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Pandora's Box: Managerial Discretion and the Problem of Corporate Philanthropy

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PANDORA'S BOX: MANAGERIAL DISCRETION AND THE PROBLEM OF CORPORATE PHILANTHROPY

Faith Stevelman Kahn*

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INTRODUCTION: THE PROBLEM OF CORPORATE PHILANTHROPY

Public corporations¹ are not presently required to disclose any information regarding their donations² to charitable organizations,³ despite the existence of a broad disclosure mandate established by Congress⁴ and made applicable to public corporations through the federal securities regulations promulgated by the Securities and Exchange Commission (the "SEC").⁵ More particularly, the federal securities regulations do not require disclosure

1. This Article addresses corporate charitable giving by public corporations. Although the issues addressed herein have relevance to minority shareholders' interests in the context of close corporations, the latter context is sufficiently distinct to warrant separate consideration beyond the scope of this work.

2. As used herein, the terms "contribution(s)," "donation(s)," and "gift(s)" denote corporate transfers to charitable organizations having qualified for tax-exempt status under § 501(c)(3) of the Internal Revenue Code, 26 U.S.C. § 501(c)(3) (1994), when the transfer is made without the expectation of a direct quid pro quo. The use of the aforesaid terms is not meant to resolve the issues pertaining to the motivation or resultant effects of these contributions (which are the subject of Parts III through VI hereof). The terminological and analytic difficulty surrounding so-called "profit-maximizing" "charitable" contributions is explicitly addressed in Part VI.

3. Unless otherwise specified, all statutory references are to the Internal Revenue Code of 1986, as amended, I.R.C. §§ 1-9722 (the "Code" or "Tax Code"). Organizations that are exempt from federal income taxes (on income arising in connection with their exempt purposes) pursuant to § 501(c)(3) of the Code are commonly referred to as "charitable organizations" and "charities," and are so referred to herein. In order to qualify for charitable status under § 501(c)(3)—according to the express language of the Code—such organizations must be *organized and operated exclusively* to perform one of the charitable purposes enumerated in § 501(c)(3). These purposes include "religious, charitable, scientific, testing for public safety, literary, or educational purposes, or to foster national or international amateur sports competition . . . or for the prevention of cruelty to children or animals." I.R.C. § 501(c)(3) (1994). (Although "charitable" is one of the descriptive categories employed within § 501(c)(3), all the enumerated purposes identified above are commonly referred to in the aggregate as "charitable" purposes.) Additional requirements pertain to qualification under § 501(c)(3). Of particular relevance to the discussion in Part V, charitable organizations are prohibited by the express terms of § 501(c)(3) from participating in elections for public office and from attempting to influence legislation as a "substantial part" of their affairs. *Id.*

4. See Securities Act of 1933, 15 U.S.C. §§ 77a-77aa (1994); Securities Exchange Act of 1934, 15 U.S.C. §§ 78a-78ll (1994) (collectively herein, the "Securities Acts"). In particular, in § 14(a) Congress granted the Securities and Exchange Commission authority to regulate proxy voting "as necessary or appropriate in the public interest or for the protection of investors." 15 U.S.C. § 78n(a) (1994). The Securities Exchange Act also requires public companies to file periodic reports with the SEC, which reports present extensive, detailed corporate information. Securities Exchange Act § 13(a), 15 U.S.C. § 78m(a). In accordance with this mandate the SEC has enacted a broad-based system of mandatory corporate disclosure. See *infra* notes 5, 7.

5. The SEC has enacted a comprehensive, integrated disclosure system to fulfill the mandates of the Securities Acts. See Adoption of Integrated Disclosure System, Securities Act Release No. 33-6383, 24 SEC Docket (CCH) 1262 (Mar. 26, 1982).

of whether a corporation has made any charitable contributions,⁶ what the value of such contributions may have been, or which organizations may have received such contributions.⁷

6. The definition of corporate charitable contributions employed herein is based on that elaborated in § 170 of the Code (as is generally consistent with common usage, as well as the accepted definition within the states' corporate philanthropy laws). Section 170(a)(1) of the Code provides the basis for the deduction of charitable contributions both by individuals and by corporations. Section 170(c) defines the term "charitable contribution," providing in pertinent part:

Charitable contribution defined.—For purposes of this section, the term "charitable contribution" means a contribution or gift to or for the use of

(2) A corporation, trust, or community chest, fund or foundation—

(A) created or organized in the United States . . . or under the law of the United States, any State, the District of Columbia, or any possession of the United States;

(B) organized and operated exclusively for religious, charitable, scientific, literary, or educational purposes, or to foster national or international amateur sports competition (but only if no part of its activities involve the provision of athletic facilities or equipment), or for the prevention of cruelty to children or animals;

(C) no part of the net earnings of which inures to the benefit of any private shareholder or individual; and

(D) which is not disqualified for tax exemption under section 501(c)(3) by reason of attempting to influence legislation, and which does not participate in, or intervene in (including the publishing or distributing of statements), any political campaign on behalf of (or in opposition to) any candidate for public office.

I.R.C. § 170(c) (1994). Contributions that relate to a taxpayer's business, but that are made with a "reasonable expectation of financial return commensurate with the amount of the transfer" may be deductible for the taxpayer as business expenses under § 162—instead of as charitable contributions under § 170. See Treas. Reg. § 1.170A-1(c)(5) (1996).

7. The S-K regulations prescribe the specific informational content of the narrative portions of shareholder proxy statements and SEC filings. 17 C.F.R. §§ 229.10–915 (1996). There is no provision of the S-K regulations that specifically calls for disclosure of corporate charitable contributions as a general matter. However, disclosure of contributions structured as "charitable awards" is required pursuant to Item 402(g) of S-K. *Id.* § 229.402; see Executive Compensation Disclosure, Release No. 33-6962, 34-31327, 57 Fed. Reg. 48,126 (Oct. 21, 1992); *infra* notes 171–176. Outside of charitable awards, it is unlikely that disclosure of corporate charitable contributions would be required pursuant to the existing S-K disclosure requirements. For example, disclosure would be required under Item 303 of S-K ("Management's Discussion and Analysis of Financial Condition and Results of Operations") only if the donations were so substantial in size as to materially adversely affect the corporation's overall financial position. 17 C.F.R. § 229.303(3) (1996). Because many public companies have tens of millions of dollars in annual earnings, millions of dollars are contributed to charity without triggering this disclosure standard.

For the SEC's requirements applying to financial statement presentation and disclosure, see Regulation S-X, *id.* §§ 210.1–12. In particular, see *id.* § 210.5.03(b)(9) ("Non-operating Expenses") (requiring explicit, separate presentation of "material amounts included under miscellaneous income deductions" (emphasis added)). Because there is no absolute standard of materiality, even in a narrow, quantitative sense, corporations have interpreted this requirement loosely, and have generally eschewed making any disclosure of their charitable contributions.

Disclosure requirements beyond the federal securities regulations, including generally accepted accounting principles,⁸ also fail to redress this informational failure.⁹ With the exception of contributions arising from separately constituted corporate foundations,¹⁰ corporations are free to make gifts to charitable organizations without creating any public record of the amount of such gifts or the identities of the recipients. While many corporations voluntarily make some anecdotal disclosure of their contributions—either directly to shareholders (most commonly in the annual report)¹¹ or in the popular media (especially where public relations benefits are anticipated)—corporate managers are unlikely to permit disclosure of gifts that might appear self-serving or prove controversial.

Compounding the significance of this informational failure is the fact that state corporation laws have adopted an extraordinarily laissez-faire approach to corporate charitable giving.¹² As described below in Part II,

8. The most relevant is ACCOUNTING FOR CONTRIBUTIONS RECEIVED AND CONTRIBUTIONS MADE, Statement of Financial Accounting Standards No. 116 (Financial Accounting Standards Bd. 1993). FAS-116 does not require corporations' financial statements to state expressly the amounts of any charitable contributions made.

9. Moreover, even a highly motivated shareholder could not compel a charitable organization to disclose the names of corporate contributors. Privacy interests and First Amendment rights of free association protect organizations from compelled disclosure of the identities of contributors or members, absent a compelling state interest. See *NAACP v. Alabama*, 357 U.S. 449 (1958); cf. *Buckley v. Valeo*, 424 U.S. 1, 64-68 (1976) (per curiam) (upholding constitutionality of FECA's mandatory disclosure and reporting provisions). In addition (except in the case of private foundations), the Code specifically exempts the names of contributors from the information that charitable organizations are required to make public. I.R.C. § 6104(b) (1994). For discussion of the principal sources of charitable contributions information, see *infra* note 22.

10. Private foundations (including corporate foundations—i.e., foundations established and funded by corporations) are themselves charitable organizations qualified under § 501(c)(3) of the Code. (Private foundations are to be distinguished from the class of "public charities" described under § 509(a)(1)-(4) of the Code.) Private foundations are subject to numerous requirements in addition to those under § 501(c)(3). For example, Chapter 42 of the Code imposes certain taxes on foundation investment income, as well as regulatory excise taxes under §§ 4940-4945. Most importantly for our purposes, private foundations are required to disclose both to the IRS and to the public detailed information regarding their finances and affairs on their annual exempt organization returns (the "Form 990-PF") pursuant to § 6033(c). Public charities are not required to submit such detailed information to the IRS. See I.R.C. § 6033(a), (b) (1994). For discussion of the extensive rules pertaining to corporate foundations, see Lauren Watson Cesare, *Private Foundations and Public Charities—Definition and Classification*, 296-3d Tax Mgmt. (BNA) (1992). See also JAMES J. FISCHMAN & STEPHEN SCHWARZ, *NON-PROFIT ORGANIZATIONS: CASES AND MATERIALS* 580-66 (1995).

11. See 17 C.F.R. § 240.14a-3(b) (1996).

12. The regulation of corporate internal affairs and the definition of corporate powers has been traditionally a matter left to the individual states. Therefore, it is state law that defines the power of business corporations to contribute to charity. Certain corporate legal scholars have ar-

the current laws represent the rejection of an earlier regulatory tradition in the states' approach to corporate charitable giving. In stark contrast to their legislative antecedents, the modern corporate philanthropy statutes impose neither substantive limitations nor procedural safeguards on corporate charitable contributions. Most importantly, the modern statutes have abrogated the requirement that corporate charitable contributions be made for the purpose of benefiting the donor corporation.¹³ In rejecting shareholder wealth maximization as the lodestar of managerial decision-making, the modern philanthropy laws depart from the traditional framework of state corporation law.¹⁴ This departure from the traditional normative concerns of corporate law is more dramatic for the fact that the modern laws fail to supply an alternative analytic framework to govern corporate charitable giving.¹⁵ Therefore, in promulgating the modern philanthropy provisions, the states have acted to authorize genuinely philanthropic corporate contributions, while they have affirmatively declined to regulate corporate charitable giving.

Thus, corporate charitable giving exists in a relative regulatory vacuum. The absence of substantive regulation in the states, in conjunction with the absence of a disclosure requirement under the federal securities regulations, reflects an outmoded and speciously simplistic view of corporate charitable contributions. Such contributions have been regarded as "merely a form of advertising," or alternatively, corporate "pocket change" benefiting the community. This Article provides a reconsideration

gued that state corporation law has universally abandoned the role of protecting shareholders. The debate has therefore turned to the appropriateness and efficacy of implementing federal standards of corporate governance. The classic writings are William L. Cary, *Federalism and Corporate Law: Reflections upon Delaware*, 83 YALE L.J. 663 (1974), which argues in favor of implementing federal standards, and Ralph K. Winter, Jr., *State Law, Shareholder Protection, and the Theory of the Corporation*, 6 J. LEGAL STUD. 251 (1977), which argues against implementation.

13. The states' elimination of the benefit-to-the-business requirement is discussed *infra* Part II.B.

14. The model of the corporation as an engine of shareholder wealth maximization is central to corporate law and mainstream corporate legal scholarship. See, e.g., ALI, PRINCIPLES OF CORPORATE GOVERNANCE: ANALYSIS AND RECOMMENDATIONS § 2.01 (1994). For an alternative perspective, see MARGARET M. BLAIR, OWNERSHIP AND CONTROL: RETHINKING CORPORATE GOVERNANCE FOR THE TWENTY-FIRST CENTURY (1995). See also PROGRESSIVE CORPORATE LAW (Lawrence E. Mitchell ed., 1995).

15. Of course, state legislators have had an interest in facilitating increased corporate charitable contributions in order to offset, in some measure, the burdens of taxation. See *A.P. Smith Mfg. Co. v. Barlow*, 98 A.2d 581, 589 (N.J. 1953) ("In encouraging and expressly authorizing reasonable charitable contributions by corporations, our State has not only joined with other states in advancing the national interest but has also specially furthered the interests of its own people who must bear the burdens of taxation resulting from increased state and federal aid upon default in voluntary giving.").

of the contemporary dimensions of corporate charitable giving as it bears on shareholders' rights¹⁶ and corporate law paradigms.¹⁷

Accordingly, Parts III through VI analyze the diverse causes and explanations for corporate charitable contributions and relate them to corporate legal norms. This analysis proceeds under the headings of: (i) managerial self-interest; (ii) corporate social responsibility; (iii) politicized philanthropy; and (iv) profit-maximizing charitable contributions. First, as described in Part III, in the absence of any form of accountability, corporate managers are apt to use their control over corporate charitable contributions to confer benefits on themselves, rather than to benefit the firm or the community. When managers use the firm's donations to pursue their personal philanthropic objectives, such donations represent a form of agency costs, and are inconsistent with the fiduciary obligations imposed by law. Second, as discussed in Part IV, when donations are made in the name of corporate social responsibility (as opposed to traditional commercial objectives), corporate managers have failed to offer adequate justification for their exclusive control over such decisions. Third, as described in Part V, corporate charitable contributions to politicized nonprofit organizations represent an increasingly significant form of corporate political speech. Such contributions, especially when they are made in the absence of disclosure, jeopardize the free speech and associational interests of corporate shareholders.¹⁸ Finally, as discussed in Part VI, although corporate executives increasingly tout the "strategic benefits" accruing from corporate

16. Because corporate contributions are funded from corporate profits, they are paid for—and therefore of special concern to—corporate shareholders. Nevertheless, a corporation's charitable contributions may frequently be of interest to nonshareholder constituencies as well (e.g., customers, employees, and the public). In practice, if firms are required to disclose their contributions in reports to shareholders or SEC filings, nonshareholder constituencies will also gain greater access to this information. (In light of the fact that shareholders fund corporate contributions (at least those that do not result in a net benefit for the firm), it is ironic that significant solicitude has been paid to *employees'* charitable preferences—through the establishment of employee matching grant programs, for example—but not to shareholders'.)

17. The central thesis of this Article is that the separation between ownership and control in the modern public corporation, in combination with an overly laissez-faire system of state and federal regulation in the area of corporate philanthropy, has created the potential for gross managerial abuse of shareholders' property and speech interests. See ADOLF A. BERLE, JR. & GARDINER C. MEANS, *THE MODERN CORPORATION AND PRIVATE PROPERTY* 68 (1932) ("[I]n the corporate system, the 'owner' of industrial wealth is left with a mere symbol of ownership while the power, the responsibility and the substance which have been an integral part of ownership in the past are being transferred to a separate group in whose hands lies control.").

18. Because the business corporation is regarded as a private body, shareholders' liberty interests do not obtain federal constitutional dimensions. However, the classification of business corporations as private entities does not diminish the gravity of shareholder coercion in regard to nonconsensual corporate political speech in my opinion. For further discussion, see *infra* Part V.

contributions, without disclosure there is no means to assess whether the firm's gifts have been structured according to value-maximizing criteria. In addition, the inherently contradictory nature of profit-maximizing charitable contributions deserves further consideration.

The absence of substantive regulation, in combination with the absence of a disclosure requirement, has meant that corporate senior executives have had a blank check to make corporate charitable contributions independent of both business objectives and shareholder preferences. In no other area of corporate affairs do managers enjoy the same degree of discretion with such a concomitant lack of accountability.¹⁹ As a response to this failure of accountability, this Article argues that the SEC should amend the federal securities regulations to require corporations to routinely disclose to their shareholders accurate and comprehensive information about the corporation's charitable contributions.²⁰ In particular, both the aggregate total and the individual amounts of the firm's charitable gifts, the identities of recipient nonprofit organizations, and the existence of any shared directors on the boards of the corporation and the charities receiving its contributions²¹ should routinely be disclosed to shareholders. In particular, the SEC should require that summary information be presented in the annual report, while affording shareholders a right to obtain a comprehensive, detailed report of the company's charitable contributions upon request.

While disclosure is not a panacea, obligatory disclosure of contributions information is likely to benefit shareholders in several respects. Required disclosure is likely to deter corporate managers from using corporate contributions to pursue narrow, personal objectives, because it will require them to sacrifice a portion of their professional capital if they are unable to justify their firms' philanthropic practices according to established shareholder preferences or accepted commercial norms. Secondly, requiring disclosure of corporate contributions is a first step in democra-

19. For instance, managerial discretion in the area of traditional corporate political activity is cabined by the operation of the Federal Election Campaign Act ("FECA") and other laws and regulations. For an overview of FECA's requirements, as they relate to corporate expenditures, see *infra* notes 246-263.

20. Corporations already maintain detailed records of their charitable contributions in order to support the deductibility of such contributions under § 170. See Treas. Reg. § 1.170A-13 (1996) ("Recordkeeping and return requirements for deductions of charitable contributions."). Therefore, SEC-mandated disclosure of contribution data should not impose any significant additional information-gathering costs on corporations.

21. For a discussion of the "corporate governance" problems raised by common directors serving on the board of the corporation and the charities receiving its contributions, see *infra* note 133 and accompanying text.

tizing the debate over corporate social responsibility, so that shareholders—who fund such expenditures—may be afforded a greater role in elaborating how, when, and according to what criteria the firm should allocate its philanthropic capital. Thirdly, disclosure will afford shareholders the option to withdraw their investment if they are opposed to the corporation's politicized charitable contributions, or to voice their opposition through various forms of shareholder activism. Finally, disclosure will afford both analysts and shareholders alike the opportunity to assess the profit-maximizing claims made in regard to corporate contributions, and will facilitate scholarly progress in the study of corporate philanthropy.

I. A BRIEF QUANTITATIVE AND PRACTICAL SURVEY OF CORPORATE PHILANTHROPY

A. Quantitative Perspectives

Corporate charitable contributions amount to several billion dollars in aggregate on an annual basis.²² Direct corporate grants and grants by cor-

22. Because there is widespread misunderstanding regarding the availability of corporate contributions information, I will describe the principal sources of this data. Since 1936, the Internal Revenue Service (the "IRS") has compiled and published statistical information on corporate charitable contributions. These figures are made publicly available by the IRS, on an aggregated and company-blind basis, in a volume entitled *Statistics of Income, Corporation Income Tax Returns* (the "SOI"). Unfortunately, there is a substantial delay in the publication of the SOI, which seriously compromises the usefulness of this data. For example, the most recent corporate contributions figures available in the SOI are for 1993. The SOI's corporate charitable contributions figures represent the total dollar valuation assigned to direct corporate contributions to qualified charitable organizations for which a deduction under § 170 has been claimed in the year (together with carryovers), including transfers to corporate foundations. (To avoid double counting, the SOI data does not reflect corporate foundations' transfers to "third-party" charitable organizations.) Despite certain technical caveats, as well as a substantial delay in its publication, the SOI has been the single most important source of quantitative information on corporate charitable contributions, providing the basis of almost all econometric study and general quantitative analysis. See CHARLES T. CLOTFELTER, *FEDERAL TAX POLICY AND CHARITABLE GIVING 195-96* (1985). As mentioned above, the crucial shortcoming of the SOI data, in relation to corporate shareholders' interests, is that the SOI does not present any contribution data on a company-specific basis. Its findings are therefore of no use to shareholders (or anyone else) interested in studying the philanthropic behavior of particular firms.

The other important source of data on corporate philanthropy is a joint survey conducted annually by the Council for Aid to Education (the "CFAE") and The Conference Board. These survey results are published annually in the organizations' separate reports. The CFAE's data is published by the American Association of Fund-Raising Counsel (the "AAFRC") in its annual report entitled, *Giving USA*. The Conference Board publishes its annual report on corporate charitable contributions under its own name. In these cases, too, the data is presented on a company-blind basis. There are slight methodological differences between these three reports, leading to slight discrepancies between the figures reported therein. Because of their greater

porate foundations totalled \$7.4 billion in 1995,²³ without including contributions arising from cause-related marketing, corporate special-event sponsorships, or corporate public affairs departments.²⁴ Nontraditional corporate "assistance" expenditures are also unreflected in the \$7.4-billion charitable contributions figure.²⁵ The vast majority of corporate charitable contributions, approximately 75%, are made directly by corporations, as opposed to through corporate foundations.²⁶ Cash predominates as the most popular currency for corporate contributions. Cash transfers have typically constituted more than 80% of the total value of corporate contributions, with the remainder representing donations of products, property, and equipment.²⁷ Although there are no established sources of company-specific data,²⁸ the IRS publishes aggregated contributions data based on industry classifications.²⁹ From this data we know that certain industries—especially pharmaceuticals; food, beverage, and tobacco; petroleum, gas, and mining; and telecommunications companies—have consistently been among the largest corporate contributors.³⁰

timeliness, the figures presented in the text are based on the CFAE and The Conference Board's survey results.

23. AAFRC TRUST FOR PHILANTHROPY, GIVING USA 1996: THE ANNUAL REPORT ON PHILANTHROPY FOR THE YEAR 1995, at 89 (1996) [hereinafter GIVING USA 1996]. Although \$7.4 billion is unquestionably a substantial sum, it should be recognized that corporate contributions represent only a small fraction of total annual charitable contributions. For 1995, which was roughly typical of previous years, they represented 5.1%. *Id.* Individuals are by far the largest class of contributors, being responsible for about 80 cents of every dollar annually contributed to charity. *Id.* at 55. Nevertheless, corporate contributions appear to function as a bellwether for contributions from other sources, and are thus regarded by some as having importance exceeding their individual amounts.

24. *Id.* at 89. For a discussion of contributions arising from cause-related marketing programs and corporate special-event sponsorships, see *infra* Part VI.

25. AUDRIS D. TILLMAN, THE CONFERENCE BD., CORPORATE CONTRIBUTIONS, 1994, at 15 (1995) [hereinafter CORPORATE CONTRIBUTIONS, 1994].

26. GIVING USA 1996, *supra* note 23, at 89. According to Foundation Center and CFAE data for 1994, corporate foundations' grants accounted for \$1.6 billion out of a total of \$6.9 billion in corporate charitable contributions. See also AAFRC TRUST FOR PHILANTHROPY, GIVING USA 1995: THE ANNUAL REPORT ON PHILANTHROPY FOR THE YEAR 1994, at 79 (1995) [hereinafter GIVING USA 1995].

27. The Conference Board reported the 1995 statistics, which reflect a slight decrease in cash giving in comparison to recent years: 78% cash, 19% corporate product, and 3% property and equipment. AUDRIS D. TILLMAN, THE CONFERENCE BD., CORPORATE CONTRIBUTIONS IN 1995: AN ADVANCE REPORT 8 (1996) [hereinafter CORPORATE CONTRIBUTIONS IN 1995].

28. See *supra* note 22.

29. See, for example, U.S. INTERNAL REVENUE SERV., STATISTICS OF INCOME, 1993—CORPORATION INCOME TAX RETURNS 1993.

30. According to The Conference Board's figures for 1995, the most heavily contributing industries were (1) pharmaceutical companies, \$325 million, (2) food, beverage, and tobacco companies, \$211 million, and (3) petroleum, gas, and mining companies, \$165 million. CORPORATE CONTRIBUTIONS IN 1995, *supra* note 27, at 6.

Notwithstanding methodological variations³¹ and incomplete data,³² there is widespread agreement that corporate contributions have increased substantially over the past twenty years³³ despite inconsistent trends in corporate profits.³⁴ Recent estimates put corporate charitable giving for 1975 at \$3.72 billion (in "constant" or inflation-adjusted dollars).³⁵ The \$7.4 billion figure for 1995 thus represents double the sum of twenty years earlier. Assessing the magnitude of corporate charitable contributions, one commentator observed that the \$6.5-billion aggregate corporate contributions figure of the late 1980s was on par with the entire annual U.S. foreign aid budget at that time.³⁶

31. Variations exist in regard to statistical sampling techniques, companies represented (public-only or public and private), carryovers from year to year, and the inclusion of corporate transfers to corporate foundations versus foundation payments to third-party charities, for example. Both *Giving USA* and The Conference Board's annual reports include detailed descriptions of their research methodologies.

32. Researchers have persistently complained about inadequate disclosure of corporate charitable contributions data, describing the resultant informational gaps as impediments to their analysis. See, e.g., AAFRC TRUST FOR PHILANTHROPY, *GIVING USA 1992: THE ANNUAL REPORT ON PHILANTHROPY FOR THE YEAR 1991*, at 25 (1992) [hereinafter *GIVING USA 1992*] ("Nonprofit managers, their donors, and researchers who study them would also benefit from accurate reporting and access to accurate information about the sector."); STEVEN R. NEIHEISEL, *CORPORATE STRATEGY AND THE POLITICS OF GOODWILL* 8-9 (1994) ("The majority of corporations do not want the public to know how much they are contributing and to whom they are contributing. Reliable data are therefore very difficult to obtain."); see also JAMES T. BENNETT, *PATTERNS OF CORPORATE PHILANTHROPY* #5, at 10 (1989) ("It is highly disturbing that many corporate managers are so secretive about the distribution of company funds for public affairs purposes; in many cases even shareholders are denied access to such information."). Further evidence that many firms resist releasing this data upon shareholders' requests is provided by corporations' efforts to exclude shareholder proposals (under the federal proxy system) calling for such disclosure. See *infra* note 223.

33. In addition to gross dollar analysis, corporate giving is also analyzed as a percentage of pretax corporate income. The average rate of corporate contributions as a percentage of corporate income was 0.82% in 1975; it was 1.24% in 1995. *GIVING USA 1996*, *supra* note 23, at 90. The highwater mark was reached in the mid-1980s, when giving briefly exceeded 2% of pretax income. Interestingly, although total corporate giving has increased on a gross dollar basis since 1992, on a percentage of income basis, giving has decreased during this period. This partly reflects the increases in corporate profits occurring during the previous few years. *CORPORATE CONTRIBUTIONS, 1994*, *supra* note 25, at 11. Such average statistics hide substantial discrepancies among individual firms, of course. For example, various groups of business organizations in major cities have established "Five Percent" and "Two Percent" clubs to encourage corporate contributions at such levels. KENNETH A. BERTSCH, *INVESTOR RESPONSIBILITY RESEARCH CTR., CORPORATE GIVING IN THE REAGAN YEARS 1* (1985).

34. For an illustration of comparative rates of corporate contributions and corporate profits, see AUDRIS D. TILLMAN, *THE CONFERENCE BD., CORPORATE CONTRIBUTIONS, 1993*, at 13 (1994).

35. *GIVING USA 1996*, *supra* note 23, at 88. The contributions data derived from *Giving USA* and presented in the text is presented in constant dollars.

36. Usha C.V. Haley, *Corporate Contributions as Managerial Masques: Reframing Corporate Contributions as Strategies to Influence Society*, 28 J. MGMT. STUD. 485, 485 (1991).

Examining the pattern of contributions over this period in closer detail, increases are represented as being continuous between 1975 and 1987.³⁷ Thereafter, beginning in the late 1980s, a period of stagnation occurred.³⁸ This stagnation, which amounted to a series of incremental decreases when inflation was taken into account, had been regarded as continuing through the mid-1990s. Research reports published in 1995 indicated that giving had slowed, and incrementally decreased in light of inflation between 1988 and 1994.³⁹ However, researchers have recently altered their estimates of corporate contributions levels in the early to mid-1990s. Reports based on data through 1995 suggest that the total contributions figures for 1993 and 1994 had previously been underestimated, so that the magnitude and duration of the decline had been overstated.⁴⁰ *Giving USA 1996* indicated that contributions increased in both current and constant dollars in 1993, 1994, and 1995.⁴¹ Contributions for 1995 represented a 4.56% increase over the prior year measured in constant dollars (7.5% in current, unadjusted dollars).⁴² And companies responding to The Conference Board's survey for 1995 predicted that moderate increases in corporate philanthropic giving would continue throughout 1996 and 1997.⁴³

Furthermore, analysts have revised their view of the relationship between traditional corporate charitable contributions and contributions arising from corporate public affairs and marketing budgets. In reports issued in 1995, commentators suggested that marketing-oriented, "strategic" giving was supplanting traditional corporate philanthropy.⁴⁴ In contrast, *Giving USA 1996* indicated that there may be a synergistic effect between traditional corporate giving and public affairs and marketing-oriented con-

37. *GIVING USA 1996*, *supra* note 23, at 88.

38. *Id.* But see Hayden W. Smith, *Corporations Are More Generous Than You Think*, *CHRON. PHILANTHROPY*, Oct. 22, 1991.

39. *GIVING USA 1995*, *supra* note 26, at 77.

40. *Giving USA 1995* reported that contributions had failed to keep pace with inflation for seven consecutive years. *Id.* at 77.

41. *GIVING USA 1996*, *supra* note 23, at 88.

42. *Id.*

43. *CORPORATE CONTRIBUTIONS IN 1995*, *supra* note 27, at 3-4.

44. *GIVING USA 1995*, *supra* note 26, at 77. At a press conference announcing the AAFRCs charitable contributions figures for 1994, the chairman of the AAFRC stated: "Traditional giving, directed by a philanthropy staff and the interests of executive officers, is giving way to more strategic and less statistically observable programs overseen by financial officers and housed in marketing and public affairs departments." AAFRC Trust for Philanthropy, *Voluntary Contributions to Non-Profits Continue to Rise, Individual Contributions Lead the Way, Corporate Giving Going Through Changes, Affecting Level of Corporate Donations* (May 25, 1995) (press release, on file with author) (emphasis added).

tributions, so that both forms of corporate giving are seen to be increasing.⁴⁵ In addition to the traditional forms of corporate contributions, corporations continue to make "corporate assistance expenditures," including subsidizing employee volunteering and executive consulting programs, the use of corporate facilities and services, and below-market transactions (including commercial loans)—all of which, again, are not reflected in the \$7.4 billion contributions figure.⁴⁶

B. The Role of Corporate Senior Executives

While in certain corporations the contributions function has been decentralized, in most public corporations senior executive officers still exert extraordinary influence over the size of gifts and the selection of beneficiary organizations. Trends in contributions-based marketing and strategic alliances with corporate public affairs departments have affected the administration of corporate charitable contributions in certain instances,⁴⁷ but a host of studies and commentaries attest to the continued control and influence exerted by senior corporate executives in relation to their firms' philanthropic practices.⁴⁸

45. GIVING USA 1996, *supra* note 23, at 89.

46. The Conference Board reported the value of such "corporate assistance expenditures" reported by survey respondents at \$157 million for 1994, \$186 million for 1993, and \$99 million for 1992. CORPORATE CONTRIBUTIONS, 1994, *supra* note 25, at 15. For further commentary, see Kenneth B. Davis, Jr., *The Discretion of Corporate Management to Do Good at the Expense of Shareholder Gain—A Survey of, and Commentary on, the U.S. Corporate Law*, 13 CAN.-U.S. L.J. 7 (1988), and, though not as timely, Phillip I. Blumberg, *Corporate Responsibility and the Social Crisis*, 50 B.U. L. REV. 157 (1971), both of which discuss the variety of channels for corporate altruism and the sources of legal authority therefor.

47. See Craig Smith, *The New Corporate Philanthropy*, 72 HARV. BUS. REV., May-June 1994, at 105.

48. NEIHEISEL, *supra* note 32, at 54 ("CEO influence is important not only where we might expect—at the level of goal setting—but it is also deep in that it extends to even determining specific beneficiaries. This is quite extraordinary given the size of the contributions function relative to other corporate functions."). (Neiheisel's work also emphasized the importance of the professional contributions staff.) A number of studies assay the power that senior executive officers and corporate directors retain over corporate contributions. See, e.g., JAMES F. HARRIS & ANNE KLEPPER, THE CONFERENCE BD., CORPORATE PHILANTHROPIC PUBLIC SERVICE ACTIVITIES (1976) (finding that top management plays a major role in setting the goals, priorities, and budget levels of the contributions function); KATHRYN TROY, THE CONFERENCE BD., THE CORPORATE CONTRIBUTIONS FUNCTION (1982) (contributions managers reported meeting with their CEOs on at least a monthly basis and rated the CEOs influence on program content and grant size as about a four on a five-point scale); Arthur H. White & John Bartolomeo, *Corporate Giving: The Views of Chief Executive Officers of Major American Corporations*, COUNCIL ON FOUNDS., May 1982, at 49, 50 (reporting that 81% of respondents surveyed indicated that the CEO had total or a large degree of influence over budgets and 68% said that the CEO had a large degree of influence in selecting specific recipients). (These studies are cited in NEIHEISEL, *supra*

C. Corporate Charitable Foundations

In contrast to direct corporate grant-making, certain firms have established separate charitable foundations to administer a portion of their philanthropic giving.⁴⁹ The principal function of these foundations—which are themselves charitable organizations qualified under § 501(c)(3)—is to disseminate the donor corporations' grants to third-party charitable organizations.⁵⁰ Private foundations are subject to special regulatory requirements and penalties, in addition to those under § 501(c)(3).⁵¹ Most significantly for our purposes, private foundations are required by the IRS to file a detailed informational return, the "Form 990-PF," and to make it available for inspection by third parties.⁵² The Form 990-PF indicates the individual amounts of the foundation's grants, and the identities of the recipients. Such required disclosure of foundation-based corporate grant-making contrasts markedly with the absence of disclosure in regard to direct corporate grant-making.⁵³

note 32, at 53–55.) See also Richard I. Morris & Daniel A. Biederman, *How to Give Away Money Intelligently*, HARV. BUS. REV., Nov.–Dec. 1985, at 151, 153 (“[Chief executive officers’] peers approach them constantly to support pet causes, and they reciprocate. A company’s full contributions budget can easily be committed in this way, and large slices of the CEO’s time are consumed in the process.”). For discussion of the philanthropy laws’ construction of decisional authority in regard to corporate contributions, see *infra* note 95 and accompanying text.

49. For an overview of key Code provisions pertaining to corporate foundations, see *supra* note 10 and the citations therein. For discussion of the historical development and public policy controversies surrounding private foundations, see, for example, COMMISSION ON FOUNDATIONS AND PRIVATE PHILANTHROPY, FOUNDATIONS, PRIVATE GIVING AND PUBLIC POLICY: REPORT AND RECOMMENDATIONS OF THE COMMISSION ON FOUNDATIONS AND PRIVATE PHILANTHROPY (1970).

50. See *supra* note 10.

51. See Cesare, *supra* note 10.

52. See I.R.C. § 6033(c) (1994). However, it should be noted that the usefulness of such foundation disclosure is compromised by the relative inaccessibility of the Form 990-PFs. Foundations are required to allow inspection of Form 990-PFs at their premises, but are not required to copy them or to allow them to be removed from their premises. See *id.* § 6104(d). The logistical problems historically associated with obtaining the informational returns of nonprofit organizations are discussed in GIVING USA 1992, *supra* note 32, at 28–29. On July 30, 1996, Congress enacted the Taxpayer Bill of Rights 2, Pub. L. No. 104-168, 110 Stat. 1452 (1996), which (among other changes) revised § 6104(e) to make Form 990 reports of public charities readily available to individuals upon request (and payment of a small fee). Curiously, the legislation did not affect private foundations’ filings (the Form 990-PF), so that corporate foundations’ reports remain relatively inaccessible.

53. The Form 990-PF disclosure requirement pertaining to private foundations’ affairs grew out of the public controversy that surrounded corporate foundations’ activities in the late 1960s. This controversy led to various investigations by private commissions and a congressional response thereto in the Tax Reform Act of 1969. See *supra* note 49. The absence of regulation in the area of direct corporate grant-making may represent a classic catch-22: The absence of a dis-

While distinct patterns and rules pertain to foundation-based corporate grant-making,⁵⁴ it is important to recall that corporate foundations are not the source of most corporate charitable contributions. As mentioned previously, approximately 75% of all corporate contributions are made on a direct basis.⁵⁵ Also significant is the fact that even where firms have established a separate foundation, a substantial portion of their donations have continued to be made on a direct basis.⁵⁶ No rule *requires* a corporation to disseminate its gifts through its charitable foundation merely because such a foundation has been established. Thus, where confidentiality is considered important, a firm may simply elect to make any "sensitive" contributions directly, thus avoiding a disclosure requirement.

Furthermore, the establishment of a corporate foundation need not curtail the influence of a corporation's senior officers. It is common practice for a company's high-level officers to serve on the board of directors of the foundation, or to closely monitor the foundation's affairs.⁵⁷ Therefore, the existence of corporate charitable foundations has largely functioned to recapitulate the issues pertaining to corporate grant-making—as they relate to shareholders' interests—on another institutional level.

In conclusion, in light of the absence of meaningful substantive standards or other mechanisms of accountability, the contemporary legal critique of corporate charitable giving must address a situation in which corporate executives maintain control over billions of dollars of corporate (and corporate foundation) resources which they may allocate to charitable entities independent of commercial considerations and according to their own pleasure.

closure requirement may be based on the relative absence of information—which may explain the absence of attention paid to the subject. It is also possible to make a public choice-oriented interpretation of the confidentiality and permissiveness that characterize the legal posture toward corporate charitable contributions; i.e., politicians derive benefits from corporate gifts to politicized charitable organizations serving their policy objectives, see *infra* Part V, and from any reduction in taxes attributable to voluntary corporate charitable support, and are thus unlikely to advocate measures intended to increase oversight in this area.

54. A thorough treatment of foundation-based corporate grant-making and its significance vis-a-vis legal policy is beyond the scope of this Article. For an analysis of the economic aspects of corporate charitable foundations' affairs, see Natalie Jeanette Webb, *Company Foundations and the Economics of Corporate Giving* (1992) (unpublished Ph.D. dissertation, Duke University).

55. See *supra* note 26.

56. Webb, *supra* note 54, at 44.

57. *Id.* at 65–71. A particular example is supplied by Mary Cunningham Agee's appointment to the presidency of Morrison Knudsen Corporation's charitable foundation. See Brian O'Reilly, *Agee in Exile*, *FORTUNE*, May 29, 1995, at 51, 56.

II. THE STATES' DECISION NOT TO REGULATE CORPORATE PHILANTHROPY

Over the course of this century, the states' approach to corporate charitable giving has undergone a complete about-face. At the turn of the century, in light of the operation of the *ultra vires* doctrine, the pervasive statutory silence concerning corporate charitable contributions was interpreted by the courts as prohibiting true corporate *philanthropy*. By mid-century, the majority of states had enacted laws that validated corporate philanthropic authority, but these statutes typically imposed substantial limitations and requirements on the practice of corporate charitable giving. After mid-century, these "regulatory" philanthropy laws were universally repealed in favor of open-ended enabling laws. These modern laws license truly philanthropic corporate giving; furthermore, in light of the statutory history preceding them, they must be regarded as reflecting a decision on the part of the state legislatures to forego the *regulation* of corporate charitable giving. But in failing to supply any objective standards or safeguards to govern corporate executives' decisions in this area, the modern corporate philanthropy laws have failed to protect shareholders' best interests.

A. The Legal Background of the Modern Philanthropy Provisions

1. The Ultra Vires Problem

From the late nineteenth century through the early twentieth century, the most pressing legal question concerning corporate charitable contributions was whether businesses had the legal authority to make them.⁵⁸ Under the doctrine of defined corporate powers, corporations were regarded as having only such powers as were granted by the state and reflected in the

58. See, e.g., *Brinson Ry. v. Exchange Bank*, 85 S.E. 634 (Ga. Ct. App. 1915); *McCrary v. Chambers*, 48 Ill. App. 445, 452-53 (1892) (directors of bank were without authority to contribute to a fund collected for purpose of retaining manufacturing firm within city's limits, despite indirect benefits that might be obtained by company and community generally); *Davis v. Old Colony R.R.* 131 Mass. 258 (1881) (finding railroad company's guarantee for payment of music festival's expenses unlawful, despite probability that company would benefit from the festival). As Phillip Blumberg noted, these decisions did not involve gifts to established charitable organizations, and are thus distinguishable from the modern corporate philanthropy decisions. See Blumberg, *supra* note 46.

corporation's charter.⁵⁹ All other acts were "ultra vires"—literally "beyond the powers" of the corporation.⁶⁰ Thus, charitable expenditures by business corporations were originally regarded as "waste" because, prior to the 1930s, almost all the states' incorporation statutes failed to include corporate philanthropic authority within the corporate powers enumerated therein.⁶¹

2. Incidental Powers as Authorization for Contributions

In the initial process of legal liberalization, various courts relied on the notion of "incidental corporate powers"⁶² to uphold the legality of nontraditional expenditures when it could be demonstrated that the corporation, and not merely the surrounding community in general, would foreseeably

59. For an early treatment of the ultra vires doctrine in the area of corporate philanthropy, see Samuel Davis, *The Application of the Doctrine of Ultra Vires to Expenditures of Corporations Outside the Usual Course of Business—Some Elementary Principles Recalled*, 1 B.U. L. REV. 99 (1921). See also *Hyams v. Old Dominion Co.*, 93 A. 747, 752 (Me. 1915) ("[C]orporate powers are limited to those expressly granted and incidental implied powers necessary to carry into effect the powers so expressly granted."). For discussion of the early contributions cases, see Blumberg, *supra* note 46, at 168-73; Theodore W. Cousins, *How Far Corporations May Contribute to Charity*, 35 VA. L. REV. 401 (1949); Davis, *supra* note 46, at 57-64; and J.J. Marticelli, Annotation, *Power of a Business Corporation to Donate to a Charitable or Similar Institution*, 39 A.L.R.2d 1192 (1955).

60. The longevity of the ultra vires concern in the context of corporate charitable contributions is reflected in the fact that as late as 1953, in the landmark case of *A.P. Smith Manufacturing Co. v. Barlow*, the New Jersey Supreme Court specifically addressed itself to the question of Smith corporation's legal authority to make the charitable gift. *A.P. Smith Mfg. Co. v. Barlow*, 98 A.2d 581 (N.J. 1953). And, of course, the ultra vires doctrine explains the rhetorical posture of the modern corporate philanthropy laws, which speak to the matter of corporate power expressly.

61. See *infra* note 66.

62. The classic description of the scope of incidental corporate powers is provided in *Steinway v. Steinway & Sons*, 40 N.Y.S. 718, 720 (Sup. Ct. 1896): "If that act is one which is lawful in itself, and not otherwise prohibited, is done for the purpose of serving corporate ends, and is reasonably tributary to the promotion of these ends, in a substantial, and not in a remote and fanciful, sense, it may fairly be considered within charter powers." From the perspective of incidental corporate powers, foreseeable financial benefits validated the legality of contributions (and other corporate acts), because the corporation's fundamental purpose was to maximize profits. See *Dodge v. Ford Motor Co.*, 170 N.W. 668, 684 (Mich. 1919) ("The difference between an incidental humanitarian expenditure of corporate funds for the benefit of employees, like the building of a hospital for their use, and the employment of agencies for the betterment of their condition, and a general purpose to benefit mankind at the expense of others is obvious A business corporation is organized and carried on primarily for the profit of the stockholders.").

benefit therefrom.⁶³ Nevertheless, the incidental powers doctrine represented an infirm legal footing for corporate philanthropy: Differing interpretations of the directness of the required benefits gave rise to substantial variation in the interpretation of the scope of permissible versus impermissible contributions.⁶⁴ In addition, the relative infrequency of litigation in the area meant that the earlier, more conservative holdings retained their precedential stature in many jurisdictions. Thus, throughout the first several decades of the twentieth century, there was substantial variation among the state jurisdictions in the law governing corporate charitable giving.

3. Early Legislative Prescriptions

Uncertainty regarding the legal authority for corporate charitable giving was regarded as inhibiting the practice of corporate philanthropy in some measure.⁶⁵ In response to this uncertainty, state corporate philanthropy law underwent yet another evolutionary step. Starting from around 1920, several states enacted philanthropy provisions as part of their corpo-

63. Charitable giving is described as an incidental corporate power in *Hutton v. West Cork Railway*, 23 Ch. D. 654, 673 (1883) (Bowen, J.): "[C]harity has no business to sit at boards of directors [as] charity. There is, however, a kind of charitable dealing which is for the interest of those who practice it, and to that extent and in that garb . . . charity may sit at the board but for no other purpose." See also *Richelieu Hotel Co. v. International Military Encampment Co.*, 29 N.E. 1044 (Ill. 1892); *Virgil v. Virgil Practice Clavier Co.*, 68 N.Y.S. 335 (Sup. Ct. 1900). The liberal interpretation of incidental corporate powers is exemplified by *Armstrong Cork Co. v. H.A. Meldrum Co.*, 285 F. 58 (W.D.N.Y. 1922), which upheld the legality of the corporation's commitment to fund the business curriculum at a local college and university on the grounds that the business might have benefited therefrom, notwithstanding the company's intervening bankruptcy.

64. See Ray Garrett, *Corporate Donations to Charity*, 4 BUS. LAW. 30 (1948); George D. Gibson, *Corporate Contributions to Charity and Enabling Legislation*, 14 BUS. LAW. 439 (1959) ("The old cases requiring that public gifts be 'reasonably incidental to the carrying on of the company's business for the company's benefit' or 'reasonably tributary to the promotion of those [corporate] ends' are among the most strained, technical and contradictory doctrines of the law, which should be gladly interred and forgotten." (footnotes omitted)).

65. See Miguel A. de Capriles & Ray Garrett Jr., *Legality of Corporate Support to Education: A Survey of Current Developments*, 38 A.B.A. J. 209 (1952) (expressing the need for continued statutory reform in order to legitimate and facilitate increased levels of corporate giving). Of course, the continued prevalence of the incidental powers doctrine (and thus the direct benefit requirement) represented a substantial legal impediment to the validation of corporate philanthropy at the national level. See Garrett, *supra* note 64, at 28-39 (describing certain contemporary corporate giving initiatives as resting "solely upon public approval and the current general acceptance of the idea by stockholders" rather than on secure legal grounds).

rations codes. By 1949, thirteen states and Hawaii had passed statutory provisions expressly licensing certain corporate charitable contributions.⁶⁶

Nevertheless, with Texas' unqualified corporate philanthropy provision as the exception,⁶⁷ the philanthropy statutes enacted prior to mid-century were highly prescriptive in nature, imposing substantial requirements and limitations on corporate charitable contributions.⁶⁸ For example, the early statutes almost universally required express board of director approval to authorize corporate contributions.⁶⁹ The laws frequently limited the permissible amount of annual corporate contributions

66. These states include Texas (1917), Ohio (1920), New York (1923), Tennessee (1925), New Jersey (1930), Massachusetts (1933), Michigan (1935), Missouri (1937), Delaware (1941), Maryland (1945), North Carolina (1945), Pennsylvania (1945), and Virginia (1947). Hawaii enacted a provision in 1947. (Illinois had enacted a contributions provision in 1917, but until 1949 it applied only to wartime donations.) For discussion of the early statutes, see Gibson, *supra* note 64, at 434; Bert S. Prunty, Jr., *Love and the Business Corporation*, 46 VA. L. REV. 467 (1960); F. EMERSON ANDREWS, *CORPORATE GIVING* app. C (Transaction Publishers 1993) (1952) ("Permissive Legislation in the States and Territories"). I have relied on Andrews' statutory appendix for the citations to the early philanthropy laws that are presented herein. (The reader is directed to these laws for the full statutory citation and for a noteworthy treatment of the early history of corporate charitable giving practices.) For additional citations, see Garrett, *supra* note 64, at 34-39. For further commentary on the development of corporate philanthropy, see RICHARD EELLS, *CORPORATION GIVING IN A FREE SOCIETY* (1956); MARION R. FREMONT-SMITH, *PHILANTHROPY AND THE BUSINESS CORPORATION* (1972); Peter Dobkin Hall, *Business Giving and Social Investment in the United States*, in *PHILANTHROPIC GIVING* 221 (Richard Magat ed., 1989). Also of relevance is JAMES W. HURST, *THE LEGITIMACY OF THE BUSINESS CORPORATION IN THE LAW OF THE UNITED STATES, 1780-1970* (1970).

67. Law of Feb. 13, 1917, Ch. 15, 1917 Tex. Gen. Laws 25.

68. A good example is provided by New York's first (extra-wartime) contributions provision, enacted in 1923. Appearing in Chapter 25 of New York's General Corporation Law, it provided: § 45. Expenditures for social and economic benefit. Nothing contained in this chapter or in any other law shall be deemed to make it unlawful for any corporation or joint-stock association to cooperate with other corporations and with natural persons in the creation and maintenance of instrumentalities conducive to the Betterment of the social and economic conditions under which such corporation or joint-stock association is operating, and its directors or trustees may appropriate and expend for such purposes such reasonable sum or sums as they may deem expedient and as in their judgment will contribute to the protection of the corporate property and tend to promote the interests of the corporation and its stockholders.

CAHILL'S CONSOLIDATED LAWS OF NEW YORK 785 (James C. Cahill ed., 1923).

69. Board approval was required in the laws enacted by Ohio (1920), New York (1923), Tennessee (1925), New Jersey (1930), Massachusetts (1933), Missouri (1937), Delaware (1941), Maryland (1945), North Carolina (1945), and Virginia (1945). ANDREWS, *supra* note 66. In contrast, board approval was not explicitly mandated under Texas' (1917) or Michigan's (1933) statutes. *Id.* Pennsylvania's law, enacted in 1945, provided that contributions could be made to the extent provided for in the corporation's bylaws or "by resolution of its shareholders." *Id.*

by establishing a maximum level of contributions within the exclusive discretion of the board, with larger gifts being permissible in the absence of a shareholder veto.⁷⁰ Pennsylvania's and Hawaii's early philanthropy laws required *shareholder* approval for corporate contributions.⁷¹ Some states required corporations to make donations to charities located nearby the business' operations, thus imposing a loose geographic version of the common law's benefit-to-the-business requirement.⁷² Many states also imposed a requirement that the company's contributions be made in con-

70. For example, New York's wartime contributions provision, enacted in 1918, provided directors with the following authority:

That during the continuance of the war any corporation organized under the laws of this state may co-operate with other corporations and with natural persons in the creation and maintenance of instrumentalities conducive to the winning of the war, and its directors or trustees may appropriate and expend for such purposes such sum or sums as they may deem expedient and as, in their judgment, will contribute to the protection of the corporate interests, provided that whenever the expenditures for such purposes in any calendar year shall in the aggregate amount to one per centum on the capital stock outstanding, then, before any further expenditure is made during such year for such purposes by the corporation, ten days' notice shall be given to the stockholders in such manner as the directors or trustees may direct of the intention to make such further expenditure, specifying the amount thereof, and if written objection be made by stockholders holding twenty-five per centum or more of the stock of the corporation, such further expenditure shall not be made until it shall have been authorized at a stockholders' meeting.

Law of Apr. 16, 1918, ch. 240, § 1, 1918 N.Y. Laws 885. Ohio (1920) and New Jersey (1930) enacted philanthropy provisions (which were not limited to wartime contributions) containing a similar shareholder-veto term. ANDREWS, *supra* note 66. New York repealed the above statute in 1923 and enacted a more general philanthropy law, which did not contain the shareholder veto term.

71. Pennsylvania's earliest law (1945) required that firms' philanthropic contributions be sanctioned by the corporation's bylaws or, otherwise, "by resolution of its shareholders." ANDREWS, *supra* note 66. Hawaii's 1947 statute provided simply that donations "may be authorized by the affirmative vote of the holders of a majority of the stock of any such corporation." *Id.*

72. For example, New York's 1923 statute authorized contributions to "instrumentalities conducive to the betterment of the social and economic conditions *under which such corporation or joint-stock association is operating.*" CAHILL'S LAWS OF NEW YORK, *supra* note 68, at 785 (emphasis added). Similarly, Massachusetts' statute, enacted in 1933, provided as follows:

Every corporation organized under the laws of this commonwealth and doing business or operating therein may, by vote of its directors, or of its officers having the powers of directors, contribute such sum or sums of money as said directors or officers may determine to be reasonable to any general fund being raised by a relief committee or agency approved by the commissioner of public welfare, as evidenced by a writing filed in his office, and formed for the purpose of raising money to be used for the betterment of social and economic conditions in any community in which such corporation is doing business.

Acts of Feb. 9, 1933, ch. 8, § 1, 1933 Mass. Laws 18, 19 (emphasis added). Missouri's statute, enacted in 1937, provided that corporations could make charitable contributions to any charitable corporations organized under the laws of Missouri. See Laws of Mar. 25, 1937, 1937 Mo. Laws.

cert with other corporations' or natural persons' contributions,⁷³ which perhaps reflected a concern that corporate directors might otherwise exploit their newfound discretion to subsidize pet charities of their own creation. In some cases the scope of authorized donations was limited to those "furthering the corporation's interests" (or some analogous criteria)—which meant that these statutes represented only a minor liberalization from the previous common-law direct benefit requirement.⁷⁴ Finally, at different times, both Ohio⁷⁵ and New York⁷⁶ imposed a disclosure requirement on corporate charitable contributions, which mandated that both the amounts of the contributions and the identities of the recipients be disclosed.

The corporate philanthropy statutes enacted prior to mid-century were an experiment in legislative balancing. A variety of factors had mandated greater legal authority for corporate charitable contributions, yet the states had historically looked to protecting corporate shareholders' property interests. Although the state legislatures acted throughout the first half of the twentieth century (and thereafter) to legitimize the contributions function as a valid corporate power, the highly prescriptive nature of the early laws reflected the legislatures' sensitivity to the potential for waste and abuse in

73. This requirement is present in the early statutes of Ohio (1920), New York (1923), New Jersey (1930), Massachusetts (1933), and Delaware (1941). ANDREWS, *supra* note 66.

74. Such states include, for example, Ohio (1920) (authorizing contributions as would "contribute to the protection of corporate interests"); New York (1923) (authorizing contributions which would "contribute to the protection of the corporate property and tend to promote the interests of the corporation and its stockholders"); New Jersey (1930) (authorizing contributions as would "contribute to the protection of corporate interests"); Delaware (1941) (authorizing contributions as "will benefit or contribute to the protection of the corporate interests"). See *id.*

75. Ohio's original legislation, from 1920, imposed the following disclosure requirement: All such corporations making appropriations and expenditures under the provisions of this act shall report annually to the secretary of state the sums so appropriated or expended and the name or names of the community funds or philanthropic, charitable or benevolent instrumentalities in whose behalf such sums are appropriated or expended. Act of Feb. 4, 1920, 108 Ohio Laws 1245. The disclosure requirement was eliminated in 1927, upon the enactment of Ohio's General Corporation Act.

76. New York enacted a disclosure requirement for the first time in 1950. It provided: A domestic corporation which submits an annual report to its stockholders and which, pursuant to the authority of this section, appropriates, spends or contributes a sum or sums aggregating in excess of five hundred dollars to or on behalf of any one donee, during the period covered by such report, shall include in such report the identity of each such donee together with the total amount appropriated, spent or contributed to it or on its behalf during such period. If such corporation does not submit such an annual report to its stockholders it shall send to each one a statement of the total amount of all such appropriations, expenditures and contributions made during each fiscal year and any stockholder, upon written request, shall be entitled to an itemized list of such donees and amounts. The corporation need not comply with such a request regarding any year more than five years prior to that in which such request is made.

Act of Mar. 30, 1950, ch. 297, § 1, 1950 N.Y. Laws 974, 975 (repealed 1951).

the area of corporate philanthropy. The imposition of precisely defined requirements and limitations in regard to corporate charitable contributions was thus intended as an accommodation between the potentially conflicting priorities of shareholder wealth maximization and corporate-funded social activism.

4. The Organized Bar Advocates "New or Improved" Corporate Contributions Statutes

The balancing-approach characteristic of the early philanthropy statutes proved short-lived. In light of congressional validation of corporate charitable giving,⁷⁷ increased statutory recognition of corporate philanthropic authority in the states,⁷⁸ and corporate practice established over the course of two world wars,⁷⁹ the organized bar took up the cause of liberalizing the states' corporate philanthropy laws.

Ray Garrett, Jr., chairman of the American Bar Association's (the "ABA") Committee on Business Corporations,⁸⁰ addressed the ABA's annual meeting in 1948, and advocated broad-based statutory reform.⁸¹ Garrett admonished those present: "If we believe that business corporations should be entitled to make donations to charity, it seems that we, as lawyers, should seek means to legalize them so far as possible."⁸² Garrett promptly formulated "a proposal that the states be urged to enact unrestricted statutes authorizing donations to community chests and to charitable, scientific and educational institutions in such amounts as the board of

77. The historical context surrounding Congress' enactment of the corporate charitable deduction in 1935 is discussed in Nancy J. Knauer, *The Paradox of Corporate Giving*, 44 DEPAUL L. REV. 1, 19-20 (1994). The enactment of the corporate charitable deduction was viewed as congressional "encouragement" of corporate charitable giving. See, e.g., *Union Pac. R.R. v. Trustees, Inc.*, 329 P.2d 398, 400 (Utah 1958) ("In 1935 Congress encouraged corporate contributions to eleemosynary causes by allowing a deduction for tax purposes in such cases." (emphasis added)).

78. As indicated previously, Ray Garrett observed that by 1949 thirteen states and Hawaii had enacted some form of statutory authorization for corporate philanthropy. Garrett, *supra* note 64, at 31.

79. For historical treatments of the development of corporate charitable giving, see *supra* note 66. In addition, the opinion in *A.P. Smith v. Barlow* describes the social and economic developments that had mandated in favor of expanded corporate philanthropic authority. *A.P. Smith Mfg. Co. v. Barlow*, 98 A.2d 581 (N.J. 1953).

80. The ABA's Committee on Business Corporations was subsequently renamed the "Committee on Corporate Laws." See de Capriles & Garrett, *supra* note 65, at 211.

81. See de Capriles & Garrett, *supra* note 65, at 209-12. The full text of Mr. Garrett's speech to the ABA Committee on Business Corporations was published in *The Business Lawyer*. See Garrett, *supra* note 64.

82. Garrett, *supra* note 64, at 33.

directors may deem proper,"⁸³ and submitted the proposal to the ABA's Committee on Business Corporations immediately thereafter.⁸⁴

In 1949 and 1950, the ABA's Committee on Business Corporations circulated the proposal advocating the adoption of unrestrictive corporate philanthropy laws to all secretaries of state and state bar association presidents.⁸⁵ The Committee's model philanthropy provision, which was characterized by the absence of any language qualifying the scope of corporate philanthropic authority, was codified as section 4(m) of the ABA's Model Business Corporation Act, first published in 1950.⁸⁶ Thereafter, the pace of legal reform accelerated dramatically. Many state legislatures enacted unqualified corporate philanthropy provisions of the kind endorsed by the ABA. Other states, having previously enacted detailed, prescriptive philanthropy provisions, repealed them in favor of the pared-down, "modernized" version endorsed by the ABA.⁸⁷

Liberalization in the courts' approach to corporate charitable contributions was also apparent at this time. Most notably, the landmark case of *A.P. Smith Manufacturing Co. v. Barlow*, decided by the New Jersey Supreme Court in 1953, reflected the changing view of corporate philanthropy.⁸⁸ In upholding the validity of Smith Corporation's \$1500 contribution to Princeton University, the court endorsed what it viewed as evolving expectations of "corporate citizenship"⁸⁹ and elaborated on busi-

83. *Id.*

84. See de Capriles & Garrett, *supra* note 65, at 211.

85. *Id.*

86. *Id.* The original Model Business Corporation Act was a product of the collaborative efforts of Mr. Garrett's ABA committee and the American Bar Foundation. The first edition of the Model Act was published in *The Business Lawyer*. See *Model Business Corporation Act*, 6 BUS. LAW. 75 (1950) ("Section 4. GENERAL POWERS. Each corporation shall have power: . . . (m) To make donations for the public welfare or for charitable, scientific or educational purposes; and in time of war to make donations in aid of war activities.").

87. As described *supra* note 66, only 13 states and Hawaii had enacted some statutory authorization for corporate charitable contributions by 1949. Yet only five years later, in 1953, the New Jersey Supreme Court noted that 29 states had enacted statutes authorizing corporate philanthropy. *A.P. Smith Mfg. Co. v. Barlow*, 98 A.2d 581, 587 (N.J. 1953). In 1959, George D. Gibson indicated that 42 states had enacted statutes authorizing corporate charitable contributions. Gibson, *supra* note 64, at 434-35.

88. The *A.P. Smith* opinion provides an extended examination of the legal, historical, social, and economic changes that mandated expanded corporate philanthropic authority. For example, the court noted the "increased" calls by the public for corporations to make additional donations and thereby "assume the modern obligations of good citizenship." *A.P. Smith*, 98 A.2d at 586, 589-90. In the same vein, see de Capriles & Garrett, *supra* note 65, at 209-12.

89. *A.P. Smith*, 98 A.2d at 586 ("[M]odern conditions require that corporations acknowledge and discharge social as well as private responsibilities as members of the communities within which they operate."); see also *Union Pac. R.R. v. Trustees, Inc.*, 329 P.2d 398, 400-01 (Utah 1958) ("The new concept of corporate social responsibility seems to have become

ness' obligation to support the conditions facilitating free enterprise.⁹⁰ In contrast, it devoted only scant attention to the issue of shareholders' property interests.

B. The Current State of the States' Philanthropy Laws

The legal progeny of the unrestrictive philanthropy provision endorsed by the ABA, the modern philanthropy laws appearing within the states' corporation codes have assumed three distinct formulations. In twenty-four states and the District of Columbia the provisions state simply that corporations shall have power "to make donations for the public welfare or for charitable, scientific or educational purposes."⁹¹ Delaware, the state in which close to two-thirds of the Fortune 500 are incorporated, has a philanthropy provision of this kind.⁹² In nineteen other states, two provisions govern corporate contributions. One authorizes contributions "furthering the business and affairs of the corporation," while the other authorizes truly

fait accompli.").

90. A.P. Smith, 98 A.2d at 586 ("More and more [businesses] have come to recognize that their salvation rests upon sound economic and social environment which in turn rests in no insignificant part upon free and vigorous nongovernmental institutions of learning.").

91. These states are as follows: Alabama, Alaska, Arizona, Arkansas, Connecticut, Delaware, Hawaii, Idaho, Kansas, Illinois, Louisiana, Maryland, Michigan, Missouri, Nebraska, Nevada, New Mexico, Ohio, Oklahoma, Pennsylvania, Rhode Island, South Dakota, Texas, and West Virginia. See ALA. CODE § 10-2A-20(13) (1994); ALASKA STAT. § 10.06.010(13) (Michie 1994); ARIZ. REV. STAT. ANN. § 10-004(A)(13) (1994); ARK. CODE ANN. § 4-26-204 (Michie 1994); CONN. GEN. STAT. § 33-291(d) (1992); DEL. CODE ANN. tit. 8, § 122(9) (1993); HAW. REV. STAT. § 415-4(13) (1994); IDAHO CODE § 30-1-4(M) (1994); ILL. COMP. STAT. ANN. 5/3.10(m) (West 1994); KAN. CORP. CODE ANN. § 17-6102(9) (West 1995); LA. REV. STAT. ANN. § 12:41(12) (West 1994); MD. CODE ANN., CORPS. & ASS'NS § 2-103(13) (1994); MICH. COMP. LAWS § 450.1261(k) (West 1996); MO. ANN. STAT. § 351.385(12), (15) (West 1994); NEB. REV. STAT. § 21-2004(13) (1993); NEV. REV. STAT. ANN. § 78.070(6) (Michie 1993); N.M. STAT. ANN. § 53-11-4(M) (Michie 1994); OHIO REV. CODE ANN. § 1701.13(D) (Banks-Baldwin 1993); OKLA. STAT. ANN. tit. 18, § 1016(9) (West 1994); 15 PA. CONS. STAT. § 1502(a)(9) (1994); R.I. GEN. LAWS § 7-1.1-4(13) (1993); S.D. CODIFIED LAWS § 47-2-58(13) (Michie 1994); TEX. BUS. CORP. ACT ANN. art. 2.02(A)(14) (West 1994); W. VA. CODE § 31-1-8(M) (1996). The District of Columbia also has this kind of contributions provision. D.C. CODE ANN. § 29-505(13) (1994). Arkansas and Maryland have statutes that generally follow this format but also require board of director approval. ARK. CODE ANN. § 4-25-103 (Michie 1994); MD. CODE ANN., CORPS. & ASS'NS § 2-103(13) (1994). Nebraska's law requires that corporations make donations "in the territory in which it operates." NEB. REV. STAT. § 21-2004 (13) (1993). The states differ slightly in their enumeration of authorized philanthropic purposes, but the differences are largely semantic. In all cases the language employed is very general.

92. DEL. CODE ANN. tit. 8, § 122(9) (1993) ("Specific Powers.—Every corporation created under this chapter shall have power to: . . . Make donations for the public welfare or for charitable, scientific or educational purposes, and in time of war or other national emergency in aid thereof.").

philanthropic contributions, as it contains no such limiting language. (The latter provisions are thus identical to the first class of laws described above, which simply authorize donations for charitable, scientific, and educational purposes.)⁹³ Seven other states—including California, New York, and New Jersey—have enacted laws authorizing corporations to make charitable contributions “irrespective of corporate benefit.” The abrogation of the benefit-to-the-business requirement is made express in the language of these statutes.⁹⁴ Exhibiting only minor semantic differences, the modern philanthropy laws are uniform in their significance. They authorize seemingly unlimited philanthropic contributions from corporate capital without regard to whether the firm will be benefited thereby.

As the above discussion illustrates, these statutes function to validate corporate philanthropic authority, but they do not *regulate* the practice of corporate charitable giving. In contrast to the early statutes, the modern laws fail to define any quantitative parameters for corporate charitable giving. They also fail to prescribe a decisional framework for corporate philanthropy: They are absolutely silent on the matter of who shall have decision-making authority over corporate charitable contributions. This silence *vis-a-vis* decisional authority abrogates any statutory claim on the part of corporate shareholders to have a right to participate in corporate philanthropic decision-making, because the states’ corporations codes allo-

93. States having such twin donations provisions include Colorado, Florida, Georgia, Indiana, Iowa, Kentucky, Mississippi (which requires also that the contributions be accounted for as an operating expense), Montana, New Hampshire, North Carolina, Oregon, South Carolina, Tennessee, Vermont, Utah, Virginia, Washington, Wisconsin, and Wyoming. See COLO. REV. STAT. § 7-103-102(m), (n) (Supp. 1996); FLA. STAT. ANN. § 607.0302(12), (14) (West 1993); GA. CODE ANN. § 14-2-302(13), (16) (1994); IND. CODE ANN. § 23-1-22-2(13), (15) (Michie 1994); IOWA CODE ANN. § 490.302(13), (15) (West 1994); KY. REV. STAT. ANN. § 271B.3-020(m), (o) (Michie 1994); MISS. CODE ANN. § 79-4-3.02(13), (15) (1993); MONT. CODE ANN. § 35-1-115(13), (15) (1995); N.H. REV. STAT. ANN. § 293-A:3.02(13), (15) (1995); N.C. GEN. STAT. § 55-3-02(a)(13), (15) (1994); OR. REV. STAT. § 60.077(2)(n), (p) (1993); S.C. CODE ANN. § 33-3-102(13), (15) (Law. Co-op. 1995); TENN. CODE ANN. § 48-13-102(13), (14) (1995); UTAH CODE ANN. § 16-10a-302(13), (15) (1994); VT. STAT. ANN. tit. 11A, § 3.02(13), (15) (1993); VA. CODE ANN. § 13.1-627(A)(12), (13) (Michie 1994); WASH. REV. CODE ANN. § 23.B.03.020(2)(o), (q) (West 1993); WIS. STAT. ANN. § 180.0302(13), (15) (West 1994); WYO. STAT. § 17-16-302(A)(XIII) (Michie 1994).

94. Such provisions have been adopted in California, Maine, Massachusetts, Minnesota, New Jersey, New York, and North Dakota. See CAL. CORP. CODE § 207(e) (West 1995) (providing authority for charitable donations “regardless of specific corporate benefit”); ME. REV. STAT. ANN. tit. 13-A, § 202(G) (West 1994); MASS. GEN. LAWS ANN. ch. B, § 9(k) (1994); MINN. STAT. ANN. § A.161(11) (West 1995); N.J. STAT. ANN. § 14A:3-4 (West 1995); N.Y. BUS. CORP. LAW § 202(12) (Consol. 1994); N.D. CENT. CODE § 10-19.1-26(11) (1993). Additionally, New Jersey and two other states require board of director approval of corporate contributions. See ARK. CODE ANN. § 4-26-204 (Michie 1994); MD. CODE ANN., CORPS. & ASS’NS. § 2-103(13) (1994).

cate plenary authority to directors and only specific, prescribed powers to shareholders. Thus, in affording them full decisional authority in regard to corporate contributions, these laws have conferred extraordinary power and discretion on corporate managers.⁹⁵

In fact, the issue of decisional authority in regard to corporate contributions has another important dimension. By failing to require board approval for corporate contributions, the law permits delegation of philanthropic authority to individual corporate executives. Full board review is the most common mechanism of intrafirm accountability within state corporation law. The absence of a requirement of board of director approval has thus contributed to lax oversight of the contributions function, and has allowed individual executive officers to pursue narrow, personal objectives in the administration of corporate charitable contributions.

The significance of this permissiveness in the modern philanthropy provisions is, of course, amplified dramatically by the eradication of the benefit-to-the-business requirement, which has meant that corporate philanthropic behavior is not constrained by the usual institutional imperative of profit maximization. In no other area of corporate affairs are managers authorized to make decisions affecting the allocation of corporate capital without regard to how they will affect the firm's financial interests.⁹⁶ In all other instances, corporate and shareholder wealth maximization operates as the fundamental, governing norm within corporate law.⁹⁷ In recognition of managers' expertise in commercial matters, and in the name of enhanced efficiency,⁹⁸ state corporation law imposes few mandatory rules

95. According to state corporation law, it is the board of directors that has authority over the business and affairs of the corporation, and thus (by default) its charitable contributions. The absence of a specific grant of authority or participation rights on behalf of shareholders means that they have no legal right to participate in corporate philanthropic decisions. See, e.g., DEL. CODE ANN. tit. 8, § 141 (1993); N.Y. BUS. CORP. LAW § 701 (Consol. 1994).

96. The corporate philanthropy laws are far more significant, therefore, as a departure from traditional profit-oriented corporate norms, than are the constituency statutes enacted by many states in the 1980s. The latter, curiously, have received far more attention. For further discussion of the constituency statutes, see *infra* notes 213-215 and accompanying text.

97. See, e.g., ALI, *supra* note 14, § 2.01.

98. For a defense of the primacy of economic (market) forces and the centrality of efficiency concerns within corporate law, see, for example, FRANK H. EASTERBROOK & DANIEL R. FISCHEL, *THE ECONOMIC STRUCTURE OF CORPORATE LAW* (1991). For a more political interpretation, see Gerald E. Frug, *The Ideology of Bureaucracy in American Law*, 97 HARV. L. REV. 1276 (1984), which argues that corporate law empowers corporate management and disempowers corporate shareholders as part of law's rationalization of bureaucracy and the status quo.

on the governance of business corporations.⁹⁹ But the flexibility within state corporation law is otherwise intended to afford corporate directors and officers the freedom to operate the firm most profitably and efficiently.¹⁰⁰ In contrast, the unregulated nature of corporate philanthropic giving affords corporate managers the authority to *depart* from profit maximization. In this regard, the philanthropy provisions are *sui generis* within corporation law.

C. The Modern Judicial Treatment of Corporate Charitable Contributions

Because they authorize corporate executives to make philanthropic donations of corporate assets irrespective of benefit to the firm, but fail to articulate any meaningful limits or requirements in relation thereto, the modern philanthropy statutes have posed an interpretive dilemma for the courts.¹⁰¹ In light of the legislatures' deliberate failure to delineate objec-

99. In responding to the transformation of the states' corporation codes into broad, "enabling" laws, Bayless Manning remarked: "[C]orporation law, as a field of intellectual effort, is dead in the United States. . . . We have nothing left but our great empty corporation statutes—towering skyscrapers of rusted girders, internally welded together and containing nothing but wind." Bayless Manning, *The Shareholder's Appraisal Remedy: An Essay for Frank Coker*, 72 *YALE L.J.* 223, 245 n.37 (1962). A 1989 symposium conducted by the *Columbia Law Review* was dedicated to the discussion of which (if any) corporation law rules should be mandatory. Symposium, *Contractual Freedom in Corporate Law*, 89 *COLUM. L. REV.* 1395 (1989). For an argument that state corporate law norms are increasingly marginal, see Bernard S. Black, *Is Corporate Law Trivial? A Political and Economic Analysis*, 84 *NW. U. L. REV.* 542 (1990).

100. See, e.g., *Aronson v. Lewis*, 473 A.2d 805 (Del. 1984); *Bayer v. Beran*, 49 N.Y.S.2d 2, 6 (Sup. Ct. 1944) ("To encourage freedom of action on the part of directors, or to put it another way, to discourage interference with the exercise of their free and independent judgment, there has grown up what is known as the 'business judgment rule'."). For a comprehensive overview of the subject, see DENNIS J. BLOCK ET AL., *THE BUSINESS JUDGMENT RULE: FIDUCIARY DUTIES OF CORPORATE DIRECTORS* (4th ed. 1993).

101. Despite the numerous questions left unresolved by the states' philanthropy provisions, corporate charitable contributions have rarely been the subject of shareholder suits. After mid-century, there are only four cases importantly addressing the scope of corporate philanthropic authority and the propriety of particular contributions. See *A.P. Smith Mfg. Co. v. Barlow*, 98 A.2d 581 (N.J. 1953); *Union Pac. R.R. v. Trustees, Inc.*, 329 P.2d 398 (Utah 1958); *Kahn v. Sullivan*, 594 A.2d 48 (Del. 1991); *Theodora Holding Corp. v. Henderson*, 257 A.2d 398 (Del. Ch. 1969). The absence of litigation in this area reflects several factors: the lack of publicly available information regarding most corporate charitable contributions; the fact that the statutes appear to sanction any corporate charitable contributions; and the fact that the governing legal standards are sufficiently broad as to make a successful shareholder suit unlikely. In addition, aca-

tive criteria, according to what guidelines or principles should the courts adjudicate the propriety of particular challenged donations? Because the modern philanthropy laws represent the legislatures' deliberate decision to deregulate corporate charitable giving (in light of the earlier existence of highly prescriptive statutes), it would seem highly inappropriate for the courts to impose a substantial scheme of judicial oversight in this area. On the other hand, a rule permitting corporate managers to make any and all contributions of corporate capital to charitable organizations seems untenable in light of the traditionally shareholder-centered orientation of corporate law.

In response to this dilemma, the courts have resorted to a permissive standard of "reasonableness" in adjudicating the propriety of particular contributions. While the early statutes and cases occasionally spoke in terms of "reasonable" donations,¹⁰² it was *Theodora Holding Corp. v. Henderson*, decided by the Delaware Chancery Court in 1969, that expressly adopted "reasonableness in amount and purpose" as the appropriate standard for defining the permissible scope of corporate contributions.¹⁰³ The standard of reasonableness was also endorsed by the Delaware Supreme Court in *Kahn v. Sullivan*,¹⁰⁴ and it appears, to date, to be the authoritative standard.

In both *Theodora* and *Kahn*, the courts constructed the normative parameters of reasonableness on the basis of the Internal Revenue Code's charitable contributions provisions.¹⁰⁵ The Code's annual ceiling for deductible corporate charitable contributions of ten percent of taxable corpo-

democratic commentators generally have failed to focus on the duty of loyalty issues arising in the area of corporate charitable giving, thereby contributing to their continued transparency. (Given the centrality of the problem of managerial accountability within modern corporate legal scholarship, the paucity of attention devoted to the subject of corporate philanthropy is indeed surprising.) Previous commentators have generally attributed the absence of litigation in the area to a consensus in favor of corporate charitable giving. See, e.g., de Capriles & Garrett, *supra* note 65, at 210.

102. See, e.g., *Armstrong Cork Co. v. H.A. Meldrum Co.*, 285 F. 58 (W.D.N.Y. 1922); *Memorial Hosp. Ass'n v. Pacific Grape Prods. Co.*, 290 P.2d 481, 484 (Cal. 1955).

103. *Theodora*, 257 A.2d at 405 ("I conclude that the test to be applied in passing on the validity of a gift such as the one here in issue is that of reasonableness, a test in which the provisions of the Internal Revenue Code pertaining to charitable gifts by corporations furnish a helpful guide.").

104. *Kahn*, 594 A. 2d at 61 ("Thus the Court of Chancery [in the opinion in *Theodora Holding Corp. v. Henderson*] concluded that the test to be applied in examining the merits of a claim alleging corporate waste 'is that of reasonableness, a test in which the provisions of the Internal Revenue Code pertaining to charitable gifts by corporations furnish a helpful guide.' We agree with that conclusion." (citations omitted)).

105. See *supra* notes 103-104.

rate profits (as defined under § 170(b)(2)),¹⁰⁶ has been adopted as the appropriate upper limit for annual corporate charitable contributions under Delaware corporation law.¹⁰⁷ And satisfaction of § 501(c)(3)'s requirements for status as a charitable organization has been used to define the scope of appropriate beneficiaries—i.e., the “reasonable purposes” for corporate charitable contributions.¹⁰⁸

Delaware's adoption of the Tax Code as the principal heuristic in defining the reasonable parameters of corporate contributions has affected both the theory and practice of corporate philanthropy. From a practical perspective, reliance on the aforementioned tax-based, quantitative standards has failed to impose any substantial constraints on corporate charitable giving. Ten percent of annual corporate profits is an extraordinarily generous “allowance” in the context of large public corporations.¹⁰⁹ And, as mentioned above, Delaware has answered the question of the reasonable purposes for corporate charitable contributions by reference to the kinds of charitable beneficiaries qualifying under § 501(c)(3) of the Code.¹¹⁰ Here again, the applicable tax-based standards are very liberal. In light of the relevance of constitutional guarantees of liberty and due process, the IRS has had difficulty delimiting which causes and groups should not be eligible to claim “charitable,” “educational,” or “religious” status.¹¹¹ Thus, because an extraordinary variety of organizations may qualify as charitable, educational, or religious for purposes of § 501(c)(3), corporate charitable contributions may be made to an extraordinarily broad spectrum of groups pursuant to this standard.

106. The enactment of the Economic Recovery Tax Act of 1981 raised the ceiling for the deductibility of corporate charitable contributions from 5% of taxable corporate income (without regard to any net operating loss or capital loss carryback) to 10%. I.R.C. § 170 (b)(2) (1994).

107. See *supra* notes 103–104.

108. See *supra* notes 103–104.

109. In fact, I believe that is inapposite to view the 10% figure as having been intended as a true “allowance” or “limit.” In enacting the corporate charitable deduction in 1935, in the aftermath of the Depression, Congress sought to *stimulate* corporate giving, not to limit it. And, in 1981, when Congress increased the upper limit from 5% to 10% of corporate pretax profits, it was operating from a similar perspective. The ten-percent-of-profits figure represents more of a target—a hortatory appeal for increased corporate largesse—than an *allowance*, as such. This view is also supported by the fact that large corporations typically contribute only 2% to 5% (or less) of their annual profits—far below the maximum allowable deduction of 10% of profits. I.R.C. § 170(b)(2). For annual corporate contributions rates as a percentage of corporate pretax income, see GIVING USA 1996, *supra* note 23, at 90. The average annual rate of contributions as a percentage of pretax corporate profit was estimated at 1.24% for 1995. *Id.*

110. Kahn v. Sullivan, 594 A.2d 48, 61 (Del. 1991); Theodora Holding Corp. v. Henderson, 257 A.2d 398, 404 (Del. Ch. 1969).

111. See, e.g., *Developments in the Law—Nonprofit Corporations*, 105 HARV. L. REV. 1578, 1612–34 (1992); see also *infra* Part V.

Because it is presently the last word on the subject—and in view of the precedential nature of Delaware corporate law decisions—the opinion in *Kahn* merits special consideration. The Delaware Supreme Court's resort to the tax-based standards described above (in adjudicating the acceptable parameters of Occidental Petroleum's planned charitable contributions) functioned as a handy short-cut therein,¹¹² as it had earlier in *Theodora*.¹¹³ But, while reliance on the standards operative under the Tax Code has lent objectivity to these determinations, it has also allowed the courts to resolve disputes about corporate charitable contributions without focusing on shareholders' interests. More particularly, an analysis of whether a corporation's gifts have conformed to the Tax Code's standards for deductibility (that is, Congress' determination of what is socially desirable in regard to charitable support) is not a proxy for an examination of *shareholders' interests* in regard to corporate-based altruism. The class of charitable organizations qualifying under § 501(c)(3) does not supply a definition of the reasonable purposes of *corporate* charitable contributions—that is, the rationale for encouraging charity at the level of the corporation, as opposed to the individual level. The invocation of the Code's ten-percent-of-corporate-profits standard appears similarly perfunctory. If donations are good for the firm, why should state law limit them? If they represent managerial largesse with the shareholders' money (either in favor of society or, even more problematically, themselves), what principle within corporate law justifies them in the first instance?

Of course, courts have had good reasons to avoid confronting the trenchant issues raised by corporate charitable contributions. Little consensus has existed regarding the causes and explanations for corporate charitable contributions. Inadequate information has existed regarding the effect of corporate philanthropy on corporate performance. And substantial disagreement has existed (and will probably continue to exist) regarding the propriety of corporate-based altruism. In addition, the overall managerial bias within corporate law has meant that courts have had little difficulty justifying their deferential posture towards corporate philanthropy.¹¹⁴

112. The court's approach, admittedly, was affected by the procedural posture of the litigation: The supreme court was reviewing the chancery court's approval of a shareholder derivative suit settlement. *Kahn*, 594 A.2d at 48.

113. *Theodora*, 257 A.2d at 404.

114. See, e.g., *Steiner v. Meyerson*, [1995 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 98,857, at 93,148 (Del. Ch. July 18, 1995):

Absent an allegation of fraud or conflict of interest courts will not review the substance of corporate contracts; the waste theory represents a theoretical exception to the statement very rarely encountered in the world of real transactions. There surely are

The legislatures' rejection of a regulatory approach to corporate charitable giving may appropriately reflect the complexity of the contributions function within modern corporate affairs, and, consequently, the courts may be unequipped to address the problem, but the potential for abuse arising from managerial control over corporate giving necessitates that some system of accountability be established. In order to address the void left by the modern laws and cases, and in order to illustrate the interests and issues at stake in this area, the remainder of this Article analyzes contemporary corporate giving practices in relation to corporate legal norms and shareholders' interests.

III. CORPORATE PHILANTHROPY AND MANAGERIAL SELF-INTEREST

Corporate charitable contributions may be used by corporate executives to confer substantial personal and professional benefits on themselves. Because traditional mechanisms of accountability are absent in this area, corporate philanthropy represents an area of corporate conduct in which managerial self-interest may flourish.

Conflicts of interest on the part of management and the potential for managerial opportunism in general are subjects of importance within corporate law and legal theory.¹¹⁵ The problem of self-interested conduct on the part of corporate management has been addressed through the promulgation of fiduciary standards of loyalty,¹¹⁶ statutory and common law standards of fairness,¹¹⁷ and requirements of ratification by disinterested parties.¹¹⁸ Although courts and commentators have failed to apply these

cases of fraud; of unfair self-dealing and, much more rarely negligence. But rarest of all—and . . . 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 *supra* note 100.

115. According to one leading casebook, "[T]he principal task of corporation law is to create a governance structure for corporations that promotes an appropriate degree of accountability among the participants." LEWIS D. SOLOMON ET AL., *CORPORATIONS: LAW AND POLICY* 9 (1994). For a comprehensive treatment of fiduciary obligation and the problem of managerial opportunism in the corporate form, see ROBERT CHARLES CLARK, *CORPORATE LAW* 141-223 (Francis A. Allen et al. eds., 1986) (chapters 4-7).

116. See SOLOMON ET AL., *supra* note 115, at 750 ("Simply put, the duty of loyalty requires a manager to place the corporation's best interests (and thus those of the stockholders) above her own.").

117. See, e.g., *Fleigler v. Lawrence*, 361 A.2d 218, 221 (Del. 1976); see also DEL. CODE ANN. tit. 8, § 144(a)(3) (1993); N.Y. BUS. CORP. LAW § 713(b) (Consol. 1994).

118. *Fleigler*, 361 A.2d at 221; see also DEL. CODE ANN. tit. 8, § 144(a)(1), (2); N.Y. BUS. CORP. LAW § 713(a)(1), (2). For discussion of ratification by disinterested directors of transactions involving managerial conflicts of interest, see WILLIAM L. CARY & MELVIN ARON EISENBERG, *CASES AND MATERIALS ON CORPORATIONS* 684-88 (7th ed. 1995).

forms of heightened scrutiny to corporate charitable-contributions decisions,¹¹⁹ it is plain that where corporate managers approve such contributions as a means of furthering their personal objectives, such contributions represent a species of agency costs,¹²⁰ and are inconsistent with the essential fiduciary fabric of corporate law.

In addition to state corporate law, the federal securities regulations have functioned to discipline corporate managers (and therefore reduce agency costs) by requiring disclosure of executive compensation arrangements and other matters potentially involving managerial conflicts of interest.¹²¹ More particularly, under Item 402 of the SEC's S-K regulations, comprehensive, detailed information about both cash and noncash director and officer compensation is required to be presented to corporate shareholders.¹²² Item 404(a) of the S-K regulations requires disclosure of corporate transactions wherein directors and officers have an interest as principals.¹²³ And Item 404(c) of the S-K regulations requires disclosure of any loans which the company makes to its directors and officers.¹²⁴

Furthermore, while the SEC's disclosure mandates have failed to address corporate philanthropy as a general matter, the SEC has recently recognized one kind of corporate charitable contributions arrangement,

119. Although the duty of loyalty issues existing in the context of corporate contributions have remained largely unaddressed within legal scholarship, the duty of loyalty is recognized to be "a residual concept that can include factual situations that no one has foreseen and categorized." CLARK, *supra* note 115, at 141. Both courts and commentators have dealt exhaustively with problems of managerial self-interest (i.e., the contours of the duty of loyalty) in the context of executive compensation, so-called "interested director transactions," and the doctrine of "corporate opportunities." The fact that benefits accrue to corporate executives from their control over corporate contributions creates analogies between the contributions function and these classic conflict scenarios. The explicit connection between corporate philanthropy and executive compensation is discussed below. See *infra* notes 173-176 and accompanying text.

120. The seminal, early treatment of the agency cost problem in the context of the modern, public corporation is BERLE & MEANS, *supra* note 17. For a concise review of modern agency theory, as applied to corporate charitable contributions, see Jia Wang & Betty S. Coffey, *Board Composition and Corporate Philanthropy*, 11 J. BUS. ETHICS 771 (1992). See generally EASTERBROOK & FISCHER, *supra* note 98; Michael C. Jensen & William H. Meckling, *Theory of the Firm: Managerial Behavior, Agency Costs and Ownership Structure*, 3 J. FIN. ECON. 305 (1976). Cf. Aleta G. Estreicher, *Beyond Agency Costs: Managing the Corporation for the Long Term*, 45 RUTGERS L. REV. 513 (1993) (arguing that corporate legal scholarship has focused myopically on agency cost issues, to the detriment of important, alternative aspects of corporate performance).

121. For a discussion of SEC-mandated disclosure as a response to the problem of agency costs, see Paul G. Mahoney, *Mandatory Disclosure as a Solution to Agency Problems*, 62 U. CHI. L. REV. 1047 (1995). See also 1 LOUIS LOSS & JOEL SELIGMAN, *SECURITIES REGULATION* 171-225 (3d ed. 1989). For recent commentary on the goals of SEC-mandated disclosure, see Edmund W. Kitch, *The Theory and Practice of Securities Disclosure*, 61 BROOK. L. REV. 764 (1995).

122. 17 C.F.R. § 229.402 (1996).

123. *Id.* § 229.404.

124. *Id.*

known as "charitable awards" or "director legacies" (collectively, "charitable awards"), as a form of "disclosable" executive compensation.¹²⁵ In 1992, in the context of broadly revising the executive compensation disclosure rules, the SEC expressly called for disclosure of any such "charitable awards" within the executive compensation disclosure presented in proxy statements and other SEC filings.¹²⁶ Thus, the SEC has recognized that corporate directors and officers may derive personal benefits from corporate charitable contributions, and has responded with a specific disclosure mandate. However, by confining the scope of required disclosure to charitable awards, the SEC demonstrated that it has yet to recognize or address the full extent of the managerial benefits inhering in "ordinary" corporate charitable contributions.

A. Managerial Discretion and Politicized Philanthropy

Part V of this Article analyzes "politicized" charitable contributions, which are consonant with the maximization of corporate profit. Of course, corporate managers may authorize donations to politically active charities as a means of furthering their own political and ideological preferences, irrespective of the firm's best interests. When corporate managers approve donations on this self-serving basis, they satisfy the letter of the law¹²⁷ but fail to fulfill their fiduciary obligation to protect corporate shareholders' property interests. Furthermore, because corporate contributions to politicized nonprofit organizations represent a form of corporate political speech (and one which is not commonly brought to the attention of shareholders), such donations also undermine shareholders' free speech and associational interests, as discussed fully in Part V.

One recent example of politicized charitable contributions made irrespective of corporate interests is provided by Morrison Knudsen Corpora-

125. Executive Compensation Disclosure, Release No. 33-6962, 34-31327, 57 Fed. Reg. 48,126 (Oct. 21, 1992).

Various corporate and other commentators maintained that charitable award or legacy arrangements need not be disclosed, since the directors are not receiving value through the arrangement. Other commentators contended that such arrangements should be disclosed to shareholders since the arrangements clearly relate to directors' board service, and the premiums can be considerable, particularly relative to amounts paid annually to directors, and are material in assessing the relationship of directors to the registrant. The Commission agrees, and thus reaffirms its initial conclusion that such arrangements are required to be disclosed pursuant to the requirements of Item 402(g).

Id. at 48,137.

126. *Id.*

127. For a discussion of the lax standards applicable under state law, see *supra* Part II.

tion's contributions to a small pro-life charity, "The Nurturing Network." As reported by *The New York Times*¹²⁸ and *Fortune* magazine,¹²⁹ Mary Cunningham Agee, the wife of Morrison Knudsen's CEO, established The Nurturing Network consistent with the couple's opposition to abortion.¹³⁰ As the president of the company's charitable foundation,¹³¹ Mary Agee presided over various direct and foundation-based donations that the company made to The Nurturing Network. While *The New York Times* reported that the company's foundation "made grants to the Nurturing Network, and the corporation itself regularly donated goods and services to the charity,"¹³² the full extent of the firm's gifts to The Nurturing Network has remained confidential—because there is no means to obtain information regarding the donations made on a direct basis.

In addition to monetary support, Mr. Agee and his wife also fostered the connection between Morrison Knudsen and The Nurturing Network by encouraging the corporation's directors to serve on the charity's board. In total, in addition to the Agees, three directors and five other directors' wives assumed board positions at The Nurturing Network.¹³³ Both the

128. Diana B. Henriques, *A Celebrity Boss Faces Exile from 2d Corporate Kingdom*, N.Y. TIMES, Feb. 10, 1995, at A1; Diana B. Henriques, *Ties That Bind: His Directors, Her Charity*, N.Y. TIMES, Mar. 21, 1995, at D1 [hereinafter Henriques, *Ties That Bind*].

129. O'Reilly, *supra* note 57, at 51.

130. *Id.* at 56 ("Mary's chief interest was the Nurturing Network, a charity she founded that offers help, including housing and jobs, to give pregnant college and working women an alternative to abortion. It was an activity that made her highly visible to bishops and cardinals in the Catholic Church, and even today, much of her life appears to revolve around it. In the days after Agee was fired, several church leaders sent letters of encouragement to her.")

131. Mary Cunningham Agee was appointed president of Morrison Knudsen's corporate foundation by her husband, the company's CEO. In addition to being the founder of The Nurturing Network, she served as its "unpaid executive director." Henriques, *Ties That Bind*, *supra* note 128, at D4; O'Reilly, *supra* note 57, at 56 ("[Bill] Agee, who should have been sensitive to nepotism charges after his experience at Bendix, put Mary in charge of another charity, the Morrison Knudsen Foundation. It spends close to \$1 million a year on social and cultural causes.")

132. Henriques, *Ties That Bind*, *supra* note 128.

133. Therefore, besides the Agees, eight Morrison Knudsen directors were affiliated with the charity's board. The interlocking directorates between Morrison Knudsen corporation and The Nurturing Network and, especially, the presence of presumably "independent," outside corporate directors and their wives on the board of the charity are suggestive of serious departures from sound corporate governance. These larger corporate governance issues were the focus of the second *New York Times* article, *The Ties That Bind*. Subtitled *Did Joining the Agees' Cause Make It Hard to Say No in the Board Room?*, the article suggested that extra-curricular affiliations between corporate insiders and purportedly "independent" outside directors may have undermined the outsiders' ability to be objective in the boardroom. *Id.* at D1. Although extremely important, this larger corporate governance question relating to extra-curricular affiliations between inside and outside directors is beyond the scope of this Article. For a discussion of the problem, see, for example, James D. Cox & Harry L. Munsinger, *Bias in the Boardroom: Psychological Foundations and Legal Implications of Corporate Cohesion*, 48 LAW & CONTEMP. PROBS. 84 (1985). This

financial and administrative support and the directorial connections through which Morrison Knudsen supported The Nurturing Network came to light only because the company had become subject to scrutiny on account of its deteriorating financial condition.¹³⁴ The company's proxy statements and its annual reports to shareholders, consistent with the SEC's current requirements,¹³⁵ contained no information about the contributions which the company made to The Nurturing Network or the interlocking directorates existing between the firm and the charity.¹³⁶

Unfortunately, the generally confidential nature of corporate philanthropy, combined with the fact that politicized donations are especially likely to be kept confidential from corporate shareholders (and other members of the public), means that it is very difficult to unearth examples of such politicized, noncommercial charitable contributions. Stories like the one above come to light only where particular news reporters have gone out of their way to uncover information. Nevertheless, the self-serving (or "rationally maximizing") aspect of human nature, the prevalence of politicized philanthropies, and the absence of mechanisms of accountability, in combination, suggest that politicized charitable contributions that satisfy managers' (but not necessarily shareholders') interests may indeed be prevalent.¹³⁷

B. Managerial Discretion and Corporate Social Responsibility

Corporate social responsibility may serve as a legitimate rationale for corporate charitable contributions, as discussed in Part IV. But "social

Article addresses the situation of "shared" directors between corporate and nonprofits' boards as it relates to the issue of managerial self-promotion, suggesting that executives use corporate contributions to "purchase" board seats at prominent charities as a system of professional and social status enhancement. See *infra* notes 158–159 and accompanying text.

134. It is tempting to speculate that mandatory disclosure of the firm's unusual philanthropic practices might have signaled the presence of other even more costly forms of waste and abuse. In fact, mandatory contributions disclosure might function, in general, as the proverbial "canary in the bird cage": Wayward contributions practices might alert shareholders to an overall lack of discipline and control.

135. Item 401(e)(2) of the S-K regulations requires disclosure of directors' other directorships with public companies, but not directorships with affiliated charitable organizations. Thus if, as it has been interpreted, the rule is intended to expose potential conflicts of interest, it is highly underinclusive. See 17 C.F.R. § 229.401 (1996).

136. This assessment is based on my review of the Morrison Knudsen proxy statements and annual reports covering the years 1990–1995.

137. It is difficult to attest to the magnitude of this problem precisely because this information is unobtainable—hence the need for obligatory disclosure of corporate charitable contributions information.

responsibility" may also function as a rationalization for managers to spend corporate resources to actualize their personal preferences in regard to social welfare and civic engagement.¹³⁸ A survey of the area has uncovered only one public corporation that has systematically empowered its shareholders to affect the allocation of the corporation's charitable capital.¹³⁹ While corporate contributions may be legitimated on the basis of corporate social responsibility, as a general matter there is no reason that *corporate managers* should control the decision to constitute the firm as a deliberate agent of social change.¹⁴⁰ Put simply, by providing for centralized decision-making in the area of corporate charitable contributions, state law has afforded corporate managers the equivalent of taxing authority. Where contributions are not employed as commercial resources (as is consistent with the charitable deduction under the Code), there is no reason to prevent shareholders from having a meaningful voice in the formulation of corporate philanthropy policies, a fortiori, for keeping contributions information confidential from them. (This issue is discussed in depth in Part IV, below.)

138. This is consistent with Adolph Berle's views expressed in the essays he exchanged with Professor Dodd. As he expressed therein, Berle's concern for licensing self-interested conduct by management led him to oppose legal validation of extra-shareholder obligations on the part of the firm. See Adolf A. Berle, Jr., *For Whom Corporate Managers Are Trustees: A Note*, 45 HARV. L. REV. 1365, 1367 (1932) ("When the fiduciary obligation of the corporate management and 'control' to stockholders is weakened or eliminated, the management and 'control' become for all practical purposes absolute. The claims upon the assembled industrial wealth and funneled industrial income which managements are then likely to enforce (they have no need to urge) are their own." (footnote omitted)).

139. This corporation is Berkshire Hathaway, Inc. under the direction of CEO Warren Buffet. See, e.g., BERKSHIRE HATHAWAY, INC., 1990 ANNUAL REPORT 54-55 (1991).

140. The problem of the authority of corporate managers to oversee corporate social activism has been widely noted. See, e.g., HENRY G. MANNE & HENRY C. WALLICH, *THE MODERN CORPORATION AND SOCIAL RESPONSIBILITY* 10 (1972) (H. Manne, first lecture) ("The concept of corporate responsibility flatters businessmen that they are the divine-elect, as Andrew Carnegie would have had it. . . . [B]usinessmen as a group are at best only slightly more expert in economic theory than the general population.").

C. Managerial Benefits Arising from Corporate Charitable Contributions

1. Managerial Utility and the Theory of the Firm

In constructing the theory of the business firm, classical economists and law-and-economics scholars have employed profit maximization as the primary incentive of management. Alternatively, various other economists,¹⁴¹ legal scholars,¹⁴² and academics in other fields¹⁴³ have taken

141. Various economists studying corporate charitable contributions have included "managerial utility maximization" within their hypotheses. See, e.g., CLOTFELTER, *supra* note 22, at 190 ("[A] company's charitable contributions may enter the utility functions of managers. Accordingly, the management may choose to sacrifice profits in order to make such contributions."); Armen A. Alchian & Reuben A. Kessel, *Competition, Monopoly and the Pursuit of Money*, in ASPECTS OF LABOR ECONOMICS 157 (1962) (business' contributions are one facet of the attempt to acquire status, prestige, and goodwill for management and the firm); Ferdinand K. Levy & Gloria M. Shatto, *The Evaluation of Corporate Contributions*, 33 PUB. CHOICE, Issue 1978, at 19-28 (managers use contributions as a "preferred expense"); Webb, *supra* note 54, at 82 ("Managers may give because they are altruistic or because they enjoy the prestige associated with being a big giver (thus contributions might be viewed as part of the compensation package for upper management).").

142. Henry G. Manne has argued that corporate managers have a fund of discretionary resources (including funds available for "pet charities") that is roughly equivalent to the transaction costs of removing them from office. MANNE & WALLICH, *supra* note 140. Addressing the incentives problem in another context, scholars have suggested that certain executives have pursued corporate growth (and thus, enhanced perquisites) independent of concerns over shareholder wealth maximization. See, e.g., John C. Coffee, Jr., *Shareholders Versus Managers: The Strain in the Corporate Web*, 85 MICH. L. REV. 1 (1986); Roberta Romano, *A Guide to Takeovers: Theory, Evidence and Regulation*, 9 YALE J. ON REG. 119, 148-49 (1992) (observing that managerial ego cannot be dismissed as an incentive to engage in takeovers). Of course, the agency cost problem has been exhaustively analyzed in the context of managerial resistance to takeover bids. See, e.g., Bryan Ford, *In Whose Interest: An Examination of the Duties of Directors and Officers in Control Contests*, 26 ARIZ. ST. L.J. 91 (1994). More generally, the desire to win esteem, status, and fellowship (as an important complement to material or economic objectives) is receiving increased attention in the legal literature. See, e.g., Richard H. McAdams, *Cooperation and Conflict: The Economics of Group Status Production and Race Discrimination*, 108 HARV. L. REV. 1003 (1995) (including citations to recent sociological literature analyzing status production and group cohesion).

143. Within management science, see Haley, *supra* note 36, at 485-504. From the perspective of sociology, see, for example, JOSEPH GALASKIEWICZ, *SOCIAL ORGANIZATION OF AN*

a broader view of managers' objectives in the allocation of corporate resources. In particular, Oliver Williamson has identified the desire for increased power, status, and prestige as being a principal motivational factor in managerial decision-making.¹⁴⁴

2. Contributions as a Source of Psychic Rewards

Sociologists have documented the function of gift giving within diverse systems of status enhancement.¹⁴⁵ As documented by the work of Joseph Galaskiewicz, corporate grant-making partakes of this larger dynamic of status competition.¹⁴⁶ Galaskiewicz's study of the grant-making economy of the Minneapolis-St. Paul area demonstrated that corporate charitable contributions have served as a medium through which corporate executives have competed for the fellowship and esteem of elite nonprofit leaders and other business executives.¹⁴⁷

According to Galaskiewicz, nonprofit leaders have fueled this status competition by applying various forms of "peer pressure," including threats of social and professional ostracism.¹⁴⁸ Galaskiewicz described peer pressure as operating through themes of reciprocity (executives approved corporate contributions requests in the expectation that their own solicitations would be favorably received in the future)¹⁴⁹ and themes of community

URBAN GRANTS ECONOMY (1985); Lisa Atkinson & Joseph Galaskiewicz, *Stock Ownership and Company Contributions to Charity*, 33 ADMIN. SCI. Q. 82, 82-100 (1988).

144. OLIVER E. WILLIAMSON, *THE ECONOMICS OF DISCRETIONARY BEHAVIOR: MANAGERIAL OBJECTIVES IN A THEORY OF THE FIRM* 28-37 (1964). Williamson identified seven objectives: salary, security, status, power, prestige, social service, and professional excellence.

145. This literature is summarized by Joseph Galaskiewicz. See GALASKIEWICZ, *supra* note 143, at 14-30. Galaskiewicz described commonalities in the status-driven gift-giving rituals practiced by Indian tribes of the Pacific Northwest (in the form of the Potlach), *id.* at 26-27, by the "Big Men" of the New Guinea Highlands and the Solomon Islands (in various feasts and rituals), *id.* at 27-28, and in the more contemporary settings of American and British "nouveau riches," *id.* at 28-30.

146. *Id.* at 214. For a recent critique of charitable giving by individuals as a system of social status enhancement, see FRANCIE OSTROWER, *WHY THE WEALTHY GIVE: THE CULTURE OF ELITE PHILANTHROPY* 133 (1995) (concluding on the basis of interviews with wealthy New Yorkers that the very affluent use charitable contributions to create a distinct social and cultural life that fosters their elite status).

147. GALASKIEWICZ, *supra* note 143, at 214.

148. *Id.* at 74 ("Of the 26 respondents, 19 made some reference to the fact that individuals would either lose face before their peers in the business community or would be excluded from certain community events. . . . Several others talked about individuals losing esteem, respect, and standing among their business peers.").

149. *Id.* at 72. One of Galaskiewicz's survey respondents stated: "Peer pressure is responding to friends. Essentially, if you don't go along with their requests and pet projects, they won't support yours." *Id.*

(executives valued the ability to participate in local professional and social networks, and therefore authorized corporate contributions as part of the "price of admission").¹⁵⁰ Galaskiewicz also discovered that local non-profit leaders had superior professional and social credentials than their peer group of CEOs.¹⁵¹ Galaskiewicz thus concluded that corporate executives approved substantial corporate contributions as a means of qualifying for membership in an elite social and professional network that, as part of its function, oversaw substantial philanthropic activity.

Galaskiewicz also observed that firms that contributed at substantial levels were more likely to be regarded as financially successful business ventures.¹⁵² According to his research, this effect was created "independent of actual average annual pretax earnings and performance indicators."¹⁵³ Thus, corporate contributions have functioned as complex signifiers in the eyes of local commercial and philanthropic leaders.¹⁵⁴ By communicating a favorable message about their firm's financial robustness through the authorization of substantial corporate contributions, the executives were also communicating a message about their own status as modern day, financial "Big Men." Galaskiewicz's work supports the view that corporate executives have sought to "upgrade" their own professional and social credentials through the currency of corporate charitable contributions.

Galaskiewicz also sought to document the *relative* importance of commercial factors, in comparison to sociological ones, as determinants of corporate giving behavior. He reported finding "considerably more support for the Contributions-as-Social-Currency thesis than the Contributions-as-Public Relations thesis."¹⁵⁵ In fact, Galaskiewicz concluded that apart from firm cash-flow, sociological factors relating to executives' social standing had had a greater effect on contributions levels than did either the market position of the firm or its dependency on the local community for

150. *Id.* at 73 ("More commonly, executives portrayed peer pressure as a sort of ritual whereby people are integrated into the business community and attain social standing. For example, being solicited is a sign that one is part of the group. Responding to a solicitation indicates that one accepts membership.").

151. *Id.* at 76 ("For example, 56.7% of the [philanthropic] elite had been the president, CEO, or chairman of a Fortune 500 or 50 firm as compared to only 20.4% of the 98 CEOs.").

152. *Id.* at 71-78.

153. *Id.* at 71.

154. Usha Haley's work has also analyzed this signalling function of corporate contributions. Employing the terminology of Renaissance dramaturgy, he described corporate contributions as "masques"—i.e., complex symbolic messages communicated to a diverse set of publics. Haley, *supra* note 36, at 485-504.

155. GALASKIEWICZ, *supra* note 143, at 79.

employees, for example.¹⁵⁶ Galaskiewicz concluded that none of these commercially-based criteria had "had a statistically significant positive effect" on the level of firm contributions.¹⁵⁷

3. Nonprofit Board Service as Form of Benefit

In addition to increased prestige, esteem, and fellowship, the social currency accruing to corporate executives from their power over corporate charitable contributions frequently translates into tangible rewards. Most notably, charitable organizations commonly make invitations to senior corporate executives to serve on their boards of directors, especially when the firm's charitable support has been extensive or when additional contributions may be anticipated.¹⁵⁸ Consistent with the previous discussion, such board positions are regarded by many people as evidence of heightened social status. Moreover, the position on the charitable board would itself represent an increase in the executive's personal power in most cases, because the directors of nonprofit organizations exercise considerable discretion in the administration of the arts, education, environmental conservation, and the provision of social services, for example.

Yet even if nonprofit board service was not in itself considered a valuable fringe benefit of the corporation's philanthropy, most executives would value such charitable board positions for the collateral benefits likely to accrue therefrom—in terms of both personal and professional opportunities. For example, the directors of nonprofit organizations typically enjoy special invitations to gala benefits and opening night performances, and special audiences with politicians and celebrities. The accretion in *professional* capital arising from multiple board service was a central focus of Michael Useem's work, *The Inner Circle*. Useem documented the existence of a super-stratum of elite business leaders (the "inner circle") active in the formulation of American and British industrial and public policy.¹⁵⁹ One of his central findings was that multiple board service, including service on high profile nonprofit organizations' boards, has played a crucial part in the grooming process by which qualified corporate executives have ascended to

156. *Id.* at 70–80.

157. *Id.* at 70.

158. See Michael Useem, *Corporate Philanthropy*, in *THE NONPROFIT SECTOR* 340, 344 (Walter W. Powell ed., 1987) ("A conventional fund-raising strategy used by many nonprofits is to invite a senior manager onto the governing board as a first step toward soliciting large-scale support from his or her firm.").

159. MICHAEL USEEM, *THE INNER CIRCLE* (1984).

the upper echelons of the power elite. Nonprofit board service has provided executives with experience and connections that have contributed to their professional ascendancy both within the corporate hierarchy and beyond the firm. Thus, Useem's work also supports the view that corporate charitable contributions are a valuable currency through which corporate senior executives have purchased a variety of benefits, including enhanced professional power.

4. When Insiders Establish Charities and Subsidize Them Through Corporate Contributions

The above analysis is incomplete in representing CEOs and corporate directors as passively waiting to exchange a commitment for increased corporate support for an invitation to serve on a prestigious nonprofit organization's board of directors. The reality is that corporate executives often seize the initiative to establish charitable organizations reflecting their personal interests and then seek to have them subsidized through the firm's contributions.

The connection between insiders' pet causes and corporate contributions was illustrated by the relationship between Mary Cunningham Agee, the wife of Morrison Knudsen's CEO, and that company's gifts to The Nurturing Network (established by Ms. Agee), as described above.¹⁶⁰ But an example of more extraordinary managerial hubris is provided by Occidental Petroleum Corporation's ("OPC") commitment to fund "The Armand Hammer Museum and Cultural Center" through corporate charitable contributions in the amount of \$85 million dollars.¹⁶¹ Although it was approved by a committee of OPC's board of directors, the plan for the museum was initiated by Dr. Hammer himself.¹⁶² In fact, Dr. Hammer had planned to donate his art collection to the Los Angeles County Art Museum, but when that museum failed to acquiesce to his extraordinary demands, Dr. Hammer informed them that he "had decided to create [his] own museum"—hence his proposal to OPC's board.¹⁶³ Because of the substantial sums involved, and Dr. Hammer's obvious self-interest in the

160. See *supra* notes 128–132 and accompanying text.

161. The facts relating to OPC's commitment to fund the museum project through its charitable contributions are set forth in *Kahn v. Sullivan*, 594 A.2d 48, 52–57 (Del. 1991). For further discussion of Dr. Hammer's life and career at Occidental, see EDWARD JAY EPSTEIN, *DOSSIER: THE SECRET HISTORY OF ARMAND HAMMER* (1996).

162. *Kahn*, 594 A.2d at 52.

163. *Id.*

project, two groups of OPC shareholders filed suit challenging the propriety of the gift.¹⁶⁴ Operating on the basis of the loose standard of reasonableness described earlier, the Delaware courts upheld a settlement in one of the derivative suits, which left OPC's plans for the museum largely intact. Nevertheless, both the Chancery Court and the Supreme Court went out of their way to articulate their displeasure with OPC's board's approval of the charitable contributions.¹⁶⁵

D. Corporate Charitable Contributions as Income to Corporate Insiders

Because corporate managers may retain control over corporate charitable contributions, and may therefore "substitute" corporate contributions for personal ones, such contributions have sometimes been analogized to dividends or additional compensation to management.¹⁶⁶

1. Tax Jurisprudence

The current approach within federal income tax jurisprudence is to honor the separate identity of the corporate contributor,¹⁶⁷ but certain early tax court rulings dealing with close corporations' contributions had suggested that the correct approach would be to "look through" the corporate entity to view the company's contributions as a constructive dividend to the controlling shareholders, followed by a personal contribution on

164. Because of the lax standards applicable in the area of corporate charitable contributions (as described above), as well as the loose definition of "independence" applied to determining the objectivity of "outside" directors, the shareholders had virtually no chance of succeeding in their challenge to the gifts. For discussion of the relevant state law standards applying to corporate charitable contributions, see *supra* notes 91-114 and accompanying text.

165. See *Kahn*, 594 A.2d at 58 n.23 ("If the Court was a stockholder of Occidental it might vote for new directors, if it was on the Board it might vote for new management and if it was a member of the Special Committee it might vote against the Museum project.").

166. As Nancy Knauer has observed, "If a corporate transfer to charity is really a substitute for a transfer by a corporate manager, then the ability to claim the deduction at the corporate level produces a favorable tax benefit for the corporate manager." Knauer, *supra* note 77, at 48. As Knauer explains, the individual level income tax deduction for the charitable contribution may not produce a neutral tax consequence for individual taxpayers receiving corporate dividends.

167. For an excellent critique of the tax code's failure to examine who is responsible for making the contribution (and hence who should enjoy the deduction) in the case of corporate level gifts, see Linda Sugin, *Theories of the Corporation and the Tax Treatment of Corporate Philanthropy*, N.Y.L. SCH. L. REV. (forthcoming 1997).

their part.¹⁶⁸ Under this earlier approach, corporate level contributions that “serve only the personal interest of the shareholder,”¹⁶⁹ could be treated as constructive income to such controlling shareholders. Tax jurisprudence has subsequently moved away from this position, validating the distinction between corporate level gifts and controlling persons’ personal contributions.¹⁷⁰ And dividends to controlling shareholders are distinct, formally, from additional compensation to corporate management. Nevertheless, the existence of this earlier, alternative approach in the tax treatment of corporate charitable contributions underscores the fact that controlling parties (controlling shareholders in close corporations, and managers in public corporations) accrue personal benefits in their administration of corporate charitable contributions—especially when such contributions are not required by law to advance the interests of the corporate donor.

2. Required Disclosure of “Charitable Awards”

Although tax jurisprudence has moved away from treating corporate charitable contributions as income to those persons authorizing them, the SEC has recently taken a position reminiscent of the earlier tax cases.¹⁷¹

168. See Rev. Rul. 68-658, 1968-2 C.B. 117 (superseding Rev. Rul. 68-314, 1968-1 C.B. 101; revoked by Rev. Rul. 79-9, 1979-1 C.B. 125):

It has been held that a payment or gratuitous disposition of property by a corporation to a third person on behalf of or for the benefit of the controlling shareholder is a distribution to the shareholder if the payment serves only the personal interests of the shareholder. (Citations omitted.) Thus, a charitable contribution by a corporation to an organization described in section 170 (c)(2) of the Code, which contribution in reality serves only the personal objectives of its sole shareholder, is tantamount to a distribution to the shareholder followed by a donation on his part to the charitable organization.

But cf. *Knott v. Commissioner*, 67 T.C. 681 (1977), acq. 1979-1 C.B. 1.

169. Rev. Rul. 68-658, 1968-2 C.B. 117. This more thoughtful approach addressed who, in particular, should qualify as making the gift and being eligible for the deduction—the entity or the individuals in control. But, unintentionally, it also raised the problem of whether gifts that did serve corporate objectives (rather than insiders’) could still qualify as “charitable” for purposes of § 170.

170. In refusing to disallow the corporate level charitable contribution in the case of *Knott v. Commissioner*, the tax court also emphasized the absence of the receipt of tangible benefits by the controlling shareholders as a result of the corporation’s contribution. *Knott*, 67 T.C. at 681.

171. In October 1992 the SEC completed its long-standing project of revising the executive compensation disclosure provisions under Item 402 of the S-K regulations. Recognizing that disclosure operates as a significant check on managerial overreaching in the area of compensation, the SEC sought to require more accurate and comprehensive disclosure of all forms of compensation arrangements. See Executive Compensation Disclosure, Release No. 33-6962, 34-31327, 57 Fed. Reg. 48,126 (Oct. 21, 1992).

In 1992, in order to provide for greater clarity and comprehensiveness therein, the SEC amended the executive compensation disclosure requirements pertaining to proxy statements and periodic reports.¹⁷² In the final release implementing the new rules, the SEC indicated that it viewed "charitable award or legacy arrangements" as forms of management compensation subject to required disclosure.¹⁷³ In the typical charitable award arrangement, the corporation makes a commitment to fund a charitable contribution in the name of the specified director or officer for the benefit of a charity of his or her choice, at a specified future date.¹⁷⁴ The contributions are characteristically funded from insurance plans, typically in the amount of \$1 million dollars, which are purchased by the corporation for this purpose. The insurance plan pay-out is usually tied to the named executive's retirement or death.¹⁷⁵ The fact that the executives never directly receive any payments in these arrangements had created confusion regarding whether such awards would be considered part of executive compensation by the SEC. However, in the final release implementing the revised executive compensation disclosure rules, the SEC stated its view that charitable awards confer substantial benefits on the named executives, and would hence be regarded as part of the required disclosure.¹⁷⁶

172. *Id.* at 48,137.

173. The release described charitable awards as follows:

Under such programs, registrants typically agree to make a future donation to one or more charitable institutions in a participating director's name, payable by the registrant upon the director's death or retirement, or some other designated event. Funding vehicles for these programs commonly take the form of corporate-owned insurance policies on the lives of participating directors.

Id.

174. See Lawrence Brody et al., *Insurance-Related Compensation*, 386-2d Tax Mgmt. (BNA) A-22 (1994) ("One of the more innovative executive perks in recent years has been executive legacy programs. . . . These programs give focus to a corporation's charitable giving strategy and turn it into a 'benefit' for executives. Even though nothing goes directly to the executive under the program, there is a perceived benefit in having a major charitable gift made in the executive's name.").

175. *Id.*

176. *Executive Compensation Disclosure*, 57 Fed. Reg. at 48,137. It should also be noted that charitable awards are not a form of *incentive-based* compensation: Neither the establishment of the award nor the circumstances that trigger a pay-out are typically related to the firm's financial performance. Scholars, commentators, and even the SEC have increasingly advocated increased levels of incentive-based compensation. See, e.g., *id.* at 48,126; see also Geoffrey S. Rehnert, Note, *The Executive Compensation Contract: Creating Incentives to Reduce Agency Costs*, 37 STAN. L. REV. 1147 (1985). *Forbes* magazine recently reported on the increasing use of charitable awards as part of compensation to outside directors. See Dana Wechsler Linden et al., *The Cosseted Director*, FORBES, May 22, 1995, at 169-73. Of particular note were the following (ag-

3. Ordinary Contributions Versus Charitable Awards

Thus, charitable awards are subject to mandatory disclosure under existing securities regulations, while "ordinary" corporate contributions are subject to no such disclosure requirement—despite the fact that corporate insiders may use ordinary contributions to confer substantial benefits on themselves, as described above. Indeed, the differences between charitable awards and ordinary contributions are frequently essentially formalistic. In both instances, the corporation funds the contributions. In the case of charitable awards, the corporation purchases an insurance policy that will generate funds for the contributions, whereas regular charitable contributions are funded from corporate earnings. In both situations, corporate directors or officers may have dispositional authority over the gift—whether through the formalized arrangements of the charitable award or through the ordinary dispositional authority that executives may retain over corporate contributions. In the case of charitable awards, the executive's name is formally associated with the donation—but this may be equally true in the case of regular contributions, as was illustrated by the example of the Armand Hammer Museum and Cultural Center.¹⁷⁷ Even when the executive's name is not formally associated with the firm's charitable gifts, he or she stands to gain both psychic income and tangible benefits from authorizing them. Indeed, these benefits more readily accrue to corporate executives in the context of ordinary contributions, because in the case of charitable awards the corporate official is typically retiring or may even be deceased.

In sum, the differences between charitable awards and ordinary corporate charitable contributions do not support disparate disclosure treatment. The managerial benefits that the SEC has recognized in the context of charitable awards may just as frequently inhere in the context of ordinary corporate contributions. The SEC's current disclosure mandate is thus substantially underinclusive: Comprehensive disclosure of corporate charitable contributions information is the appropriate standard that should be implemented by the SEC.

gregated) charitable awards: Vernon Jordan, Jr. (\$3.25 million), Frank Carlucci (\$2 million), Clayton Yeutter (\$1.5 million), Harold Brown (\$1 million), and Ann McLaughlin (\$1 million). According to the *Forbes* article, Ayco Co. (a financial advisory firm) indicated that it was setting up charitable awards for directors at the rate of one every two weeks. *Id.* at 170.

177. See *supra* note 161 and accompanying text.

E. Disclosure and the Problem of Managerial Self-Dealing

The federal securities laws reflect the view that systematic, required disclosure of corporate information, in conjunction with the operation of the marketplace, will operate as a check on various forms of managerial opportunism.¹⁷⁸ This view is evident in the SEC's regulations requiring disclosure of interlocking corporate directorships, loans to insiders and other "interested" corporate transactions, executive compensation generally, and charitable awards in particular.¹⁷⁹ In each of these cases, state corporation law and federal disclosure requirements (taken in combination) reflect a consensus that, while the underlying behavior should be (or must be, in the case of executive compensation, for example) permitted, a system of accountability based on required publicity is needed to deter corporate waste and mismanagement. Corporate charitable contributions present analogous problems of managerial conflicts of interest, and yet there are strong arguments for continuing to permit corporations to make charitable contributions.¹⁸⁰ Moreover, the argument in favor of a precise system of substantive regulation, and attendant penalties for noncompliance, is undermined by the difficulty of measuring and offsetting potential gains to

178. The extensive legislative history surrounding the enactment of the Securities Acts is presented in LEGISLATIVE HISTORY OF THE SECURITIES ACT OF 1933 AND SECURITIES EXCHANGE ACT OF 1934 (Jack S. Ellenberger & Ellen P. Mahar eds., 1973) [hereinafter LEGISLATIVE HISTORY]. Concerns over insider overreaching and the disempowerment of public shareholders are expressed, in particular, in S. REP. NO. 73-1455, at 30 (1934) (the "Fletcher Report"), reprinted in 5 LEGISLATIVE HISTORY, *supra*, at Item 21, which describes trading and operational abuses and the need to enlighten shareholders through enhanced disclosure and improved mechanisms of shareholder suffrage, and H.R. REP. NO. 73-1383, at 13 (1934) (the "Rayburn Report"), reprinted in 5 LEGISLATIVE HISTORY, *supra*, at Item 18 (section entitled "Control of Unfair Practices by Corporate Insiders"). The classic statement of disclosure's operation as a prophylaxis against abuse is that of Louis D. Brandeis: "Sunlight is said to be the best of disinfectants; electric light the most efficient policemen." LOUIS D. BRANDEIS, OTHER PEOPLE'S MONEY 92 (1914). Also noteworthy is President Roosevelt's statement upon the enactment of the Securities Act: "What we seek is to return to a clearer understanding of the ancient truth that those who manage banks, corporations, and other agencies handling or using other people's money are trustees acting for others." S. REP. NO. 73-47, at 6-7 (1933), quoted in 1 LOSS & SELIGMAN, *supra* note 121, at 178-79. For analysis of the SEC's mandate, pursuant to the Exchange Act, to effectuate systematic corporate reporting for the protection of investors, see Jill E. Fisch, *From Legitimacy to Logic: Reconstructing Proxy Regulation*, 46 VAND. L. REV. 1129 (1993).

179. For the relevant S-K disclosure requirements, see 17 C.F.R. §§ 229.401, .402, .404 (1996). The release announcing the amended executive compensation disclosure rules also describes disclosure as a means of deterring abuse. See Executive Compensation Disclosure, 57 Fed. Reg. at 48,137. For recent commentary on the relationship between rigorous financial reporting standards and the promotion of effective corporate governance, see Louis Lowenstein, *Financial Transparency and Corporate Governance: You Manage What You Measure*, 96 COLUM. L. REV. 1335 (1996).

180. These arguments are presented *infra* note 187.

insiders from corporate contributions, potential gains to corporations therefrom, and the increased costs of shareholder litigation arising from such a regulatory initiative. Nevertheless, the ability of managers to use corporate contributions to benefit themselves at the expense of shareholders, without there necessarily being any offsetting benefits to the corporation, is not only a real and significant potentiality, but one that is presently condoned by state and federal law. Consistent with the general philosophy of the federal securities laws and regulations, required disclosure of corporate charitable contributions is likely to import an appropriate measure of judiciousness in corporate executives' oversight of corporate contributions programs. The means to effect the professionalization of the contributions function are increasingly available to corporate management, so are the means to inquire about shareholders' preferences in regard thereto. A disclosure requirement would signal to managers, and to shareholders, the need to value contributions as strategic resources, or alternatively, the need to evaluate philanthropic practices in light of shareholder preferences.

IV. CORPORATE DONATIONS AND CORPORATE SOCIAL RESPONSIBILITY

Many public corporations donate millions of dollars each year in the name of "corporate social responsibility."¹⁸¹ Corporate executives frequently cite corporate social responsibility as the principal motivation behind their charitable donations,¹⁸² and public corporations' reports to

181. The definitional problems presented by the term "corporate social responsibility" are discussed *infra* note 191. At this juncture, I wish to clarify that this Article does not take a position in the debate over the propriety of philanthropically motivated corporate charitable contributions. Rather, my central objective in this Part of the Article is to emphasize that views on corporate social responsibility (including philanthropically motivated corporate contributions) are inherently political. I argue, therefore, that they should be subject to a more democratic decisional process than applies in regard to traditional, commercial corporate conduct. See David L. Engel, *An Approach to Corporate Social Responsibility*, 32 STAN. L. REV. 1, 1 (1979) ("The resolution of nearly every issue of corporate social responsibility depends heavily on one's beliefs about how our political process operates and one's convictions about the ideal political process.").

182. See, e.g., *A.P. Smith Mfg. Co. v. Barlow*, 98 A.2d 581, 582-83 (N.J. 1953) (testimony of Smith company executives describing corporate social responsibility as a basis for corporate philanthropy); NEIL J. MITCHELL, *THE GENEROUS CORPORATION: A POLITICAL ANALYSIS OF ECONOMIC POWER passim* (1989); Business Roundtable, *Corporate Governance and American Competitiveness March 1990*, 46 BUS. LAW. 241 (1990); Linda D. Lerner & Gerald E. Fryxell, *CEO Stakeholder Attitudes and Corporate Social Activity in the Fortune 500*, BUS. & SOC'Y, Apr. 1994, at 58, 59 ("Top managers increasingly operate from a perspective that recognizes the importance of managing or balancing the needs and demands of a variety of constituencies or stakeholder groups."). Various studies have documented executives' favorable views of corporate social responsibility and of corporate charitable giving as a vehicle for fulfilling corporate obligations to society. See, e.g., Joseph Galaskiewicz, *Corporate Contributions to Charity: Nothing More than a*

shareholders have frequently spoken in terms of corporate "citizenship" and "corporate obligations to the community" in describing corporate charitable contributions. The media, too, has fostered the image of the socially responsible corporation in its popular reporting on corporate gifts.¹⁸³ Some of the statements about business' social responsibilities have reflected shrewd business strategy,¹⁸⁴ but arguments about business' "enlightened self-interest" have not replaced the notion of the truly philanthropic corporation.¹⁸⁵ In light of its durability throughout this century,¹⁸⁶ the

Marketing Strategy?, in PHILANTHROPIC GIVING 246, 249-50 (Richard Magat ed., 1989) (describing 1982 study for Council on Foundations finding that "[a]bout 7 in 10 [executives] claim to be motivated by a desire to help the needy in the communities in which their company has plants/locations and by a desire to do what is ethically correct," along with less altruistic goals); Charles Peter Corcoran, *Corporate Philanthropy: Attitudes of Institutional Shareholders, Individual Shareholders, and Corporate Philanthropy Executives* 201 (1987) (unpublished Ph.D. thesis, University of Minnesota) (on file with author) (finding broad-based support among corporate executives for the proposition that "shareholders' interests go beyond purely economic considerations," notwithstanding that "profits from corporate philanthropy are uncertain"); John J. Siegfried & Katherine Maddox McElroy, *Corporate Philanthropy in the U.S.* (1980) (Working Paper No. 81-W26, Vanderbilt University, Department of Economics) (surveys indicated that corporate managers overseeing philanthropy programs regarded corporate social responsibility as the most important reason for making contributions), cited in CLOTFELTER, *supra* note 22, at 172.

183. Prior to the late 1980s, the media routinely described corporate charitable contributions in terms of social responsibility. This has changed, however. The current trend in media reporting, and in executives' remarks describing contributions, is to highlight the "strategic benefits" that may accrue to the firm therefrom—for example, favorable publicity, public goodwill, and political favor. In this vein, see, for example, RICHARD STECKEL & ROBIN SIMONS, *DOING BEST BY DOING GOOD* (1992); Smith, *supra* note 47.

184. The goodwill generated from the firm's reputation for generosity may be translatable, in certain instances, into monetary gains. For this reason, corporate charitable contributions are frequently described as being a matter of business' "enlightened self-interest." For an influential treatment of the concept of business' enlightened self-interest, see W.J. Baumol, *Enlightened Self-Interest and Corporate Philanthropy*, in COMMISSION ON FOUNDATIONS AND PRIVATE PHILANTHROPY, *supra* note 49, at app. VI (1970). The term has gained widespread currency. For further discussion, see Part VI *infra*.

185. From a philosophical perspective, various authors have questioned the soundness of speaking of the firm as capable of acting "charitably." See, e.g., Bill Shaw & Frederick R. Post, *A Moral Basis for Corporate Philanthropy*, 12 J. BUS. ETHICS 745 (1993); Menlo Smith & Patrick Mendis, *Should Corporations Be Charitable?*, 89 BUS. & SOC'Y REV. 19 (1994). More generally, for a discussion of altruism within economic theory, see, for example, Natalie S. Glance & Bernardo A. Huberman, *The Dynamics of Social Dilemmas*, SCI. AM., March 1994, at 76; John Haltiwanger & Michael Waldman, *The Role of Altruism in Economic Interaction*, 21 J. ECON. BEHAV. & ORG. 1 (1993); Herbert A. Simon, *Altruism and Economics*, AM. ECON. REV., May 1993, at 156; Robert Sugden, *Thinking as a Team: Towards an Explanation of Nonselish Behavior*, SOC. PHIL. & POL'Y, Winter 1993, at 69.

186. The belief that corporations should affirmatively embrace social responsibilities beyond wealth maximization has had distinguished critics. See, e.g., Milton Friedman, *The Social Responsibility of Business Is to Increase Its Profits*, N.Y. TIMES, Sept. 13, 1970, (Magazine), at 32; see also MILTON FRIEDMAN, *CAPITALISM AND FREEDOM* 133-34 (1962); MANNE & WALLICH, *supra* note 140; STUART NOLAN, *PATTERNS OF CORPORATE PHILANTHROPY* (1994); Eugene V. Rostow, *To Whom and for What Ends Is Corporate Management Responsible?*, in THE

notion of the philanthropic corporation (as one incident of the socially responsible corporation) deserves distinct consideration as a matter of law and policy.¹⁸⁷

A. Managerial Control over Corporate Social Responsibility

As described above, state law has validated corporate authority to make donations irrespective of benefit to the firm. But because the law has stopped short of *mandating* corporate charitable giving, decisions regarding the allocation of corporate capital for charitable purposes must be made individually by each firm. For this reason, the establishment of a corporate philanthropy program as part of the firm's objectives is inextricably linked to the question of the allocation of decision-making power within the firm. The centralized administration of corporate resources has traditionally been legitimated on the basis of managerial expertise,¹⁸⁸ but this rationale is

CORPORATION IN MODERN SOCIETY 46 (Edward S. Mason ed., 1960); Paul H. Weaver, *After Social Responsibility*, in THE U.S. BUSINESS CORPORATION: AN INSTITUTION IN TRANSITION 133 (John R. Meyer & James M. Gustafson eds., 1988). Corporate social responsibility has also had formidable advocates. See, e.g., RALPH NADER ET AL., TAMING THE GIANT CORPORATION (1976); CHRISTOPHER D. STONE, WHERE THE LAW ENDS (1975).

187. Although they are too complex to be discussed in depth, some of the arguments both in favor of and against philanthropic corporate contributions may be summarized as follows. (Only the first rationale is directly tied to shareholders' interests.) First, the centralized administration of corporate contributions saves shareholders time and effort, in comparison to the process of individual contributing. Of course, the very serious trade-off is a loss of individual choice in the selection of beneficiaries. Moreover, tax expenditures are meant to foster individual choice and diversity, values that are undermined when the federal subsidy is located at the corporate level. Second, the current tax system provides a substantial incentive for firm-level giving. If one (or society) is primarily concerned with maximizing the value of contributions received by charities, corporate giving is superior to individual giving after the receipt of corporate dividends. Of course, at least theoretically, the tax system could be changed to eliminate this preference, but no such change is likely to be forthcoming. Third, the centralized administration inherent in corporate grant-making, and the ability of corporate grant makers to wield substantial resources, may increase accountability and good management at charitable organizations. On the other hand, it is inherently risky for charitable organizations to become too dependent on a small group of large donors, such as corporations. Fourth, in an environment of underregulation, corporate charitable contributions may reflect the internalization of costs which would otherwise be imposed on innocent third parties (e.g., gifts to environmental groups reduce the effects of pollution). Firms may attempt to forestall further, mandatory regulation in this manner, potentially reducing costs overall. However, the potential for firms effectively to address larger social problems in this ad hoc manner, in the absence of stated public policies and objectives, is uncertain. Also, certain commentators argue that contributions function as fancy bribes, thereby undermining the political (and regulatory) process. Lastly, the distribution of benefits to the community (i.e., free-riders) through philanthropic contributions, as a side-effect of benefits targeted at employees, may be regarded as an acceptable cost of doing business.

188. For the alternative argument that claims of managerial expertise within corporate law operate as political sops designed to legitimize the status quo, see Frug, *supra* note 98.

inapposite in the context of corporate altruism. Thus, the present managerial control over philanthropically motivated corporate contributions has failed to offer a sufficient account of its legitimacy.

In fact, the problem of legitimacy or decisional authority in regard to philanthropically motivated corporate charitable contributions is ultimately a crucial one. Serious consideration of the corporate social responsibility debate yields the conclusion that there cannot be a definitive, authoritative resolution to the problem of allocating responsibility between government, business, and individual persons.¹⁸⁹ Rather, assertions regarding corporate social responsibility mask complex, normative conclusions about the interrelation of the public and private sectors, the functioning of the capital markets, the power of corporate management, and the nature of corporate shareholdership. The existing empirical analysis in this area fails to resolve the problem of defining (or designing) optimal institutional arrangements. Because questions relating to corporate social responsibility and philanthropically motivated corporate contributions are properly regarded as matters of social policy or politics, principles of consensus-building and accountability must be substituted for objective assertions of right. With respect to the best interests of shareholders, therefore, the question of whether the firm should make philanthropically motivated charitable contributions is best addressed through a process of controlled experimentation in an environment promoting managerial accountability and receptivity to shareholders' concerns.¹⁹⁰

B. The Definition and Development of Corporate Social Responsibility

1. Defining Corporate Social Responsibility

There is no authoritative definition of corporate social responsibility,¹⁹¹ but its central tenet can be described as the belief that busi-

189. Engel, too, concluded that these fundamental normative questions cannot be resolved on the level of generalities, but rather require issue by issue analysis in particular substantive areas. See Engel, *supra* note 181, at 3-4.

190. In this vein, see *Medical Committee for Human Rights v. SEC*, 432 F.2d 659 (D.C. Cir. 1970), *vacated as moot*, 404 U.S. 403 (1972).

191. The profound difficulty in arriving at an acceptably clear definition of corporate social responsibility has been noted throughout the literature. For a good working definition, see Engel, *supra* note 181, at 5-6: "The term [corporate social responsibility] is most useful if taken to denote the obligations and inclinations, if any, of corporations organized for profit, voluntarily to pursue social ends that conflict with the presumptive shareholder desire to maximize profit." See also MANNE & WALLICH, *supra* note 140, at 3-8. In light of definitional and other conceptual difficulties, a substantial portion of the social responsibility literature has existed at a high level of

nesses, especially large, public corporations, have an obligation to contribute to the betterment of society in a manner distinct from the maximization of corporate profit and obedience to the law.¹⁹²

Typically, the arguments in favor of corporate social responsibility can be reduced to three distinct conceptual grounds.¹⁹³ First, there is an appeal to social *necessity*: The financial needs of arts, education, and community service organizations exceed the capacity of individuals and the government to fund them.¹⁹⁴ Second, there is an appeal based on corporate *capacity*: As a result of their vast scale and scope, American business corporations are in a position to be agents of social progress.¹⁹⁵ Lastly there is an appeal based on *morality*, in which the corporation is likened to a "citizen" having moral and ethical responsibilities analogous to those of natural persons.¹⁹⁶ In sum, the ideology of corporate social responsibility

abstraction or, otherwise, has addressed the problem of "means" without resolving other basic issues. For an important critique of the means literature, and particularly the notion that a system of independent directors might resolve social responsibility issues, see Victor Brudney, *The Independent Director—Heavenly City or Potemkin Village?*, 95 HARV. L. REV. 597 (1982). For an intelligent critique of the corporate social responsibility debate as a dialectic about the scope of public and private affairs, see Alan Wolfe, *The Modern Corporation: Private Agent or Public Actor?*, 50 WASH. & LEE L. REV. 1673 (1993). See also William T. Allen, *Our Schizophrenic Conception of the Business Corporation*, 14 CARDOZO L. REV. 261 (1992) (arguing that corporate law's inability to choose between private property and social responsibility norms reflects the fundamental duality of human nature). Definitional problems have also hindered economic analysis of the relation between corporate social responsibility expenditures and corporate financial performance. See, e.g., Kenneth E. Aupperle et al., *An Empirical Examination of the Relationship Between Corporate Social Responsibility and Profitability*, 28 ACAD. MGMT. J. 446–63 (1985); Arieh A. Ullmann, *Data in Search of a Theory: A Critical Examination of the Relationships Among Social Performance, Social Disclosure, and Economic Performance of U.S. Firms*, 10 ACAD. MGMT. REV. 540 (1985).

192. Within the management science literature, see, for example, William C. Frederick, *From CRS 1 to CRS 2: The Maturing of Business-and-Society Thought*, BUS. & SOC'Y, Aug. 1994, at 150. See also Lerner & Fryxell, *supra* note 182.

193. This intellectual construct is based on my interpretation of the charitable contributions cases, as well as a survey of the commentary on corporate social responsibility, as cited herein.

194. See, e.g., *Theodora Holding Corp. v. Henderson*, 257 A.2d 398 (Del. Ch. 1969); *A.P. Smith Mfg. Co. v. Barlow*, 98 A.2d 581, 585–86 (N.J. 1953) ("With the transfer of most of the wealth to corporate hands and the imposition of heavy burdens of individual taxation, [individuals] have been unable to keep pace with increased philanthropic needs. They have therefore, with justification, turned to corporations to assume the modern obligations of good citizenship in the same manner as humans do."); MANNE & WALLICH, *supra* note 140; Blumberg, *supra* note 46. For influential arguments in favor of corporate responsibility efforts, see NADER ET AL., *supra* note 186; STONE, *supra* note 186.

195. *A.P. Smith*, 98 A.2d at 584 ("Control of economic wealth has passed largely from individual entrepreneurs to dominating corporations, and calls upon the corporations for reasonable philanthropic donations have come to be made with increased public support.").

196. Such personification is evident in the ALI's treatment of the subject of corporate purpose, for example. See ALI, *supra* note 14. In defining the objective and conduct of the corporation, § 2.01(b) provides, in pertinent part:

holds that in light of pressing social needs, the vastness of corporate wealth and power, and evolving ethical norms, corporate America should make increased social expenditures.¹⁹⁷

2. A Brief Intellectual and Legal History

The evolution of corporate social responsibility as a distinct perspective on industrial and social organization has been associated with economic and intellectual developments occurring within the United States early in the twentieth century. By the teens and the twenties, with the themes of Progressive-era politics in the air, there was no denying the increasing concentration of wealth in corporate hands.¹⁹⁸ According to Neil Mitchell's *The Generous Corporation*, by this time the notion of free competition no longer supplied satisfactory justification for the visible accumulation of corporate wealth. Corporate executives therefore turned to corporate "social" spending as a means to persuade both labor and the general public that business' wealth and power would not be subversive to the public interest.¹⁹⁹ According to Mitchell, most of these expenditures were directed at employees and their families. They included corporate-funded pension benefits, life insurance, access to medical care, improved working conditions generally, and of course, charitable contributions.²⁰⁰ From a legal perspective, it was during this period that certain states first enacted statutes authorizing corporate charitable contributions.²⁰¹

Even if corporate profit and shareholder gain are not thereby enhanced, the corporation, in the conduct of its business: . . .

. . . .
 (2) May take into account ethical considerations that are reasonably regarded as appropriate to the responsible conduct of business;

Id. § 2.01(b). The question of corporate moral agency has, historically, been related to discussions of the nature of the corporation. See, e.g., Allen, *supra* note 191; David Millon, *Theories of the Corporation*, 1990 DUKE L.J. 201. For a slightly different perspective, see Jeffrey Nesteruk, Bellotti and the Question of Corporate Moral Agency, 1988 COLUM. BUS. L. REV. 683.

197. As others have noted, the combined operation of the corporate philanthropy statutes and the business judgment rule has meant that executives' social responsibility decisions will generally be immune from shareholder attack. See Davis, *supra* note 46. Defenses of managerial prerogative in this area have often been couched in the language of long-term benefit to the firm, as noted by Davis and Chancellor Allen. See Allen, *supra* note 191, at 273 ("The long-term/short-term distinction preserves the form of the stockholders oriented property theory, while permitting, in fact, a considerable degree of behavior consistent with a view that sees public corporations as owing social responsibilities to all affected by their operation.").

198. See, e.g., BERLE & MEANS, *supra* note 17; see also MITCHELL, *supra* note 182.

199. MITCHELL, *supra* note 182, at 10-25.

200. *Id.*

201. See *supra* notes 66-76 and accompanying text.

Thereafter, the problem of business' social responsibilities received serious academic consideration in the early 1930s in a series of polemical essays exchanged between Columbia Law School's Adolf A. Berle, Jr. and Harvard Law School's E. Merrick Dodd, Jr.²⁰² In *The Modern Corporation and Private Property*, Berle and Means had described the increasing separation of ownership from control in the public corporation as having "placed the community in position to demand that the modern corporation serve not alone the owners or the control but all society."²⁰³ In light of his concern over licensing managerial overreaching, Berle backed away from this position in his essay, *Corporate Powers as Powers in Trust*. But it was too late to quell debate. In 1932, Dodd argued that the new institution of the modern corporation was consistent with business assuming increased responsibility to address social problems.²⁰⁴ In fact, Dodd argued that "public opinion" had already made "substantial strides in the direction of a view of the business corporation as an economic institution which has a social service as well as a profit-making function."²⁰⁵ And, consistent with Dodd's view of the matter, Congress enacted a federal income tax deduction for corporate charitable contributions in 1935.²⁰⁶

Claims regarding business' social responsibilities and the propriety of managers allocating corporate capital on this basis have been made throughout the second half of the twentieth century. Consistent with what Jeffrey Gordon has described as the "high tide of benevolent managerialism"²⁰⁷ and in light of the various economic advantages enjoyed by American business at the time, the 1950s witnessed the enactment of unrestrict-

202. Adolf A. Berle, Jr., *Corporate Powers as Powers in Trust*, 44 HARV. L. REV. 1049 (1931); Berle, *supra* note 138, at 1365; E. Merrick Dodd, Jr., *For Whom Are Corporate Managers Trustees?*, 45 HARV. L. REV. 1145 (1932) [hereinafter Dodd, *For Whom Are Corporate Managers Trustees?*]; E. Merrick Dodd, Jr., *Is Effective Enforcement of the Fiduciary Duties of Corporate Managers Practicable?*, 2 U. CHI. L. REV. 194 (1935); see also A.A. Sommer, Jr., *Whom Should the Corporation Serve? The Berle-Dodd Debate Revisited Sixty Years Later*, 16 DEL. J. CORP. L. 33 (1991) (describing issues addressed in the Berle-Dodd debate in relation to the evolving jurisprudence on hostile tender offers).

203. BERLE & MEANS, *supra* note 17, at 356.

204. Dodd, *For Whom Are Corporate Managers Trustees?*, *supra* note 202, at 1153.

205. *Id.* at 1148.

206. The enactment of the corporate charitable contribution deduction in 1935 must be viewed as congressional validation of genuinely philanthropic corporate contributions, because business-related donations would already have been deductible under existing Code provisions. Revenue Act of 1936, ch. 690, 49 Stat. 1648, 1661 (1936); see also *Union Pac. R.R. v. Trustees, Inc.*, 329 P.2d 398, 400 (Utah 1958) ("In 1935 Congress encouraged corporate contributions to eleemosynary causes by allowing a deduction for tax purposes in such cases.").

207. Jeffrey N. Gordon, *Corporations, Markets, and Courts*, 91 COLUM. L. REV. 1931, 1982 (1991).

tive corporate philanthropy laws by many states. In fact, without conceding that he had been wrong, Berle acknowledged in 1954 that the theory of corporate social responsibility advocated by Dodd (consistent with Dodd's prediction) had come to occupy the field of popular opinion and the law.²⁰⁸ Thereafter, throughout the social upheaval of the late 1960s and early 1970s, increasingly vocal demands were made on business to take part in ameliorating social problems.²⁰⁹

3. Recent Developments

Despite the increasingly conservative tone of political debate since the early 1980s, notions of corporate social responsibility have become embedded in public policy discourse and in the law. Several U.S. presidents, including former Presidents Reagan and Bush, have called for increased corporate social spending.²¹⁰ And from a legislative perspective, in 1981,

208. Twenty years ago, the writer had a controversy with the late Professor E. Merrick Dodd, of Harvard Law School, the writer holding that corporate powers were powers held in trust for shareholders while Professor Dodd argued that these powers were held in trust for the entire community. The argument has been settled (at least for the time being) squarely in favor of Professor Dodd's contention.

ADOLF A. BERLE JR., *THE TWENTIETH CENTURY CAPITALIST REVOLUTION* 169 (1954); see also *A.P. Smith Mfg. Co. v. Barlow*, 98 A.2d 581, 586 (N.J. 1953) ("[M]odern conditions require that corporations acknowledge and discharge social as well as private responsibilities as members of the communities within which they operate.").

209. Engaging in some hyperbole, the Delaware Chancery Court, in the case of *Theodora Holding Corp. v. Henderson*, described the corporate philanthropy statutes in the states as reflecting "[t]he recognized obligation of corporations towards philanthropic, educational and artistic causes." *Theodora Holding Corp. v. Henderson*, 257 A.2d 398, 404 (Del. Ch. 1969) (emphasis added). The same sensibility is reflected in Blumberg, *supra* note 46. Also, the Project on Corporate Social Responsibility initiated "Campaign GM" in 1970, in which approval of GM's shareholders was sought in regard to a number of social responsibility initiatives. For description and commentary, see Donald E. Schwartz, *The Public-Interest Proxy Contest: Reflections on Campaign GM*, 69 MICH. L. REV. 419 (1971); and for a history of the development of the shareholder proposal system, which has been used as a vehicle for substantial shareholder advocacy in the area of social responsibility since the 1970s, see Jayne W. Barnard, *Shareholder Access to the Proxy Revisited*, 40 CATH. U. L. REV. 37 (1990); Fisch, *supra* note 178.

210. On December 3, 1981, President Ronald Reagan announced the establishment of the Task Force on Private Sector Initiatives, which called upon businesses to devote time and money to working with community organizations to address social problems (in light of reduced public sector aid). See *Reagan Names 44 to Special Group on Charity*, N.Y. TIMES, Dec. 3, 1981, at D27; see also *Reagan Delivers Challenge to Business*, WASH. POST, Feb. 14, 1982, at K1; *Reagan Study Group Urges Donations of 5% for Charity*, N.Y. TIMES, Mar. 25, 1982, at A26; *Roundtable Urges CEOs to Increase Volunteerism*, INDUSTRY WEEK, June 28, 1982, at 14; 32 *State Private Sector Initiative Panels Formed*, INDUSTRY WEEK, June 28, 1982, at 14. As part of his America 2000 educational reform initiative, President Bush announced the establishment of the New American Schools Development Corporation, which immediately raised \$30 million "from business interests

in the context of enacting the Economic Recovery Act, Congress reinforced its commitment to encouraging corporate philanthropy by increasing the annual ceiling pertaining to the corporate charitable deduction from 5% to 10% of annual corporate profits.²¹¹ In so doing, Senators Byrd and Kennedy spoke emphatically about the need for increased corporate philanthropy and the importance of corporate social responsibility in general.²¹²

Within corporation law, certain commentators have interpreted the enactment of the so-called "constituency statutes" by many states during the 1980s as evidence of the continued currency of theories of corporate social responsibility.²¹³ Enacted in the context of an active market for corporate control, these statutes describe the discretion of corporate managers to consider the interests of employees, customers, creditors, and the community, as well as shareholders' "long-term" interests, within their decision-making.²¹⁴ Although their obvious application is to takeover defense, the expanded discretion they afford corporate managers is not confined thereto according to the express language of the statutes.²¹⁵ In the absence of interpretive precedent, the full significance of the constituency statutes remains unclear, but their express terms provide authority for corporate executives to make decisions based on expanded social responsibility criteria.

represented on the board." See Janet Bass, *Corporation Formed to Raise Money for New Schools*, UPI, July 8, 1991, available in LEXIS, News Library, UPI File (listing group's leaders drawn from business, government, and education); *Short Takes: New Schools' Funding*, WASH. POST, July 9, 1991, at A17; see also Karen De Witt, *Brought to You by Exxon—School Reform*, N.Y. TIMES, July 21, 1991, (Week in Review), at A4; Margaret Spillane & Bruce Shapiro, *Bush's New American Schools: A Small Circle of Friends*, 258 NATION 278 (1992). It is ironic and fascinating that the conservative push towards privatization has sparked renewed interest in corporate social expenditures.

211. I.R.C. § 170(b) (1994). For commentary on the increase in the annual upper limit of deductible contributions pursuant to the Economic Tax Reform Act of 1981, see Knauer, *supra* note 77, at 19–20, 28–32.

212. 127 CONG. REC. S8353 (1981) (statement of Sen. Byrd); *id.* at S5352 (statement of Sen. Kennedy).

213. For citation and commentary, see, for example, William W. Bratton, *Confronting the Ethical Case Against the Ethical Case for Constituency Rights*, 50 WASH. & LEE L. REV. 1449 (1993); David Millon, *New Directions in Corporate Law, Communitarians: Contractarians, and the Crisis in Corporate Law*, 50 WASH. & LEE L. REV. 1373 (1993); Lawrence E. Mitchell, *A Theoretical and Practical Framework for Enforcing Corporate Constituency Statutes*, 70 TEX. L. REV. 579 (1992); Eric W. Orts, *Beyond Shareholders: Interpreting Corporate Constituency Statutes*, 61 GEO. WASH. L. REV. 14 (1992).

214. See, e.g., CONN. GEN. STAT. ANN. § 33-313(d) (West 1987); N.J. STAT. ANN. §§ 14A:6-1(2), 6-14(4) (West 1995); N.Y. BUS. CORP. LAW § 717(b) (McKinney Supp. 1988); PA. CONS. STAT. ANN. §§ 515–16 (West 1995).

215. See sources cited *supra* note 214. According to Mitchell, by 1992, 28 states had enacted some form of constituency statute. See Mitchell, *supra* note 213, at 579 n.1.

The continuing legal vitality of corporate social responsibility is evident also in certain judicial opinions analyzing the permissible rationales for the deployment of takeover defenses. Certain Delaware cases have described the "community of interests" making up the corporation in defining the circumstances justifying management's resistance to unsolicited takeover bids.²¹⁶ In addition, the American Law Institute's *Principles of Corporate Governance*, finalized in 1994, describes corporate managers as having authority to make decisions on the basis of "ethical considerations that are reasonably regarded as appropriate to the responsible conduct of business"—in addition to their particular authority over corporate charitable contributions.²¹⁷

From a political perspective, with the Republican congressional victory in 1994 and the presidential race in 1996, discussions of "limited government" and increased private initiative—which inevitably raise the issue of the social responsibilities of business—moved to the forefront of national debate.²¹⁸ Irrespective of particular political outcomes, the notion that business must give something back to the community will continue to play a part in the evolution of modern political debate.

C. Democratizing the Social Responsibility Debate

The question of corporations' social responsibilities has been debated throughout this century. Yet the centralized administration of corporate

216. See especially *Paramount Communications, Inc. v. Time Inc.*, 571 A.2d 1140 (Del. 1989); *Unocal Corp. v. Mesa Petroleum Co.*, 493 A.2d 946 (Del. 1985); see also Allen, *supra* note 191; Jeffrey N. Gordon, *Corporations, Markets and Courts*, 91 COLUM. L. REV. 1931 (1991) (suggesting that the *Paramount* decision reflected judicial concern over the nonmonetary costs imposed on shared community values by an unrestrained market in corporate control). More generally, the idea that takeovers imposed undue costs on nonshareholder constituencies gave rise to renewed concern during the 1980s for creditors, employees, and the larger community surrounding the corporation. See, e.g., William W. Bratton, Jr., *The New Economic Theory of the Firm: Critical Perspectives from History*, 41 STAN. L. REV. 1471 (1989); Millon, *supra* note 196.

217. ALI, *supra* note 14, § 2.01(b)(2), (3).

218. The issue of corporate social responsibility was highly visible in the political debate surrounding the 1996 presidential race. See, e.g., Alison Mitchell, *Republicans and Democrats Jumping on the Issue of Corporate Social Responsibility*, N.Y. TIMES, Feb. 15, 1996, at B15. Beginning on March 3, 1996, *The New York Times* published a series of seven special reports on the subject of corporate downsizing that explicitly faced the question of corporate social responsibilities and the effect of corporate layoffs on employees and local communities. See also Robert B. Reich, *How to Avoid These Layoffs?*, N.Y. TIMES, Jan. 4, 1996, at A21 (arguing in favor of expanded legal and political support (e.g., public sector subsidies) for corporations which are solicitous of the needs of employees and other nonshareholder constituencies); cf. William Safire, *The New Socialism*, N.Y. TIMES, Feb. 26, 1996, at A13 (arguing that calls for increased corporate social responsibility amount to a revived form of socialism).

affairs has hindered a more democratic approach to the issue, particularly one that would take account of the views of corporate shareholders—the parties who fund such expenditures. While a perfectly democratic system is unattainable in light of the collective-action problems affecting the shareholder franchise in the public corporation, the lack of an *ideal* system of shareholder participation has too readily functioned as a justification for maintaining the status quo. The dangers implied by the concentration of not only the factors of production, but also communal resources in the hands of corporate management, mandates in favor of implementing reasonable measures to involve corporate shareholders in decisions regarding philanthropic corporate contributions.

D. Disclosure and Philanthropic Contributions: From Information to Action

A variety of mechanisms would serve to facilitate shareholder involvement in corporate philanthropy. The proxy-voting mechanism established by federal law and SEC regulation is readily adaptable to this purpose: The system adopted by Berkshire Hathaway corporation under Warren Buffett's direction provides a working, practical model.²¹⁹ The increased opportunities for intrashareholder communication created by recent amendments to the proxy rules may also facilitate the ability of shareholders to express their views on corporate philanthropy.²²⁰ Additionally, the shareholder proposal system under the federal proxy rules should provide a vehicle for shareholders to communicate their views on corporate philanthropy to management.²²¹ Finally, shareholders may express their views on corpo-

219. For citations to the company's annual reports, see *supra* note 140.

220. See Regulation of Communications Among Shareholders, Exchange Act Release No. 34-31326, 57 Fed. Reg. 48,276 (1992).

221. There is a long history of shareholders submitting proposals on corporate philanthropy under Rule 14a-8. As provided under Rule 14a-8(c)(7), companies may omit a proposal that "deals with a matter relating to the conduct of the ordinary business operations of the registrant." 17 C.F.R. § 240-14a-8(c)(7) (1996). For many years, the SEC's position had been that the allocation of corporate funds by management among various charitable recipients, as well as other matters pertaining to corporate philanthropy, involved significant matters of corporate policy and hence, could not be excluded as "ordinary business." See *Union Pacific Corp.* (Feb. 5, 1993); *Bristol Myers Squibb Co.* (Mar. 7, 1991); *McDonnell Douglas Corp.* (Feb. 8, 1990); *Quaker Oats Co.* (Aug. 4, 1987); *Archer Daniel Midland Co.* (Aug. 14, 1987); *International Business Machines Corp.* (Mar. 7, 1988); *E.I. du Pont de Nemours and Co.* (Jan. 25, 1984); *Dow Chemical Co.* (Jan. 18, 1979); *Humana, Inc.* (Oct. 10, 1979). However, in the early 1990s, the staff of the Division of Corporate Finance "reconsidered" certain of its prior determinations and held that a firm's decision to commence contributions to a particular cause or group would be viewed by the staff as a matter of "ordinary business." See, e.g., *Aetna Life and Casualty Co.* (Feb. 13, 1992);

rate philanthropy, and corporate social responsibility in general, when voting for directors and through their investment decisions, if they so choose.²²² However, shareholders will be able to pursue these avenues for involvement and assume a meaningful role in the formulation of corporate-philanthropy policies only if corporations provide them with accurate and complete information regarding their charitable contributions—something that most firms have failed to do voluntarily.²²³

V. THE POLITICAL DIMENSIONS OF CORPORATE PHILANTHROPY

Corporations engage in political advocacy in order to increase the rewards and reduce the penalties accruing to them through political and legal channels. Certain forms of corporate political activity are overt—namely, lobbying and campaign-finance spending conducted through political action committees (“PACs”).²²⁴ Less obviously, but no less deliberately, corporations have used technically philanthropic donations²²⁵ to politicized charities²²⁶ to promote their long-term financial interests in the political arena. Corporate philanthropy obtains expressly political

SCE Corp. (Feb. 20, 1992); Pacific Telesis Group (Feb. 20, 1992). Therefore, the ability of shareholders to employ the shareholder proposal process as a means of affecting corporations' giving practices remains in doubt under current SEC practice.

222. Certainly, the continued development of computer-based information technology will increasingly facilitate the process of information gathering and communication between shareholders and managers in these matters.

223. Corporations' resistance to disclosure of charitable contributions information is illustrated, for example, by companies' attempts to exclude shareholder proposals requesting such disclosure. See, e.g., IBM Corp. (Jan. 31, 1994); Superior Oil Co. (Mar. 9, 1982); The Upjohn Co. (Feb. 17, 1982); E.I. du Pont de Nemours (Leeds) (Jan. 16, 1981); American Telephone and Telegraph Co. (Jan. 9, 1979); Marriott Corp. (Sept. 17, 1976); West Point-Pepperell, Inc. (Oct. 2, 1979).

224. Corporate PACs are increasingly being studied by political scientists. See, for example, DAN CLAWSON ET AL., *MONEY TALKS: CORPORATE PACS AND POLITICAL INFLUENCE* (1992); THEODORE J. EISMEIER & PHILLIP H. POLLOCK, *BUSINESS, MONEY, AND THE RISE OF CORPORATE PACS IN AMERICAN ELECTIONS* (1988); FRANK J. SORAUF, *INSIDE CAMPAIGN FINANCE: MYTHS AND REALITIES* (1992); M. Margaret Conway & Joanne Connor Green, *Political Action Committees and the Political Process in the 1990s*, in *INTEREST GROUP POLITICS* 155 (Allen J. Cigler & Burdett A. Loomis eds., 4th ed. 1995).

225. I have elected to continue to refer to the donations described herein as “charitable” and “philanthropic” in order to emphasize that they are made to charitable organizations qualified under § 501(c)(3) of the Code—as opposed to PACs or other entities.

226. For a technical analysis of the lobbying and campaign finance limitations pertaining to charitable organizations under the Code, see Jasper L. Cummings, Jr., *Lobbying and Political Expenditures*, 613-2d Tax Mgmt. (BNA) (1996). For an insightful discussion of the issue, see Laura B. Chisolm, *Exempt Organization Advocacy: Matching the Rules to the Rationales*, 63 *IND. L.J.* 201 (1987). Many of the charitable organizations described in this section of the Article skirt the outer boundaries of permissible nonprofit advocacy.

dimensions in corporate gifts to politicized foundations, legal defense funds, and special interest groups—all of which may constitute themselves tax-exempt, charitable organizations under § 501(c)(3) of the Code, as described below.

Charitable contributions that are made for the purpose of advancing the corporation's political interests are consonant with traditional corporate legal norms (i.e., wealth maximization). At least theoretically, they pose no threat to shareholders' *property* interests. Nevertheless, because politicized corporate charitable contributions are a form of corporate political speech, they may impinge on shareholders' *speech and associational* interests. In light of the fact that shareholders are typically not provided with information regarding the firm's charitable contributions, the investment decision cannot represent a legitimate proxy for shareholder consent to politicized charitable contributions.²²⁷ As commentators have elsewhere noted, a deep conflict exists between the firm's right to promote its political interests and the shareholders' interest in not being compelled to subsidize speech with which they are in disagreement. This section of the Article analyzes this conflict in the context of politicized corporate charitable contributions.

A. The Legal Basis for the Politicization of the Nonprofit Sector

Politically motivated corporate philanthropy is used to influence a variety of constituencies within the United States, including members of Congress and the judiciary, organized interest groups, and the public in general.²²⁸ Of course, corporate charitable contributions would be relatively ineffective political instruments were it not for the increasingly political nature of many charitable organizations.²²⁹

227. See Victor Brudney, *Association, Advocacy, and the First Amendment*, 4 WM. & MARY BILL RTS. J. 1 (1995) [hereinafter Brudney, *Association, Advocacy, and the First Amendment*]; Victor Brudney, *Business Corporations and Stockholders' Rights Under the First Amendment*, 91 YALE L.J. 235 (1981) [hereinafter Brudney, *Business Corporations*]; cf. Alan J. Meese, *Limitations on Corporate Speech: Protection for Shareholders or Abridgment of Expression?*, 2 WM. & MARY BILL RTS. J. 305 (1993); Larry E. Ribstein, *Corporate Political Speech*, 49 WASH. & LEE L. REV. 109 (1992).

228. The diverse forms of political influence that may be exerted through corporate charitable contributions are discussed in NEIHEISEL, *supra* note 32. See also Haley, *supra* note 36, at 496–97.

229. That is, the charitable organizations function as conduits for corporate political advocacy. Many charities engage in political advocacy as a crucial aspect of furthering their public service objectives. Karen W. Arenson, *Legislation Would Expand Restrictions on Political Advocacy by Charities*, N.Y. TIMES, Aug. 7, 1995, at A10 (“Those at the bottom of the ladder very often need both the social services and the advocacy . . .” (quoting Sara Melendez, president of

While the language of § 501(c)(3) would seem to deny charitable organizations a meaningful political life, this has not been the case. The lobbying limitations and absolute proscription on campaigning that apply to charitable organizations under § 501(c)(3)²³⁰ have not prevented charitable organizations from becoming politically active. The inclusion of "education" as a charitable purpose under § 501(c)(3),²³¹ and the Treasury regulations' broad definition thereof,²³² has supplied a basis for considerable advocacy on the part of charitable organizations, and especially educational foundations.²³³ In light of the relevance of constitutionally

Independent Sector)). Nonprofit political advocacy has been a source of recent controversy. In July 1995, three representatives introduced legislation that would "sharply circumscribe not just lobbying efforts, but also all other attempts to influence public policy at the national, state or local level by [nonprofit] recipients of Federal grants." *Id.* For related discussion, see *infra* note 239.

230. See I.R.C. § 501(c)(3) (1994). An organization qualifying for charitable status pursuant to § 501(c)(3) is one in which

no substantial part of the activities of which is carrying on propaganda, or otherwise attempting, to influence legislation (except as otherwise provided in subsection (h)), and which does not participate in, or intervene in (including the publishing or distributing of statements), any political campaign on behalf of (or in opposition to) any candidate for public office.

Id. In response to the ambiguity surrounding the "substantial part" test, the IRS enacted § 501(h) as part of the Tax Reform Act of 1976. Pub. L. No. 94-455, 90 Stat. 1720, 1723 (1976). Section 501(h) is a safe harbor permitting qualified electing organizations to spend a precisely defined amount of their funds on lobbying without running afoul of the § 501(c)(3) substantial part test.

231. I.R.C. § 501(c)(3).

232. Treas. Reg. § 1.501(c)(3)-(d)(3) (1996) ("An organization may be educational even though it advocates a particular position or viewpoint so long as it presents a sufficiently full and fair exposition of the pertinent facts as to permit an individual or the public to form an independent opinion or conclusion."). However, the "full and fair exposition" test was held unconstitutionally vague by the Court of Appeals for the District of Columbia. *Big Mama Rag, Inc. v. United States*, 631 F.2d 1030 (D.C. Cir. 1980). The IRS has therefore resorted to a "methodology test," which identifies various factors for consideration in making the distinction between education and advocacy. See Rev. Proc. 86-43, 1986-2 C.B. 729. Of course, the IRS cannot base any such determinations on the content of the ideas expressed without running afoul of the First Amendment.

233. The issue of political advocacy by nonprofit organizations has received congressional attention, but is not susceptible to easy resolution. See *Hearings on Lobbying and Political Activities of Tax-Exempt Organizations Before the Subcomm. on Oversight of the House Comm. on Ways and Means*, 100th Cong. (1987); SUBCOMMITTEE ON OVERSIGHT OF THE COMM. ON WAYS AND MEANS, 100TH CONG., REPORT AND RECOMMENDATIONS ON LOBBYING AND POLITICAL ACTIVITIES OF TAX-EXEMPT ORGANIZATIONS (Comm. Print 1987). For an important discussion of the Code's and Treasury regulations' treatment of the definition of "education" in the context of foundations identified with particular politicians, see Francis R. Hill, *Newt Gingrich and Oliver Twist: Charitable Contributions and Campaign Finance*, 66 TAX NOTES 237 (Jan. 9, 1995); see also Laura Brown Chisolm, *Sinking the Think Tanks Upstream: The Use and Misuse of Tax Exemption Law to Address the Use and Misuse of Tax-Exempt Organizations by Politicians*, 51 U. PITT. L. REV. 577 (1990). Political spending by charitable foundations had attracted substantial controversy in

guaranteed liberties, the IRS has had a difficult time distinguishing between permissible educational activities, permissible advocacy, and impermissible lobbying, propagandizing, and campaigning.²³⁴ Furthermore, § 501(c)(3) itself provides a basis for some lobbying by charitable organizations, so long as such lobbying does not constitute a substantial part of the organizations' activities.²³⁵ The Treasury regulations have further facilitated the political empowerment of charitable organizations by providing particular, itemized exceptions to the definition of prohibited lobbying,²³⁶ and by distinguishing judicial, executive and administrative bodies from those "legislative bodies" that may not be lobbied consistent with § 501(c)(3).²³⁷

Thus, the porous nature of § 501(c)(3)'s requirements and that of the accompanying regulations, combined with the increasingly factionalized, interest-group-based nature of society and politics,²³⁸ has meant that the universe of politically empowered § 501(c)(3) charitable organizations has expanded dramatically in the last three decades.²³⁹ Many of these entities

the mid- and late 1960s. Congress took steps to prevent future abuses by enacting new rules and penalties pertaining to foundations as part of the Tax Reform Act of 1969. For historical background on the controversy and on Congress' reaction thereto, see COMMISSION ON FOUNDATIONS AND PRIVATE PHILANTHROPY, *supra* note 49. Congress failed to confront the problem of direct corporate giving, however.

234. See, e.g., Daniel Shaviro, *From Big Mama Rag to National Geographic: The Controversy Regarding Exemptions for Educational Publications*, 41 TAX L. REV. 693 (1986). For additional commentary on the tax-based limitations pertaining to political advocacy by nonprofit organizations, see Chisolm, *supra* note 226; Laura Brown Chisolm, *Political Advocacy Meets the Internal Revenue Code: 'There's Got to Be a Better Way'* (1994) (New York University School of Law, Program on Philanthropy and the Law).

235. See *supra* note 230.

236. Most significantly, pursuant to Treas. Reg. § 56.4911-2(c)(1)-(4) (1996), charitable organizations may engage in "nonpartisan" analysis and make their finding available to governmental bodies, may examine and discuss broad social and economic problems (including problems government would ultimately be expected to address), may address governmental bodies if they do so in response to an invitation therefrom, and may appear before governmental bodies in regard to matters affecting the powers and duties of the charitable organization itself.

237. See Treas. Reg. § 56.4911-2(d)(3) (1996) ("Legislative body" does not include executive, judicial, or administrative bodies.).

238. Political scientists have observed that organized interest groups have played an increasingly critical role in politics since the 1970s. See, e.g., KAY LEHMAN SCHLOZMAN & JOHN T. TIERNEY, *ORGANIZED INTERESTS AND AMERICAN DEMOCRACY* (1986); see also *INTEREST GROUP POLITICS*, *supra* note 224.

239. The problem of distinguishing the appropriate characteristics and limits of charitable organizations (as opposed to "advocacy" organizations) is at the heart of the recent controversy regarding the Combined Federal Campaign (the "CFC"), a federally-sponsored charity fundraising effort through which federal employees make charitable contributions (to the groups they select). In June of 1995, Representative John L. Mica (R-Fla.) criticized the presence of "advocacy-oriented" charities within the CFC, and held hearings to consider banning them from continued participation therein. See, e.g., *Statement of Chairman John Mica: Hearing on Combined*

are unrelated to the classes of causes and problems historically associated with philanthropy, and many of them, as mentioned above, are at least informally committed to influencing public policy.²⁴⁰ Thus, the breadth of politicized causes and entities qualifying for § 501(c)(3) charitable status has enhanced the opportunities for corporations to use philanthropic contributions to accomplish political objectives.

B. The Limitations and Disincentives Attaching to Traditional Corporate Political Advocacy

Significant legal limitations apply to traditional corporate campaign-finance activities²⁴¹ and substantial tax-based, financial disincentives pertain to traditional corporate lobbying.²⁴² Corporate philanthropy has therefore become an especially attractive vehicle for corporate political advocacy. By pursuing political objectives through technically philantro-

Federal Campaign Before the Subcomm. on Civil Serv. of the House Comm. on Gov't Reform, Federal Document Clearing House Congressional Testimony, June 7, 1995, available in LEXIS, Legis History, CNGTST File; *Testimony of Charles Stephen, Senior Staff Attorney NAACP Legal Defense Fund: Hearing on Combined Federal Campaign Before the Subcomm. on Civil Serv. of the House Comm. on Gov't Reform*, Federal Document Clearing House Congressional Testimony, June 7, 1995, available in LEXIS, Legis History, CNGTST File. Prior to the 1980s, the CFC was limited to charitable organizations providing direct services in the area of human health and welfare; however, litigation brought by the NAACP Legal Defense Fund succeeded in opening the CFC to a wider group of charities. Although it has received some support, groups across the political spectrum have criticized Mica's proposal to ban the "bad," advocacy groups from the CFC, noting the impossibility of distinguishing between "advocacy" and "non-advocacy" oriented charities. Mica himself acknowledged that he had not entirely figured out how to distinguish advocacy groups from charities. See Constance Casey, *Congress Targets 'Good,' 'Bad' Charities*, CLEV. PLAIN DEALER July 10, 1995, at 3E (quoting Mica as stating, "I know what they aren't. . . . It's sort of like pornography. I'd know what one was when I saw it."). Mica's initiative, conducted as chairman of the House Civil Service Subcommittee, has understandably been viewed as part of recent Republican efforts to "defund the left". See Jeff Shear, *The Ax Files*, 27 NAT'L J. 924 (1995); "War on Nonprofits" Heats Up, NONPROFIT WORLD, Jan./Feb. 1996, at 8.

240. See *supra* note 229. In addition to the limitations described above, § 501(c)(3) requires that qualifying organizations be "organized" and "operated" exclusively to fulfill a charitable purpose. I.R.C. § 501(c)(3) (1994). These organizational and operational requirements are further elaborated in Treas. Reg. § 1.501(c)(3)-1(b)-(c) (1996). Entities which engage in impermissible advocacy are classified as "action organizations." See I.R.C. § 501(c)(4); Treas. Reg. § 1.501(c)(3)-1(c)(3)(ii), (iv) (1996).

241. For discussion of the Federal Election Campaign Act, see *infra* notes 246-263 and accompanying text.

242. In 1993, the Revenue Reconciliation Act of 1993 amended § 162(e) of the Code to eliminate the deduction for business lobbying expenses (except those pertaining to local lobbying). An analysis of the 30-year life of the business lobbying deduction is presented in Cummings, *supra* note 226.

pic contributions, corporations may lawfully avoid the limitations and disincentives pertaining to traditional corporate political advocacy.

1. Laws and Regulations Affecting Traditional Corporate Political Activity

The most important laws governing traditional corporate political activity are the Federal Election Campaign Act ("FECA")²⁴³ (and analogous state laws)²⁴⁴ and the Code's provisions governing the deductibility of business lobbying expenses.²⁴⁵ The significance of the under-regulated nature of corporate philanthropy becomes apparent when compared to the heavily regulated nature of traditional corporate political activity.

a. Corporate Campaign Spending and FECA

FECA absolutely prohibits corporations and labor unions from making contributions and expenditures to federal election campaigns.²⁴⁶ These

243. The Federal Election Campaign Act of 1971, 2 U.S.C. §§ 431-455 (1994). There are a variety of other federal laws affecting lobbyists' activities. In fact, Congress passed significant lobbying reform measures in 1995, in the form of rules limiting gifts that could be accepted by Members (these rules were enacted separately by each House). It also passed the Lobby Disclosure Reform Act of 1995, which requires for the first time that public disclosure be made of paid lobbyists' efforts to influence the legislative and regulatory process in both the legislative and the executive branches. See Alice A. Love, *Congress Approves First Overhaul of Lobby Disclosure Law Since '40's*, ROLL CALL, Nov. 30, 1995; *Reforming Congress; Changing the Way Washington Works*, HERITAGE FOUND. REPS., Dec. 1995, No. 29, at 1. In addition, see Lobbying Disclosure Act of 1995, 2 U.S.C.S. §§ 1601-1611 (Law. Co-op. 1996); Truth in Lobbying Act, 31 U.S.C. § 1352 (1994).

244. See, e.g., CONN. GEN. STAT. ANN. § 9-330(a) (West 1992); MASS. ANN. LAWS ch. 55, § 7 (Law. Co-op. 1990); MICH. COMP. LAWS ANN. § 169.254 (West 1992); MO. ANN. STAT. § 130.029 (West 1980); N.Y. ELEC. LAW § 14-116 (McKinney 1978 & Supp. 1996); OHIO REV. CODE ANN. § 3599.03(A) (Banks-Baldwin 1995); 25 PA. STAT. ANN. § 3253 (West 1994). For further citation to the states' campaign finance laws, see *State Capital Law Firm, Lobbying, PACs and Campaign Finance*, 50 STATE HANDBOOK (1994). For commentary on the states' campaign finance laws, see COMMON CAUSE, *CAMPAIGN FINANCE REFORM IN THE STATES 14* (Aug. 1985); Christopher Cherry, Note, *State Campaign Finance Laws: The Necessity and Efficacy of Reform*, 3 J.L. & POL. 567 (1987); John M. Hamilton, Note, *State Campaign Finance Schemes and Equal Protection*, 61 IND. L.J. 251 (1986). See also *Austin v. Michigan Chamber of Commerce*, 494 U.S. 652 (1990) (upholding constitutionality of state campaign finance law prohibiting corporations from using corporate funds for independent expenditures in support of or in opposition to candidates running in state elections).

245. I.R.C. § 162(e) (1994).

246. 2 U.S.C. § 441b(a). For a politically savvy account of FECA's effect on the federal election process, see SORAUF, *supra* note 224.

prohibitions reflect the view that unrestrained corporate campaign spending would pose a substantial threat to the democratic political process, and create at least the appearance of unseemly political quid pro quos.²⁴⁷ FECA also reflects concern for the potentially coercive nature of corporate (and union) campaign spending vis-a-vis the individual political beliefs of dissenting shareholders and union members.²⁴⁸

FECA's seemingly absolute prohibition on corporate campaign spending is mitigated by the fact that the Act permits corporations to establish and administer "separately segregated funds"—commonly referred to as PACs.²⁴⁹ Under FECA, corporations may establish a PAC and pay all of its administrative expenses (including its office space, salaries, phone bills, bank charges, and solicitation expenses, etc.),²⁵⁰ but the funds that the PAC will donate to federal election campaigns must come from voluntary contributions from stockholders, employees, and their families.²⁵¹ Such contributions cannot come from corporate treasury funds.²⁵² These requirements are intended to prohibit corporations from using their PACs as conduits for corporate campaign contributions.²⁵³

b. FECA's Regulations Affecting Corporate PACs

While the distinction between corporate funded administrative costs and "pass-through contributions" is problematic, FECA imposes other regulatory safeguards on corporate PACs' involvement in federal election

247. These views are enunciated in the various Supreme Court cases testing the constitutionality of FECA's provisions. See *Buckley v. Valeo*, 424 U.S. 1 (1976) (per curiam); *United States v. UAW*, 352 U.S. 567 (1957); *United States v. Painters Local Union*, 79 F. Supp. 516 (D. Conn. 1948). For discussion of the historical antecedents of FECA, see Jeremiah D. Lambert, *Corporate Political Spending and Campaign Finance*, 40 N.Y.U. L. REV. 1033 (1965).

248. *UAW*, 352 U.S. at 567; *United States v. CIO*, 335 U.S. 106 (1948); *United States v. Pipefitters Local Union No. 562*, 434 F.2d 1116 (8th Cir. 1970), *rev'd in part and vacated in part*, 407 U.S. 385 (1972); *Ash v. Cort*, 350 F. Supp. 227 (E.D. Pa. 1972), *aff'd* by 471 F.2d 811 (3rd Cir. 1973).

249. Organizational matters pertaining to PACs (or "Separately Segregated Funds") are prescribed under 2 U.S.C.S. § 432 (Law. Co-op. 1996). See also *United States v. Boyle*, 482 F.2d 755 (1973); 11 C.F.R. § 114.5(b) (1996).

250. 11 C.F.R. § 114.5(b) (Separate Segregated Funds—Use of Treasury Monies); *id.* § 114.1(b) (Definitions—Establishment, Administration and Solicitation Costs).

251. 2 U.S.C.S. § 441b(a)(4)(A) & (B).

252. *Id.* § 441b(a); see also 11 C.F.R. §§ 114.2(b), 114.5(b).

253. 11 C.F.R. § 114.2(b), 114.5(b). The distinction is somewhat artificial, of course. To the extent that corporations fund the administration and basic operations of a PAC, they free up other capital to go to election campaigns.

campaigns. In particular, FECA limits the amount that individuals and other noncorporate organizations²⁵⁴ may contribute to PACs.²⁵⁵ It also imposes various procedural requirements and amount limitations on the contributions that PACs may make in federal election campaigns.²⁵⁶

FECA also imposes strict reporting obligations on PACs and on politicians.²⁵⁷ All PACs are required to register with the Federal Election Commission within ten days of their establishment.²⁵⁸ And FECA requires PACs to disclose the total contributions that they have received,²⁵⁹ as well as to identify information regarding any contributors who have given more than \$200 to the PAC in a given year.²⁶⁰ The PAC, in turn, must disclose information regarding all campaign contributions it makes, irrespective of amount.²⁶¹ Finally, FECA imposes disclosure obligations on federal election candidates themselves: They must disclose the amounts of PAC contributions they receive and identify information pertaining to PAC contributors.²⁶² These disclosure obligations provide additional legal prophylaxis against the invisible political exercise of corporate wealth in federal elections.²⁶³

c. The Nondeductibility of Business Lobbying Expenditures

In comparison to other business related expenses, the Code has placed a disincentive on traditional corporate lobbying. In 1993, pursuant to the Revenue Reconciliation Act of 1993, Congress amended § 162(e) of the Code to deny corporations (and other business taxpayers) a deduction for most lobbying expenses.²⁶⁴ With the exception of expenses attributable to lobbying local government, the Revenue Reconciliation Act of 1993 eliminated the deduction for expenses incurred in direct attempts to influ-

254. Again, corporations may not make any contributions to the PACs' campaign funds; they are only permitted to fund the PACs' operations. See *supra* note 252.

255. 2 U.S.C.S. § 441a(a).

256. *Id.*

257. *Id.* § 434.

258. *Id.* § 433(a).

259. *Id.* § 434(b)(2).

260. *Id.* § 434(b)(3).

261. *Id.* § 434(b)(4) & (5).

262. *Id.* § 434(b)(5) & (6).

263. See *Pichler v. Jennings*, 347 F. Supp. 1061 (S.D.N.Y. 1972).

264. I.R.C. § 162(e) (1994).

ence legislation, expenses attributable to communicating with high federal executive office personnel (whether or not in connection with specific legislation), trade association dues attributable to state and federal lobbying, and grass roots lobbying expenses.²⁶⁵

2. In Comparison to Political Philanthropy

As the previous discussion illustrates, corporations get a three-fold benefit from structuring their political activity as philanthropy. First, charitable contributions to foundations associated with particular politicians or party platforms provide an alternative to traditional campaign contributions, which corporations are prohibited from making, at least on a direct basis, under FECA and analogous state laws. Second, so long as a firm's annual charitable contributions do not exceed ten percent of its taxable income, such donations would generally be tax-deductible for the corporation under § 170 of the Code—in contrast to the currently nondeductible status of corporate lobbying expenses. Third, by using technically philanthropic contributions to accomplish political objectives, corporations lawfully avoid the disclosure requirements applicable under FECA.

C. Politicized Philanthropies: Foundations Identified with Politicians and Party Platforms

Because of the difficulty of arriving at a constitutionally sound, justiciable standard for distinguishing education from advocacy,²⁶⁶ § 501(c)(3) "educational" foundations have been relatively free to engage in campaign-related and legislative advocacy. This readily occurs in situations where a politician has developed a particular affiliation with an educational foundation.²⁶⁷ In such cases, with a modicum of care paid to the partisan nature of its statements, the foundation may serve as a mouthpiece for the candidate, one dedicated to disseminating his or her political message and, indi-

265. See Cummings, *supra* note 226, at A-4 ("The reasons for this abrupt about face are not entirely clear. In part, the 1993 revision was revenue driven. The Congress may have intended to penalize and possibly reduce business lobbying, which may be further explained as a change of view about 'neutrality' in the tax treatment of lobbying expenses." (footnote omitted)). For an argument that Congress went too far in disallowing the deduction for business lobbying, see Jasper L. Cummings Jr., *Tax Policy, Social Policy, and Politics: Amending Section 162(e)*, 9 EXEMPT ORG. TAX REV. 137 (1994). For discussion of the issue of the Tax Code's "neutrality" in the matter of nonprofit organizations' advocacy, see Chisolm, *supra* note 234.

266. See Shaviro, *supra* note 234.

267. See Chisolm, *supra* note 233.

rectly, advancing his or her political career.²⁶⁸ The problems raised by affiliations between candidates, office holders (that is, potential candidates), and educational foundations are particularly nettlesome. Describing the "candidate organization dilemma" as "virtually unaddressed," Francis Hill, a tax expert in the area, has indicated that such foundations provide a mechanism for enterprising politicians to "treat themselves as their political supporters' favorite charities."²⁶⁹

Hill has described politician-charity links as being common across the political spectrum,²⁷⁰ but a particularly striking example is provided by Newt Gingrich's affiliation with several nonprofit educational foundations, and especially The Progress and Freedom Foundation ("PFF").²⁷¹

268. *Tax Notes* described the broad boundaries of what Mr. Gingrich could talk about in conducting his college course without running afoul of the Code's limitations on nonprofits' advocacy: "[H]e could say pretty much whatever he wanted, as long as it did not include 'and vote for me,' or 'join the Republican Party,' or something like that." See Lee A. Sheppard, *Is Gingrich's Think Tank Too Partisan for Exemption?*, 65 *TAX NOTES* 1173, 1173 (1994).

269. Hill, *supra* note 233, at 249. As Hill notes, campaign finance reform may actually exacerbate "political overreaching" by educational foundations. "Congress has never found the political courage to enact a meaningful package of campaign finance reforms . . . for determining whether § 501(c)(3) organizations are participating impermissibly in electoral politics." *Id.* at 238. Hill does an excellent job of elucidating the labyrinthine rules pertaining to charitable foundations' political advocacy. In addition to the education-advocacy distinction, pertinent issues include whether the politicized foundation's work has conferred a benefit on a charitable class, whether it conferred an impermissible private benefit on Mr. Gingrich as a politician or on the Republican party, whether Gingrich received private inurement as a product of the arrangement, and whether the charitable organization functioned merely as a conduit for contributions to flow to Gingrich or other organizations affiliated with him. See also David Shenk, *Nonprofits: How to Lobby Like a Corporation and Pay Taxes Like a Charity*, *WASH. MONTHLY*, Dec. 1991, at 35 ("Because the groups span the political spectrum, nonprofit reform isn't any party's plank, and cozy relations between established nonprofits and incumbent politicians mean that Congress isn't likely to press the IRS for tighter oversight.").

270. Hill, *supra* note 233, at 238.

271. Like the other foundations under discussion herein, PFF was recognized as a § 501(c)(3) educational foundation by the IRS. For discussion of the charitable purposes described in PFF's application for tax exemptions, see Sheppard, *supra* note 268, at 1173; more generally, see Glen R. Simpson, *New Addition to Gingrich Family Tree: The Progress and Freedom Foundation*, *ROLL CALL*, Sept. 12, 1994, at 1, and Glenn F. Bunting, *Gingrich's Politics Got Boost from Nonprofits*, *L.A. TIMES*, June 25, 1996, at A1 (describing the network of five nonprofit foundations associated with Mr. Gingrich). Of these several foundations, PFF and The Abraham Lincoln Opportunity Foundation ("ALOF") were the most important to the fulfillment of Mr. Gingrich's larger political strategy. From 1990-1993, tax deductible contributions to ALOF funded nationally broadcast satellite television programs featuring Mr. Gingrich and his political message. In 1993, PFF largely took over this function. Aside from The American Opportunity Foundation, which was funded and run directly by Mr. Gingrich, these foundations were each organized and operated by persons affiliated with GOPAC, the political action committee that Mr. Gingrich chaired from 1986-1995. The foundations typically shared GOPAC's officers, staff, office space, and telephone number. Some even took loans from GOPAC. *Id.*; see David E. Rosenbaum, *Middle Ground on Ethics*, *N.Y. TIMES*, Dec. 25, 1996, at A1.

Although Mr. Gingrich was deeply connected to PFF and its work,²⁷² he shrewdly eschewed any *official* connection to the foundation.²⁷³ (Because the foundations are intended to be organized and operated exclusively to fulfill a charitable purpose, the absence of a formal tie between the politician and the foundation helps to forestall (but does not preclude) charges of tax and campaign finance abuses.)²⁷⁴ PFF was established in 1993 by Jeffrey Eisenach, a close associate of Mr. Gingrich, who had served as executive director of GOPAC from 1991 to 1993.²⁷⁵ Eisenach is reported to have launched PFF from GOPAC's offices,²⁷⁶ where he had spent "several

272. In a 1993 PFF newsletter, Eisenach credited the idea for the establishment of PFF to "a series of conversations with my friend Newt Gingrich." Mary Beth Regan & Richard S. Dunham, *A Think Tank with One Idea: The New World Order*, BUS. WK., July 3, 1995, at 49; see also Jeanne Cummings, *Gingrich Confidant; Eisenach: A Whiz Behind the Scenes*, ATLANTA J. & CONST., July 25, 1995, at 4A [hereinafter Cummings, *Gingrich Confidant*] ("Although Gingrich and Eisenach do not see each other on a daily basis, Eisenach routinely communicates with the speaker's office by fax and refers to himself as a close adviser to Gingrich.").

273. As Hill makes plain, such a formal connection is unnecessary to the advancement of the politician's platform. Hill, *supra* note 233, at 245-46 ("The officeholder or candidate may simply appear at organizational events or endorse the organization's positions on issues. Fund-raising solicitations may or may not refer to the politician, but will prominently invoke his or her views. The § 501(c)(3) organization commonly solicits contributions from the section 527 political organization's contributors.").

274. See, e.g., *American Campaign Finance Academy v. Commissioner*, 92 T.C. 1053 (1989); see also *United Cancer Council v. Commissioner*, 100 T.C. 162 (1993). The extraordinarily high-profile nature of Mr. Gingrich's politicized foundations, and their formal connection to GOPAC, ultimately resulted in Democratic representatives filing ethics charges. These charges lead to an investigation by a subcommittee of the House Committee on Standards of Official Conduct (the "Ethics Committee") and the appointment of a special counsel, James M. Cole. On January 17, 1997, the subcommittee announced its determination that Mr. Gingrich had failed to conform to the House's standards of conduct in that he had failed to be appropriately attentive (in regard to seeking legal counsel, etc.) to whether his network of politicized charitable foundations conformed to tax law requirements. (It also concluded that he had failed to supply accurate, complete, and comprehensive information to the panel.) On this basis, on the same day, the full Ethics Committee voted to reprimand the Speaker and to fine him \$300,000. See Adam Clymer, *Panel, Citing Pattern of Ethics Flaws, Seeks a Gingrich Reprimand*, N.Y. TIMES, Jan. 18, 1997, at A1. (Mr. Gingrich had been reelected as Speaker of the House on January 7, 1997.) On January 21, 1997, the full House voted overwhelmingly in favor of the reprimand and the fine. See Adam Clymer, *House, in a 395-28 Vote, Reprimands Gingrich*, N.Y. TIMES, Jan. 22, 1997, at A1. Nevertheless, the Ethics Committee failed to reach a determination regarding whether Mr. Gingrich's network of politicized foundations constituted a violation of the tax laws. Thus, there still remain many fundamental, unresolved issues regarding the scope of permissible advocacy activities by educational foundations affiliated with individual politicians and political parties.

275. See Cummings, *Gingrich Confidant*, *supra* note 272, at 4A.

276. According to *Roll Call* (a Capitol Hill newspaper), only the lower-level employees of PFF lacked any prior association with Gingrich. See Simpson, *supra* note 271.

months" organizing Mr. Gingrich's college course.²⁷⁷ The course, "Renewing American Civilization," was funded from charitable contributions made to PFF.²⁷⁸ Designed to foster a grass roots citizens' movement of conservative political activists, the course and Mr. Gingrich's cable television show played a significant role in paving the way for him to assume the position of Speaker of a Republican-dominated House.²⁷⁹ *Business Week* magazine reported that "PFF appears to have almost single-mindedly promoted the Speaker. During its first twenty months, roughly forty-three percent of the group's \$1.4 million budget went to funding Gingrich's televised, college lecture series . . . and his cable television show."²⁸⁰

While other politicians have established affiliations with educational foundations, none have been as daring as Mr. Gingrich. Clearly, the activities of PFF, and the other educational foundations with which he has been associated, have tested the outer limits of what is "educational," as opposed to "political." According to one account, PFF's founders "readily admit that they are trying to convince people to become what might loosely be called 'conservatives,'" but the more trenchant question is "whether [PFF] is trying to make [the college] students into *Republicans*"—an objective inconsistent with its status as a § 501(c)(3) educational foundation.²⁸¹ Clearly the distinction is an abstruse one, and there is no clear answer to whether PFF's and ALOF's activities resulted in Mr. Gingrich having re-

277. Regan & Dunham, *supra* note 272, at 49. Mr. Gingrich taught his course in 1993 at Kennesaw State College, and in 1994 and 1995 at private Reinhardt College, both in Georgia. It was broadcast around the country on cable television networks, and was available to tens of thousands of students. The central theme of the course was the need to replace the "welfare state" with the "opportunity society," which was also GOPAC's central message. See, e.g., Charles R. Babcock, *Use of Tax-Exempt Groups Integral to Political Strategy*, WASH. POST, Jan. 7, 1997, at A1.

278. Contributors to PFF were able to earmark their contributions to go exclusively to Gingrich's course. Sheppard, *supra* note 268, at 1174. Mr. Gingrich came under special criticism from Reinhardt College for including laudatory statements about large corporate contributors to GOPAC and PFF within the course's materials "with scant mention of their financial support." *Id.* at 1175. Furthermore, "contributors to the Foundation were expressly told that they could participate in the development of the Renewing American Civilization course for a \$25,000 or \$50,000 donation, according to an internal memo obtained by Roll Call." *Id.*

279. In regard to the partisan nature of the course, "[m]emos promoting the course said it would train thousands of Republican activists." *Ethics Panel Looks at Outside Counsel*, COMMERCIAL APPEAL (Memphis), Aug. 8, 1995, at 4A.

280. Regan & Dunham, *supra* note 272, at 49. For discussion of PFF projects that have been unrelated to Gingrich's course, see Sheppard, *supra* note 268, at 1174-75.

281. Sheppard, *supra* note 268, at 1176. For an excellent discussion of the IRS' approach to distinguishing educational from partisan activities, as applied to PFF, see *id.* at 1175.

ceived an improper taxpayer subsidy.²⁸² In addition, PFF and ALOF provided Mr. Gingrich (and the Republican party more generally) an opportunity to benefit from corporate charitable contributions (as described immediately below)—contributions that would have been unlawful under FECA if made directly to him or to his political action committee; and thus important and unresolved campaign finance issues have also been raised by Mr. Gingrich's political affairs.²⁸³

After the November 1994 election, PFF assumed a highly visible role in public policy debates. Having become "a major source of research for the new Republican leadership's reform plans," the foundation afforded business contributors and wealthy individuals the potential to affect policy formation at the highest levels.²⁸⁴ The "darling think tank of the Republican Revolution," PFF released three policy papers during the summer of 1995²⁸⁵ and has remained an important influence on congressional policy initiatives.²⁸⁶ The foundation underwent "explosive growth" during this period.²⁸⁷ PFF's staff reportedly included twenty-six full-time employees by the summer of 1995,²⁸⁸ and the foundation had projected revenues of \$6 million for that year.²⁸⁹ Described by *Business Week* as "flush with corporate cash," PFF's success was subsidized in part by charitable contribu-

282. See Hill, *supra* note 233. Although ultimately unresolved, the issue of tax abuse was central to the Ethics Committee investigation. For an argument that Mr. Gingrich violated the tax laws and should be held financially liable, see Michael J. Graetz, *What Gingrich Owes Us*, N.Y. TIMES, Jan. 8, 1997, at A15.

283. While the House subcommittee gave extensive consideration to the issue of tax abuse, it failed adequately to address the campaign finance issues raised by Gingrich's partisan use of PFF and ALOF. See *Text of 'Analysis and Conclusion,' from Report by House Ethics Counsel*, N.Y. TIMES, Jan. 18, 1997, at A11.

284. See Cummings, *Gingrich Confidant*, *supra* note 272, at 4A; see also Regan & Dunham, *supra* note 272, at 49 (statement of American Enterprise Institute scholar J. Gregory Sidak, who worked as an adviser on PFF's FCC study: "We're getting the ear of people on Capitol Hill who really matter").

285. Regan & Dunham, *supra* note 272, at 49 ("Flush with corporate cash, its pumping out policy prescriptions for dumping the Federal Communications Commission, axing federal block grants, and privatizing safety and efficacy reviews of prescription drugs and medical devices.").

286. See, e.g., Steve Lohr, *Conservatives Split on How to Regulate the Internet*, N.Y. TIMES, Nov. 9, 1995, at D4 (describing PFF as helping to "lead the push for a self-regulatory approach" to screening material from the Internet).

287. Cummings, *Gingrich Confidant*, *supra* note 272.

288. *Id.*

289. Regan & Dunham, *supra* note 272, at 48 ("Since the election, times have been good. Revenues are expected to hit \$6 million in 1995, putting PFF on the same financial footing as seasoned groups such as the libertarian-leaning Cato Institute. For fiscal 1994, which ended Mar. 31, 1995, PFF raised \$2.2 million, up from \$656,000 in 1993. And in the first three months of 1995 alone, it took in \$866,000 with \$650,000 in contributions mostly from large corporate sponsors." (emphasis added)).

tions from AT&T, Bell Atlantic, Bristol Myers Squibb, Coca Cola, Eli Lilly, and Marion Merrell Dow, among other business contributors.²⁹⁰ Because of PFF's charitable status, these contributions would generally have been deductible for their corporate donors under § 170, unlike sums expended in traditional corporate lobbying efforts. In light of PFF's bold deregulatory initiatives in the pharmaceuticals and telecommunications areas and its continued favor in congressional circles, such technically philanthropic contributions to PFF may prove to have been shrewd business investments.

Notwithstanding the legal controversy that surrounded the activities of PFF, in April 1995 Robert Dole (then Senate Majority Leader and a presidential candidate) and Mr. Gingrich (then Speaker of the House and a potential presidential candidate) announced their creation of The Economic Growth and Tax Reform Commission ("EGTRC").²⁹¹ In June of 1995, the group applied for status as an educational foundation under § 501(c)(3).²⁹² Dole and Gingrich appointed Jack Kemp (a former presidential candidate, housing secretary, and congressman, and subsequent to EGTRC's creation, the Republican vice-presidential nominee for the 1996 presidential campaign) to act as EGTRC's chairman. Dole and Gingrich also appointed the group's thirteen other members.²⁹³ Reportedly all Republicans,²⁹⁴ EGTRC's members—former politicians, government officials, business executives, and entrepreneurs²⁹⁵—have been charged with "studying" the subject of tax reform and designing "a 21st century tax code," in the words of Mr. Kemp.²⁹⁶

290. *Id.* at 48 ("Donations overwhelmingly come from companies in telecommunications and medicine, areas where PFF is crafting bold deregulation plans."); see also Sheppard, *supra* note 268, at 1174 (noting that by December 1994 PFF had amassed \$1.5 million in donations, with approximately half of the sum coming from other conservative foundations and the other half "about equally from corporations, including many telecommunications businesses, and wealthy individuals").

291. Barbara Kirchheimer, *Kemp Tax Reform Commission Meets, Files for Tax-Exempt Status*, 67 TAX NOTES 1559, 1559 (1995).

292. The group filed for § 501(c)(3) status as a charitable trust. *Id.*

293. Barbara Kirchheimer, *Flat Tax Enjoys Wide Support Among Members of Kemp Commission*, 95 TAX NOTES TODAY 108-4, June 5, 1995, available in LEXIS, Tax Library, TNT File.

294. Bennett Minton, *Kemp Commission to Meet in Ways and Means Hearing Room*, 95 TAX NOTES TODAY 125-5, June 28, 1995, available in LEXIS, Tax Library, TNT File.

295. A list of EGTRC's members appears in Kirchheimer, *supra* note 293. For the names of EGTRC's full time staff, see Kirchheimer, *supra* note 291, at 1559.

296. Kirchheimer, *supra* note 291, at 1559. The text of the EGTRC's official charge is presented in National Commission on Economic Growth and Tax Reform, 'Charge' of National Commission on Economic Growth and Tax Reform Available at Commission Hearing, 95 TAX NOTES TODAY 190-41, Sept. 28, 1995, available in LEXIS, Tax Library, TNT file [hereinafter *Charge of*

As of January 1997, the IRS had still failed to reach a determination regarding EGTRC's charitable status.²⁹⁷ As described earlier, the lobbying limitations present under § 501(c)(3) would appear to prevent EGTRC from formulating specific legislative proposals to be enacted by Congress as part of tax reform.²⁹⁸ Nevertheless, the ambiguities present within certain Treasury regulations prescribing the scope of permissible legislative advocacy by charitable organizations²⁹⁹—particularly, the ability of charitable organizations to provide “technical advice or assistance to a government body” in response to a written request therefrom³⁰⁰—may provide a basis for the group to issue “a report that will lead to changes” fundamental to federal tax policy³⁰¹ while maintaining its status as a charitable organization.

Tax experts agree that the issues raised by the creation of EGTRC are not addressed in the existing precedent.³⁰² Some have wondered whether “the group's activities won't be inherently political, either in the form of lobbying or participating in a presidential campaign.”³⁰³ With Jack Kemp as its chairman, and Dole and Gingrich as its founders, it is inevitable that EGTRC's work will be intimately tied to the development of these politicians' platforms as well as their political careers. And while Mr. Kemp has described the group as “like a think tank,”³⁰⁴ it has not pursued its educational objectives in the ivory tower. During the summer of 1995, EGTRC held information-gathering sessions on the subject of tax reform, with special consideration regarding the implementation of a business-friendly “flat tax,” in the House Ways and Means Committee hearing room.³⁰⁵ Thus, EGTRC has taken on many of the attributes of a congressionally sponsored

National Commission]. The author of that report wryly noted that the group's creation has raised more tax policy questions than it has resolved.

297. See *Tax Reform, Kemp Commission Asking All Donors for Permission to Release Names*, Daily Rep. for Executives, Feb. 13, 1996, at G29 [hereinafter *Asking All Donors*]. A search of the relevant records and databases failed to uncover such a ruling.

298. I.R.C. § 501(c)(3) (1994).

299. See especially Treas. Reg. § 56.4911-2(c)(1), (3) (1996).

300. See Treas. Reg. § 56.4911-2(c)(3).

301. This is the group's stated objective, as set forth in its official charge. See *Charge of National Commission*, *supra* note 296.

302. Kirchheimer, *supra* note 291, at 1560 (quoting Francis R. Hill and Greg Colvin).

303. *Kemp's Tax Reform Committee Redefines Irony*, 65 TAX NOTES 1557, 1557 (1995). The issue was exacerbated by Jack Kemp's status as the G.O.P. vice-presidential nominee, of course.

304. Kirchheimer, *supra* note 291, at 1559.

305. Barbara Kirchheimer, *Kemp Tax Commission Borrows Ways and Means Hearing*, 68 TAX NOTES 7, 7 (1995). This arrangement was regarded by commentators as highly unusual.

commission,³⁰⁶ except that its members are privately appointed, it is funded from private donations, and because of its (pending) charitable status, the identities of its contributors need not be disclosed.³⁰⁷ Thus, EGTRC appears to represent a radical experiment in privatizing congressional policy formation through the nonprofit sector.³⁰⁸

Both PFF and EGTRC represent high-profile, ostensibly educational foundations that have contributed to the political ascendancy of current and former members of Congress and the promotion of policies friendly to big business. And of course, PFF and EGTRC are not the only examples of these extraordinary entities. By supporting candidate-identified, educational foundations through charitable contributions, corporations have contributed to the ascendancy of particular policies and politicians, and have sought to ensure that their own political fortunes will remain ascendant.

D. Contributions to Public Policy Institutes in General

1. Policy Institutes of National Prominence

As described above, PFF and EGTRC have been closely associated with the careers of particular politicians. But there are many policy institutes (or think tanks) unaffiliated with particular politicians that have significantly influenced the general development of American politics and public policy. Important policy institutes that have § 501(c)(3) status include: The American Enterprise Institute, The Brookings Institute, The Center for Strategic and International Studies, The Heritage Foundation, The Urban Institute, and more recently, The Progressive Policy Institute

306. In fact, EGTRC's spokesperson, Ari Fleischer, referred to the organization as a "congressionally sponsored commission" in speaking to the press. *Id.* Nevertheless, Kemp and other commission members insisted that EGTRC is not an "official governmental commission." *Id.*

307. If EGTRC qualifies as a charitable organization, it is under no legal obligation to disclose its contributors—in comparison to PACs, which are subject to stringent disclosure requirements under FECA. (For a discussion of FECA's disclosure requirements, see *supra* notes 257–263.) Soon after EGTRC's formation, Mr. Gingrich promised that information regarding EGTRC's contributors would be made public. Kirchheimer, *supra* note 291, at 1559. However, notwithstanding that at least \$375,000 in donations have been received, no donor information appears to have been made public. *Asking All Donors*, *supra* note 297, at G29. Representatives Sam Gibbons (D-Fla.) and John Dingell (D-Mich.) had written to EGTRC asking for this information. *Id.*

308. House Ways and Means Committee Chairman Bill Archer (R-Tex.) described EGTRC as "the 'lever-pull' for whatever action Congress takes on tax reform." Kirchheimer, *supra* note 305, at 7.

and The Cato Institute.³⁰⁹ Various studies have documented the flow of corporate funds to these and other policy institutes.³¹⁰ While there is no basis to conclude that such contributions have co-opted public policy debate at these institutions, they have undoubtedly helped to assure corporate America a seat at the negotiating table.

The Cato Institute's recent rise to prominence provides an interesting example of the synergy between corporate charitable contributions and public policy initiatives.³¹¹ Cato's founder, Edward Harrison Crane III, has indicated that seventy percent of the foundation's annual budget of approximately \$6 million is derived from individual contributions, but corporations have also been substantial contributors.³¹² According to the *Los Angeles Times*, corporate contributors have included oil companies such as Exxon, Shell Oil, and Tenneco Gas; tobacco and alcohol companies such as Joseph A. Seagram & Sons and Philip Morris Companies, Inc.; and financial interests, including Prudential Securities and the Chase Manhattan Bank.³¹³ The businesses that have contributed, which have also included Federal Express and Tele-Communications Inc., have had an

309. These policy institutes are each described in the appendix to JAMES ALLEN SMITH, *THE IDEA BROKERS, THINK TANKS AND THE RISE OF THE NEW POLICY ELITE* (1991). See also Robin Toner, *New, Old Think Tanks Compete for Funds*, L.A. DAILY J., Jan. 17, 1986, at 17.

310. The most explicit data is made available in the report on corporate public affairs giving published annually by The Capital Research Center ("CRC"), under the title "Patterns of Corporate Philanthropy." CRC relies on voluntary responses to surveys mailed to Forbes 250 corporations as well as a review of corporate foundations' Form 990s. CRC's publications have argued that corporate public affairs giving reflects a persistent liberal bias. The CRC has estimated total annual corporate public affairs giving at approximately \$28 million in recent years. See, e.g., NOLAN, *supra* note 186, at 11.

311. The Cato Institute is a libertarian organization founded in the late 1970s by Edward Harrison Crane III. Cato has become extraordinarily prominent in recent years, especially since the November 1994 congressional elections. According to the *Los Angeles Times*, in one week in February of 1995, for example, Cato staffers made appearances on 7 radio and TV shows, had 8 op-ed pieces in major papers, and had citations in 22 news stories. The *Los Angeles Times* also reported that "Cato's policy directors testified before congressional committees 20 times in the first month of the current session"; and the institute has published a 358-page "Handbook for Congress." Nina J. Easton, *Making America Work: Red, White and Small*, L.A. TIMES, July 9, 1995, (Magazine), at 14.

312. *Id.* at 29.

313. *Id.*

obvious interest in promoting the "less-regulation, lower-taxes" program that is at the heart of Cato's libertarian philosophy.³¹⁴

2. State-Level Conservative Think Tanks

The political influence enjoyed by think tanks having national prominence and headquarters in the nation's capital has recently led to growth, in terms of both influence and numbers, of conservative, state-level policy institutes.³¹⁵ As the political climate has changed so that ideas relating to federalism and limited government have become more central to political debate, conservative organizations have sought to use state level think tanks to influence state and local governments towards their free market, laissez-faire views.³¹⁶ In February of 1995, *The Washington Times* reported on the recent establishment of thirty-two such conservative policy institutes (qualified as § 501(c)(3) educational organizations), describing their influence on state and local policy as "formidable."³¹⁷ The newspaper also described the work of the affiliated national organization, The State Policy Network, which reportedly conducts research on policy issues, helps to establish new state policy institutes, and advises them on "how to become influential forces in local policy-making."³¹⁸ In addition to the thirty-two organizations with which it was already affiliated, The State Policy

314. Cato appears to have prevented itself from becoming a pawn of either big business or the Republican party. See, e.g., STEPHEN MOORE & DEAN STANSEL, *CATO INST., ENDING CORPORATE WELFARE AS WE KNOW IT* (1995).

315. For the factual basis of this section of the Article, I have relied on Joyce Price, *Conservative Think Tanks Gain in Number, Respect Nationwide; Growing Influence Shows in State, Local Policy-Making*, WASH. TIMES, Feb. 2, 1995, at A4.

316. Writing in *The Washington Times*, Byram Lamm, executive director of The State Policy Network, described his organization as endorsing "free-market solutions to public policy, with an emphasis on individual rights and fiscal responsibility." The newspaper also quoted Joe Dolan, former treasurer and finance committee chairman of The State Policy Network: "Behind a lot of the new ideas coming from governors these days are state policy think tanks." It also cited a letter from Michigan Governor John Engler to the Mackinac Center, describing the Center's work as "critical" to the progress his Republican administration had made in "putting government in its proper place and liberating the entrepreneurial spirit." *Id.*

317. *Id.*

318. *Id.*

Network was described as being actively involved in establishing new conservative policy institutes in six additional states.³¹⁹ This network of state-level policy institutes has afforded corporations the opportunity to use charitable contributions to influence the political environment at the level of state and local government.

3. Affiliations Between § 501(c)(3) Educational Organizations and Politically Active § 501(c)(4) Organizations

Both the candidate-identified foundations and the public policy institutes discussed above have relied principally on the educational purposes provision of § 501(c)(3) as the basis for their charitable status, and therefore, their eligibility to receive donor-deductible philanthropic donations.³²⁰ But despite its extraordinary malleability, the educational purposes provision of § 501(c)(3) is not sufficient to accommodate unlimited political advocacy by charitable organizations. Most significantly, when legislative lobbying is part of an organization's principal objectives, such an organization would be classified as an "action organization" and hence, ineligible for charitable status under § 501(c)(3).³²¹ Alternatively, "social welfare" organizations, having tax-exempt status under § 501(c)(4), are unencumbered by any lobbying limitations, but the Code does not afford their contributors a tax deduction for such contributions.

In response to this dilemma, organizations seeking to offer potential donors the financial incentive of tax deductibility,³²² but wishing to avoid the lobbying limitations existing under § 501(c)(3), have adopted a strategy known as the "c3/c4 split."³²³ In this arrangement, politically ambitious groups splinter themselves into twin organizations, legally distinct but

319. *Id.*

320. Section 170 permits taxpayers a federal income tax deduction for their gifts to § 501(c)(3) charitable organizations. No such allowance exists for donations to § 501(c)(4) social welfare organizations (also referred to as "action organizations"), which are frequently committed to substantial lobbying as part of their charitable objectives. See I.R.C. § 501(c)(3), (c)(4) (1994).

321. Section 501(c)(3) requires that charitable organizations be "organized and operated" exclusively for charitable purposes. I.R.C. § 501(c)(3) (1994). An organization that is deemed an "action organization," by virtue of engaging in (or stating that it shall engage in) impermissible political advocacy, cannot qualify for tax exempt status under § 501(c)(3). For the attributes of action organizations, see Treas. Reg. § 501(c)(3)-1(c)(3)(ii), (iii) & (iv) (1996).

322. The federal income tax deduction applying to charitable contributions is regarded as a crucial stimulus to charitable giving.

323. Shenk, *supra* note 269.

ideologically and functionally entwined.³²⁴ One piece is constituted as a § 501(c)(3) organization—thus able to receive tax-deductible charitable contributions, but unable to engage in substantial lobbying. The other piece of the entity is qualified as a § 501(c)(4) tax-exempt social welfare organization—thus permitted to engage in unlimited lobbying, but ineligible to afford its donors a tax deduction for their donations. Such hybrid organizations were relatively uncommon until the late 1970s. Tax planners generally regarded the arrangement as overly clever.³²⁵ This changed with the Supreme Court's 1983 decision in *Regan v. Taxation with Representation*.³²⁶ In reviewing a charitable organization's First Amendment challenge to § 501(c)(3)'s lobbying limitations, the Court noted that "[t]he constitutional defect that would inhere in § 501(c)(3) alone is avoided by § 501(c)(4)."³²⁷ In effect, the Supreme Court invited charitable organizations to establish affiliated § 501(c)(4) entities under their control,³²⁸ to administer any lobbying activities connected to the accomplishment of their charitable purposes.

Accordingly, most prominent advocacy organizations have established an affiliated "research and education" entity, qualified under § 501(c)(3), through which they fund activities not directly connected to lobbying.³²⁹ Section 501(c)(4) organizations have become extraordinarily prominent on

324. The organizations commonly share headquarters, staff, mailing lists, etc. They also frequently combine their solicitation materials so that contributors may "check the box" to allocate their contributions among the "c3" or the "c4" parts of the organization. As stated in the text, this system of organization was sanctioned in *Regan v. Taxation with Representation*, 461 U.S. 540, 545 n.6 (1983): "The IRS apparently requires only that the two groups be separately incorporated and keep records adequate to show that tax-deductible contributions are not used to pay for lobbying." See also Cummings, *supra* note 226, at A-38 ("[T]hese opinions suggest that the (c)(4) organization may be the 'alter ego' of the (c)(3) organization so long as records show that their finances are kept separate.").

325. Cummings, *supra* note 226, at A-38.

326. *Regan*, 461 U.S. at 540; see also *Rust v. Sullivan*, 500 U.S. 173, 175 (1991). For further discussion of charitable organizations' use of "non-(c)(3)" affiliates, see Chisolm, *supra* note 226; Cummings, *supra* note 226, at A-37 to A-38.

327. *Regan*, 461 U.S. at 552 (Blackmun, J., concurring).

328. *Id.* at 553 ("Should the IRS attempt to limit the control these organizations exercise over the lobbying of their § 501(c)(4) affiliates, the First Amendment problems would be insurmountable. It hardly answers one person's objection to a restriction on his speech that another person, outside his control, may speak for him.").

329. It is now relatively easy to ascertain whether a charitable organization has a related § 501(c)(4) body. In January 1993, the IRS released a new Schedule A to accompany the Form 990 Informational Return required of all public charities. The Schedule A requires presentation of information about affiliated § 501(c)(4) organizations and any other noncharitable affiliates. See 93 TAX NOTES TODAY 43-15, Jan. 1, 1993, available in, LEXIS, Tax Library, TNT File.

the domestic policy landscape. They include the National Rifle Association, the National Abortion and Reproductive Rights Action League, the American Conservative Union, the American Association of Retired Persons, People for the American Way, the NAACP, and the Sierra Club, for example.³³⁰ Each of the former organizations has established a complementary § 501(c)(3) entity dedicated to disseminating its views and producing the analysis that forms the basis of its lobbying efforts.³³¹ Notwithstanding serious questions regarding whether these organizations in fact segregate their funds as legally required, and the limited capacity of the IRS to monitor potential abuses,³³² the principle behind these hybrid c3/c4 organizations is sound. From the perspective of this analysis, however, the important observation is that the c3/c4 split has facilitated the politicization of the nonprofit sector, and hence has expanded the political uses of corporate charitable contributions.

E. Corporate Donations to Corporate-Oriented PILFs

Corporations have contributed to the politicized nonprofit organizations described above in order to effect favorable *electoral and legislative* outcomes. In yet another form of philanthropic advocacy, corporations have used charitable contributions to pro-business legal defense funds, constituted as § 501(c)(3) organizations, to influence the development of the law. Professor Oliver Houck has written a comprehensive history of the development of public interest legal foundations ("PILFs") "created, funded and . . . largely directed by leaders of American business corporations."³³³ These PILFs included, for example, the Pacific Legal Foundation (the forerunner of the "business" PILFs), the Mountain States Legal Foundation, the Gulf and Great Plains Legal Foundation, the Mid-American Legal Foundation, the New England Legal Foundation, the Southeastern Legal Foundation, and the Capital Legal Foundation.³³⁴

According to Houck, politically conservative, business-funded PILFs were established en masse after the mid-1970s, as a result of business leaders' perception that liberal PILFs (and especially pro-environmental PILFs) were leveraging their nonprofit advantages in ways that represented a threat

330. These examples are drawn from Shenk, *supra* note 269.

331. *Id.* at 37.

332. Shenk accuses several organizations of lax oversight and loose control over separate accounts. He is also highly skeptical of the IRS' capacity to monitor this conduct, describing it as the "see no evil IRS." Shenk, *supra* note 269, at 35.

333. Oliver A. Houck, *With Charity for All*, 93 YALE L.J. 1415, 1419 (1984).

334. *Id.* at 1420.

to corporate interests.³³⁵ Donations to these corporate-funded PILFs have most commonly funded appearances as amicus curiae on behalf of pro-business positions in litigation involving commercial development and general environmental matters.³³⁶ Nevertheless, pro-business PILFs have also become active in advocating business-friendly legal reform outside of the litigation context.³³⁷

Houck's research examined the existence and practices of business PILFs from the perspective of tax policy. In particular, his work analyzed whether these entities had violated prohibitions on private inurement, and whether their practice of law could be reconciled with the established definitions of charity under tax law and jurisprudence.³³⁸ From the perspective of this analysis, the existence of business-funded legal foundations constituted as § 501(c)(3) charitable organizations demonstrates that corporate charitable contributions have been used, both within and beyond the courtroom, to influence the law in the corporate interest.³³⁹

F. A Critique of Politicized Corporate Philanthropy as Corporate Speech

Corporate expenditures in support of political and cultural affairs have been recognized by the Supreme Court as speech entitled to protection under the First Amendment.³⁴⁰ Yet the fact that such speech emanates

335. *Id.*

336. *Id.* at 1421.

337. For example, the Washington Legal Foundation ("WLF") publishes a newsletter entitled *The Legal Backgrounder*. See, e.g., Jared G. Carter, *Reduce Incentives That Encourage Activist Environmental Lawsuits*, LEGAL BACKGROUNDER, Aug. 11, 1995; Daniel J. Popeo, *It's Time to Scrutinize HUD Funding of Activist Groups*, LEGAL BACKGROUNDER, July 21, 1995; Lawrence Savell, *Guidelines to Keep Advertisers out of Court*, LEGAL BACKGROUNDER, Sept. 1, 1995. During the summer of 1995, WLF joined with drug and medical device companies to limit FDA restrictions on "off-label" or unapproved uses of drugs. See *Pharmaceutical Cos: Challenging Marketing Rules*, HEALTH LINE, Aug. 31, 1995, available in LEXIS, News Library, Cumws File. WLF has also petitioned OSHA to adopt rules safeguarding employers' rights during inspections and investigations. See *OSHA Should Honor Employer Rights During Inspection*, WLF Recommends, OCCUPATIONAL HEALTH & SAFETY LETTER, Aug. 21, 1995.

338. Houck, *supra* note 333, at 1416.

339. For further discussion of corporate advocacy in the area of legal reform, see, for example, ALLIANCE FOR JUSTICE, JUSTICE FOR SALE: SHORTCHANGING THE PUBLIC INTEREST FOR PRIVATE GAIN (1993).

340. *Austin v. Michigan Chamber of Commerce*, 494 U.S. 652 (1990) (application of FECA's campaign expenditure limitations to chamber of commerce held constitutional—*notwithstanding the recognition of the chamber's free speech interests*—in light of state's interest in avoiding the potential for political corruption); *FEC v. Massachusetts Citizens for Life, Inc.*, 479 U.S. 238 (1986) (application of FECA's campaign expenditure limits to nonprofit corporation created expressly to advance political and ideological views held unconstitutional under the First Amendment); *Consolidated Edison Co. v. Public Serv. Comm'n*, 447 U.S. 530 (1980) (Public

from a legal entity, rather than from the natural persons who compose it, means that corporate speech implicates multiple layers of associational and free speech interests—those of the corporate entity and those of its individual shareholders.³⁴¹ Furthermore, both of these speech interests are at a zenith where the entity's speech obtains political dimensions,³⁴² as it does in the politicized corporate charitable contributions discussed above. Therefore, the corporation's right to free participation in the marketplace of ideas must be reconciled with, or at least weighed alongside, the free speech and associational interests of corporate shareholders.³⁴³

Notwithstanding the recognition of corporate-level speech rights, the judiciary has in a variety of contexts taken note of the unfairness resulting from forced subsidization of entity-level expression. Thus, the ratepayers of a publicly regulated utility,³⁴⁴ persons governed by an agency shop arrange-

Service Commission's order prohibiting utility from including policy statements in monthly billing inserts held to abridge utility's First Amendment rights); *First Nat'l Bank v. Bellotti*, 435 U.S. 765 (1978) (Massachusetts law limiting corporate spending on referenda held unconstitutional under First Amendment). On the relation between spending and speech, see, for example, *Buckley v. Valeo*, 424 U.S. 1, 19 (1976) (per curiam): "[V]irtually every means of communicating ideas in today's mass society requires the expenditure of money."

341. The protection of *individuals'* rights of free speech and association, of course, predates the recognition of speech rights at the entity level. For a comprehensive consideration of the intersection of individuals' and entities' speech rights, see Brudney, *Association, Advocacy, and the First Amendment*, *supra* note 227.

342. *Buckley*, 424 U.S. at 14–15 (although First Amendment protections are not confined thereto, extraordinary solicitude is afforded speech concerning political, governmental, or civic matters).

343. For discussion of the problems generated by corporate level political speech, see Brudney, *Business Corporations*, *supra* note 227, at 235; Michael J. Garrison, *Corporate Political Speech, Campaign Spending, and First Amendment Doctrine*, 27 AM. BUS. L.J. 163 (1989). For a less troubled view of corporate political speech, see Ribstein, *supra* note 227. See also Meese, *supra* note 227.

344. *Cahill v. Public Serv. Comm'n*, 556 N.E.2d 133 (N.Y. 1990) (holding that commission's policy authorizing utilities to include cost of charitable contributions within rate payments impinges upon ratepayers' First Amendment rights).

ment,³⁴⁵ and members of an integrated bar association³⁴⁶—with narrow exception³⁴⁷—cannot constitutionally be compelled to subsidize entity-level political speech with which they are in disagreement. Of course, the former contexts are distinguishable from involuntary shareholder funding of corporate charitable contributions on the basis that state action is absent in the corporate context.³⁴⁸ For this reason, the speech and associational interests of corporate shareholders, as they are affected by the speech-related acts of the corporate entity, do not obtain *federal constitutional* proportions.³⁴⁹

Nevertheless, the dangers inherent in compelled speech have long been recognized—even outside the area of governmental coercion. When Thomas Jefferson declared that “to compel a man to furnish contributions

345. *Abood v. Detroit Bd. of Educ.*, 431 U.S. 209 (1977) (holding that First Amendment prohibits funds received under agency shop arrangement from being used to support political or ideological affairs nongermane to collective bargaining against the will of the contributors).

346. *Keller v. State Bar*, 496 U.S. 1 (1990) (mandatory bar membership dues may not be used to fund ideological activities unrelated to regulation of legal profession against contributors' objections); *Lathrop v. Donohue*, 367 U.S. 820 (1961). For commentary on the bar association cases, see James B. Lake, Comment, *Lawyers, Please Check Your First Amendment Rights at the Bar: The Problem of State-Mandated Bar Dues and Compelled Speech*, 50 WASH. & LEE L. REV. 1833 (1993).

347. The union and bar association cases illustrate the scope of the permissible curtailment of members' free speech interests, as required by the operation of compelling state interests. See, e.g., *Keller*, 496 U.S. at 1 (state bar association expenditures of compulsory dues on matters necessarily or reasonably related to the regulation of the legal profession held constitutional; whereas expenditure of compulsory fees on political and ideological activities not thus related violated petitioners' First Amendment speech rights); *Ellis v. Brotherhood of Ry., Airline & S.S. Clerks*, 466 U.S. 435 (1984); *Abood*, 431 U.S. at 209; *Railway Employees' Dep't v. Hanson*, 351 U.S. 225 (1956) (union shop provision of the Railway Labor Act held constitutional based on importance of collective bargaining and disruptive effect of free-riding employees, despite compromise of First Amendment principles).

348. Business corporations—even those described as “public” on the basis that they have raised financing from the national securities markets—are regarded as private entities.

349. State action is a predicate to the operation of federal constitutional guarantees. See, e.g., *Lugar v. Edmondson Oil Co.*, 457 U.S. 922, 936–37 (1982).

of money for the propagation of opinions which he disbelieves, is sinful and tyrannical,"³⁵⁰ there is no reason to believe that he meant to confine his observation exclusively to governmentally imposed coercion. Shareholders have an interest in avoiding compelled subsidization of corporate level speech even if the interest is not cognizable under the United States Constitution. Although mainstream corporate speech jurisprudence has focused principally on entity level speech rights, shareholders' "negative speech interests" have been recognized in a variety of legal contexts. For example, FECA's limitations on corporate campaign spending are regarded as reflecting a concern for the free speech interests of dissenting shareholders³⁵¹ in addition to other societal concerns.³⁵² Concern over dissenting shareholders' speech interests in the presence of corporate level speech has also been expressed in the Supreme Court's corpus of free speech cases, and has gained some increased support in recent years.³⁵³ Furthermore, Victor Brudney, a noted corporate legal scholar whose treatment of shareholders' speech interests has been cited by the Court,³⁵⁴ has argued that a statu-

350. For Jefferson's quotation and explication of the historical context, see IRVING BRANT, *JAMES MADISON: THE NATIONALIST, 1780-1787*, at 354 (1948). Jefferson's statement is quoted in the majority opinion in *Abood*. See 431 U.S. at 235 n.31.

351. Extensive discussion of FECA's legislative history and the concerns underlying its enactment appears in *Pipefitters Local Union No. 562 v. United States*, 407 U.S. 385, 414-15 (1972) ("The dominant concern in requiring that contributions be voluntary was, after all, to protect the dissenting stockholder or union member."). For further commentary on Congress' long-standing concern over compelled speech in the context of unions and corporations, see *United States v. UAW*, 352 U.S. 567 (1957); *United States v. CIO*, 335 U.S. 106 (1948); *Ash v. Cort*, 350 F. Supp. 227 (E.D. Pa. 1972), *aff'd* by 471 F. 2d 811 (3rd Cir. 1973).

352. FECA is recognized as acknowledgment of the danger that corporate wealth (amassed with the cooperation of the state) might otherwise dominate the democratic process, swaying election outcomes in a manner inconsistent with the political views of individual persons. See, e.g., *Austin v. Michigan State Chamber of Commerce*, 494 U.S. 652, 659-60 (1990) ("Regardless of whether this danger of 'financial quid pro quo' corruption may be sufficient to justify a restriction on independent expenditures, Michigan's regulation aims at a different type of corruption in the political arena: the corrosive and distorting effects of immense aggregations of wealth that are accumulated with the help of the corporate form and that have little or no correlation to the public's support for the corporation's political ideas." (citation omitted)).

353. See *FEC v. Massachusetts Citizens for Life, Inc.*, 479 U.S. 238, 260 (1986) (noting legitimacy of concern that corporations may use shareholders' money for political purposes not favored by such individuals). A strong defense of shareholders' (and union members') interests in avoiding forced subsidization of entity level speech appears in Justice Brennan's concurrence in *Austin*, 494 U.S. at 674-75 (Brennan, J., concurring). A similar concern for dissenting shareholders' "negative speech interests" was articulated by Justice White in his dissenting opinion in *Bellotti*. See *First Nat'l Bank v. Bellotti*, 435 U.S. 765, 818 (1978) (White, J., dissenting) ("Clearly the State has a strong interest in assuring that its citizens are not forced to choose between supporting the propagation of views with which they disagree and passing up investment opportunities.").

354. *Austin*, 494 U.S. at 675 (Brennan, J., concurring) (citing Brudney, *Business Corporations*, *supra* note 227, at 247).

tory requirement of absolute shareholder consent for corporate level political expenditures would be constitutionally sound, based on the state's interest in protecting shareholders' rights.³⁵⁵

In contrast, other scholars have portrayed corporate political speech as merely an alternative form of profit maximization or, otherwise, as a public good (in the tradition of *First National Bank v. Bellotti*³⁵⁶), and have thus been less solicitous of shareholders' speech interests.³⁵⁷ These scholars have argued that market mechanisms, the nature of the corporation as a "nexus of contracts,"³⁵⁸ and efficiency concerns (e.g., the problem of free-riding dissenters enjoying unpaid-for financial benefits) either reduce the potential for coercion or otherwise mandate against imposing limitations on corporate political speech in the interest of protecting dissenting shareholders. These divergent views of corporate speech and of the interests furthered thereby are not easily reconciled.

G. Shareholders' Negative Speech Rights and the Remedial Limits of Disclosure

My contribution at this juncture, in this discussion of politicized corporate charitable contributions, is the observation that theories of corporate speech—from the libertarian (and entity-friendly) viewpoint advocated by Professor Ribstein, for example, to the more pro-regulatory (and thus shareholder-friendly) one advocated by Professor Brudney—in each case depend on *some* notion of shareholder consent. Brudney's model contemplates a requirement of consent in fact.³⁵⁹ Alternatively, scholars defending the status quo rely on the notion that shareholders consent to all profit-maximizing acts, including corporate political speech, when they make their investment decision (or, secondarily, on the idea that shareholders, at least theoretically, have the ability to alter charter terms to prescribe optimal standards of corporate conduct, and thus should be deemed to have consented to corporate speech).

355. Brudney, *Business Corporations*, *supra* note 227.

356. 435 U.S. 765, 777 (1978) ("If the speakers here were not corporations, no one would suggest that the State could silence their proposed speech. It is the type of speech indispensable to decisionmaking in a democracy, and this is no less true because the speech comes from a corporation rather than an individual.")

357. Ribstein, *supra* note 227; Meese, *supra* note 227.

358. For a critique of the nexus-of-contracts model of the corporation, see Wolfe, *supra* note 191, at 1676–83. See also BLAIR, *supra* note 14, at 17–93; Bratton, *supra* note 216; Henry N. Butler, *The Contractual Theory of the Corporation*, 11 GEO. MASON UNIV. L. REV. 99 (1989).

359. Brudney, *Business Corporations*, *supra* note 227.

The problem is that each of these notions of shareholder consent depends on an assumption about the existence of adequate information,³⁶⁰ and in the area of corporate charitable contributions, such information rarely has been made available to shareholders. The pervasive inability of shareholders to acquire accurate and complete information regarding their firms' charitable contributions subverts the operation of any meaningful notion of shareholder consent in regard thereto, thus delegitimizing corporate charitable contributions as a form of corporate political expression. Although Congress has given the SEC the authority to promulgate disclosure requirements in the public interest and for the protection of investors,³⁶¹ the SEC has yet to acknowledge this facet of shareholders' rights or to protect them by requiring disclosure of corporate charitable contributions.

This is not to suggest that disclosure of politicized charitable contributions will resolve the conflict between corporate and individual speech rights. On the contrary, initially, disclosure will serve merely to make the conflict visible. Of course, coercion cannot be addressed if it is not visible, and disclosure will at least allow dissenting shareholders to seek partial redress through advocacy or disengagement (selling). Future legal and practical developments will have to address, and will reflect, the accommodation that we as a society endorse between these potentially conflicting corporate- and individual-level speech rights.

VI. DONATIONS BENEFITING THE BUSINESS

Both courts and corporate executives have described corporate charitable contributions as a source of financial benefits for the firm.³⁶² Such

360. All metaphors based on freedom of contract depend on assumptions of adequate, or at least equal, information. This is readily apparent in the context of patient informed consent to medical procedures, for example.

361. See Securities and Exchange Act of 1934, 15 U.S.C. § 78n(a) (1994).

362. As described *supra* in notes 62-64 and accompanying text, prior to the enactment of the enabling statutes, courts upheld donations when they believed benefits would accrue to the firm as a result thereof. See, e.g., *Armstrong Cork Co. v. H.A. Meldrum Co.*, 285 F. 58, 58-59 (W.D.N.Y. 1922) (describing the potential benefits accruing from donations supporting improved business education, as well as the value of the goodwill of influential citizens and patrons); *Memorial Hosp. Ass'n v. Pacific Grape Prod. Co.*, 290 P.2d 481, 483 (Cal. 1955) (describing the benefits potentially accruing to employees from more accessible and improved hospital facilities as the basis for finding that the president was within his authority to authorize the gifts); cf. *Kahn v. Sullivan*, 594 A.2d 48, 62 (Del. 1991) (though benefit to the firm was not required, the court observed that public relations benefits were likely to arise from the company-funded museum). Of course, corporate managers have an incentive to describe contributions in terms of revenue enhancement, in order to insulate such contributions (and their decision-making in regard thereto)

profit-maximizing charitable contributions have included a broad spectrum of corporate conduct, some of it closely analogous to traditional marketing and advertising, with other contributions having a more attenuated connection to revenue creation or cost reduction.³⁶³ Donations made in the interest of benefiting the corporation are consistent with the traditional, commercial norms of corporate law. From the perspective of corporate law, profit-maximizing charitable contributions are uncontroversial.

Part of the problem in this area is practical. Without systematic disclosure, shareholders have no ability to assess whether corporate managers have administered the firm's charitable contributions according to value-maximizing criteria. Because managers may accomplish self-serving objectives through their allocation of the firm's charitable contributions, as described above, some system of accountability is required. Additionally, the dearth of company-specific data in the area of corporate philanthropy has hindered the progress of empirical analysis.³⁶⁴ Systematic disclosure would provide economists and other analysts the data required to assess the profit-maximizing claims made in regard to corporate charitable contributions.

There is also a deeper, conceptual problem inhering in the notion of profit-maximizing charitable contributions. Donations that are foreseeably profit maximizing should not rightly be considered philanthropic. Under both tax policy and the common understanding of "charity," the donor cannot anticipate a net gain from a *charitable* contribution.³⁶⁵ Thus, while profit-maximizing charitable contributions are uncontroversial from

from scrutiny.

363. For academic discussions of the strategic benefits that may arise from charitable contributions, see, for example, Galaskiewicz, *supra* note 182, at 246-60; Haley, *supra* note 36, at 485-504; Peter Navarro, *Why Do Corporations Give to Charity?*, 61 J. BUS. 65-93 (1988). Within the tax literature, Nancy Knauer has described contributions as commercially driven (and has thus argued for the repeal of the corporate *charitable* deduction under § 170). Knauer, *supra* note 77, at 96. The empirical studies analyzing the connection between corporate charitable contributions and corporate profit maximization are summarized in Webb, *supra* note 54, at 77-132. And within the marketing-oriented and popular literature see, for example, STECKEL & SIMONS, *supra* note 183; Philip Maher, *What Corporations Get by Giving*, BUS. MARKETING, Dec. 1984, at 80-89; Timothy S. Mescon & Donn J. Tilson, *Corporate Philanthropy: A Strategic Approach to the Bottom-Line*, CAL. MGMT. REV., Winter 1987, at 49-61; Smith, *supra* note 47, at 105.

364. See, e.g., Navarro, *supra* note 363, at 65 ("[T]he empirical efforts have been hampered by the lack of firm-specific data."); Craig Smith, *Desperately Seeking Data*, 9 CORP. PHILANTHROPY REP. 10-11 (Oct. 1993); see also Maher, *supra* note 363, at 84 ("Despite the billions of dollars donated each year, there is a remarkable dearth of hard data on its use or, especially, its effectiveness.").

365. Knauer has confronted this analytic problem directly, arguing that the mercenary nature of these transfers should disqualify them from being deductible as charitable contributions. Knauer, *supra* note 77, at 96.

the perspective of corporate law, they are highly controversial as a general theoretical matter, and from the perspective of tax policy analysis.

The transfers most readily observed to be profit maximizing, that is, those arising from cause-related marketing ("CRM") promotions and corporate special-event ("CSE") sponsorships, are most directly in conflict with the charitable paradigm operative under § 170.³⁶⁶ Because the expectation of a quid pro quo underlies these arrangements, such transfers fail to satisfy the "contribution or gift" requirement of § 170.³⁶⁷ On this basis, contributions arising from corporate marketing programs are increasingly being regarded as forms of business transfers distinguishable from charitable giving,³⁶⁸ ones more appropriately deducted as business expenses under § 162 than as charitable contributions under § 170.³⁶⁹ And, indeed, contributions arising from CRM promotions and CSE sponsorships are not included in the annual aggregate corporate charitable contributions figures presented in *Giving USA*, and elsewhere.³⁷⁰

Alternatively, outside of CRM and CSE promotions, most charitable contributions by corporations have had only a tenuous connection to revenue enhancement or cost reduction.³⁷¹ The resulting "gossamer civic

366. My analysis is consistent with the holding in *Hernandez v. Commissioner*, 490 U.S. 680, 691 (1989), which adopts a quid pro quo oriented analysis in relation to the "contribution or gift" requirement pertaining to charitable contributions. For commentary on the *Hernandez* decision, see Knauer, *supra* note 77, at 35-41. See also *United States v. American Bar Endowment*, 477 U.S. 105 (1986) (holding that no portion of individual taxpayers' premium payments constitutes a charitable contribution).

367. Section 170(c) defines the term "charitable contribution." I.R.C. § 170 (1994). Of further relevance is Treas. Reg. § 1.170A-1(c)(5) (as amended in 1990). See *supra* note 7.

368. See, e.g., STECKEL & SIMONS, *supra* note 183, at 76 ("Cause-related marketing is just that: marketing. It happens to have a philanthropic result, but its primary purpose is sales."); P. Rajan Varadarajan & Anil Menon, *Cause-Related Marketing: A Coalignment of Marketing Strategy and Corporate Philanthropy*, 52 J. MARKETING, July 1988, at 58-74, 59-60 (describing essential marketing thrust of CRM promotions); see also Knauer, *supra* note 77, at 11 ("In practice, corporate managers and fundraisers agree that corporate transfers to charity represent a calculated purchase of advertising services or goodwill.").

369. From the perspective of the corporation, the classification of the transfer as charitable or as a business-related expense is generally not a substantial concern (outside of the context of lobbying). The transfers would be deductible under § 170 in the former case, or under § 162 in the latter case. However, where § 170 treatment is inapposite, the company's costs might have to be capitalized pursuant to § 263 in some instances, thus rendering the distinction between business related expenses and charitable contributions of greater practical relevance. See I.R.C. § 263 (1994).

370. See *supra* note 22.

371. See *supra* note 364; see also Galaskiewicz, *supra* note 182, at 248 ("Research on the relationship between company giving and public opinion is scanty and inconclusive."). For a skeptical view of the touted strategic benefits accruing from charitable contributions, see USEEM, *supra* note 159, at 146-49; Haley, *supra* note 36, at 492: "Despite managerial claims, there are almost no corporate data to verify that contributions affect corporate profits."

goodwill³⁷² has too readily supplied a justification for unlimited managerial discretion in the area of corporate philanthropy.³⁷³ Thus, systematic disclosure is required in order to provide an appropriate accommodation between shareholders' interest in accountability and managers' interest in flexibility, and to advance the study of corporate philanthropy.

A. Contributions-Based Corporate Marketing

There is considerable empirical evidence that charitable contributions have been assimilated into corporate marketing and advertising functions,³⁷⁴ either as a complement to or as a substitute therefor.³⁷⁵ CRM and CSE promotions have allowed firms to publicize both their individual products and the corporation's "good image" generally.³⁷⁶ These highly

372. *Cahill v. Public Serv. Comm'n*, 556 N.E.2d 133, 137 (N.Y. 1990).

We agree and understand that charitable contributions may enhance important quality of life aspects in selected spheres of the affected communities, thus benefiting in many intangible ways the utilities' employees, customers and boosters. . . . But the effects of this gossamer civic goodwill on the elementary provision of utility services are at best speculative

373. Although a corporation is not required to demonstrate that financial benefits will result to it as a result of its contributions (as described in Part II), courts have uniformly responded favorably when the potential for a benefit has been alleged. See, e.g., *Kahn v. Sullivan*, 594 A.2d 48, 62 (Del. 1991). On a related point, I would argue that the business judgment rule should apply to donations that are foreseeably profit-maximizing—but the dilemma is discerning which gifts should properly be so categorized.

374. Economists regard advertising as an attempt to enhance revenues by manipulating the demand for the firm's product. For a summary of the literature on commercial advertising, see David W. Schumann et al., *Corporate Advertising in America: A Review of Published Studies on Use, Measurement and Effectiveness*, 20 J. ADVERTISING, Sept. 1991, at 35. The variables affecting a firm's propensity to advertise are discussed in Richard E. Caves & Peter J. Williamson, *What Is Product Differentiation, Really?*, 34 J. INDUS. ECON. 113, 113–32 (1985).

375. Empirical studies finding a complementary relationship between advertising and contributions are discussed in ROBERT S. BURT, *CORPORATE PROFITS AND COOPTATION* 197–221 (1983) (presenting evidence that firms with greater consumer dependencies engage in higher levels of charitable contributions as support for the notion that contributions are part of corporate efforts to coopt consumers); CLOTFELTER, *supra* note 22, at 188–89 (assessing the existing empirical evidence and concluding that "there is good reason to believe that at least some portion of a corporation's contributions have a profit-related motive attached to it, much of it serving to improve the company's public image"); Galaskiewicz, *supra* note 182, at 247–48; Navarro, *supra* note 363, at 89 (collecting empirical evidence "lending support to the conclusion here that contributions are a form of advertising"—but noting the existence of contradictory evidence). For a more circumspect view of the correlation between contributions and advertising expenditures, see Haley, *supra* note 36, at 488 ("Contradictory findings exist about relationships between contributions and advertising budgets.").

376. For a discussion of the marketing objectives that may be realized through CRM promotions, see, for example, Varadarajan & Menon, *supra* note 368, at 60–64.

structured, contributions-based marketing programs achieved prominence during the 1980s,³⁷⁷ yet on an informal basis, corporations have for decades attempted to attract consumers by publicizing certain of their charitable contributions.³⁷⁸

1. Cause-Related Marketing

The distinguishing feature of a CRM program is that the firm's commitment to transfer a percentage of the revenues earned from the promotion to the specified charitable organizations is used as the basis of an appeal to consumers.³⁷⁹ The popularity of CRM from the corporate perspective has been based on its consumer appeal³⁸⁰ and on the ability of corporations to adapt CRM promotions to their precise commercial needs.³⁸¹ The principal variables in CRM promotions include the selection of the charitable beneficiaries, the duration of the promotion, the particular consumer group targeted, and the breadth of the campaign (i.e., local, national, or international).³⁸² In addition, CRM promotions have often garnered attention from the news media, so the participating corporations (and charities) have frequently received favorable publicity independent of their own advertising.³⁸³

While CRM promotions have generally proved beneficial for the participating charitable organizations,³⁸⁴ they are fundamentally regarded both by the business community and by nonprofit leaders as part of corporate marketing efforts.³⁸⁵ The essential marketing thrust of CRM promo-

377. A comprehensive survey of the development of CRM and CSE promotions appears in Knauer, *supra* note 77, at 60-71.

378. Perhaps the most famous example is Texaco's "Live at the Met" broadcasts, which commenced in 1940. Mescon & Tilson, *supra* note 363, at 55.

379. See Varadarajan & Menon, *supra* note 368, at 60.

380. See, e.g., STECKEL & SIMONS, *supra* note 183, at 75-87.

381. *Id.*; see also Varadarajan & Menon, *supra* note 368, at 63-67.

382. Varadarajan & Menon, *supra* note 368, at 63-67.

383. See STECKEL & SIMONS, *supra* note 183, at 76-78 (describing media interest in American Express' CRM promotions). CRM promotions receive a great deal of publicity: A Lexis-Nexis search in the Current News file retrieved approximately 500 stories discussing corporate CRM promotions for the years 1993-1995. These press accounts rarely included any precise details about the terms of the promotions, however.

384. STECKEL & SIMONS, *supra* note 183, at 78 (describing large charities, such as Big Brothers Big Sisters, the Special Olympics, the American Cancer Society, and the American Heart Association as having raised millions of dollars from corporations' CRM campaigns).

385. See Knauer, *supra* note 77, at 53-60.

tions is illustrated, for instance, by the fact that contributions arising from CRM promotions are typically funded from advertising and marketing budgets, as opposed to corporate philanthropy budgets.³⁸⁶ Also significant is the fact that corporate advertising and administration costs in CRM promotions, which frequently amount to millions of dollars, typically exceed the amount contributed to charities by a substantial sum.³⁸⁷

As stated above, CRM promotions are a relatively recent innovation in contributions-based marketing. American Express launched the first national CRM promotion in 1983.³⁸⁸ The company committed itself to contributing one cent for each use of its charge card and one dollar for each new card to the Statue of Liberty/Ellis Island Foundation's restoration project throughout the duration of the campaign.³⁸⁹ According to company officials, as a result thereof, card use increased by more than 20% and applications increased by 45% during the promotion.³⁹⁰ From a total corporate marketing expenditure of \$6 million, the restoration project received contributions from the company totalling \$1.7 million.³⁹¹ In light of American Express' successes, many other companies have sought to implement CRM programs.³⁹² Especially in industries where product differentiation is difficult and rate competition severe (as in the case of credit card

386. Varadarajan & Menon, *supra* note 368, at 59.

387. *Id.*

388. The most comprehensive discussion of American Express' 1983 CRM campaign in support of the Statue of Liberty/Ellis Island restoration appears in Mescon & Tilson, *supra* note 363, at 57 (citing Wendy L. Wall, *Companies Change the Ways They Make Charitable Donations*, WALL ST. J., June 21, 1984, at 1). Similarly detailed descriptions of other early CRM promotions appear in Maher, *supra* note 363.

389. Varadarajan & Menon, *supra* note 368, at 59.

390. *Id.*

391. *Id.*

392. For instance, more recently, Salant Corporation is reported to have ignited a trend in men's neckwear by incorporating designs and logos associated with the Save the Children organization on its neckties. Under the terms of Salant's CRM promotions (which subsequently expanded to include additional charitable organizations), five percent of the revenues produced from the necktie sales were pledged to the charities. Other men's apparel firms have sought to duplicate Salant's successes. Randa Corp. entered into a licensing agreement with C.A.R.E. in 1993 under which a portion of the neckties' sales proceeds were pledged to C.A.R.E. through a CRM promotion. And Wemco, Inc. has marketed a line of "Endangered Species" ties under CRM promotions benefiting a variety of environmental conservation organizations. Elena Hart, *Tie Makers Still Sticking Their Necks out for Good Causes*, DAILY NEWS REC., June 13, 1994, at 16, available in LEXIS, News Library, ARCNWS File.

companies,³⁹³ long distance telephone carriers,³⁹⁴ and airlines³⁹⁵) businesses have increasingly relied on CRM promotions to attract and retain consumers.

2. Corporate Special-Event Sponsorships

Like CRM programs, CSE sponsorships represent strategic partnerships from which both the corporation and the nonprofit organization anticipate financial benefits. Corporate executives have described CSE sponsorships as even more efficient than traditional advertising in terms of the cost of publicity in comparison to the resultant media exposure.³⁹⁶ The typical arrangement in a CSE sponsorship is that the charity's special event will prominently display the corporation's name, logo, or products in exchange for the receipt of a substantial sponsorship payment.³⁹⁷ Because the IRS has defined "acknowledgments" very broadly, the charity can generally avoid having unrelated business income tax on the sponsorship payments.³⁹⁸ Thus, CSE sponsorships are essentially exchange transactions

393. See, e.g., STECKEL & SIMONS, *supra* note 183, at 80-81 (describing 1987 CRM campaign by MasterCard that allowed consumers to select among a variety of charitable recipients); see also Valerie Block, *Blockbuster and NationsBank Cobranding a Visa Card*, AM. BANKER, Mar. 22, 1995, at 1 (describing cobranded Visa card under which two companies cosponsored a CRM campaign to benefit the "End Hunger Network"); Robert Jennings, *First USA Goes Angling for Outdoor Types with Cause-Tied Orvis Conservation Card*, AM. BANKER, July 19, 1995, at 10; Robert Jennings, *Fleet Joins Charity Marketing Race with a Card Tied to Special Olympics*, AM. BANKER, July 3, 1995, at 12.

394. See, e.g., Shelby Gilie, *Long-Distance Is Reaching Out to Left and Right*, SEATTLE TIMES, Aug. 9, 1995, at E1, available in LEXIS, News Library, CURNWS File; MCI Sponsors Kenny Loggins Tour, PR Newswire, July 5, 1994, available in LEXIS, News Library, ARCNWS File (describing "MCI Friends and Family Tour" benefitting the National Park Foundation).

395. See STECKEL & SIMONS, *supra* note 183, at 84 (describing CRM campaign by Continental Airlines to benefit Colorado's homeless); *Airline Partners with Others to Expand Its Giving*, 51 PR News, May 1, 1995, available in LEXIS, Market Library, IACNWS File (describing CRM promotion sponsored by Northwest Airlines); Mescon & Tilson, *supra* note 363, at 57 (discussing American Airlines' CRM campaign to benefit Dallas Symphony).

396. Companies "piggyback" on the news coverage associated with the event. Mescon & Tilson, *supra* note 363, at 54 (SCM executives estimated that \$200,000 museum sponsorship payment produced publicity that would have cost \$51 million per year for five years in advertising payments to reach equivalent customers).

397. As Knauer has observed, CSE sponsorships invert the commercial relationship present in the CRM context. In CRM promotions, the corporation pays the equivalent of a licensing fee (the "contributions") in order to tie the charity to the company's marketing campaign. In special event sponsorships, in contrast, the company lends its name to the charity's event. Knauer, *supra* note 77, at 67.

398. In 1991 the IRS issued a technical advice memorandum addressing college bowl sponsorship payments in which the payments were classified as unrelated business income to the donee nonprofit organizations. See Tech. Adv. Mem. 91-47-007 (Aug. 16, 1991). After an extensive lobbying campaign by nonprofit organizations, the IRS issued proposed regulations in

in which the corporation receives substantial media exposure and favorable acknowledgements (if not "advertising") in exchange for the contributions it makes to the nonprofit organization hosting the event.³⁹⁹ Highly flexible arrangements, CSE promotions can be coordinated with CRM programs as well as traditional advertising campaigns in order to produce the maximum favorable publicity for the corporation.⁴⁰⁰ The most common event sponsorships, for obvious reasons, have been arts performances and amateur athletic events—the regular⁴⁰¹ and Special Olympics⁴⁰² and college bowl football games⁴⁰³ being the most salient examples of the latter.

Because CRM campaigns and CSE sponsorships represent contexts in which corporate contributions have been closely assimilated to traditional corporate marketing efforts, the profit-maximizing claims made in regard thereto are highly credible. Accordingly, in light of their commercial nature, such contributions should not be deductible under § 170 as charitable contributions. Transfers to charitable organizations arising from CRM campaigns appear to be the most ill-suited for treatment under § 170, because the existence of the contribution is directly tied to the occurrence of a revenue producing transaction for the firm. There is little precedent addressing the tax treatment of CRM campaigns,⁴⁰⁴ but the IRS has continued to support the charitable framework supporting CSE sponsorships, perhaps as a result of extensive lobbying by charitable organizations.⁴⁰⁵ Nevertheless, companies continue to derive a valuable package of services

1993. These regulations adopted a significantly more liberal approach to CSE sponsorships. Most importantly, they focused on the nature of the services performed by the donee organization (as opposed to the corporate donor's motivation or resulting publicity), and provided that nontaxable "acknowledgments" would be defined broadly. Prop. Treas. Reg. § 1.512(a)-(e), 58 Fed. Reg. 5687, 5689 (1994); Prop. Treas. Reg. § 1.513-4, 58 Fed. Reg. 5690 (1993).

399. See Prop. Treasury Reg. § 1.512(a)-(e); Prop. Treas. Reg. § 1.513-4. For a transactional approach to CSE sponsorships, see Francis R. Hill, *Corporate Sponsorships in Transactional Perspective: General Principles and Special Cases in the Law of Tax Exempt Organizations* (unpublished manuscript, on file with author).

400. See, e.g., STECKEL & SIMONS, *supra* note 183, at 82 (describing linkages between CRM campaigns and CSE sponsorships).

401. Marlis L. Carson, *Corporate Sponsorship and the Olympics*, 68 TAX NOTES 651, 651-52 (1995).

402. See Kate Fitzgerald, *Special Olympics Wins over Sponsors*, ADVERTISING AGE, Apr. 10, 1995, at 2; Kirk Johnson, *The Selling of the Special Olympics*, N.Y. TIMES, June 23, 1995, at B1, B4 (describing sponsorship payments, largely from big corporations, as reaching \$28 million in 1995).

403. See Nathan Wirtschafter, *Fourth Quarter Choke: How the IRS Blew the Corporate Sponsorship Game*, 27 LOY. L.A. L. REV. 1465 (1994).

404. *But see* Sierra Club Inc. v. Commissioner, 86 F.3d 1526 (9th Cir. 1996).

405. The 1993 proposed regulations are the latest official word from the IRS on CSE sponsorships. See *supra* note 398.

from CRM promotions and CSE sponsorships (and tax experts continue to question the charitable nature of the arrangement).⁴⁰⁶ In sum, there is considerable consensus that CRM campaigns and CSE sponsorships are profit maximizing for the donor corporation, but for this very reason the *charitable* nature of the payments arising therefrom is suspect.

3. Advertising the Firm's Philanthropic Image to Influence Consumers

Since the late 1970s, corporations have increasingly sought to advertise their contributions in order to improve the public's perception of the firm in general.⁴⁰⁷ The most popular form of contributions-based, *firm-level* advertising is the marketing of the "socially responsible" corporation.⁴⁰⁸ Corporations have frequently publicized their efforts to support environmental conservation,⁴⁰⁹ education,⁴¹⁰ and women's and minori-

406. Thus the law in this area is far from settled. See Hill, *supra* note 399; Knauer, *supra* note 77.

407. For discussions of consumer interest in socially responsible products and firms, see Varadarajan & Menon, *supra* note 368, at 71-72. For a discussion of increasing corporate interest in strategic philanthropy, see, for example, Smith, *supra* note 47, at 105-16; Edward J. Stendardi, *Corporate Philanthropy: The Redefinition of Enlightened Self-Interest*, 29 SOC. SCI. J. 21, 21-30 (1992). Recent developments of strategic partnerships of many varieties are described in ROSABETH MOSS KANTER, *WORLD CLASS: THRIVING LOCALLY IN THE GLOBAL ECONOMY* (1995).

408. Of course, the socially responsible corporation is not the only persona marketed by business. Corporations have frequently advertised their affiliations with prestigious or avant garde performing arts organizations as a way of communicating a message to the public about the firm's sophistication, financial success, or savvy. See Smith, *supra* note 47, at 109 (describing the AT&T Foundation's decision to support avant garde arts performances in order to communicate a message to the public about the state of the art nature of the company's goods and services).

409. See, e.g., WILLIAM T. POOLE, *HERITAGE FOUND., THE ENVIRONMENTAL COMPLEX: PART III* (Institution Analysis No. 4, June 1982) (documenting proenvironmental work on the part of nonprofit organizations created with the help of corporate funds); *Environmental Groups' Corporate Marketing Policies*, GREEN MARKETALERT, March 1994, at 4 (describing nonprofit conservation groups' policies and efforts to establish strategic partnerships with corporations); Jeffery D. Zbar, *Firms Go Green with Conservancy*, ADVERTISING AGE, Jan. 11, 1993, at 16 (describing corporate donations to The Nature Conservancy); *Corporate Environmental Philanthropy*, GREEN MARKETALERT, October 1993, at 4 (describing substantial corporate contributions to major environmental groups); James T. Harris, *Working with Environmental Groups*, PUB. REL. J., May 1992, at 24 (same); Keith Schneider, *Natural Foes Bankroll Environmental Groups*, N.Y. TIMES, Dec. 23, 1991, at A12 (same).

410. Educational groups, defined very broadly, receive the greatest percentage (33.5%) of corporate charitable contributions. See *GIVING USA 1996*, *supra* note 23, at 91. In fact, Exxon has a separate "Educational Foundation." See Smith, *supra* note 47, at 107-08. Also notable was President Bush's plans for the "New American Schools Development Corporation"—envisioned as a private think tank largely funded by business donations that would produce research and recommendations for revitalizing American education. See *supra* note 210.

ties' rights,⁴¹¹ as well as other programs, through corporate charitable contributions. Surveys attest to considerable consumer support for socially responsible products and firms, as do the resounding successes of consumer consciousness publications such as *Shopping for a Better World*⁴¹² and the establishment of socially conscious mutual funds.⁴¹³

The practice of touting the firm's contributions, along with any other socially-conscious expenditures, has become common in the consumer products area. For example, Ben & Jerry's Ice Cream and The Body Shop have aggressively sought to appeal to consumers on the basis of their support for the environment and other progressive causes. From a different perspective, petroleum, chemical, and automotive manufacturers have used charitable contributions to pro-environmental causes, in combination with extensive advocacy advertising,⁴¹⁴ to counter their negative images as polluters.⁴¹⁵ Thus, while corporate social responsibility represents a distinct explanation for corporate philanthropy, as discussed previously, contributions-based social-responsibility expenditures have also been used as part of corporate marketing efforts. Ironically, notwithstanding that firms have made substantial investments in these areas, the evidence regarding the ability of such expenditures to enhance revenues or reduce costs is conflicting and inconclusive.⁴¹⁶

B. Other Profit-Maximizing Strategies Involving Contributions

1. Donating Products to Increase the Consumer Base

Contributions might also contribute to revenue enhancement by securing or enlarging the firm's consumer base.⁴¹⁷ Particularly prevalent has been the practice of computer and other technology firms contributing equipment and other products to schools. For example, IBM, Apple, and

411. See NOLAN, *supra* note 186.

412. See, e.g., SHOPPING FOR A BETTER WORLD (1994).

413. See *infra* note 427.

414. See S. PRAKASH SETHI, ADVOCACY ADVERTISING AND LARGE CORPORATIONS (1977); see also Anne Louise Page, *We're Good Guys: Image Propaganda from Mobil Oil*, BUS. & SOC. REV., Spring 1995, at 33. For a discussion of advocacy advertising in conjunction with charitable contributions, see Haley, *supra* note 36, at 501.

415. For citations, see *supra* note 409. See also NEIHEISEL, *supra* note 32, at 60-61.

416. See Smith, *supra* note 364; *supra* note 32.

417. Galaskiewicz, *supra* note 182, at 247-48.

Hewlett Packard have annually made contributions of computer equipment to schools valued in the tens of millions of dollars.⁴¹⁸

2. Charitable Contributions and Research and Development

Corporations have used charitable contributions to university science programs to "out-source" some of their research and development ("R&D").⁴¹⁹ Contributions to R&D conducted at universities may either substitute for research that would be too costly to fund internally or complement intrafirm R&D.⁴²⁰ Contributions supporting university R&D may provide the donor-firms with access to research programs and faculty members' technical expertise. Corporations active in agriculture, pharmaceuticals, defense technology, and telecommunications (including computer technology) have been particularly apt to use contributions to university science departments in conjunction with intrafirm research and development.⁴²¹ In order for these contributions to be revenue enhancing for the donors, they must sow the seeds of the firms' future technological innovations.⁴²²

3. Donations That Benefit Employees

Employee-matching grant programs confer obvious benefits on employees. The matching grant affords the employee the psychic gratification of augmenting the gift that he or she is responsible for making without increasing the employee's personal expenditure. In addition, the employee can exercise his or her discretion to direct the gift to local charitable orga-

418. Section 170(e)(4) of the U.S. Code (enacted in 1981) created a special tax incentive for businesses to contribute property and equipment to educational institutions for research purposes. I.R.C. § 170(e) (1994). For discussion of corporate donations of computer equipment, see, for example, Useem, *supra* note 158, at 341, which describes tens of millions of dollars worth of computer equipment donated by computer companies in the 1980s. See also Maher, *supra* note 363, at 86 (describing IBM's practice of combining gifts of computer equipment with multimillion-dollar educational grants in the area of information technology).

419. One commentator has described the program run out of the Massachusetts Institute of Technology, in which "hundreds of corporations contribute tens of thousands of dollars annually," as the "granddaddy" of all such corporate contributions-based research programs. STECKEL & SIMONS, *supra* note 183, at 24.

420. See, e.g., Haley, *supra* note 36, at 488 ("[C]ontributions may substitute for corporate R&D by funding basic innovation at research institutions. More often, contributions may complement corporate R&D by funding extensions of corporate projects.").

421. *Id.*; see also Smith, *supra* note 47.

422. Haley, *supra* note 36, at 488.

nizations, such as hospitals, arts organizations, or community services organizations, from whose services the employee may benefit. For this reason, such matching programs are generally regarded as corporate efforts to improve employee morale and loyalty to the firm.

Of course, corporations may directly contribute to charitable organizations that benefit employees apart from employee-matching grant programs. Corporations have contributed to community day care and geriatric care, as well as to community hospital and health organizations, domestic violence programs, and specific local public/private partnerships.⁴²³ Corporate charitable contributions that improve community and educational services and other quality of life variables may affect employees' morale and productivity, as well as retention rates, and thus increase revenues or reduce costs.⁴²⁴ The value resulting to firms from such expenditures is, however, difficult or impossible to measure.

4. Reinforcing the Economic Infrastructure

Another, but even more attenuated commercial justification for corporate charitable contributions has been that such donations help sustain the educational and communal infrastructure necessary to support markets and profitable businesses.⁴²⁵ This rationale has most commonly been applied in the context of contributions to national charities or colleges and universities having national standing—situations where the gifts benefit populations in which the company's employees do not predominate. Because of the numerous variables involved, unlimited time horizons, and obvious free-rider problems, it is impossible to document the existence of any firm-specific benefits resulting from gifts of this nature.⁴²⁶

423. Smith, *supra* note 47, at 111.

424. See, e.g., NEIHEISEL, *supra* note 32, at 34–35; Haley, *supra* note 36, at 498; Navarro, *supra* note 363, at 68.

425. The connection between charitable contributions, the economic and social infrastructure, and corporate profitability is described, for example, in *A.P. Smith Manufacturing Co. v. Barlow*, 98 A.2d 581 (N.J. 1953), and *Theodora Holding Corp. v. Henderson*, 257 A.2d 398 (Del. 1969). Nevertheless, the high degree of speculation required to support the connection is noted by Haley and others. Haley, *supra* note 36, at 489 (“No systematic evidence exists; yet, anecdotal data suggest that contributions which rebuild infrastructure may reduce corporate costs.”).

426. See Galaskiewicz, *supra* note 182, at 250 (“Skeptics in the management literature correctly point out that it is impossible to measure the impact of responsible behavior on future sales and public opinion and that espousing the ethic of enlightened self interest is not rational from an economic point of view.”).

5. Attracting Investor Capital Through Social Responsibility

Investors have become increasingly interested in monitoring corporations' social responsibility efforts, including their charitable contributions practices. The second half of this century has witnessed successive waves of investor social activism, especially in the areas of environmentalism, affirmative action, human rights, and product safety. Such interest has recently been institutionalized in the establishment of socially conscious mutual funds.⁴²⁷ It is possible that these funds may facilitate capital formation for companies having an established record of charitable support, and thus reduce the costs of capital for such firms. However, the relative novelty of social-choice funds, as well as the relatively little amount of capital under their management, suggest that it is unlikely such entities will play a major role in affecting the cost of capital.

C. Disclosure and the Question of Profit-Maximizing Contributions

As the above discussion indicates, obvious financial benefits accrue to firms as a result of CRM and CSE promotions. However, because of the quid pro quo nature of such arrangements, the contributions arising therefrom should not be considered part of corporate philanthropy. In contrast, any financial benefits that accrue to firms from the other charitable contributions described in this section are far more elusive. The charitable status of such contributions is more secure precisely because their profit maximizing effects are less certain.

Apart from CRM and CSE promotions, the ambiguous nature of the financial benefits claimed to arise from corporate charitable contributions complicates the project of defining the appropriate regulatory approach thereto. The absence of definitive empirical support for the value-enhancing function of such expenditures does not mean they should necessarily be considered a form of corporate waste. Alternatively, in light of the inconclusive empirical evidence and the vested interests that corporate managers, marketing executives, and fundraisers have in describing contributions in terms of corporate profit maximization, it is equally inappropriate to regard charitable contributions (outside of CRM and CSE promotions) as

427. For a discussion of the rapidly evolving field of socially conscious investing, see, for example, PETER D. KINDER ET AL., *INVESTING FOR GOOD* (1993); Maria O'Brien Hylton, "Socially Responsible" Investing: Doing Good Versus Doing Well in an Inefficient Market, 42 AM. U. L. REV. 1 (1992), and W. Scott Klinger, *Social Investing in a Changing World*, BEST'S REV.-LIFE/HEALTH INSUR. ED., Feb. 1994, at 68.

being closely analogous to other traditional, value-maximizing forms of corporate conduct. Courts have too readily deferred to the statements of corporate managers in this area, or glossed over the problem by asserting the existence of goodwill benefits. As a matter of legal policy, a middle ground must be established between absolutely prohibiting corporate charitable contributions and absolutely allowing them without any meaningful system of accountability.

Of course, the argument for disclosure to shareholders is weakest, and the argument in favor of deference to managers' business judgment is strongest, where contributions give rise to increased value or reduced cost. (Indeed, shareholders do not bear the cost of profit-maximizing contributions because they involve no net reduction in profits.) But absent disclosure, it is impossible to assess whether the firm's philanthropic capital has been employed in the firm's commercial interest. Unlike the traditional costs of production, corporate contributions are acutely susceptible to being administered without regard to the firm's commercial interests and in furtherance of the personal interests of corporate elites. As Louis Lowenstein has recently written, "You manage what you measure."⁴²⁸ By failing to require that corporate charitable expenditures be reflected either in the narrative portion of corporate reports or in the financial statements accompanying them, the SEC has contributed to mismanagement and unprofessionalism in the administration of corporate charitable contributions.

CONCLUSION

This Article has analyzed corporate charitable contributions from the perspective of corporate legal norms and the interests of shareholders. The absence of any system of accountability in this area—that is, the absence of substantive regulation under state corporation law, in combination with the absence of a disclosure requirement under the federal securities (or other) regulations—has created the potential for abuse with respect to both shareholders' property interests and in regard to their interests in avoiding compelled subsidization of entity-level political expression. Furthermore, firms have prevented shareholders from having a meaningful voice in the formulation of corporate philanthropy policies by keeping charitable-contributions information confidential. To the extent that corporate charitable contributions represent an expression of corporate social responsibility, this assertion of managerial prerogative is unjustified, as managers

⁴²⁸ See Lowenstein, *supra* note 179.

have no special expertise in matters of this nature. In regard to politicized philanthropy, furthermore, fundamental democratic principles also mandate in favor of required corporate contributions disclosure.

In light of the rapid development of the charitable sector and the sophistication of corporate affairs generally, a precisely defined system of substantive regulation would be difficult and costly to design and to administer. In the alternative, a system of accountability based on required disclosure of corporate charitable contributions would represent a more fruitful and practicable accommodation between shareholders' interests in accountability and managers' interests in flexibility in the administration of corporate affairs. Congress has afforded the SEC the authority to promulgate rules in the public interest and for the protection of investors, and the SEC has responded by implementing an extensive system of required corporate disclosure. Disclosure of corporate charitable contributions information should now be made part of this regime.