

Teaching Corporation Law in a Transnational Era

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Economists often believe that efficient institutions will diffuse quickly and that inefficient institutions will not survive for extended periods of time. Many lawyers hold the view that the era of globalization will also be the era of harmonization and convergence among legal systems. These scholars are perplexed by the fact that the business corporation, a core legal-economic institution, is financed, owned and regulated differently in different economies.

In some countries, corporations are financed by way of equity that is widely dispersed among many small shareholders, and power lays in the hands of management. In some, it is concentrated in the hands of a few large controlling shareholders together with relatively powerless minority shareholders. Concentrated ownership structure often places debt next to equity as a major source of long-term finance in some places, but this is not always the case. In a few advanced countries, and many other countries, the controlling shareholders, often family members, never go public and outsiders have no equity stake. In some of these economies, the major producers are large closely-held corporations, while in others they are the small corporations, partnerships and family firms. In yet others, the state plays important role in financing and controlling for-profit corporations.

The direction of causality has been fiercely debated. Scholars often argue that it runs from governance and finance to law, which is to say that different economies develop different corporation laws. Recent studies hold that different legal systems shape different types of business organizations and lead to diverging performance in terms of economic growth. What cannot be disputed is the fact that differences do persist. Further,

differences persist between advanced economies, such as the US and Japan, Britain and France, Germany and Italy. Transition economies as well do not seem to follow a single model.

With these observations in mind, my aim is to discuss the transnational challenges involved in teaching corporation law. My first-hand experience with these challenges began when I first developed a corporation law course in Israel. I immediately realized that the American literature with which I was familiar from my studies in the US was not entirely relevant for my purposes. It was primarily concerned, on the levels of both theory and doctrine, with the agency problem in the relationship between weak shareholders and strong managers. Not more than a handful of Israeli corporations, and mostly minor ones, faced this agency problem. The large majority of Israeli public corporations have concentrated ownership. They are controlled by a large shareholder (or block of connected shareholders) who often hold more than 50% of the shares. This also created the view that the issue of mergers and acquisitions is irrelevant for Israeli students despite the important role it plays in the US, both in corporate practice and corporate theory.. The conflicts of interests between minority shareholders and majority shareholders and between shareholders and creditors seemed to be considerably more relevant for Israeli students. When I returned to the US to teach a basic corporations course a few years later, I had to go through the reverse process. I also had to consider the fact that while Israel is a unitary state, in the American system corporation law is within the powers of the individual states whereas securities regulation law is dominated by the federal level. The competition among states in corporation law became one of the central themes of the course.

I could present this same exercise with Britain, as well. One of my main research topics is the history of English corporations. Until the year 2000, Israel's Companies Act was based on the English Companies Act of 1929 transplanted to Mandatory Palestine in that same year, and then considered cutting edge legislation in the field. The persistent phenomenon of widely-dispersed shareholding in Britain is totally different from the ownership structure in Israel of 2004 or in Mandatory Palestine of 1929. The history of English corporation law, while relevant for our understanding the origins of the Act, turned almost irrelevant for understanding contemporary corporation difficulties in Israel.

Should legal educators in Israel develop their own endogenous curriculum? Should they teach only Israel case law? Should they include English cases on their reading lists because of the historical origins of Israeli law in the Imperial metropolis? Are these ought to be limited only to pre-1929 English cases? Should they ignore the American law & economics literature on corporations because it concerns a totally different corporate governance environment? Should German, French or Italian law be used because of the similarities in governance and finance? But how can the Israeli legal system - primarily a common law system - be reconciled with Continental jurisprudence in which European corporation law is embedded?

My conviction is that Israeli legal educators are not alone in struggling with such questions. Dilemmas of this kind concerned legal educators in various post-colonial and transplanted systems. They occupy educators in small legal systems that rely on larger systems as a source of inspiration. However, several features make the field of corporation law somewhat unique. First, the persistence of differences between forms of governance and finance. Second, the divergence within families of legal systems and

among developed economies. Third, the fact that legal and economic factors interplay, at times to the extent that they are inseparable, due to the manifested business and profit orientation of this legal field. A fourth factor is the effect of globalization on this field in the form of multinational corporations. These often have shareholders across the globe, their shares are at times traded in several stock markets, and they often have subsidiaries that are incorporated in various states. Transnational mergers and acquisitions intensify the trend. Fifth, competition among jurisdictions evolved in a unique manner in this field of law because in many systems the choice of law is determined by place of incorporation. In the US, competition among States has been ongoing for more than a century and Delaware is the current leader. Elsewhere, this is a much newer phenomenon. Competition within the EU is gathering momentum due to recent ECJ decisions and global competition is evolving. Israeli high-tech startups, for example, in some circumstances prefer incorporation in Delaware over incorporation in Israel. An interesting aspect of the current phase of competition over incorporation is that it involves not only large public corporations but also smaller closely held corporations.

Lawyers in a transnational era will not be able to serve their clients well without familiarity with incorporation options beyond their own jurisdiction and with the laws that govern the business organizations in which their clients or their counterparts are involved. However, it seems that cooperation with legal firms from other countries or within multinational firms will not be a full solution as productive cooperation depends on basic common grounds. My view is that these are lacking in the legal education that most lawyers receive. When the system in which a lawyer is educated does not experience a severe conflict of interest between shareholders and managers, its

corporations law course will not illuminate the tension and its lawyers will not have a good grasp of it. When a system does not have many public corporations with minority shareholders, the case law that governs this relationship will not be developed and accordingly its curriculum will marginalize the topic. A system whose high profile corporate practice involves publicly-traded corporations will highlight the law that governs them; in an economy that is based on state-owned business enterprises or on family firms, this law will not be studied.

A transnational lawyer will need to learn something about all these aspects of the corporation. Without an understanding of the three basic conflicts (management-shareholders, majority-minority, creditors-shareholders), of the interplay between them and governance and finance, of the different problems faced by public and private corporations, and of the organizational choices among entities other than corporations (general partnerships, limited partnerships, LLPs, LLCs), transnational lawyers will have only a limited understanding of reality. Without such understanding, lawyers will not be able to communicate with their colleagues from other legal systems. Such understanding involves a knowledge of basic concepts and theories that should be studied in law schools rather than on-the-job or in practical training. Shaping the curriculum for corporation courses that do this is not a trivial matter. Disagreements with respect to the needs of transnational lawyers, tensions between conflicting interests and viewpoints in the bar, academia and the political sphere, and limits in teaching resources will play their part. Different legal systems and different law schools are likely to shape different programs. Most law schools around the globe will have to reckon with this new challenge to the old and isolated ways of teaching corporation law.