this type of scenario).

275. Cf. Richard A. Epstein, *Citizens United v. FEC: The Constitutional Right that Big Corporations Should Have But Do Not Want*, 34 HARV. J.L. PUB. POL'Y 639, 656-67 (2011) ("[T]he last thing that . . . a corporation [should do] is get involved with election campaigns when it is clear that no candidate embodies all the positions – and only those positions – that are ideal for the firm [N]o sensible corporation should take that risky step.").

276. Charitable organizations may not devote a "substantial part" of their time to political activities such as lobbying and political campaigns. See I.R.C. § 501(c)(3) (2012). However, some charitable organizations do engage in "considerable" political advocacy under the guise of "education." See Kahn, *supra* note 165, at 638, 644-51.

277. See *infra* notes 407-411 and accompanying text.

ports some but not all of its policy goals is a more effective way of spending its money than supporting a charitable organization. Elective officials may serve many masters, but they are closer to the actual levers of power. The question is a matter of deciding whether the risk of supporting a politician with views on many issues is worth the possibility of a positive result on a specific issue – a classic business judgment.

e. Politicians Do Not Necessarily Keep Their Promises

Another difference between political contributions and charitable donations, according to Nelson, is that political contributions “do not reasonably assure that the corporation will receive the benefits contemplated by those expenditures” because there is no assurance that a political candidate who is elected will follow through on her promises.²⁷⁸ This point about candidates not keeping their promises shows promise, but is not well developed.

Politicians are often accused of changing their positions (i.e., “flip-flopping”) or not keeping their campaign promises once they are on office. By contrast, charitable organizations are rarely if ever castigated for “flip-flopping.” Unlike politicians, who conduct polling and are often accused of having no core beliefs other than the desire to be re-elected to office, charitable organizations seem to have relatively stable core missions that do not change drastically over time. Yet, absent empirical data, one cannot state with certainty that politicians keep promises about how they will act less often than charities do.

Still, a fundamental difference in the way that political contributions and charitable contributions work suggests that Nelson’s hypothesis is correct. Donors to charity can – and often do – require as a condition of the gift that the donation be directed to some specific purpose. For example, donations to colleges and universities often are restricted to be used for a particular purpose, whether it be to fund a particular scholarship or department, to build a specific building wing, or to endow a chair for a particular professor.²⁷⁹ These gift restrictions are enforceable by contract or by the state’s attorney general.²⁸⁰

Further, donors to charity can make the donation in exchange for a specific benefit – for example, the donor’s name being placed on a building at

278. See Nelson, *supra* note 31, at 160 (positing that “a political candidate’s platform to get elected could vary drastically from what the politician actually accomplishes in office”).

279. See, e.g., Kiki Barnes, *Donations to U. Grow Increasingly Specific*, BROWN DAILY HERALD (Mar. 5, 2013), <http://www.browndailyherald.com/2013/03/05/donations-to-u-grow-increasingly-specific/>.

280. See Alan F. Rothschild, Jr., *Planning and Documenting Charitable Gifts*, GP SOLO L. TRENDS & NEWS: EST. PLANNING (Am. Bar Ass’n, Chicago, Ill.), Sept. 2007, available at https://www.americanbar.org/newsletter/publications/law_trends_news_practice_area_e_newsletter_home/planningcharitablegifts.html.

the university or the donor receiving a ticket to the charity's annual gala.²⁸¹ Although a donor may lose some or all of her tax deduction if she receives a quid pro quo benefit from the charity, such a quid pro quo is not generally prohibited by law.²⁸² Unlike politicians, charities may sell goods or services in order to raise money to support their charitable goals.

Corporate political contributions are an entirely different matter. Although donors can designate how corporate political contributions must be used (e.g., to support a particular advertising campaign), political contributions must, by law, come with no strings attached.²⁸³ Any intended quid pro quo, whether stated or unstated, could land both the donor and the politician in jail because politicians, unlike charities, are prohibited from selling their office.²⁸⁴ This presumably is true not only for direct contributions, but also for independent expenditures. Accordingly, any result that a corporation intends to achieve by making a political contribution is necessarily, by law, more speculative than any result that the corporation intends to receive in exchange for a charitable donation.

f. Elected Officials Rarely Act Alone

Nelson's comment about what a politician can "accomplish in office" also suggests another way in which charitable contributions differ from corporate political contributions: charitable organizations can work alone if they wish, but elected officials *must* by law work together. Except perhaps on the local level, governments in the United States are typically separated into executive, legislative and judicial branches – and often a combination of two or more branches working together is required in order to take action.²⁸⁵

As a result, corporate political contributions in favor of one politician may not result in the desired benefit to the corporation – even if the candidate wins election to office and keeps her campaign promises – unless the candidate is able to convince other elected officials to support her agenda. Therefore, even if a corporation made a political contribution to President Barack Obama to support his 2012 re-election campaign with the goal of enacting a policy that was among the centerpieces of his campaign platform, that corporation likely has not achieved its goal. Although President Obama was re-elected and has attempted to promote some of the policies that he advocated in his campaign, little legislation has passed Congress and appeared on his

281. *See id.*; *see also* 26 C.F.R. § 1.170A-1(e) (2008).

282. *See* § 1.170A-1(e).

283. *See* I.R.C. § 501(c)(3) (2012); *see also* 18 U.S.C. § 201 (2012).

284. *See supra* note 159 and accompanying text.

285. For example, in order for a federal law to be enacted, the legislature (both houses of Congress) must enact the same bill (or must meet in conference to work out any differences), the president must sign the bill into law (and perhaps the Supreme Court must declare it constitutional, if it is challenged). *See School House Rock: I'm Just a Bill* (ABC television broadcast Mar. 27, 1976).

desk for his signature because the House of Representatives is controlled by conservative Republicans.²⁸⁶

Yet, this goal-oriented lens on corporate political spending is founded upon a narrow, and possibly naive, understanding of why businesses make political contributions to politicians. It is widely understood that most corporations support politicians not to gain passage of specific policies, but rather to “buy access” to the politicians once they are in office.²⁸⁷ “Access” essentially means the ability to have the politician listen to your lobbyists when they come calling.²⁸⁸ This desire for access, it is argued, fuels the seemingly strange practice of corporations donating money to politicians “on both sides of the aisle” – i.e., Republicans and Democrats²⁸⁹ – despite that these politicians’ goals may be largely antithetical.

If “access,” rather than enacting any specific legislation, is the goal of most corporate political contributions, then it does not matter if the corporation’s political candidate of choice is able to enact her legislative proposals or not – so long as she wins office and keeps her doors open.

g. Charitable Contributions May Require No Business Purpose

The foregoing analysis is premised on the assumption that charitable contributions are just like ordinary business transactions in that they require a business purpose; if not, they will be deemed subjective waste. But in fact, in many states (albeit not Delaware), corporate law statutes carve out a special place for corporate philanthropy. In such states “management need not defend charitable giving as serving the interests of the corporation, no matter how those interests are defined.”²⁹⁰ Indeed, some states’ corporate law stat-

286. See Jon Perr, *The Republicans’ Unprecedented Obstructionism by the Numbers*, CROOKSANDLIARS.COM (Oct. 13, 2011, 5:00 PM), <http://crooksandliars.com/jon-perr/republicans-unprecedented-obstructionism-by-numbers>.

287. See *McConnell v. FEC*, 540 U.S. 93, 124-25 (2003), *overruled by* *Citizens United v. FEC*, 558 U.S. 310 (2010); see also John M. de Figueiredo & Elizabeth Garrett, *Paying for Politics*, 78 S. CAL. L. REV. 591, 593 (2005).

288. See *McConnell*, 540 U.S. at 119 n.5.

289. See Jason Cohen, *The Same Side of Two Coins: The Peculiar Phenomenon of Bet-Hedging in Campaign Finance*, 26 N. ILL. U. L. REV. 271, 293 (2006); Tamara R. Piety, *Against Freedom of Commercial Expression*, 29 CARDOZO L. REV. 2583, 2616 n.151 (2008) (“[A] desire for influence, not principles, surely explains why so many corporate donors regularly contribute to both parties.”); Vicki Kemper & Deborah Lutterbeck, *The Country Club*, 22 COMMON CAUSE MAG. 16, 17-18 (1996) (explaining that corporations often make “large contributions to both political parties to guarantee access, influence and agenda-setting power no matter . . . which party controls Congress”); see, e.g., Don Van Natta, Jr., *Enron’s Collapse: The Politicians; Enron Spread Contributions on Both Sides of the Aisle*, N.Y. TIMES (Jan. 21, 2002), <http://www.nytimes.com/2002/01/21/us/enron-s-collapse-politicians-enron-spread-contributions-both-sides-aisle.html?pagewanted=all&src=pm>.

290. See Fisch, *supra* note 165, at 765; but see BAINBRIDGE, *supra* note 165, at 436.

utes (including New York's) "explicitly authorize management to make charitable donations 'irrespective of corporate benefit.'"²⁹¹ As a result, it may be "legal and . . . appropriate for corporations to make donations that cannot be justified in business terms."²⁹² As a result, it is "nearly impossible to challenge" corporate philanthropy through shareholder litigation.²⁹³ In this regard, charitable donations "are *sui generis* within corporate law."²⁹⁴

By contrast, no state corporation law statutes known to this author exempt political contributions from the business purpose requirement. Accordingly, even if courts have perhaps given charitable contributions a "free pass" in light of their statutory exemption from the business purpose requirement,²⁹⁵ this pass is inapplicable to political activity.

2. Evaluating the Argument: Do These Differences Matter?

Having fleshed out some arguments in support of Nelson's basic (but undeveloped) point that political contributions are different from charitable contributions, we now ask the critical question: Do any or all of these arguments support a claim that political contributions constitute waste under either the subjective or objective standard?

a. Target Corporation and MN Forward/Emmer

Consider the worst-case scenario of Target's contribution to MN Forward in support of gubernatorial candidate Tom Emmer, described above.²⁹⁶ Was this contribution waste? Most certainly not – even if we assume that the only benefit to the corporation will result from the candidate being elected to office. The fact that politics is a binary, winner-take-all game does raise the stakes somewhat. However, this does not ultimately mean that no reasonable person would bet on Emmer or that, by doing so, Target's management necessarily acted against the corporation's best interests. Rather, the question under the objective standard for waste is whether the bet was irrational at the time it was made.²⁹⁷ Clearly, Target's support of Emmer does not satisfy that standard. Emmer ran neck and neck with Dayton and fell less than 9,000 votes short of election.²⁹⁸ Further, the stakes of the contribution were not necessarily known to Target's board at the time; if in fact the board members were supporting Emmer and MN Forward solely due to economic issues, they

291. Fisch, *supra* note 165, at 765.

292. *Id.* (emphasis added).

293. *Id.*

294. Kahn, *supra* note 165, at 605.

295. See *infra* Part V.E. (discussing charitable contribution cases).

296. See *supra* Part IV.B.1.b.

297. See *supra* note 132 and accompanying text.

298. See *2010 Minnesota Governor's Race*, POLITICS IN MINN., <http://politics.inminnesota.com/2010-mn-governor-race/> (last visited June 14, 2014).

might not have anticipated that their contribution could backfire so badly. The decision, terrible in retrospect, cannot be deemed irrational based on the facts known to the board at the time. Regardless of one's politics, it was not *utterly irrational* to support Emmer. Nor, as explained above, was there no corporate purpose for Target to be supporting (what it viewed as) Minnesota's economy. Further, once we relax our assumptions and recognize that a corporation could benefit even if the candidate it supports loses, it becomes clear that waste is not a viable theory.

The zero sum nature of politics and the fact that political spending is an arms race does nothing to undermine this conclusion. If Target's management was not irrational to believe that helping elect the Republican candidate for governor would benefit Target, the zero sum nature of politics made it *even more* critical for Target to join in the fray and contribute rather than stand on the sidelines. Every dollar that Democrats spent in support of Dayton was a dollar that, in theory, undermined the Minnesota that Target's management envisioned would be best for Target's shareholders – a Minnesota led by Emmer. Even if there were other reasonable alternative approaches by which Target could have served its goals,²⁹⁹ the close nature of the election suggests that it was not irrational to make a contribution, even if that contribution led deep-pocketed Democrats to spend more in response. Unfortunately, the whole problem with an arms race is that all participants would be better off if there were *no* arms race, but no participant can unilaterally disarm without damaging its position *vis-à-vis* the other participants.³⁰⁰

The insight that politicians are people who do not act alone and do not always keep their promises also fails to prove that Target's gamble on Emmer was irrational. Even if we assume that the sole reason that Target supported Emmer was its stated reason of supporting jobs for Minnesota's citizens, the fact that Emmer could not enact his agenda alone is not reason to withhold support. Governors can have coattails. Moreover, the Republicans were in a good position – and won decisively – in the 2010 election, taking control of both houses.³⁰¹ In short, if Emmer had won, he would have been in a *fantastic* position to enact his legislative agenda. Even if Republicans had *not* taken over the legislature, they would have had a better chance of enacting their legislative agenda with a Republican governor than without one. Further, while there is no certainty that Emmer would have kept *all* of his campaign promises if he had won the election, he would have been precluded from keeping *any* of his promises if he had lost the election. Thus, if a contribution to MN Forward would help Emmer become elected, it was rational for Target to make a contribution.

299. For example, a better strategy for Target might have been to keep its powder dry in an attempt to promote a *détente* rather than an arms race among deep-pocket corporate donors.

300. See Laura Onken, *Game Theory and Citizens United*, 9 GEO. J.L. & PUB. POL'Y 517, 527-28 (2011).

301. See *Minnesota Election Results 2010*, N.Y. TIMES, <http://elections.nytimes.com/2010/results/minnesota> (last visited June 14, 2014).

In sum, although political contributions do differ in many ways from charitable donations due to the differences between the way political elections and charities operate, none of these differences suggest that, by making a political contribution, a board of directors has acted irrationally or without regard to the best interests of the corporation. Such a conclusion can only be made in hindsight, based on the unfavorable results of the contributions, or based on untenable assumptions. Even though Emmer was an extremely conservative candidate, he was not on the absolute fringe; forty-four percent of the electorate in Minnesota supported him.³⁰² While perhaps it was not reasonable to risk upsetting half of Target's clientele, reasonableness is not the applicable standard for waste. Only the most rabid partisan would deem supporting Emmer to be utterly irrational.

b. The Actual Worst Case Scenario: Waste Exemplified

Although spending money in support of Emmer was not irrational, the foregoing analysis suggests that political contributions to *some* candidates could constitute waste. In truth, Emmer was *far* from the worst-case scenario political candidate. Indeed, he was not even the worst – in terms of most unelectable or farthest from the mainstream – Republican-endorsed candidate in Minnesota in recent years. That honor belongs to Kurt Bills, U.S. Senate candidate in 2012.³⁰³ Yet, spending money in support of a major-party candidate, even a long-shot like Bills, probably is never waste. Underdog candidates pull off major upsets from time to time.³⁰⁴

Nonetheless, a contribution to a Super PAC that advocates in support of a candidate who is both *far* outside of the political mainstream and personally offensive to most Americans – an American Nazi Party candidate, for example – would undoubtedly constitute waste under both the objective and sub-

302. *Id.*

303. Bills, who once advocated that Minnesota adopt its own currency, lost the 2012 race for U.S. Senate to popular incumbent Amy Klobuchar by nearly one million votes, winning about thirty-one percent of votes cast. See Joe Loveland, *How In the World Did Minnesota GOPers Screw Up Their Golden Opportunity?*, MINNPOST.COM (Nov. 7, 2012), <http://www.minnpost.com/minnesota-blog-cabin/2012/11/how-world-did-minnesota-gopers-screw-their-golden-opportunity>. This was the second worst finish by a Republican candidate in modern Minnesota history. See Eric Ostermeier, *GOP Bracing for 2nd Worst Finish in MN US Senate Race Since Great Depression*, SMART POLITICS (Oct. 19, 2012), http://blog.lib.umn.edu/cspg/smartpolitics/2012/10/gopbracing_for_2nd_worst_fini.php.

304. For example, in 1992, Paul Wellstone – a “virtual unknown” college professor who ran a “quirky” campaign – unseated incumbent Minnesota U.S. Senator Rudy Boschwitz, whose victory was viewed as “inevitable” at the time. See *GOP's Bills Likens Underdog Minn. Bid to Wellstone*, CBS MINN. (July 30, 2012, 7:24 PM), <http://minnesota.cbslocal.com/2012/07/30/gops-bills-likens-underdog-minn-bid-to-wellstone/>. Knowing of his own underdog status, Bills played up the comparison between himself and Wellstone in the 2012 Senate race. See *id.*

jective standard. Not only is there a near-zero chance that such a candidate would be elected to office, it is virtually certain that most Americans – Target’s customers – would be outraged if they learned that the company supported such a candidate. Thus, while the boycotts that Target suffered were certainly *possible* if Target donated to an organization that opposed gay marriage, an issue on which Americans are divided, boycotts would be *near certain* if Target supported a Nazi candidate, since almost all Americans presumably abhor the views espoused by such a candidate. A contribution to the American Nazi Party would have *essentially zero* potential upside and a *massive, near certain* downside. This is a paradigmatic irrational transaction. This is classic corporate waste.

D. What Do the Cases Tell Us?

Based on the foregoing analysis, it seems clear that corporate political contributions will rarely, if ever, satisfy either the objective or subjective standard for corporate waste. But it would be too hasty to so conclude without first reviewing the relevant case law. Legal tests divorced from actual facts are more prone to manipulation than legal tests analyzed in the context of specific facts.

Unfortunately, the cases Nelson proffers provide little help to derivative plaintiffs. Nelson discusses the two aforementioned³⁰⁵ political spending cases, *Stern* and *Marsili*.³⁰⁶ However, because neither case held that the corporate political spending at issue was waste,³⁰⁷ neither case will offer much comfort to shareholder plaintiffs challenging corporate political contributions as waste.

Cases where the plaintiff claiming waste *did* survive a motion to dismiss (for failure either to state a claim or to make a demand) also offer no support for plaintiffs pursuing the waste theory. Three recent Delaware cases expose the limitations of Nelson’s argument: *In re Citigroup Inc. Shareholder Derivative Litigation*,³⁰⁸ *Telxon Corp. v. Bogomolny*,³⁰⁹ and *Lewis v. Vogelstein*.³¹⁰

First, in *Citigroup*, Citigroup, Inc. shareholders sued the board, alleging that its approval of an agreement to compensate the company’s departing CEO was waste because the CEO was at least partially responsible for the

305. See *supra* Part III.C.

306. See Nelson, *supra* note 31, at 151-53.

307. See *id.* at 153, 154; *Stern v. Gen. Elec. Co.*, 924 F.2d 472, 477 (2d Cir. 1991); *Marsili v. Pac. Gas & Elec. Co.*, 124 Cal. Rptr. 313, 321 (Cal. Ct. App. 1975). Indeed, the *Marsili* court couched its analysis in terms of the *ultra vires* doctrine, not the corporate waste doctrine. See *Marsili*, 124 Cal. Rptr. at 318.

308. 964 A.2d 196 (Del. Ch. 2009).

309. 792 A.2d 964 (Del. Ch. 2001).

310. 699 A.2d 327 (Del. Ch. 1997).

company's recent multi-billion dollar losses.³¹¹ The agreement provided the former CEO with \$68 million in salary, bonuses, and other perks.³¹²

The Delaware Court of Chancery, applying the objective waste standard, held that the plaintiffs' allegations raised "a reasonable doubt as to whether the letter agreement meets the admittedly stringent 'so one sided' standard."³¹³ In particular, the allegations raised a reasonable doubt as to how much of the departing CEO's compensation from the agreement was in fact additional compensation that Citigroup paid in return for non-compete, non-disparagement, non-solicitation and release of claims agreements, and how much of the departing CEO's compensation from the agreement simply fulfilled prior contractual obligations.³¹⁴ The larger the portion of the settlement that constituted additional compensation, the more likely it was to be waste.³¹⁵ The court reasoned that the case presented an extreme set of facts where the agreement was approved at the same time the company reported significant losses and, therefore, raised a reasonable doubt that the CEO's compensation was "so disproportionately large as to be unconscionable and constitute waste."³¹⁶

The facts of *Citigroup* stand in stark contrast to a situation where a corporation contributes to a Super PAC that supports a candidate for elective office in hopes that the candidate will win the election and enact policies favorable to the corporation. In *Citigroup*, the company had *already* decided to fire the outgoing CEO and was negotiating his departure package and attempting to head off any legal claims he might file.³¹⁷ As such, the CEO was not providing any future benefit to the company. Any benefit from settling potential claims should have been weighed against the harm to the company caused by the CEO, who had overseen the destruction of billions of dollars of shareholder wealth. In short, *Citigroup* involved a situation where the board was acting in hindsight and could see the damage that the CEO had caused the company, and nonetheless paid to make him go away without a fuss. There was no potential upside to the deal, merely a minimization of downside. Therefore, it was at least plausible for plaintiffs to argue that no reasonable person would have approved millions of dollars in severance for the outgoing CEO.

Second, in *Telxon*, shareholders brought a derivative action (later converted to a direct action) against the chairman of Telxon Corporation's board

311. See *Citigroup*, 964 A.2d at 111-12. The company had recently announced a fifty-seven percent decline in profit from the previous year, and had announced significant write downs from sub-prime exposures amounting to \$55 billion. See *id.* at 113.

312. See *id.* at 138.

313. *Id.*

314. See *id.*

315. See *id.*

316. *Id.*

317. See *id.*

and six other directors.³¹⁸ The complaint alleged that a stock option grant to the chairman constituted waste.³¹⁹ The grant provided the chairman with the right to acquire ten percent of the equity of a wholly-owned subsidiary, Aironet, at \$1.86 per share.³²⁰ The chairman funded the purchase of the options with a non-recourse note, thereby eliminating his risk in the transaction.³²¹ Three years later, Aironet made a public offering of shares at \$11 per share.³²² Shortly thereafter, Cisco Systems, Inc. merged with Aironet, raising its stock price to \$82 per share and the value of the chairman's stock to \$66 million.³²³

In deciding whether to dismiss the suit, the Court of Chancery, applying the objective standard of waste, evaluated whether reasonable directors could have expected the corporation to benefit from the grant of the stock option.³²⁴ If not, the court reasoned, the consideration received by the corporation might be “so disproportionately small as to lie beyond the range at which a reasonable person might be willing to trade.”³²⁵ Ultimately, the court denied the motion to dismiss because the circumstances were “unusual.”³²⁶

As in *Citigroup*, the facts of *Telxon* stand in stark contrast to the facts of a typical political contribution. In *Telxon*, the chairman of the board, who already was subject to a generous compensation package, “purchased” options from the company – but the purchase was fully funded by the company due to the no-recourse note.³²⁷ Further, the options, once vested, resulted in a large windfall to the chairman. As a result, there was a plausible argument that the corporation had received essentially nothing in return for the stock options that it provided to the chairman.

Third, *Lewis*, is perhaps the paradigmatic waste case. In *Lewis*, shareholders sued the Mattel, Inc. board to challenge an “unusual,” one-time grant of options for 15,000 shares of common stock to the company's outside directors; the grant was valid for ten years.³²⁸ The value of the stock grant was \$180,000 per director.³²⁹ In denying the board's motion to dismiss, the *Lewis* court – applying the objective waste standard – concluded that there might be a set of facts under which the option grant constituted waste.³³⁰

318. *Telxon Corp. v. Bogomolny*, 792 A.2d 964, 967-68 (Del. Ch. 2001).

319. *See id.* at 968.

320. *See id.* at 969.

321. *See id.*

322. *See id.* at 970.

323. *See id.*

324. *See id.* at 976.

325. *Id.*

326. *Id.*

327. *See id.* at 969.

328. *See Lewis v. Vogelstein*, 699 A.2d 327, 329-30 (Del. Ch. 1997). The corporation's shareholders also ratified the grant. *Id.*

329. *Id.* at 331.

330. *See id.* at 339.

Even more than *Citigroup* and *Telxon*, *Lewis* shows why a corporate political contribution is rarely waste. In *Lewis*, there was a plausible argument that the large, one-time stock option grant was *additional* compensation to the outside directors for the same job that they were already contracted to perform to the corporation. Although companies are allowed to award performance bonuses, such bonuses must satisfy the test for objective waste.³³¹ That is to say, they must plausibly benefit the corporation – by, for example, encouraging future loyal service from the directors. But there was no evidence of such a benefit in *Lewis*. Accordingly, the court concluded that it was plausible that the large, one-time option grant would result in essentially zero benefit to the corporation.³³²

In contrast to each of these cases, corporate political contribution will only in rare instances – such as in the case of an American Nazi Party contribution, as described above – offer essentially zero potential benefit to the corporation. If the candidate in question has a non-zero chance of winning the election and if the contribution could result in the officeholder subsequently providing “access” to the corporation’s lobbyists – or even “openness” to considering the enactment of policies that benefit the corporation – that is a plausible benefit to the corporation.³³³ The whole point of the business judgment rule is that courts will not second-guess the board’s decision that the political contribution was worth the potential benefit, despite the potential risk of that benefit coming to fruition.³³⁴

V. CHALLENGING CORPORATE POLITICAL CONTRIBUTIONS AS SELF-DEALING

A. What is Self-Dealing?

“Self-dealing” occurs when a director receives a “personal financial benefit from a transaction that is not equally shared by the stockholders.”³³⁵

331. *See id.* at 336.

332. *See id.* at 339.

333. *See* Winkler, *supra* note 101, at 1265 (“[I]t is hard to imagine any case in which shareholders could prove no benefit whatsoever to the corporation from [political] contributions; management could justify almost any contribution as an attempt to open a candidate’s eyes to see corporate needs.”).

334. *See In re Cox Radio, Inc. S’holders Litig.*, No. 4461-VCP, 2010 WL 1806616, at *14 (Del. Ch. May 6, 2010) (“While hindsight is generally 20/20, it cannot be used to second guess the business judgment of Delaware directors[.]”), *aff’d*, 9 A.3d 475 (Del. 2010); *In re Citigroup Inc. S’holder Derivative Litig.*, 964 A.2d 106, 122 (Del. Ch. 2009) (“[T]he business judgment rule . . . prevents judicial second guessing of [a] decision if the directors employed a rational process and considered all material information reasonably available[.]”).

335. *Rales v. Blasband*, 634 A.2d 927, 936 (Del. 1993) (citing *Aronson v. Lewis*, 473 A.2d 805, 812 (Del. 1984), *overruled by Brehm v. Eisner*, 746 A.2d 244 (Del. 2000)).

This personal financial benefit must be “material.”³³⁶ In this context, material means “significant enough ‘in the context of the director’s economic circumstances, as to have made it improbable that the director could perform her fiduciary duties . . . without being influenced by her overriding personal interest.’”³³⁷ When an event is uncertain to occur, Delaware courts typically hold that materiality depends “‘upon a balancing of both the indicated probability that [the] event will occur and the anticipated magnitude.’”³³⁸

The paradigmatic conflicted transaction is “direct” self-dealing, when a director herself “stands on both sides of” a transaction with the corporation. For example, direct self-dealing occurs when a director personally sells goods or services to the corporation.³³⁹ However, a conflict of interest need not be direct in order to constitute self-dealing. An “indirect” conflict of interest – that is to say, a transaction in which someone *other* than the director of the corporation stands on the opposite side of a transaction with the corporation – also can be self-dealing.³⁴⁰ “Indirect” self-dealing can take many forms. Transactions between a corporation and a director’s spouse³⁴¹ or a close relative such as a sibling or child who lives with the director³⁴² are examples of indirect self-dealing. So are transactions between a

336. See *Orman v. Cullman*, 794 A.2d 5, 23 (Del. Ch. 2002).

337. *Id.* (italics omitted) (quoting *In re Gen. Motors Class H S’holders Litig.*, 734 A.2d 611, 617 (Del. Ch. 1999)).

338. *In re Oracle Corp.*, 867 A.2d 904, 938 n.149 (Del. Ch. 2004) (quoting *Basic Inc. v. Levinson*, 485 U.S. 224, 238 (1988)), *aff’d sub nom. In re Oracle Corp. Derivative Litig.*, 872 A.2d 960 (Del. 2005).

339. See BAINBRIDGE, *supra* note 72, at 307.

340. Further, the personal financial benefit to the person other than the director must be material to the director. See *Orman*, 794 A.2d at 23.

341. See BAINBRIDGE, *supra* note 72, at 308; see, e.g., *Bayer v. Beran*, 49 N.Y.S.2d 2, 7 (N.Y. Sup. Ct. 1944) (applying entire fairness standard to a transaction between a corporation and the spouse of the corporation’s CEO).

342. In Texas, for example, self-dealing encompasses “a contract or transaction between a corporation” and a director or between a corporation and an “associate” of a director. TEX. BUS. ORGS. CODE ANN. § 21.418(a) (2011). “Associate” is defined to include a director’s “spouse or a relative . . . related by consanguinity or affinity who resides with the person[.]” § 1.002(2)(C). So presumably in Texas, when a corporation buys goods from the sister-in-law of its CEO, and the sister-in-law lives next door to the CEO, this would nonetheless *not* constitute self-dealing.

Other jurisdictions, like Delaware, do not limit the definition of self-dealing to a specific list of “related” persons. See *infra* notes 383-387 and accompanying text. As such, transactions between a corporation and a director’s close relatives such as a sibling could in theory be deemed self-dealing even if the sibling does not live with the director.

However, a transaction between the corporation and a director’s cousin is generally not self-dealing. See BAINBRIDGE, *supra* note 72, at 319 (explaining that, even under the current version of the MBCA, “cousins are not related persons under the statute” – so a transaction with a cousin does not constitute self-dealing); Mary Siegel, *The Erosion of the Law of Controlling Shareholders*, 24 DEL. J. CORP. L. 27, 77 n.254 (1999) (same); Comm. on Corporate Laws, *Changes in the Model Business Corpora-*

corporation and an entity controlled by a director, or an entity in which a director has a material financial interest.³⁴³ For simplicity's sake, all of these transactions can be described as transactions between the corporation and a "proxy" for one of its directors.

Finally, in order to constitute self-dealing, the director's conflict of interest must relate to a specific transaction.³⁴⁴ If a director faces a conflict of interest outside of the context of a specific transaction, courts will not necessarily treat the issue as a matter of self-dealing.³⁴⁵

B. How Do Courts Review Self-Dealing?

The plaintiff bears the burden of establishing that a director engaged in a self-dealing transaction.³⁴⁶ In cases of indirect self-dealing, this burden can be difficult to satisfy unless the proxy for the director or office is obvious (for example, a spouse). This is because "[w]hile it may be possible to show that . . . [an] action taken by the corporation benefited [a director], it is extremely difficult to prove that this advantage came at the expense of the other shareholders."³⁴⁷

When a court concludes that a director engaged in self-dealing, the business judgment rule's presumption that directors act without a conflict of interest is rebutted.³⁴⁸ As a result, the court will not defer to the board's

tion Act – Amendments Pertaining to Directors' Conflicting Interest Transactions, 44 BUS. LAW. 1307, 1322 (1989) ("If a plaintiff charges that a director had a conflict of interest with respect to a transaction of the corporation because the other party was his cousin, the answer of the court should be: 'No.'").

343. See, e.g., DEL. CODE ANN. tit. 8, § 144(a) (2010); TEX. BUS. ORGS. CODE ANN. § 1.002(1).

344. See DEL. CODE ANN. tit.8 § 144(a) (defining self-dealing solely with regard to "contract[s] or transaction[s]"); MODEL BUS. CORP. ACT § 8.60 (2010) (defining directors' "conflicting interest transaction"); 2 MODEL BUS. CORP. ACT ANN. § 8.60 at 8-373 (Supp. 1997) ("[T]he subchapter is applicable only when there is a 'transaction' by or with the corporation."); § 8.60 at 8-382-83 ("To constitute a director's conflicting interest transaction, there must first be a transaction by the corporation . . . in which the director has a financial interest. . . . [S]ubchapter F [has] no application to circumstances in which there is no 'transaction' by the corporation, however apparent the director's conflicting interest.").

345. See, e.g., *Mueller v. Zimmer*, 124 P.3d 340, 352-53 (Wyo. 2005); *Glad Tidings Assembly of God v. Neb. Dist. Council of the Assemblies of God, Inc.*, 734 N.W.2d 731, 737-38 (Neb. 2007). But see *Cooke v. Oolie*, No. 11134, 2000 WL 710199, at *13 n.39 (Del. Ch. 2000) (noting that Delaware's director conflict statute did not strictly apply because "in this case, no transaction has occurred[.]" but applying the statute by analogy due to policy considerations).

346. See *In re Citigroup Inc. S'holder Derivative Litig.*, 964 A.2d 106, 124 (Del. Ch. 2009).

347. Jens Dammann, *Corporate Ostracism: Freezing Out Controlling Shareholders*, 33 J. CORP. L. 681, 694 (2008).

348. See *Disney I*, 906 A.2d 27, 52 (Del. 2006).

decision to enter the transaction.³⁴⁹ Instead, the court will review the transaction itself to determine whether the transaction was fully disclosed, approved by disinterested persons and/or fair to the corporation.³⁵⁰ If the transaction was approved by disinterested (and probably independent³⁵¹) directors or the (probably disinterested and independent³⁵²) shareholders who were fully informed about the transaction, this may sanitize the transaction – to varying degrees, depending on the jurisdiction – under so-called state “safe harbor” statutes.³⁵³ Absent informed, disinterested approval, the defendant director must show that the transaction was “entirely” (or “intrinsically”³⁵⁴) fair to the corporation.³⁵⁵

Entire fairness means objective fairness.³⁵⁶ Entire fairness has two components: fair price and fair dealing.³⁵⁷ Fair price concerns all conceivable “economic and financial considerations,” like whether the corporation received fair market value;³⁵⁸ it means “a price that is within the range of prices that would be expected to result from arms-length negotiations between the two independent parties with relatively equal information and bargaining

349. *See id.* However, a *single* director’s conflict will “not deprive a board of the protections of the business judgment rule unless . . . the interested director dominated and controlled the board.” Lewis H. Lazarus & Brett M. McCartney, *Standards of Review in Conflict Transactions on Motions to Dismiss: Lessons Learned in the Past Decade*, 36 DEL. J. CORP. L. 967, 972 (2011). Thus, in order to rebut the business judgment rule with respect to the *entire* board, the plaintiff must show that a *majority* of the board shares the conflict of interest with, or is dominated by, the conflicted director. *Id.* at 975. Alternatively, the plaintiff could establish that a majority of the board was not sufficiently informed about the conflicted director’s conflict of interest. *See Teachers’ Ret. Sys. v. Aidinoff*, 900 A.2d 654, 667 (Del. Ch. 2006). For this reason, this Article follows Professor Bainbridge’s lead in using a corporation’s CEO in all of its hypothetical examples. A CEO presumably dominates any inside directors who report to her – and could plausibly, depending on the circumstances of that particular case, even be shown to dominate the outside directors.

350. *See Disney I*, 906 A.2d at 52-53.

351. *See* GEVURTZ, *supra* note 87, at 291; *Cinerama, Inc. v. Technicolor, Inc.*, 663 A.2d 1156, 1169 (Del. 1995).

352. *See* GEVURTZ, *supra* note 87, at 291; *Fliegler v. Lawrence*, 361 A.2d 218, 221 (Del. 1976).

353. *See, e.g.*, DEL. CODE ANN. tit. 8 § 144(a) (2010).

354. Bradley R. Aronstam et al., *Delaware’s Going-Private Dilemma: Fostering Protections for Minority Shareholders in the Wake of Siliconix and Unocal Exploration*, 58 BUS. LAW. 519, 523 n.31 (2003) (“Delaware courts frequently use the terms ‘intrinsic fairness’ and ‘entire fairness’ interchangeably.”).

355. *See Disney I*, 906 A.2d at 52; *Cinerama, Inc. v. Technicolor, Inc.*, 663 A.2d 1156, 1163 (Del. 1995).

356. *See* *Gesoff v. IIC Indus., Inc.*, 902 A.2d 1130, 1145 (Del. Ch. 2006) (“Not even an honest belief that the transaction was entirely fair will be sufficient to establish entire fairness. Rather, the transaction itself must be objectively fair, independent of the board’s beliefs.”).

357. *Weinberger v. UOP, Inc.*, 457 A.2d 701, 711 (Del. 1983).

358. *Id.*

power.”³⁵⁹ Fair dealing relates to how “the transaction was timed, . . . initiated, structured, negotiated, disclosed to the directors, and how the approvals of the directors and the stockholders were obtained.”³⁶⁰

The entire fairness standard requires careful judicial scrutiny of the transaction in question. Indeed, the entire fairness standard is often described as “onerous,” “exacting” or “rigorous”³⁶¹ – and rightly so, when compared to the defendant-friendly business judgment rule. The business judgment rule essentially requires courts to defer to almost any rational, good faith, non-conflicted board decision – and requires that the plaintiff bear the burden of proving that a decision was irrational, in bad faith, or conflicted.³⁶² By contrast, under the entire fairness standard, the defendant must show that, on balance, the transaction was fair to the corporation.³⁶³

As a result, a court’s decision to apply either the business judgment rule or the entire fairness standard is, in many cases, outcome determinative: When a court applies the former, the plaintiff almost always loses; if a court applies the latter, management usually loses.³⁶⁴

359. Aaron Rachelson, CORPORATE ACQUISITIONS § 9:11 (2013); see also Claire Hill & Brett McDonnell, *Sanitizing Interested Transactions*, 36 DEL. J. CORP. L. 903, 922 (2011); Ethan G. Stone, *Business Strategists And Election Commissioners: How the Meaning of Loyalty Varies with the Board’s Distinct Fiduciary Roles*, 31 J. CORP. L. 893, 932 (2006).

360. *Weinberger*, 457 A.2d at 711.

361. See, e.g., *Mills Acquisition Co. v. MacMillan, Inc.*, 559 A.2d 1261, 1279 (Del. 1989) (under entire fairness review “the challenged transaction must withstand rigorous judicial scrutiny”); *Reis v. Hazelett Strip-Casting Corp.*, 28 A.3d 442, 459 (Del. Ch. 2011) (“Entire fairness is Delaware’s most onerous standard.”); Robert T. Miller, *Wrongful Omissions by Corporate Directors: Stone v. Ritter and Adapting the Process Model of the Delaware Business Judgment Rule*, 10 U. PA. J. BUS. & EMP. L. 911, 924 (2008) (“[T]he entire fairness standard is so onerous for corporate directors that defendants faced with an entire fairness review often move quickly to settle[.]”); Robert A. Prentice & John H. Langmore, *Hostile Tender Offers and the “Nancy Reagan Defense”: May Target Boards “Just Say No”? Should They Be Allowed To?*, 15 DEL. J. CORP. L. 377, 406 n.1415 (1990) (“The most exacting form of review is the ‘entire fairness’ . . . standard[.]”).

362. See *supra* Part III.A (explaining business judgment rule standard).

363. See *Weinberger*, 457 A.2d at 710 (“The requirement of fairness is unflinching in its demand that where one stands on both sides of a transaction, he has the burden of establishing its entire fairness, sufficient to pass the test of careful scrutiny by the courts.”).

364. See *Mills Acquisition Co.*, 559 A.2d at 1279 (“[B]ecause the effect of the proper invocation of the business judgment rule is so powerful and the standard of entire fairness so exacting, the determination of the appropriate standard of judicial review frequently is determinative of the outcome of derivative litigation.”) (quoting *AC Acquisitions v. Anderson, Clayton & Co.*, 519 A.2d 103, 111 (Del. Ch. 1986)).

C. Romiti's Argument for Self-Dealing and a Critique Thereof

1. Political Contributions to a Friend Are Not Self-Dealing

The first derivative suit proponent, Jonathan Romiti, urges that lawsuits for breach of the fiduciary duty are “the best way to reduce harmful political spending post-*Citizens United*.”³⁶⁵ He posits that a duty of loyalty claim might arise “if a director designates a particular sum of corporate money for a political advocacy group led by a close friend.”³⁶⁶ By way of example, Romiti points to a contribution from News Corporation (News Corp.) to the Republican Governor's Association (RGA) in 2010. According to News Corp.'s CEO, Rupert Murdoch, the company contributed to the RGA to support John Kasich, a candidate for governor of Ohio, because Kasich was Murdoch's close friend.³⁶⁷ A News Corp. spokesman later distanced the company from Murdoch's remarks, saying that the donation was made to support the RGA's “pro-business agenda.”³⁶⁸

As Romiti describes it, a shareholder's derivative claim against News Corp.'s board and/or Murdoch based on the RGA/Kasich contribution would be premised on the theory of self-dealing:

When directors abuse positions of power to further their own political or social views, shareholders could respond by alleging a violation of the duty of loyalty. . . . [D]irectors engaged in making self-interested political contributions using funds from a corporation's general treasury do not enjoy a presumption that their dealings are fair. Rather, it is incumbent upon those directors to prove the good faith of the transaction and to show that it is fair to the corporation and its shareholders.³⁶⁹

Unfortunately, Romiti is wrong. A corporate donation to “a political advocacy group led by a close friend” of the CEO is *not* a self-dealing claim subject to the exacting entire fairness standard. A transaction is only self-dealing when the director or her proxy obtains a personal *financial* benefit from the transaction³⁷⁰ that is material *to the director*.³⁷¹ Simply advancing

365. Romiti, *supra* note 31, at 762.

366. *Id.* at 759.

367. *See id.* at 763; Donald B. Tobin, *CEOs Shouldn't Use Corporate Treasury as Personal Political Piggy Bank* Roll Call (Nov. 1, 2010, 12:07 PM), <http://www.rollcall.com/news/-51140-1.html> (quoting Murdoch as stating that the contribution “had nothing to do with Fox News” because it “actually [was a result] of my friendship with John Kasich.”).

368. *See* Romiti, *supra* note 31, at 763.

369. *Id.* 760 (emphasis added). Although Romiti uses the term “self-interested” rather than “self-dealing,” his reference to the director's burden to show fairness suggests that he views the above scenario as an instance of self-dealing.

370. *See supra* text accompanying note 335.

the director's own "political or social views" is not sufficient unless there is a direct connection between the director's political views and her pocket-book.³⁷² Moreover, a "close friend" is not a proxy for a director, and as such, a court would not attribute any material financial gain of the close friend to the director.³⁷³

Romiti cites no case where a transaction with a friend was deemed to be self-dealing,³⁷⁴ and there appears to be none.³⁷⁵ Instead, Romiti seems to base his argument entirely on a quotation from an article by Professor David Yosifon.³⁷⁶ In the relevant article, Yosifon posits that:

371. See *supra* text accompanying note 337.

372. See BAINBRIDGE, *supra* note 72, at 319 (explaining that "when a director's allegedly conflicted interest grows out of nonfinancial considerations," the transaction is not self-dealing under the statute); CLARK, *supra* note 18, at 146, 148-49 (describing "mixed motives" situations as differing from traditional self-dealing in that, in "mixed motives" situation, a director has "some interest in a side effect" of the corporation's transaction with a third party, rather than a direct financial interest in the third party or the transaction itself); Margaret M. Blair & Lynn A. Stout, *A Team Production Theory of Corporate Law*, 85 VA. L. REV. 247, 299 (1999) (writing before *Stone* placed the concept of "bad faith" within the duty of loyalty and explaining that "the duty of loyalty," as traditionally understood – i.e., self-dealing – "does not apply" to "decisions that provide nonmonetary benefits to [directors] themselves at shareholders' expense," such as "donations to their favorite charities," which Dean Clark called "mixed motives" situations)(quoting CLARK, *supra* note 18, at 142); see also Hill & McDonnell, *supra* note 19, at 835 ("Courts recognize self-dealing . . . where a director . . . has clearly identifiable, specific monetary interests at stake in a decision that puts her own self-interest at odds with the interests of the corporation.").

373. Cf. Velasco, *supra* note 133, at 1242 ("[M]any types of conflict that a layperson might think would compromise a director's objectivity are not deemed to rise to the level of self-dealing. The most obvious is friendship and collegiality among the directors on a board.").

374. Romiti cites two cases, *Bellotti* and *Bayer*. See Romiti, *supra* note 31, at 760 nn.146-49 (citing *First Nat'l Bank v. Bellotti*, 435 U.S. 765, 795 (1978) and *Bayer v. Beran*, 49 N.Y.S.2d 2, 6 (N.Y. Sup. Ct. 1944)). Neither case supports Romiti's proposition. *Bellotti*, a Supreme Court corporate political speech case, addresses derivative lawsuits in passing and did not even involve an instance of self-dealing. 435 U.S. at 794-95. In *Bayer*, the court concluded that a corporation's transaction with the CEO's wife were self-dealing. 49 N.Y.S.2d at 9-10.

375. A research assistant searched Westlaw for such cases, to no avail.

376. See Romiti, *supra* note 31, at 760 nn.146, 149 (citing David G. Yosifon, *The Public Choice Problem in Corporate Law: Corporate Social Responsibility after Citizens United*, 89 N.C. L. REV. 1197, 1228-29 (2011)).

Romiti also makes a similar assertion elsewhere in note. See *id.* at 772 ("Delaware law requires that directors carry out their duties free from self-interested motives."). However, his citations there do not even purport to support his contention that a contribution in favor of a friend is self-dealing. The case that Romiti cites, *Lyondell Chemical Company v. Ryan*, 970 A.2d 235, 243-44 (Del. 2009), deals with bad faith, not self-dealing – and the second item that he cites there is a newspaper article.

[W]here directors spend on behalf of candidates who are family members or friends . . . then corporate law provides a remedy through shareholder derivative suits that put the onus on directors to demonstrate that “interested” transactions were entirely fair to the corporation and its shareholders.³⁷⁷

For support, Yosifon cites a well-known treatise by Professors James Cox and Thomas Hazen.³⁷⁸ But nowhere in the cited sections does the treatise say that a corporation transacting business with *friends* is a self-dealing transaction, subject to the onerous entire fairness standard rather than the protective business judgment rule.³⁷⁹ Indeed, some jurisdictions³⁸⁰ and the most recent version of the influential Model Business Corporation Act (MBCA) *explicitly* limit the definition of self-dealing to include transactions between a corporation and certain specified relatives or subsidiaries of a director – i.e., “related persons.”³⁸¹ Friends and pet projects are not included on the list of “related persons.”³⁸²

It is true that Delaware,³⁸³ and states adopting older versions of the MBCA,³⁸⁴ use the concept of “indirect” self-dealing rather than specific statutory definitions of “related persons.”³⁸⁵ As a result, in such states, transactions with friends are not specifically excluded as examples of self-dealing.

377. Yosifon, *supra* note 376, at 1229 (emphasis added). The ellipses in Yosifon’s quotation above remove the language “especially where such candidacies or projects are wholly irrelevant to or at odds with the corporate purpose.” *Id.* Setting aside its tautological nature, this caveat (which is not reflected in Romiti’s summary of Yosifon’s point) does make it more likely that the director in question has breached her duty of loyalty. However, the breach resulting due to this omitted language would *not* be self-dealing. A corporate political contribution that is “wholly irrelevant to or at odds with the corporate purpose” would be *waste*. See *supra* Part IV.A.2. The transaction would only constitute self-dealing if it *also* resulted in a material financial benefit to a director (or her proxy). See *supra* text accompanying notes 335-337.

378. Yosifon, *supra* note 376, at 1229 (citing JAMES D. COX & THOMAS L. HAZEN, CORPORATIONS § 10.09, at 202-05 (2d ed. 2003)).

379. Nor did several other well-known treatises reviewed by this author. See also Balotti & Hanks, *supra* note 164, at 982-83 (describing ways that corporate philanthropy constitutes “personal aggrandizement” for directors – but noting that none of these instances fall “squarely within what courts traditionally have regarded as a breach of the duty of loyalty” – i.e., self-dealing).

380. See, e.g., *supra* note 342 (Texas).

381. See MODEL BUS. CORP. ACT § 8.60(1) (2010) (defining self-dealing to include any transaction in which the fiduciary has a known “material financial interest” or in which a “related person” to the fiduciary has such an interest).

382. See § 8.60(5) (defining related person only to include the fiduciary’s spouse and several other relatives of the fiduciary).

383. See DEL. CODE ANN. tit. 8 § 144(a) (2010).

384. See MODEL BUS. CORP. ACT § 41 (1979).

385. See BAINBRIDGE, *supra* note 72, at 318; FREER & MOLL, *supra* note 94, at 276.

Further, unlike the recent version of the MBCA,³⁸⁶ Delaware's conflicted transaction statute does not preempt the common law.³⁸⁷ As a result, in theory a court could conclude that the common law deemed one friend to be a proxy for the other friend in the context of assessing whether a transaction constituted self-dealing.

However, this author is unaware of any case from any jurisdiction where a transaction between a corporation and a friend of a director was deemed to be self-dealing by that director – i.e., that a direct material financial benefit to *the friend* was deemed to be an indirect material financial benefit to *the director*.³⁸⁸ Indeed, a recent high-profile case – *In re the Walt Disney Company Derivative Litigation*³⁸⁹ – seemingly holds otherwise. In *Disney*, plaintiffs challenged a massive severance package for Michael Ovitz, the outgoing president of the Walt Disney Company, who had been hired by his alleged best friend – the company's CEO, Michael Eisner.³⁹⁰ In *Disney*, the plaintiffs proceeded on theories of waste and bad faith in large part because the court concluded that the case did not involve self-dealing.³⁹¹

386. See *id.* (FREER & MOLL, *supra* note 94), at 150-51 (discussing MODEL BUS. CORP. ACT sup-chapter F, §§ 8.60, 8.61); Comm. on Corporate Laws, *supra* note 342, at 1322 (“If a transaction is not a . . . conflicting interest transaction as defined in section 8.60, then [it] may not be enjoined . . . [as] a conflict of interest In that sense, subchapter F is . . . both comprehensive and exclusive.”) (italics omitted).

387. See *Marciano v. Nakash*, 535 A.2d 400, 404 (Del. 1987); Comm. on Corporate Laws, *supra* note 342, at 1322.

388. A review of cases and leading treatises reveals no such cases. A recent derivative suit against News Corp. that alleged, *inter alia*, that “Rupert Murdoch Advances His Political Agenda With Company Funds” recently settled before any court passed on the complaint. See Kevin M. LaCroix, *D&O Insurance to Fund Entire “Largest Ever” \$139 Million News Corp. Derivative Suit Settlement*, D & O DIARY (Apr. 23, 2013), <http://www.dandodiary.com/2013/04/articles/shareholders-derivative-litigation/do-insurance-to-fund-entire-largest-ever-139-million-news-corp-derivative-suit-settlement/>.

389. *Disney I*, 906 A.2d 27 (Del. 2006).

390. See *id.* at 35-36; Hill & McDonnell, *supra* note 19, at 850 (explaining that in *Disney*, “[t]here was no cognizable duty of loyalty breach” because “[n]o director or officer was on both sides of the table, no relative of a director or officer was being hired, and no other classic category of self-dealing . . . was at issue”); *id.* at 845-46 (explaining that according to the *Disney* court, “mere friendship” between Eisner and Ovitz “did not give Eisner a problematic interest in [Ovitz’s] compensation”).

391. In *Disney*, the court explained that bad faith was the better vehicle for addressing the situation where Eisner hired his good friend Ovitz because there was no “disabling conflicts of interest, such as a patently self-dealing transaction” at issue in the case. *Disney IV*, 907 A.2d 693, 760 n.487 (Del. Ch. 2005), *aff’d* 906 A.2d 27 (Del. 2006).

2. Self-Interested Motives Are Not Self-Dealing Transactions

In addition to arguing that political contributions to a friend constitute self-dealing, Romiti also argues that:

When . . . directors exploit their positions of power to further their own political or personal interests, this should be a plain violation of their fiduciary obligations Delaware law requires that directors carry out their duties free from self-interested motives. Subordinating the interest[] . . . in a company's growth in favor of a director's own political or social views is not only an abuse of the trust relationship necessary to the proper functioning of the corporation, but it is also a clear violation of Delaware law.³⁹²

However, this is simply wrong; or, at least, the problem is not an issue of self-dealing. Again, self-dealing occurs when the directors have a material *financial* interest in the transaction.³⁹³ It is not necessarily self-dealing for a director to act with a motive other than the corporation's best interests in mind.³⁹⁴ A director may act with mixed motives so long as she rationally believes that her *own* self-serving actions *also* serve the corporation's best interest or so long as her primary purpose is to serve the corporation's best interest.³⁹⁵ In sum, contrary to Romiti's assertion, Delaware law does not require that directors "carry out their duties *free from* self-interested motives." Rather, Delaware law requires that directors refrain from waste, self-dealing, bad faith, intent to harm the corporation, and the like.³⁹⁶

D. Are Some Corporate Political Contributions Nonetheless Self-Dealing?

If Romiti is urging that corporate political contributions *necessarily* constitute self-dealing transactions, he is simply wrong. However, he may be arguing that self-interested corporate political spending *can in some instances* constitute self-dealing. If so, he fails to develop the scenarios under which a political contribution is in fact self-dealing, because he fails to address the requirement that the transaction provide a material *financial* benefit to the director or proxy.

Similarly, if Professor Bainbridge means to urge that corporate political contributions *never* constitute self-dealing transactions, he is wrong. There

392. See Romiti, *supra* note 31, at 771-72 (emphasis added).

393. See *supra* text accompanying notes 335-337.

394. See *supra* text accompanying notes 379-391. Nor is it waste. See *supra* Part IV.A.

395. See *supra* text accompanying note 95.

396. However, if the directors make a contribution primarily for the purpose of advancing their own political views rather than the best interest of the corporation, this would constitute bad faith. See Leahy, *supra* note 43.

certainly are scenarios where a CEO causing her corporation to make a political contribution does indeed constitute self-dealing. To explore these scenarios, let us return to Professor Bainbridge's hypothetical.³⁹⁷

1. Can Corporate Giving *Ever* Be Self-Dealing?

On the bare facts presented by Professor Bainbridge – a CEO causes her corporation to make a “massive donation” to her alma mater – there is no basis to conclude that the CEO engaged in self-dealing. Even if the CEO receives a psychological boost from donating to the school that she holds dear, and even if that donation raises her standing in the community,³⁹⁸ courts simply will not recognize these emotional and social benefits as sufficient to overcome the presumption of the business judgment rule.³⁹⁹ What's more, even if the donation may result in some future benefit to the CEO – such as an improvement in her prospects of future employment as a business school professor at the university – no court is likely to deem such an uncertain future benefit as sufficiently material to render the donation “self-dealing.”

Yet, this does not mean that self-dealing could not possibly exist in the context of a charitable donation like the one hypothesized by Professor Bainbridge. Indeed, such a charitable contribution could easily constitute self-dealing, depending on the facts of the situation. This is easily demonstrated by adding just a few facts to Professor Bainbridge's hypothetical.

For instance, we could posit that the CEO has a *second* job as the chancellor of her alma mater. We could suppose further that, as head of the university, the CEO's compensation includes a bonus based on the success or failure of her fundraising efforts for the school. This would render the contribution a blatant example of self-dealing, because the CEO would be profiting *directly* from the corporation's massive gift to the university. Of course, this scenario is highly improbable, as positions as the CEO of a large corporation and president of a university are both presumably full-time jobs.⁴⁰⁰

397. See *supra* note 372 and text accompanying notes 335-337.

398. These are common motivations for corporate philanthropy. See Kahn, *supra* note 165, at 616-18 (discussing JOSEPH GALASKIEWICZ, SOCIAL ORGANIZATION OF AN URBAN GRANTS ECONOMY (1985)).

399. See *supra* note 372 and text accompanying notes 335-337.

400. However, it is not uncommon for a non-executive director to be the president of a university. See, e.g., *In re Goldman Sachs Grp., Inc. S'holder Litig.*, No. 5215-VCG, 2011 WL 4826104, at *10 (Del. Ch. Oct. 21, 2011) (Goldman Sachs donated \$200,000 to Brown University while its president served on the board). In such a case, the corporation's donation to the university would be self-dealing *for that director*, except in the highly unusual case that the university president is uncompensated. Cf. *In re Walt Disney Co. Derivative Litig.*, 731 A.2d 342, 359 (Del. Ch. 1998) (concluding that director, president of Georgetown University, was not dominated by CEO Eisner, despite that Eisner had personally donated over \$1 million to the university, in part because the director, a Jesuit priest, did not keep his director's fees), *aff'd in part, rev'd in part sub nom.* *Brehm v. Eisner*, 746 A.2d 244 (Del. 2000).

Since this *direct* self-dealing seems highly unlikely, let us imagine that the CEO in question has a spouse who happens to be the president of the CEO's alma mater. Now we have an obvious instance of *indirect* self-dealing, since the spouse is a proxy for the CEO. Yet, such a coincidence seems unlikely to occur in the real world.⁴⁰¹

Other, less direct (and perhaps less unlikely) scenarios also are possible. Suppose the CEO's spouse is not the president of the CEO's alma mater, but rather a tenured professor with an endowed chair. Assuming that the spouse's salary and benefits from the academic institution constitute the predominant portion of the spouse's compensation, this is nonetheless arguably an indirect self-dealing transaction. Here, although the CEO's spouse does not have an interest in the transaction at issue, the spouse's position at that academic institution certainly could be a material factor in the CEO's decision to cause the corporation to make the massive contributions to her alma mater. That is sufficient for self-dealing.

Other indirect (and even more realistic) examples of self-dealing abound. Let us hypothesize that the CEO's son – a mediocre student – is a junior in high school. The CEO's alma mater is prestigious, and its graduates gain access to a network of highly successful professionals. Admission is highly competitive. Further, assume that the CEO's status as an alumna, combined with her modest personal donations over the years, might have been sufficient to persuade the academic institution to admit Junior as a “legacy” were Junior a better student; unfortunately, Junior is simply *not* college material. On these facts, it seems plausible that the CEO's decision to donate to her alma mater could be influenced by the mere possibility of helping her offspring gain admission to a prestigious college. That is to say, the potential financial benefit to her son might be a material factor in the CEO's decision to cause the corporation to contribute to her alma mater.⁴⁰²

Hence, it is certainly *possible* that a charitable contribution would constitute a self-dealing transaction, and thereby allow plaintiffs to overcome the business judgment rule presumption. That is to say, it is *possible* that any particular charitable contribution will result in a material *financial* benefit to a director who causes the contributions to occur or to persons who are closely related to the director and therefore qualify as proxies. However, it will depend entirely on the facts.

401. Yet, it is not unheard of for a corporation to donate money to a charity headed up the CEO's spouse. For example, the Morrison Knudsen Corporation donated money to The Nurturing Network, a pro-life charity founded by the wife of then-CEO William Agee, while Agee was CEO. The money was funneled through the company's charitable foundation, of which Agee's wife was the president at the time. See Kahn, *supra* note 165, at 611-12.

402. Of course, the CEO could simply increase her own level of giving – like Disney CEO Eisner, who donated over \$1 million of his own money to Georgetown University, the alma mater of one of his sons. See *In re Walt Disney Co.*, 731 A.2d at 359. But why should a CEO reach into her own pocket when she can reach into the corporation's much deeper pocket?

2. Are Corporate Political Contributions *Typically* Self-Dealing?

Let us now concede for purposes of argument that, even if the situations hypothesized above are not rare, there is no reason to believe that such instances are common, either. Thus, absent empirical proof that corporate charitable contributions *commonly* implicate material *financial* interests of directors, let us accept that such contributions do not *typically* constitute self-dealing.

Therefore, to be fair to Professor Bainbridge, he undoubtedly meant that when a CEO causes the corporation to make a charitable donation, the contribution will not *typically* constitute self-dealing, because only in rare instances will a corporate donation to charity obviously benefit a clear proxy for the CEO like her spouse or child. Further, Professor Bainbridge surely assumed that the same is true for corporate political contributions.

But is the latter assumption correct? Are corporate political contributions like charitable donations in that they rarely implicate self-dealing? Or does the typical corporate political contribution differ from a charitable donation in that the former more plausibly constitutes self-dealing? That is to say, is a typical political contribution plausibly self-dealing despite that the typical charitable contribution is not? To investigate this question, let us return to Professor Bainbridge's hypothetical, but alter it slightly to reflect a political contribution.

a. Proxies and Indirect Self-Dealing

Assume that a CEO causes the corporation she commands to give a massive contribution to a Super PAC that supports a single candidate for state or federal office. On the face of this bare-bones hypothetical, there is no self-dealing. Even if we assume that the contribution promotes the CEO's personal political beliefs and helps her own preferred candidate win an election, this is nonetheless *not* self-dealing. There is no reason to believe that the political contribution results in a material *financial* benefit to the CEO that is not shared equally by the rest of the shareholders.

That said, we could easily add facts to the hypothetical (just as we did with a donation to the CEO's alma mater in the hypothetical above), to raise an obvious issue of direct self-dealing.⁴⁰³ Yet these sorts of situations, while

403. For example, the candidate that the Super PAC supports could be the CEO herself. This would be direct self-dealing. Or, the candidate could be the CEO's spouse or child – an example of indirect self-dealing. Further, in states like Delaware, with less specific self-dealing statutes, the candidate could perhaps even be a sibling or parent or in-law who does not live with the director. *See supra* notes 383-385 and accompanying text. *Cf.* Kesten, *supra* note 101, at 21 (describing a donation to “the CEO's sister's campaign” as an “obvious” conflict). Other, more realistic, examples of indirect self-dealing also abound. The CEO's spouse or child could be a salaried staffer for the Super PAC, or supporter of the candidate who hopes to obtain a job or political appointment if the candidate is elected.

possible, seem too fantastic to warrant much discussion. If it is rare for a corporate charitable donation to result in a material financial benefit to the CEO or her close relative, it is probably just as rare for a corporate political contribution to result in such a material financial benefit.⁴⁰⁴

b. Political Contributions Versus Charitable Donations:
Expectation of Financial Benefit

The more interesting question is: Does the *typical* political contribution differ from the *typical* charitable contribution in that the benefits accruing from the former are *regularly* material financial benefits while the benefits accruing from the latter are not? Even if political contributions do not regularly result in a direct or certain material financial benefit to the contributor, are they regularly made with the hope that an uncertain and/or indirect benefit will accrue to the contributor? If so, then when a director causes a corporation to contribute to her pet Super PAC, perhaps she does more than support a political candidate that espouses her own personal political views – perhaps she or her proxies stand, directly or indirectly, to gain a material financial benefit from the contribution.

To assess this question we must again inquire how the nature of political contributions differs from the nature of charitable donations. The question is simple: Is the *typical* political contribution less altruistic – and more often made with a personal financial gain in mind – than the *typical* charitable contribution? In light of some additional differences between charitable contributions and political spending, the answer is quite possibly “yes.”

i. Charity Is Supposed to Be Altruistic; Politics Need Not Be

First, charities are supposed to be altruistic ventures. The word “charity” essentially means “to help others.”⁴⁰⁵ As such, it is not ostensibly possible to charter a tax-deductible charitable organization⁴⁰⁶ with the purpose of advancing one’s own personal financial interests, or the personal financial interests of one’s family, to the exclusion of the best interests of the general

404. Caveat: since political views tend to run in families and politics often is a family business (e.g., the Bushes, Clintons, Doles, etc.), if the CEO is active in politics the CEO’s close relatives may tend to be active in the same party.

405. See *Definition of Charity*, MERRIAM-WEBSTER, <http://www.merriam-webster.com/dictionary/charity> (last visited June 15, 2014) (“1: benevolent goodwill toward or love of humanity; 2a: generosity and helpfulness especially toward the needy or suffering; also: aid given to those in need; b: an institution engaged in relief of the poor; c: public provision for the relief of the needy; 3a: a gift for public benevolent purposes . . .”).

406. Such organizations are governed by Section 501(c)(3) of the Internal Revenue Code.

public.⁴⁰⁷ Although one could create a charity that advances one's own interests along with the interests of others in need,⁴⁰⁸ the point of the charity must nonetheless be to help the public, not just its founder and/or her family. Further, when one explicitly creates a "social welfare" organization⁴⁰⁹ to help people who are similarly situated,⁴¹⁰ contributions to such organizations generally are *not* tax deductible (unless they are otherwise deductible, for example, as business expenses).⁴¹¹

The opposite is true for political parties. There is nothing untoward about founding a political party solely to serve the interests of its founders and/or its core members. For example, a group of workers are perfectly within their rights to form a party called the "Labor Party," the principal goal of which is to serve the interests of workers, not management or owners. Or a party could explicitly support only those policies that benefit its own constituents and explicitly reject policies that benefit the constituents of another party. For example, a party whose constituents include many wealthy, rural farmers but few members of the urban poor could explicitly support a bill to provide farm subsidies without including the food stamp provisions that dis-

407. See *Exemption Requirements: 501(c)(3) Organizations*, IRS, [http://www.irs.gov/Charities-&-Non-Profits/Charitable-Organizations/Exemption-Requirements-Section-501\(c\)\(3\)-Organizations](http://www.irs.gov/Charities-&-Non-Profits/Charitable-Organizations/Exemption-Requirements-Section-501(c)(3)-Organizations) (last visited June 15, 2014) ("To be tax-exempt under section 501(c)(3) of the Internal Revenue Code, an organization must be organized and operated exclusively for exempt purposes set forth in section 501(c)(3), and none of its earnings may inure to any private shareholder or individual."); *Exempt Purposes – Internal Revenue Code Section 501(c)(3)*, IRS, [http://www.irs.gov/Charities-&-Non-Profits/Charitable-Organizations/Exempt-Purposes-Internal-Revenue-Code-Section-501\(c\)\(3\)](http://www.irs.gov/Charities-&-Non-Profits/Charitable-Organizations/Exempt-Purposes-Internal-Revenue-Code-Section-501(c)(3)) (last visited June 15, 2014) ("The exempt purposes set forth in section 501(c)(3) are charitable, religious, educational, scientific, literary, testing for public safety, fostering national or international amateur sports competition, and preventing cruelty to children or animals. The term charitable . . . includes relief of the poor, the distressed, or the underprivileged; advancement of religion; advancement of education or science; erecting or maintaining public buildings, monuments, or works; lessening the burdens of government; lessening neighborhood tensions; eliminating prejudice and discrimination; defending human and civil rights secured by law; and combating community deterioration and juvenile delinquency.").

408. *E.g.*, a cancer survivor could create a charitable organization to assist cancer survivors.

409. Such organizations are governed by Section 501(c)(4) of the Internal Revenue Code.

410. *E.g.*, an Italian-American can create an organization to promote the interests of Italian-Americans.

411. See *Donations to Section 501(c)(4) Organizations*, IRS, [http://www.irs.gov/Charities-&-Non-Profits/Other-Non-Profits/Donations-to-Section-501\(c\)\(4\)-Organizations](http://www.irs.gov/Charities-&-Non-Profits/Other-Non-Profits/Donations-to-Section-501(c)(4)-Organizations) (last visited Mar. 21, 2014) ("Contributions to civic leagues or other section 501(c)(4) organizations generally are not deductible as charitable contributions for federal income tax purposes. They may be deductible as trade or business expenses, if ordinary and necessary in the conduct of the taxpayer's business.").

proportionally help benefit the urban poor (which traditionally have been included with farm bills).⁴¹²

Although modern political parties, wanting to win elections, often attempt to justify their policies by urging that they are best for society as a whole, this is not required by law or logic. Therefore, while there is no doubt that many candidates for office *claim* that their goals are quasi-charitable in nature, there is no *legal requirement* that a political party act charitably.

Since the purpose of eleemosynary organizations is to promote the *public* welfare, any material *financial* gain accruing to the director of the corporate donor (or the director's proxy) will be extremely indirect and tenuous. Even to the extent that management causes a corporation to donate to charity for management's benefit, the indirect benefits accruing to management from such a donation would seem less likely to be financial than the benefit to management from a political contribution. While the good publicity from a charitable contribution may help the corporation's bottom line, the CEO and her proxies are more likely to gain in terms of prestige and social recognition. While sitting on the charity's board, being recognized with an award, or obtaining social approval from one's peers are certainly self-interested reasons to cause a corporation to donate money, they are only indirectly likely to lead to financial benefits. Increasing the company's bottom line by giving to charity, and obtaining greater sales through good publicity, seem like far more uncertain paths to riches than investing that money in the corporation's business.

ii. Charities Do Not Hold the Reins of Power

Second, charities are not state actors. They therefore do not possess the coercive power of the state. They cannot raise armies (other than, perhaps, "salvation armies") or command police forces. They do not have the power to assess and collect taxes (as tithing is merely a moral obligation, not a legal one). As a result, while donations to support a charity will make the charity richer, and thereby make the charity's leaders more powerful, such donations do not have nearly the same effect as campaign contributions. Political contributions can lead to a candidate being elected to office and gaining power over the machinery of the state. Although this power is limited by laws and checked by the power of other elected officials, it is potent nonetheless. Election to a local office – be it prosecutor, sheriff, or even dogcatcher – provides the candidate with the ability to determine the outcome of many local events. Election to statewide office – such as governor or attorney general – or national office – such as United States Representative or Senator – results in the ability to determine events on an even grander scale. And election as Presi-

412. See, e.g., Ross Douthat, *The Farm Bill and the Common Good*, N.Y. TIMES (July 12, 2013), <http://douthat.blogs.nytimes.com/2013/07/12/the-farm-bill-and-the-common-good/> (criticizing the farm bill passed by the Republican-controlled House of Representatives, which did not include a food stamp bill).

dent of the United States clothes the elected person in immense power.⁴¹³ There is simply no comparison between the power wielded by elected officials – especially those in the executive branch – and the power wielded by leaders of non profit organizations of similar size and wealth.⁴¹⁴

As a result, the stakes are much higher when a corporation makes a political contribution than when a corporation makes a charitable donation. When management causes the corporation to make a charitable donation, one charity becomes richer and its leaders become more powerful. But when management causes the corporation to make a political contribution, management is supporting one candidate's bid to become clothed in the coercive power of the state.

The increased stakes for such contributions therefore magnifies the potential harm that can result from such contributions. If the agency cost problem manifests itself and management causes the corporation to make a contribution to a political candidate that favors management's interests over the interests of the shareholders, the harm to the shareholders could conceivably be worse than if management caused the corporation to make a charitable donation that favors the interests of management over the interests of the shareholders. In the latter instance, management is simply choosing to promote the general welfare in a way that promotes management's view of a better society as compared to the shareholders' view of a better society. But in the former instance, management could support the election of a candidate who could exercise the power of the state in a way that benefits management to the detriment of shareholders.

To provide a concrete example, let us make the reasonable assumption that the management of a large public company consists entirely of wealthy men and women. By contrast, let us assume that the individual shareholders (i.e., natural persons) of that company range from the very rich to the solidly middle class. If the wealthy executives of the company cause it to donate money to so-called "rich people's charities" – such as opera houses or art museums⁴¹⁵ – some middle class shareholders might be miffed, but will suffer little, if any, harm. Indeed, people of all classes enjoy opera and art museums, so the donation may simply open the doors of a rich person's world to the less wealthy by allowing the opera to charge less for performances and allowing the art museum to charge less for admission to its galleries. Thus, while some middle class shareholders might have preferred, on balance, that

413. See Joshua Zeitz, *Fact-Checking 'Lincoln': Lincoln's Mostly Realistic; His Advisers Aren't*, THE ATLANTIC (Nov. 12, 2012, 9:02 AM), <http://www.theatlantic.com/entertainment/archive/2012/11/fact-checking-lincoln-lincolns-mostly-realistic-his-advisers-arent/265073/>.

414. Anyone who equates the power of the two different types of leaders is confusing influence with power. See, e.g., Caroline Howard, *The 72 Who Rule the World*, FORBES (Oct. 30, 2013, 7:44 AM), <http://www.forbes.com/sites/carolinehoward/2013/10/30/the-worlds-most-powerful-people-2013/> (ranking leaders of non profit organizations and nation-states together on list of world's "most powerful people").

415. See BAINBRIDGE, *supra* note 72, at 437.

the corporation's money be spent in a different way, the donation to the arts is by no means at odds with their interests.

By contrast, if the wealthy company executives cause the corporation to contribute to a "rich person's" political candidate, and that candidate is elected, the result could be far worse for the middle class shareholders. That candidate might prefer policies that favor the rich over policies that favor the middle class. For example, that candidate might favor raising income taxes on the middle class and lowering income taxes on the rich. Or, the candidate might favor reduced public funding for education and large tax deductions for private school education, or reduced taxes on luxury goods and sales taxes on regular food and clothing.

Since political contributions are by their nature intended and allowed to be less altruistic than charitable donations, it is therefore at least plausible that the typical political contribution is motivated less by altruism than the typical charitable donation.⁴¹⁶ As a result, it is at least plausible that political contributions are regularly made with the hope that they will result in a material financial gain to the contributor – or, in the case of a corporation, to the director who causes the corporation to make the contribution.

3. Examples of Political Contributions that Might Be Self-Dealing

Next, let us consider some specific examples of political contributions that might constitute self-dealing. Let us start with "local" politicians who represent small, distinct constituencies. Is it plausible that a CEO who causes her corporation to donate money to a Super PAC that supports a candidate for the local zoning board could obtain a material financial benefit from that contribution? Yes, certainly. Even if we assume the contribution is not itself an unlawful bribe or gratuity, plausible scenarios abound where the CEO or her proxies might obtain a material financial benefit as a result of the zoning board candidate's election. For example, suppose the zoning board candidate ran on a platform of promoting a wholesale rezoning of a blighted area for redevelopment – and the CEO's immediate family is in the real estate business. Alternatively, suppose the zoning board candidate ran on a platform of using zoning laws to break up "red light" districts – and the CEO's family are slumlords whose properties will increase in value when the strip clubs and bong shops move to other parts of the cities and the neighborhoods again become friendly to families and upscale businesses.⁴¹⁷ Or, suppose the city

416. Of course, the altruistic or selfish nature of any particular donation will obviously depend on the specific facts of that donation. Some people may give charitable donations for entirely selfish reasons; some people might make political contributions for entirely altruistic reasons.

417. Many other possible situations exist where management's personal financial interests could diverge from that of most shareholders. *See, e.g.*, Michael A. Behrens, *Citizens United, Tax Policy & Corporate Governance*, 12 FL. TAX REV. 589, 590-91 (2012) (positing examples in which management and certain shareholders' financial

has a zoning regulation requiring that developers set aside a substantial portion of their development for parkland, and the zoning candidate ran on a platform of eliminating that requirement – and the CEO’s immediate family is in the business of developing new residential housing.

In each case, the CEO has caused the corporation to support a candidate in whose positions the CEO believes – but also, from whose platform the CEO or her family stands to gain financially. Thus, by causing the corporation to give money to the candidate, the CEO has increased her likelihood of receiving an actual, financial gain. If the potential gains are large enough and the likelihood of the contribution helping the candidate win is substantial, the CEO’s personal financial situation could influence her decision making – in other words, the potential financial benefit could be *material*.

Next, corporate political contributions made in support of a *national* political candidate: Could they result in (or at least increase the likelihood of) a financial benefit to a director? Again, the answer is yes. For example, suppose a CEO causes the corporation to give money in support of the campaign of a Democratic member of Congress (perhaps even the chairperson of an important budget subcommittee) who runs on a platform that includes expanding direct government support for “green technology” – and the CEO’s family owns a company that manufactures solar cells. Alternatively, suppose the CEO, who flies everywhere in a private jet provided free of charge by the corporation but who must pay for her own fuel for personal vacations, gives money to a Republican who opposes a proposal to substantially raise taxes on jet fuel. In each instance, the corporate contribution by no means guarantees that the CEO or her family will obtain a financial benefit. However, in each case, *if* the contribution is sufficiently large that it plausibly increases the candidate’s chance of being elected, and *if* the candidate’s chance of election plausibly increases the chance of the measure in question being enacted, it seems fair to conclude that the CEO’s decision regarding whether to make the contribution would likely be affected by her own financial interests – that is to say, that her potential *financial* gain from the contribution would be *material*.

Finally, is it possible that a CEO who causes the corporation to donate money in support of a presidential campaign stands to gain a material financial benefit from that contribution? Once again, the answer is yes. Suppose that the Democratic candidate for president is running on a platform of substantially raising taxes on wealthy Americans – in particular, on those people making over \$1 million per year. By contrast, the Republican candidate for president is running on a platform of lowering taxes for all Americans – but in particular, taxes that hit the wealthy (e.g., the estate tax), who the Republican candidate believes already pay more than their fair share of taxes.⁴¹⁸

interests would diverge on the declaration of dividends whether the tax on dividends should be high or low).

418. See, e.g., Kelly Phillips Erb, *Election Day Primer: Comparing the Obama and Romney Tax Plans*, FORBES (Nov. 3, 2012, 10:39 AM), <http://>

Suppose the CEO makes many millions of dollars per year (and presumably will leave a large estate to her children), so she stands to gain a substantial tax cut if the Republican, rather than the Democrat, is elected.⁴¹⁹ While it is possible that our CEO would support the Republican simply out of a shared belief about what is best for the nation, it would be difficult to argue that the chance to lower her own taxes is not material.⁴²⁰

The only question is whether or not the connection between a political contribution and the eventual election of a president – who, of course, cannot pass legislation by herself – is too uncertain and contingent to be sufficiently material.⁴²¹ Undoubtedly a president has more control over the legislative agenda than most ordinary senators or members of Congress. But in order to plausibly influence the outcome, a contribution in support of a presidential campaign must be much, much larger than is necessary to influence the outcome of a congressional election. Thus, in the probability times magnitude test,⁴²² these two phenomena may be a wash – unless, perhaps, the contribution is very large and the race is very close. Ultimately, this will be a question for the fact-finder, since materiality is predominantly an issue of fact.⁴²³ But it is certainly plausible that a jury (or, in the Delaware Chancery Court, a chancellor⁴²⁴) would conclude that a corporate political donation constitutes self-dealing by the corporation’s rich directors or officers, even if the contribution also plausibly benefits the corporation.⁴²⁵

www.forbes.com/sites/kellyphillipsrb/2012/11/03/election-day-primer-comparing-the-obama-and-romney-tax-plans/ (comparing Obama and Romney tax plans, including proposals for estate tax and taxing income over \$1 million); John D. McKinnon, *Study: Romney’s Tax Plan Hits Middle Class*, WASH. POST (Aug. 1, 2012, 9:01 AM), <http://blogs.wsj.com/washwire/2012/08/01/study-romneys-tax-plan-hits-middle-class/> (“A new study released Wednesday suggests that Mitt Romney’s tax plan would benefit the rich and hurt the poor and middle class.”).

419. See Erb, *supra* note 418.

420. Many other possible situations exist where management could have a different personal financial interest from that of certain shareholders. See, e.g., Behrens, *supra* note 417, at 590-91.

421. Cf. BAINBRIDGE, *supra* note 72, at 307 (“[A]s the director’s interest becomes more attenuated, an indirect transaction may not rise to the level of a legitimate conflict of interest.”).

422. See *supra* note 338 and accompanying text.

423. See *Pfeffer v. Redstone*, 965 A.2d 676, 685 (Del. 2009).

424. The Delaware Court of Chancery is a court of equity, and as such, the chancellors perform fact finding after bench trials. See Leo E. Strine, Jr., “*Mediation-Only*” Filings in the Delaware Court of Chancery: Can New Value Be Added by One of America’s Business Courts?, 53 DUKE L.J. 585, 588 (2003). However, the chancellors may in their discretion submit factual issues to be determined by a jury in the Delaware Superior Court. See DEL. CODE ANN. tit. 10, § 369.

425. As this Article was being edited for publication in early 2014, Professor James Kwak published an article that makes essentially this same point. See James Kwak, *Corporate Law Constraints on Political Spending*, 18 N.C. BANKING INST. 251, 276-77 (2013) (observing that the difference between the Obama and

E. The Charitable Donation Self-Dealing Cases That Weren't

There appears to be no judicial decision in which a director of a corporation caused the corporation to contribute to a political organization that resulted in a material financial benefit to an obvious proxy like a spouse or child.⁴²⁶ Nor has there been any decision involving any of the other potential examples of self-dealing political contributions discussed above.⁴²⁷ However, in the context of charitable giving, there are two closely analogous Delaware cases – *Theodora Holding Corp. v. Henderson*⁴²⁸ and *Kahn v. Sullivan*⁴²⁹ – in which a director caused the corporation to donate money to his “pet” charity (although, in neither case was the court willing to admit as much). These cases are instructive because in each case the court did not even address the issue of whether the director engaged in self-dealing.

In *Henderson*, a shareholder challenged a holding company’s donation of \$528,000 to a charitable foundation dominated by the corporation’s controlling shareholder.⁴³⁰ The Court of Chancery first held that charitable con-

Romney tax plans was worth “about \$600,000 per year” to a CEO with the median total compensation among CEOs of S&P 500 companies, and concluding that “[c]orporate donations that increase the chances of securing low individual income tax rates . . . provide a ‘personal financial benefit’ to . . . people responsible for the donations.”). Professor Kwak did not specifically address the issue of materiality. However, he nonetheless concluded that it is “unclear” whether Delaware courts will deem corporate political contributions to candidates who favor lower taxes as self-dealing, because such contributions are “an ancillary personal benefit [to directors] that is difficult to quantify.” *Id.* at 278. Subsequently, in a blog post, Professor Kwak agreed with this Article’s conclusion that, due to the attenuated nature of any benefit to the board, self-dealing claims based on corporate political contributions are “likely to fail in most circumstances, given the current attitudes of” the Delaware courts. James Kwak, *More on Wasting Shareholders’ Money*, THE BASELINE SCENARIO (Mar. 25, 2014), <http://baselinescenario.com/2014/03/25/more-on-wasting-shareholders-money/#comments>. Yet, Professor Kwak opined that “there is enough precedent . . . for the Delaware Chancery Court to uphold such a challenge, if one of the chancellors wants to.” *Id.* This author agrees: Materiality is essentially a question of fact, and the chancellors are the Chancery Court’s fact finders. *See supra* notes 423, 425. The issue is entirely in their hands.

426. A research assistant’s extensive searches on Westlaw disclosed no such cases.

427. Although the recent derivative suit against News Corp. involved allegations to this effect, there were not couched in terms of self-dealing and the case settled before any court passed on the complaint. *See* Jeff Bercovici, *News Corp. Shareholders in Class Action over Hacking*, FORBES (July 11, 2011, 10:47 AM), <http://www.forbes.com/sites/jeffbervovici/2011/07/11/news-corp-shareholders-in-class-action-over-hacking/>.

428. 257 A.2d 398 (Del. Ch. 1969).

429. 594 A.2d 48 (Del. 1991).

430. *Henderson*, 257 A.2d at 401. The foundation ran a summer camp for underprivileged boys. *Id.* at 402.

tributions were permitted generally under Delaware law,⁴³¹ and then decided that specific contributions should be upheld if they are reasonable.⁴³² In assessing whether the donation at issue was reasonable, the court analogized to the federal income tax deduction limit (then five percent of a corporation's gross income); the donation fell below this limit.⁴³³ The court also concluded that any loss of income to plaintiff was "far out-weighed" by the long-term benefit of the charitable donation, which helped "provid[e] justification for large private holdings."⁴³⁴ As a result, the *Henderson* court upheld the donation.⁴³⁵ In so doing, the court did not address whether the contribution to the controller's pet charity constituted indirect self-dealing.⁴³⁶

Kahn involved the art collection of Armand Hammer, CEO of Occidental Petroleum Corporation (Occidental), which was valued at \$300 to \$400 million.⁴³⁷ Occidental donated approximately \$85 million to build and fund the Armand Hammer Museum of Art and Cultural Center,⁴³⁸ which was to house Hammer's art collection upon his death.⁴³⁹ The Court of Chancery approved the donation, concluding that it was protected by the business judgment rule⁴⁴⁰ because the plaintiffs failed to prove that any of the directors had a personal financial interest or motive for entrenchment in the donation.⁴⁴¹ The court concluded that "[t]he business judgment rule . . . stands as an almost impenetrable barrier to the plaintiffs."⁴⁴² The court "reached this conclusion despite the absence of any proffered business purpose for the donation."⁴⁴³ Having concluded that the donation was a valid exercise of the

431. *See id.* at 404-05 (quoting, *inter alia*, DEL. CODE ANN. tit. 8, § 122(9)).

432. *See id.* at 405.

433. *See id.* The corporation's gross income for that year was \$19 million. *Id.*

434. *Id.* The court did not consider whether the donation furthered the holding company's business. *See id.*

435. *See id.*

436. To the contrary, the *Henderson* court rejected as dicta language from a prior New Jersey case stating "pet charities" might be actionable in a shareholder derivative lawsuit. *See id.* at 404 (discussing *A.P. Smith Mfg. v. Barlow*, 98 A.2d 581 (N.J. 1953), and reasoning while that the *Barlow* court "pointed out that there was no showing that the gift in question was made . . . to a pet charity in furtherance of personal rather than corporate ends, the actual holding of [*Barlow*] appears to be that a corporate charitable . . . gift to be valid must merely be . . . reasonable").

437. *Hammer II*, 594 A.2d 48, 51 (Del. 1991). The procedural posture of the case was somewhat unusual: the court was deciding whether a settlement (which it described as "meager") was "fair and reasonable" to the corporation. *Hammer I*, No. 10823, 1990 WL 114223, at *1, *5 (Del. Ch. Aug. 7, 1990). Thus, the court did not analyze the merits of the case, *per se*. Rather, the court considered the likelihood of plaintiffs' success on the merits at a time when both sides had agreed to settle. *See id.*

438. *Hammer II*, 594 A.2d at 54.

439. *See id.* at 51-52.

440. *See id.* at 48.

441. *See id.* at 60.

442. *Hammer I*, 1990 WL 114223, at *5.

443. Fisch, *supra* note 165, at 767.

board's business judgment, the court applied *Henderson*'s reasonableness standard and concluded that the donation was reasonable in size.⁴⁴⁴ The Delaware Supreme Court later affirmed the decision.⁴⁴⁵

Scholars have sharply criticized these cases for failing to deem the charitable contributions at issue as self-dealing.⁴⁴⁶ Moreover, *Kahn* is roundly criticized for applying the business judgment rule rather than the "reasonableness" standard used in *Henderson* to review charitable contributions.⁴⁴⁷ Although *Henderson* and cases from outside Delaware have suggested that a plaintiff might successfully challenge donations to a director's pet charity,⁴⁴⁸ *Kahn* may foreclose this possibility in Delaware.

The overarching concern of these commentators seems to be that donations to pet charities ought to be deemed self-dealing. If a charity created with the sole purpose of building an entire museum dedicated to housing the CEO's personal art collection is *not* a pet charity – then what *is*? As one commentator put it:

Although *Kahn* presents one of the more egregious cases of self-dealing masquerading as philanthropy, the courts refused to look behind the Occidental board's superficial justification of the expenditures in affording the transactions the presumptive protection of the business judgment rule.⁴⁴⁹

Yet, perhaps these scholars are wrong. Perhaps *Kahn* simply represents the Delaware courts' implicit decision to follow the same rule (despite the lack of a statutory basis for it) as other states that have statutorily exempted corporate charitable philanthropy from the business purpose requirement.⁴⁵⁰ If so, this simply means that charitable contributions are not subject to the *subjective* waste inquiry; such contributions should still be actionable if they constitute *objective* waste.

What's more, these cases – especially *Kahn* – may simply show that Delaware courts take seriously the rule that a plaintiff who alleges self-dealing must allege the defendant director (or a proxy) received a

444. See *Hammer I*, 1990 WL 114223, at *6; see also *Hammer II*, 594 A.2d at 61.

445. See *Hammer II*, 594 A.2d at 63.

446. See, e.g., Kostant, *supra* note 117, at 425-26 ("Delaware courts [have] tended to define self-dealing so narrowly that the duty of loyalty provided minimal protection to corporations and their constituents."); *id.* at 425, n.27 ("One notorious example occurred in *Kahn*[.]").

447. See Joo, *The Modern Corporation*, *supra* note 19, at 72, n.425 (criticizing *Kahn* for failing to explain why the business judgment rule applies to charitable contributions, particularly when *Henderson* reviewed a contribution for reasonableness).

448. See *A.P. Smith Mfg. Co. v. Barlow*, 98 A.2d 581, 590 (N.J. 1953); see generally Jayne W. Barnard, *Corporate Philanthropy, Executives' Pet Charities and the Agency Problem*, 41 N.Y. L. SCH. L. REV. 1147 (1997).

449. Fisch, *supra* note 165, at 767.

450. See *supra* notes 290-293 and accompanying text.

material *financial* benefit from the challenged donation. Hammer, who was donating his art collection to the museum, arguably did not derive a material financial benefit from the donation. Although the company's donation facilitated Hammer's own charitable gift to the museum, Hammer could have given his art away even in the absence of the corporate donation. Indeed, he had previously planned to donate his art collection to the Los Angeles County Museum, only to change his mind when the museum would not display the art as he desired.⁴⁵¹ Hence, the key benefit to Hammer from Occidental's donation to his pet charity was psychological: He wanted the public to see all of his art together as a *single* collection, with *his* name on it. On this theory, the board did not approve a self-dealing transaction by Hammer. Rather, it approved a charitable donation to his pet charity as a favor. This is simply *not* self-dealing.⁴⁵²

Therefore, it may be that the charitable donation cases are distinguishable and do not prevent a court from deeming a corporate political contribution to be self-dealing in the limited circumstances described above. In short, a court might plausibly conclude that a director who causes a corporation to make a typical political contribution in support of a candidate for public office – for example, a donation to a Republican candidate for president who will lower the director's taxes – stands to gain a material financial benefit as a result of the donation.

F. Why Self-Dealing is Often a Superior Approach to Waste

At this point, a plaintiff who wishes to file suit to challenge a corporate political contribution might wonder whether she should argue waste, self-dealing or both. While waste is a likely loser, self-dealing is no sure winner and will depend entirely on the plaintiff's ability to make a plausible argument, supported by particularized facts, that the corporation's directors or their proxies stood to gain a material financial benefit as a result of the political contribution. A brief comparison of the two causes of actions may therefore prove helpful to the potential plaintiff.

Let us return again to Professor Bainbridge's hypothetical, but modify it to reflect a plausible instance of self-dealing. A CEO causes her corporation to make a massive contribution to a Super PAC that devotes all of its funds to support the Republican candidate for president. A central plank in the party's platform, which that candidate ostensibly supports, is to lower taxes on people who make more than \$1 million per year. The CEO makes more than \$1 million per year, but not every shareholder makes more than \$1 million per

451. See Robert A. Jones, *Battle for the Masterpieces: The Armand Hammer-County Museum Deal: A Saga of Art, Power and Big Misunderstandings*, L.A. TIMES (May 22, 1988), http://articles.latimes.com/1988-05-22/magazine/tm-4568_1_armand-hammer-collection.

452. *Contra* Balotti & Hanks, *supra* note 164, at 984 (conflating the concepts of independence and financial interest, and therefore concluding that charitable donations that give rise to non-financial benefits could be self-dealing).

year. Which theory should the plaintiff advance: waste or self-dealing? To make the question more interesting, let us also assume that the CEO is an outspoken conservative (like Rupert Murdoch) who is best friends with the Republican presidential candidate, a former commentator for Fox News (someone like John Kasich).

The answer is still clearly self-dealing. As explained above, the waste standard would require that the contribution either be irrational (objective waste)⁴⁵³ or serve no corporate purpose whatsoever (subjective waste).⁴⁵⁴ Regardless of what one thinks of the Republican Party these days, there is simply no colorable argument that contributing to the Republican candidate for president is irrational. In the 2012 election, literally hundreds of thousands of people contributed to the Republican candidate for president, Mitt Romney, and to Super PACs that supported him.⁴⁵⁵ Further, more than sixty million people, or 47.2 percent of those voting, voted for the Republican candidate.⁴⁵⁶ Only the most rabidly partisan Democrat would argue that all of these people are irrational. There is simply no argument that a corporation's management could not rationally and in good faith believe that supporting Romney was in the corporation's best interest.

Arguing that the contribution serves no corporate purpose also is a sure loser – even if the CEO concedes (as Murdoch did) that she caused the corporation to spend money to advance *her own* political ideology and promote the candidacy of *her personal* friend. Undoubtedly, the CEO will hire a team of expensive lawyers to plausibly argue in court that the CEO's own political ideology *also* advances the best interests of the corporation and its shareholders – i.e., a “pro-business agenda.” The court must then decide whether to accept or reject the CEO's argument.

This is where the standard of review becomes critical. When assessing whether a transaction constitutes waste, the business judgment rule applies. Thus, the court must defer to a decision by the corporation's directors unless it is utterly irrational. As a result, when management argues that a transaction served the corporation's best interests and a plaintiff argues that it did not, the business judgment rule requires that the court defer to management. That is to say, in the absence of a conflict of interest by management that rises to the level of self-dealing, the business judgment rule requires that a court defer to management on the question of whether a transaction serves the corporation's best interest.⁴⁵⁷ Hence, the court will defer to the

453. See *supra* Part IV.A.1.

454. See *supra* Part IV.A.2.

455. See FEC, OFFICIAL 2012 PRESIDENTIAL ELECTION RESULTS (2013), available at <http://www.fec.gov/pubrec/fe2012/2012presgeresults.pdf>.

456. See Jeremy Ashkenas et al., *The 2012 Money Race: Compare the Candidates*, N.Y. TIMES, <http://elections.nytimes.com/2012/campaign-finance> (last visited June 15, 2014) (compiling data from Federal Election Commission).

457. See *Aronson v. Lewis*, 473 A.2d 805, 812 (Del. 1984); see, e.g., *Paramount Communc'ns, Inc. v. Time, Inc.*, 571 A.2d 1140 (Del. 1989); *Marsili v. Pac. Gas & Elec. Co.*, 124 Cal. Rptr. 313, 319 (Cal. Ct. App. 1975) (“[M]anage-

CEO's view that the political contribution serves the corporation's best interest and the plaintiff will lose.

The court's inquiry in the context of self-dealing is different – and possibly outcome determinative. First, the plaintiff must show that the political contribution was self-dealing by the powerful CEO – in other words, that she stood to gain a material financial benefit as a direct or indirect result of the contribution. This is a difficult burden, but it is plausible that the plaintiff will overcome the burden under these circumstances.⁴⁵⁸ Once the plaintiff establishes that the political contribution is self-dealing, however, the business judgment rule no longer applies and the court no longer defers to the CEO and her expensive lawyers. Instead, absent fully-informed disinterested director or shareholder approval of the transaction, the CEO has the burden of proving that the transaction was objectively fair to the corporation.⁴⁵⁹

This shift in the standard of review (from business judgment deference to entire fairness scrutiny) and burden of proof (from plaintiff to CEO) is the critical reason why a self-dealing claim is superior to a waste claim. Although the initial threshold of establishing self-dealing is difficult to surmount, once self-dealing has been established *it simply does not matter* that the CEO has a plausible argument that the self-dealing political contribution *also* benefits the corporation. In contrast to a waste claim, where the court must defer to any remotely plausible justification for the business decision proffered by the CEO, for a self-dealing claim the CEO can proffer plausible justifications to her heart's content; however, she bears the burden of proving to the court's satisfaction that the contribution did in fact, on balance, serve the best interests of the corporation.

VI. CONCLUSION

Ultimately, a close review of two potential theories that shareholders could employ to challenge corporate political contributions via a derivative lawsuit leaves us exactly where we started: the business judgment rule will

ment . . . [is] primarily responsible for judging whether a particular act or transaction is . . . expedient for the attainment of corporate purposes [A] court cannot determine that a particular transaction is beyond the powers of a corporation unless it clearly appears to be so as a matter of law.” (internal citations omitted). *Cf.* Stephen M. Bainbridge, *Corporate Philanthropy*, PROFESSORBAINBRIDGE.COM (July 28, 2008), <http://www.professorbainbridge.com/professorbainbridge.com/2008/07/corporate-philanthropy.html> (“[C]orporate charitable giving typically is defended on grounds that it produces . . . favorable publicity. In effect, charitable giving is simply another form of advertising. As such, it supposedly results in more business and higher profits. Who knows for sure if that is true? Maybe GM really does really sell more luxury sport utility vehicles because it sponsors PBS – or maybe not. But that is not the right question. The right question is: who decides? The board of directors or the courts?”).

458. *See supra* notes 418-420 and accompanying text.

459. *See supra* Part V.B.

defeat most such suits. In particular, waste claims are unlikely to succeed except in the rarest of circumstances, such as when a corporation supports a candidate who both cannot win and is extremely offensive to almost everyone. Self-dealing claims might succeed, but only when the directors of the corporation stand to obtain a material financial benefit that is not shared by the other shareholders. Yet, even then, any financial benefit to the director or her proxies will be indirect and highly uncertain, so plaintiffs will have to show that the financial benefit was sufficiently important in order to be material to the donor.

As a result, a shareholder who objects to a corporate political contribution should think twice before suing derivatively to challenge the contribution. However, if the shareholder does sue, she should consider advancing theories other than waste and self-dealing in order to overcome the business judgment rule⁴⁶⁰ – assuming, of course, that the business judgment rule applies at all.⁴⁶¹

460. See, e.g., Leahy, *supra* note 43.

461. But see Joseph K. Leahy, *Intermediate Scrutiny for Corporate Political Contributions* (working paper) (on file with author).