Notes

REGULATING CORPORATIONS THE AMERICAN WAY: WHY EXHAUSTIVE RULES AND JUST DESERTS ARE THE MAINSTAY OF U.S. CORPORATE GOVERNANCE

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ABSTRACT

At the dawn of the twenty-first century, a flurry of media reports revealed that pervasive corporate and accounting scandals were infecting U.S. financial markets. As investors panicked and stock prices plummeted, a determined Congress scrambled to restore order by ushering in the Sarbanes-Oxley Act, the most exacting regulatory imposition on corporate America since the Great Depression. Burdened with the Act's enormous administrative and transactional costs, many corporations pulled their shares from U.S. markets and relocated them to exchanges in nations with less onerous governance strictures. This exodus has deeply concerned many U.S. political, financial, and legal commentators, who argue that the American corporate governance regime must be revamped to resemble the less burdensome and principles-based soft law structure that operates in countries like the United Kingdom. This Note assesses the viability of such an overhaul. It ultimately concludes that given the longstanding and singularly American predilection for rules-based regulation and litigation, any large-scale transplant of soft law principles into U.S. corporate governance is a practical impossibility.

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INTRODUCTION

By the end of August 2002, it was clear something was rotten in the state of corporate America.[1] In less than ten months' time Enron had collapsed,[2] WorldCom had imploded,[3] and federal investigators had uncovered large-scale corporate and accounting imbroglios at nineteen other major exchange-traded companies.[4] As reports of unprecedented malfeasance and fraud poured from media outlets at an extraordinary rate,[5] alarmed investors abandoned public securities markets in droves.[6]

An alarmed Congress was likewise quick to react, hastening to draft the Public Company Accounting Reform and Investor Protection Act of 2002, commonly called the Sarbanes-Oxley Act after its principal legislative sponsors.[7] With eleven titles and nearly 150 pages of text, Sarbanes-Oxley is replete with regulatory prescriptions that compel public companies to beef up their internal controls and overhaul their governance structures.[8] It also directs the Securities and Exchange Commission (SEC) to draft a vast body of

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1. *See* WILLIAM SHAKESPEARE, HAMLET, PRINCE OF DENMARK act 1, sc. 4, l. 90 (Joseph Quincy Adams ed., Riverside Press 1929).

2. Richard A. Oppel Jr. & Andrew Ross Sorkin, *Enron Collapses as Suitor Cancels Plans for Merger*, N.Y. TIMES, Nov. 29, 2001, at A1.

3. *See* Simon Romero & Riva D. Atlas, *WorldCom Files for Bankruptcy*, N.Y. TIMES, July 22, 2002, at A1 (reporting that WorldCom, after once listing more than $107 billion in assets, submitted the largest bankruptcy filing in United States history).

4. Penelope Patsuris, *The Corporate Scandal Sheet*, FORBES, Aug. 26, 2002, http://www.forbes.com/2002/07/25/accountingtracker.html.

5. *See, e.g.*, Will Hutton, *Bye Bye American Pie*, THE OBSERVER (London), June 30, 2002, at 25 (commenting that the United States was struck with "an orgy of unprecedented corporate fraud, plunder and malfeasance that has demanded the connivance of its most reputable accounting firms, business leaders and banks"); Gary Strauss, *How Did Business Get So Darn Dirty?*, USA TODAY, June 12, 2002, at 1B (observing that although "[g]reed and corruption have always lingered at the edges of Corporate America, ... the new millennium . . . ushered in a wave of fraud, corporate malfeasance, investment scams, ethical lapses and conflicts of interest unprecedented in scope").

6. Editorial, *Stock Market Blues*, MIAMI HERALD, July 21, 2002, at 6L ("Spooked by recent corporate scandals, investors have sent U.S. stocks tumbling into one of the worst market dives in three decades.").

7. John Paul Lucci, *Enron—The Bankruptcy Heard Around the World and the International Ricochet of Sarbanes-Oxley*, 67 ALB. L. REV. 211, 215 (2003) ("[Sarbanes-Oxley] became law a mere seven months after Enron filed for bankruptcy."); *see* Sarbanes-Oxley Act of 2002, Pub. L. No. 107-204, 116 Stat. 745 (codified as amended in scattered sections of 11, 15, 18, 28, and 29 U.S.C.).

8. Sarbanes-Oxley Act of 2002.

implementing rules[9] that fill more than three thousand pages.[10] Collectively, these requirements—and the nearly $2 million in operational costs and legal fees Sarbanes-Oxley annually imposes on many companies[11]—have led commentators to denounce it as the most heavy-handed regulatory imposition on public corporations in more than seventy years.[12]

An increasing number of corporations have therefore chosen to take their business outside the United States, where regulatory oversight is less stringent and compliance costs are less exorbitant.[13] Their exodus has exacted a heavy toll on the once preeminent U.S. capital markets, which have slipped behind Europe and Asia on key indicators of economic vitality.[14] Sarbanes-Oxley's many critics have

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9. *See* 15 U.S.C. § 7202(a) (Supp. V 2005) ("The [SEC] shall promulgate such rules and regulations, as may be necessary or appropriate . . . in furtherance of this Act.").

10. Silvia Ascarelli, *One Size Doesn't Fit All: In Europe, Corporate-Governance Rules Are Not in the Details*, WALL ST. J., Feb. 24, 2003, at R6 ("[W]hile the U.S. has turned to explicit rules—3,000 pages written by the SEC to flesh out the Sarbanes-Oxley Act, and still going—many other countries have let industry lay out new guidelines and left enforcement to peer pressure.").

11. Adrian Michaels, *Companies Balk at Cost of Compliance*, FIN. TIMES (London), Aug. 12, 2004, at 25; *see also What's Wrong with Wall Street*, ECONOMIST, Nov. 25, 2006, at 11, 11 ("[Sarbanes-Oxley] greatly increased the reporting burden on companies.").

12. *E.g.*, Symposium, *Lessons from Enron: A Symposium on Corporate Governance*, 54 MERCER L. REV. 731, 732 (2003) (inquiry of Michael Rosenzweig) (labeling Sarbanes-Oxley "the most sweeping federal regulation of public corporations since the federal securities laws were enacted some seventy years ago"); Justin O'Brien, *The Politics of Symbolism: Sarbanes-Oxley in Context*, *in* INTERNATIONAL CORPORATE GOVERNANCE AFTER SARBANES-OXLEY 9, 9 (Paul U. Ali & Greg N. Gregoriou eds., 2006) (observing that Sarbanes-Oxley has been both heralded and denigrated "as the most far-reaching change to the governance of corporations and the markets in which they operate since the 1930s").

13. *See* Silvia Ascarelli, *Citing Sarbanes, Foreign Companies Flee U.S. Exchanges*, WALL ST. J., Sept. 20, 2004, at C1 (discussing the increasing number of foreign corporations that are delisting from U.S. stock markets and deregistering with the SEC to escape mounting Sarbanes-Oxley compliance costs).

14. *See, e.g.*, *Down on the Street*, ECONOMIST, Nov. 25, 2006, at 69, 70 (reporting that the New York Stock Exchange's share of initial public offerings, as measured by proceeds, has been surpassed by both London and Hong Kong).

been quick to take notice[15] and have called for a significant trimming of its vast web of regulatory red tape.[16]

Even more importantly, a growing number of business executives, political leaders, and legal observers view Sarbanes-Oxley as part of a much larger problem, namely the entire rules-based system of U.S. corporate governance.[17] They advocate far-reaching legislative and administrative measures[18] that would strip the U.S. regulatory regime of its rules-based structure, which they perceive as hopelessly "complex," "murky," and "harder to understand and harder to follow" than more flexible regimes in other nations.[19] In its place, they propose adopting a more principles-based approach, similar to the regime operating in the United Kingdom under its

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15. *See, e.g.*, Roberta Romano, *The Sarbanes-Oxley Act and the Making of Quack Corporate Governance*, 114 YALE L.J. 1521, 1589 (2005) (criticizing Sarbanes-Oxley for creating regulations that burden corporations with debilitating transaction costs that drive them out of the United States); William A. Niskanen, *Enron's Last Victim: American Markets*, N.Y. TIMES, Jan. 3, 2007, at A21 ("[Sarbanes-Oxley] has proven counterproductive in the extreme. . . . [It] has seriously harmed American corporations and financial markets without increasing investor confidence . . . . [and has] created an expensive and arguably unconstitutional new regulatory agency to regulate the audit firms' activities."); *see also* Ascarelli, *supra* note 10 ("The U.S. emphasis on detailed rules has perplexed many European political and business leaders, who criticize Sarbanes-Oxley as poorly written legislation drafted in haste."); *Special Report: The Rules of the Game*, ECONOMIST, Sept. 15, 2007, at 16, 18 (noting that Sarbanes-Oxley is "often blamed for making America a less attractive place for doing business").

16. *See What's Wrong with Wall Street*, *supra* note 11, at 11 (observing that many critics have argued that "America is also responsible for its financial markets' decline by tangling them up in red tape. Nowhere is this clearer than the Sarbanes-Oxley act . . . .").

17. *See* COMM'N ON THE REGULATION OF U.S. CAPITAL MKTS. IN THE 21ST CENTURY, U.S. CHAMBER OF COMMERCE, REPORT AND RECOMMENDATIONS, EXECUTIVE SUMMARY 2 (2007), *available at* http://www.capitalmarketscommission.com/portal/capmarkets/default.htm (advocating "quick and decisive adjustments in the U.S. legal and regulatory framework"); Tom Bawden, *Bush Says Sarbanes Hurts US Markets*, TIMES (London), Feb. 1, 2007, at 53 (discussing President George W. Bush's belief that overregulation of American capital markets has damaged the U.S. economy); Jeremy Grant, *Bernanke Calls for US to Follow UK's "Principles-Based" Approach*, FIN. TIMES (London), May 16, 2007, at 1 (reporting Federal Reserve Chairman Ben Bernanke's concern that the rules-based system of regulation is no longer suitable for American markets).

18. *See* MANSOOR DAILAMI, WORLD BANK, GLOBAL DEVELOPMENT FINANCE VOLUME I: REVIEW, ANALYSIS, AND OUTLOOK 101 (2007) ("Recognizing the advantages of the European approach [to corporate governance], in 2006 the U.S. Committee on Capital Markets Regulation recommended a more principles-based approach to regulation to enhance shareholder rights while reducing overly burdensome regulations and litigation.").

19. Cary Coglianese et al., *The Role of Government in Corporate Governance*, N.Y.U. J.L. & BUS., Fall 2004, at 219, 229.

Combined Code on Corporate Governance (Combined Code).[20] In contrast to Sarbanes-Oxley, the Combined Code incorporates a set of guiding principles—rather than copious lists of exhaustive rules—that are designed to keep corporate abuses in check.[21]

By highlighting specific differences in U.S. and U.K. regulation of audit committee financial experts as a point of reference, this Note examines the feasibility of exchanging the rules-based regime of U.S. corporate governance for a principles-based replacement akin to the Combined Code. Due to several dominant historical and cultural threads woven deep into the fabric of a uniquely American legal ethos, this Note concludes that any significant shift toward a more principles-based regime would be short-lived.

Part I defines the scope of the problem, highlighting key differences between the U.S. and U.K. regulatory systems and describing the arguments of those who have called for dramatic change to the U.S. system. Part II focuses more specifically on the Combined Code and its theoretical and practical dissonance with the U.S. scheme for regulating corporate governance. Particular emphasis is given to essential differences in U.K. and U.S. enforcement and ideology, as well as the differences in each nation's regulation of audit committees and financial experts. Part III illustrates the significant roles U.S. history and culture have played in the cultivation of rules-based regulation, including the roles they continue to play in cementing its perpetuity. Finally, this Note concludes that these cultural and historical forces are ultimately both too firmly fixed and too transcendent to accommodate any large-scale adoption of principles-based regulation into U.S. law. Indeed, even if such an adoption were theoretically possible, a principles-based regime in the United States would have no viable chance of long-term survival.

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20. FINANCIAL REPORTING COUNCIL, THE COMBINED CODE ON CORPORATE GOVERNANCE (2006) [hereinafter COMBINED CODE], *available at* http://www.frc.org.uk/corporate/combinedcode.cfm (follow the "Combined Code June 2006" hyperlink).

21. *See* BOB GARRATT, THIN ON TOP: WHY CORPORATE GOVERNANCE MATTERS AND HOW TO MEASURE AND IMPROVE BOARD PERFORMANCE 21 (2003) (asserting that any "notion of there being a single, integrated Anglo/US governance model is untrue" because "US and UK corporate governance practices are significantly different—especially in their approach to compliance issues").

I. DEFINING THE PROBLEM

Comprehensive sets of prophylactic rules have long been the *sine qua non* of U.S. corporate regulation. For reasons rooted partly in U.S. social and economic history,[22] congressional efforts to curtail corporate fraud have customarily been marked by copious bright-line tests, elaborate compilations of rules, multiple exceptions for each rule, and a high level of regulatory detail[23] intended to provide a clear answer to every possible situation and to address all conceivable eventualities.[24]

For example, in the 1970s Congress countered the pervasive foreign bribery and corporate political contribution scandals by enacting the rules-saturated Foreign Corrupt Practices Act (FCPA).[25] To the dismay of many public company executives,[26] the FCPA mandated a costly overhaul of all corporate auditing programs, including the implementation of a more rigorous system of internal accounting controls.[27] Similarly, in response to the shocking insider trading scandals of the 1980s, Congress adopted the intricate and "woefully . . . confusing"[28] Insider Trading and Securities Fraud

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22. *See infra* Part III; *see also* Coglianese et al., *supra* note 19, at 219 ("[M]uch of the existing system of corporate regulation in the United States emerged in response to vagaries of the late 1920s and the subsequent stock market crash."); Jeremy Grant, *Paulson Vows to Bolster US Competitiveness*, FT.COM, Mar. 13, 2007, http://www.ft.com/cms/s/0/eb34ca58-d19f-11db-b921-000b5df10621.html (commenting that the U.S. "'rules-based' system [was] forged in the post-Depression years of investor protection").

23. William W. Bratton, *Rules, Principles, and the Accounting Crisis in the United States*, *in* AFTER ENRON: IMPROVING CORPORATE LAW AND MODERNISING SECURITIES REGULATION IN EUROPE AND THE US 265, 271 (John Armour & Joseph A. McCahery eds., 2006); *see* GARRATT, *supra* note 21, at 21 (stating that rules support the quintessentially U.S. "emphasis . . . on external agencies ensuring compliance and, if necessary, litigation").

24. Coglianese et al., *supra* note 19, at 229.

25. Foreign Corrupt Practices Act, Pub. L. No. 95-213, 91 Stat. 1494 (1977) (codified as amended in scattered sections of 15 U.S.C.); *see* GEORGE C. GREANIAS & DUANE WINDSOR, THE FOREIGN CORRUPT PRACTICES ACT: ANATOMY OF A STATUTE 1 (1982) ("The Foreign Corrupt Practices Act of 1977 has been characterized as the most extensive application of federal law to the regulation of corporations since the passage of the 1933 and 1934 securities acts.").

26. Daniel Pines, Comment, *Amending the Foreign Corrupt Practices Act to Include a Private Right of Action*, 82 CAL. L. REV. 185, 189 (1994) ("From the instant the [Foreign Corrupt Practices] Act was implemented, American corporations complained about the Act's provisions and clamored for amendment.").

27. JOHN C. COFFEE, JR., GATEKEEPERS: THE PROFESSIONS AND CORPORATE GOVERNANCE 144 (2006).

28. JONATHAN R. MACEY, INSIDER TRADING: ECONOMICS, POLITICS, AND POLICY 65 (1991).

Enforcement Act of 1988 (ITSFEA).[29] Like Sarbanes-Oxley and the FCPA, the ITSFEA has been criticized for both its severity and its abstruse impenetrability.[30]

This approach is anathema to the regulatory approach in many nations, including the United Kingdom. Following the failures at Enron and WorldCom, the Financial Reporting Council,[31] an independent regulatory panel staffed with British corporate luminaries, issued an important soft law[32] document titled "The Combined Code on Corporate Governance."[33] The Combined Code

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29. Insider Trading and Securities Fraud Enforcement Act of 1988, Pub. L. No. 100-704, 102 Stat. 4677 (codified as amended in scattered sections of 15 U.S.C.) (amending the Securities and Exchange Act of 1934 [hereinafter "Exchange Act"] by adding §§ 21A(a)(3) and (b)(1)). The insider trading scandals of the early 1980s led more immediately to Congress' enactment of the Insider Trading Sanctions Act of 1984. James D. Cox, *The Role of Empirical Evidence in Evaluating the Wisdom of the Sarbanes-Oxley Act*, 40 U.S.F. L. REV. 823, 823 (2006). The Act "authorize[d] the SEC to impose a civil penalty of up to three times the amount of profits made or losses avoided by any person who violated the antifraud rules by inside trading or tipping." James D. Cox & Randall S. Thomas, with the assistance of Dana Kiku, *SEC Enforcement Heuristics: An Empirical Inquiry*, 53 DUKE L.J. 737, 745 n.25 (2003). However, the Act failed to prevent two highly-publicized scandals in the mid-1980s involving, respectively, Dennis Levine and Ivan Boesky. *See, e.g.*, Kurt Eichenwald, *Wages Even Wall St. Can't Stomach*, N.Y. TIMES, Apr. 3, 1989, at D1 ("Mr. Boesky, the envy of Wall Street in 1985, when he made an estimated $100 million, paid that much to settle insider trading charges the following year."); Nathanial C. Nash, *An Insider Scheme Is Put in Millions*, N.Y. TIMES, May 13, 1986, at A1 ("A Wall Street merger specialist [Dennis Levine . . .] was charged today with using confidential information illegally in a trading scheme that reaped at least $12.6 million in profits . . . ."). In response to these (and other) scandals, Congress quickly enacted more sweeping regulation with the Insider Trading and Securities Fraud Enforcement Act of 1988 (ITSFEA). *See* H.R. REP. NO. 100-910, at 7 (1988), *as reprinted in* 1988 U.S.C.C.A.N. 6043, 6044 ("The [ITSFEA] represents the response of this Committee to a series of revelations over the last two years concerning serious episodes of abusive and illegal practices on Wall Street.").

30. *See* Thomas W. Joo, *Legislation and Legitimation: Congress and Insider Trading in the 1980s*, 82 IND. L.J. 575, 608 (observing that Congress passed ITSFEA after "fram[ing] insider trading as an issue of immorality and punishment . . . of good versus evil," which allowed it to place excessive liability on defendants in a way that was draconian). Further, because the ITSFEA "increased penalties for 'insider trading' without defining [insider trading]" itself, it has drawn broad criticism for being incomplete and confusing. *Id.*

31. *See* FINANCIAL REPORTING COUNCIL, THE UK APPROACH TO CORPORATE GOVERNANCE 4 (2006), *available at* http://www.frc.org.uk/corporate (follow "The UK Approach to Corporate Governance" hyperlink). The Council declares that "[t]he UK's system of business regulation, which is principles rather than rules based, reduces the cost to global businesses of introducing procedures to comply with detailed regulations, many of which unnecessarily constrain business practice and innovation." *Id.* at 1.

32. "'[S]oft law[s,]' [broadly defined, are] those regulatory instruments and mechanisms of governance that, while implicating some kind of normative commitment, do not rely on binding rules or on a regime of formal sanctions." Anna di Robilant, *Genealogies of Soft Law*, 54 AM. J. COMP. L. 499, 499 (2006).

33. COMBINED CODE, *supra* note 20.

proposes a small number of recommended "best practices" and compels companies wishing to list on the London Stock Exchange[34] to comply, or alternatively, to state their reasons for noncompliance in their annual reports.[35] If companies choose noncompliance, it is assumed investors will either accept the noncompliance or pressure those companies to conform—by voting their shares or by selling their shares in the open market.[36] Hence, the principles-based system is essentially shareholder regulated.[37]

Principles-based regulation has drawn praise from many influential U.S. political and business leaders who view the rules-based system as a sort of millstone around the neck of U.S. capital markets. For example, in January 2007, President George W. Bush cautioned that legislative rulemaking had created "excessive litigation and overregulation [that] threaten to make our capital markets less attractive to investors, especially in the face of rising competition from capital markets abroad."[38] Shortly thereafter, a bipartisan commission established by the U.S. Chamber of Commerce recommended "quick and decisive adjustments in the U.S. legal and regulatory framework,"[39] including a shift to a more principles-based system focused on "providing informal guidance to market participants . . . that . . . do[es] not require rulemaking."[40] The commission gravely observed, "[I]t has become increasingly clear that the United States lacks an overall vision for how its legal and regulatory framework should respond to . . . new market developments."[41] In May 2007, Federal Reserve Chairman Ben Bernanke urged that the U.S. turn away from its traditional rules-based regulation and candidly advocated "a consistent, principles-

34. JEAN JACQUES DU PLESSIS ET AL., PRINCIPLES OF CONTEMPORARY CORPORATE GOVERNANCE 306 (2005).

35. *Id.*; John Friedland, *Reforming Disclosure and Corporate Governance in the UK: Between Scylla and Charybdis*, 1 INT'L J. DISCLOSURE & GOVERNANCE 35, 36 (2003).

36. Ascarelli, *supra* note 10.

37. *See* NEIL COWAN, RISK ANALYSIS AND EVALUATION 99 (2d ed. 2005) (noting that the United Kingdom's enforcement is "market-led and driven by stakeholder groups who will enforce good governance by 'voting with their feet' in respect of withdrawing financial support from companies that do not follow the voluntary code").

38. Bawden, *supra* note 17.

39. COMM'N ON THE REGULATION OF U.S. CAPITAL MKTS. IN THE 21ST CENTURY, *supra* note 17, at 4.

40. *Id.* at 7.

41. *Id.* at 11.

based, and risk-focused approach" similar to the one used in the United Kingdom.[42]

Still, others have advocated caution in considering these calls for change. U.S. Treasury Secretary Henry M. Paulson, Jr., has publicly recommended an examination of "whether it would be practically possible and beneficial to move toward a more principles-based regulatory system," given that rules-based regulation "has served [the United States] very well over the course of [its] history. . . . [and] is part of the foundation for [its] prosperity and growth."[43] Paulson's concern forms the basis for this Note, which investigates whether it is practical and beneficial to adopt a more principles-based regulatory framework into U.S. corporate governance.

II. CORPORATE GOVERNANCE IN THE UNITED STATES AND IN THE UNITED KINGDOM

Although U.S. and U.K. approaches to corporate regulation are fundamentally different, they also share some areas of common ground. This Part describes both their essential differences and their similarities.

A. Essential Differences

Why is it unfeasible to adopt a principles-based regime of corporate governance into U.S. law? There are at least two general reasons. First, such an adoption is hampered by several key and essential differences that distinguish the U.S. approach to corporate governance from its U.K. counterpart. This Section discusses those differences, which are—at their essence—differences in enforcement and ideology. Second, as Part III discusses, a uniquely American history and legal culture play a fundamental role in cementing the preeminence of rules in U.S. corporate governance.

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42. Ben S. Bernanke, Chairman, Bd. of Governors of the Fed. Reserve System, Speech to the Federal Reserve Bank of Atlanta's 2007 Financial Markets Conference, Sea Island, Ga. (May 15, 2007), *available at* http://www.federalreserve.gov/newsevents/speech/bernanke20070515a.htm.

43. Henry M. Paulson, Jr., U.S. Treasury Sec'y, Opening Remarks at Treasury's Capital Markets Competitiveness Conference at Georgetown Univ. (Mar. 13, 2007), *available at* http://www.treasury.gov/press/releases/hp306.htm.

Sarbanes-Oxley and its implementing rules grant the SEC[44]—and arguably private citizens[45]—authority to enforce the Act's provisions through litigation. Meanwhile, the United Kingdom has no corporate governance legislation whatsoever and therefore no comparable lever to pry open the courthouse doors.[46] Instead, the London Stock Exchange—a self-regulatory organization—simply requires U.K.-listed companies to comply with the Combined Code's recommended principles or to explain publicly why they do not comply.[47] This public reporting presumably allows investors themselves to promote conscientious corporate governance by choosing to invest with those companies that practice it and to pull their funds from those that do not.[48] This enforcement regime may punish corporate misdeeds in the marketplace but it does not punish them in the courtroom.

A narrower enforcement distinction arises from the differing degrees of auditor flexibility allowed by the governance structures of each country. In the United States, Sarbanes-Oxley makes it unlawful for an audit firm to engage in any of eight specific types of nonaudit services contemporaneous with its audit of a public company.[49] This regulation is intended to safeguard the audit firm's independence and

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44. *See* 15 U.S.C. § 7202(a), (b)(1) (Supp. V 2005) ("The [SEC] shall promulgate such rules and regulations, as may be necessary or appropriate . . . in furtherance of this Act. . . . A violation . . . [of] any rule or regulation of the [SEC] issued under this Act . . . shall be treated for all purposes in the same manner as a violation of the Securities Exchange Act of 1934 . . . .").

45. *See* Lewis D. Lowenfels & Alan R. Bromberg, *Implied Private Actions Under Sarbanes-Oxley*, 34 SETON HALL L. REV. 775, 776, 805 (2004) (contending that Sarbanes-Oxley "contains a number of provisions expressly granting private parties the right to sue for violations of the Act" and creates "additional duties and obligations . . . [that] provide fuel for new implied private actions"). *But see* PAUL W. MACAVOY & IRA M. MILLSTEIN, THE RECURRENT CRISIS IN CORPORATE GOVERNANCE 105 (2003) ("There is no new private right of action for investors created by Sarbanes-Oxley."). MacAvoy and Millstein affirm however that Sarbanes-Oxley "permit[s a] private right of action to recover profits improperly obtained by insiders during pension fund black out periods" and requires "certain certifications . . . [that] could provide the basis of a private action." *Id.* at 105 n.20.

46. COWAN, *supra* note 37, at 98.

47. *Id.*

48. *Id.* at 99.

49. *See* 15 U.S.C. § 78j-1(g) (Supp. V 2005) (listing these services as "(1) bookkeeping or other services related to the accounting records or financial statements of the audit client; (2) financial information systems design and implementation; (3) appraisal or valuation services, fairness opinions, or contribution-in-kind reports; (4) actuarial services; (5) internal audit outsourcing services; (6) management functions or human resources; (7) broker or dealer, investment adviser, or investment banking services; (8) legal services and expert services unrelated to the audit"). Also prohibited are any services that the Public Company Accounting Oversight Board, established by 15 U.S.C. § 7211, determines are impermissible. *Id.*

preempt foreseeable conflicts of interest with the audited firm.[50] Unfortunately, it may also burden the audited firm with the additional expense of hiring multiple companies to provide multiple services. The auditing firm could likely provide the nonaudit services less expensively than any of these other companies by virtue of the understanding gained through its audit of the client.[51]

In the United Kingdom, the Auditing Practices Board (APB), which is part of the Financial Reporting Council, is charged with establishing auditing standards that instill confidence in the auditing process.[52] It has developed a more flexible approach to non-audit activities than the eight Sarbanes-Oxley categories by issuing a form of guidance called the "APB Ethical Standard: Non-Audit Services Provided to Audit Clients."[53] Among other things, the "APB Ethical Standard" suggests that if a lead auditor detects a possible or actual breach of one of its provisions, that auditor should "assess the implications of the breach, determine whether there are safeguards that can be put in place or other actions that can be taken to address any potential adverse consequences and consider whether there is a need to resign from the audit engagement."[54] Authority for enforcement thus rests with the auditor, not with an outside legal entity.[55]

The United States and the United Kingdom also approach corporate governance from opposite ideological angles, as indicated by official statements about the purposes of Sarbanes-Oxley and the Combined Code respectively. Sarbanes-Oxley was expressly created "[t]o protect investors by improving the accuracy and reliability of

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50. Paul Davies, *Enron and Corporate Governance Reform in the UK and the European Community*, *in* AFTER ENRON: IMPROVING CORPORATE LAW AND MODERNISING SECURITIES REGULATION IN EUROPE AND THE US, *supra* note 23, at 415, 432.

51. *Id.*

52. The Auditing Practices Board Home Page, http://www.frc.org.uk/apb/ (last visited Jan. 19, 2008).

53. AUDITING PRACTICES BD., APB ETHICAL STANDARD 5: NON-AUDIT SERVICES PROVIDED TO AUDIT CLIENTS (2004), *available at* www.frc.org.uk/images/uploaded/documents/ES5vprint.pdf.

54. *Id.* para. 3.

55. The authority of APB pronouncements is slightly—but only slightly—more substantial than is indicated here, as auditing firms in Britain must register with supervisory administrative bodies and these bodies have been included to adopt APB standards and guidance as a requirement for the firms registered with them. *See* AUDITING PRACTICES BD., THE AUDITING PRACTICES BOARD–SCOPE AND AUTHORITY OF PRONOUNCEMENTS (REVISED) para. 12 (2006), *available at* http://www.frc.org.uk/images/uploaded/documents/ (follow "The Auditing Practices Board - Scope and Authority of Pronouncements _Revised_ 2006.pdf" hyperlink).

corporate disclosures made pursuant to the securities laws."[56] The legislative focus was explicitly on augmenting corporate reporting—which simultaneously increases corporate transaction costs—to restore investor confidence and to safeguard the integrity of U.S. markets.[57] This "rules and enforcement first" approach not only "made the whole business of operating a company in the United States a lot more tiresome,"[58] it also made it much more expensive, with Sarbanes-Oxley compliance costs reportedly reaching approximately $6 billion in 2006.[59] Studies indicate that these forces are driving securities issuers away from the United States.[60]

Conversely, flexibility is the touchstone of the Combined Code[61] and the British have allowed the more fluid forces of the capital markets to dictate the ways corporations choose to govern themselves.[62] The Combined Code's stated purpose is to "enabl[e] UK listed companies to be led in a way which facilitates entrepreneurial success and the management of risk."[63] Important emphasis is placed on "entrepreneurial success" and corporate profitability, not on costly legal disclosures and protective

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56. Sarbanes-Oxley Act of 2002, Pub. L. No. 107-204, 116 Stat. 745, 745 (codified as amended in scattered sections of 11, 15, 18, 28, and 29 U.S.C.).

57. *Implementation of the Sarbanes-Oxley Act of 2002: Hearing Before the S. Comm. on Banking, Housing, and Urban Affairs*, 108th Cong. 35 (2003) (statement of William H. Donaldson, Chairman, Securities and Exchange Commission). Sarbanes-Oxley's principal objectives "can be grouped into the following themes: [t]o strengthen and restore confidence in the accounting profession; [t]o strengthen enforcement of the Federal securities laws; [t]o improve the 'tone at the top' and executive responsibility; [t]o improve disclosure and financial reporting; and [t]o improve the performance of 'gatekeepers.'" *Id.*

58. James Harding, *London Calling*, TIMES ONLINE (London), Mar. 13, 2007, http://business.timesonline.co.uk/tol/business/columnists/article1503880.ece.

59. Deepak Gopinath, *Why the Big Deals No Longer Call Wall Street Home*, GLOBE & MAIL (Toronto), Feb. 21, 2007, at B15.

60. *Id.*

61. *See* COMPANY LAW REVIEW STEERING GROUP, MODERN COMPANY LAW FOR A COMPETITIVE ECONOMY: DEVELOPING THE FRAMEWORK para. 3.10 (2000) (observing that the United Kingdom's corporate system's flexibility is a "great strength," which is likely to prove a major competitive advantage in the marketplace); PETRI MÄNTYSAARI, COMPARATIVE CORPORATE GOVERNANCE: SHAREHOLDERS AS A RULE-MAKER 86 (2005) (stating that "UK company law is regarded as flexible"); Andrew Hurst, *London Keeps Edge Over Wall St. for Now*, REUTERS, Nov. 16, 2006, http://www.reuters.com/article/InvestmentBanking06/idUSL1682039720061116 ("Speakers at a Reuters Investment Banking Summit singled out for praise Britain's principles-based system of market regulation . . . .").

62. Ascarelli, *supra* note 10.

63. FINANCIAL REPORTING COUNCIL, REVIEW OF THE IMPACT OF THE COMBINED CODE 1 (2007), *available at* http://www.frrp.co.uk/press/pub1299.html (follow "Consultation Paper: Review of the Impact of the Combined Code" hyperlink).

mechanisms to safeguard investors. Some commentators believe that this company-friendly focus has allowed London to surpass New York as the world's most vibrant economic center.[64]

B. Audit Committees and Financial Experts

Despite these contrasting enforcement mechanisms and ideologies, Sarbanes-Oxley and the Combined Code share certain patches of common regulatory ground, especially with regard to corporate audit committees. This Section describes the contours of that common ground.

1. *Audit Committees.* Audit committees in both the United States and the United Kingdom are generally structured in the same fashion and serve the same functions. All committee members must be independent non-executive directors.[65] Under Sarbanes-Oxley, the audit committee is legally accountable for appointing, compensating, and overseeing the work of the outside auditor.[66] Under the Combined Code, however, the committee "*should* . . . review and monitor the external auditor's independence and objectivity and the effectiveness of the audit process,"[67] but "no regulatory enforcement proceeding or class action is prompted by non-compliance."[68] Indeed, although corporations in the United Kingdom are directed by the Combined Code to comply with its provisions or explain their reasons for noncompliance,[69] no legal penalties arise from their failure to comply with or explain any of these provisions unless the corporation is listed on a U.K. stock exchange. If a corporation is listed, and it

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64. *See* Hurst, *supra* note 61 ("Britain's flexible financial regulatory regime is giving London a strong edge over New York, especially in attracting foreign company listings, and there is no sign Wall Street can close the gap soon.").

65. *Compare* 15 U.S.C. § 78j-1(m)(3)(A) (Supp. V 2005) ("Each member of the audit committee . . . shall be a member of the board of directors of the issuer, and shall otherwise be independent."), *with* COMBINED CODE, *supra* note 20, § C.3.1 ("The board should establish an audit committee of . . . members, who should all be independent non-executive directors.").

66. 15 U.S.C. § 78j-1(m)(2).

67. COMBINED CODE, *supra* note 20, § C.3.2 (emphasis added).

68. Thomas J. Dougherty, *The Political Economy of Corporations: Varying Approaches to Corporate Governance Around the World* (ALI-ABA Continuing Legal Education Course of Study, May 4–5, 2006), WL SL085 ALI-ABA 253, 256.

69. *See* COMBINED CODE, *supra* note 20, pmbl. at 1 (stating that "the company has either to confirm that it complies with the Code's provisions or—where it does not—to provide an explanation").

fails to comply or explain, it may be subject to prosecution under the U.K. Listing Authority.[70]

In both the United States and the United Kingdom, the audit committee serves a policing role to ensure that those managing corporate affairs comply with accepted accounting principles.[71] This safeguard gives shareholders and investors increased confidence in a company's reports about its financial health.[72] Of course, at Enron, WorldCom, and other large U.S. corporations that have folded, breakdowns in the auditing process prevented shareholders from obtaining such accurate information.[73] Auditors at these firms did not require strict management compliance with general accounting standards because their interests were entwined with those of the management.[74] Under Sarbanes-Oxley and the Combined Code, members of a public company's audit committee must be independent, meaning their interests are dissociated from those of corporate executives.[75]

2. *Financial Expertise under the Combined Code*. Although both Sarbanes-Oxley and the Combined Code also seek to provide a certain level of financial expertise on corporate audit committees,

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70. Iain MacNeil & Xiao Li, *Comply or Explain: Market Discipline and Non-Compliance with the Combined Code*, 14 CORP. GOVERNANCE 486, 488 n.11 (2006) ("[B]reach of the Listing Rules . . . can be sanctioned by public censure, fine or suspension from listing under the Financial Services and Markets Act 2000.").

71. *See* JAMES HAMILTON & TED TRAUTMANN, SARBANES-OXLEY ACT OF 2002: LAW AND EXPLANATION 13 (2002) (stating that a goal is to "improve quality and transparency in financial reporting by those companies"); Jonathan Shirley, *International Law and the Ramifications of the Sarbanes-Oxley Act of 2002*, 27 B.C. INT'L & COMP. L. REV. 501, 508 (2004) (stating that "[a]uditors ensure that the management complies with accounting standards").

72. Matthew M. Benov, *The Equivalence Test and Sarbanes-Oxley: Accommodating Foreign Private Issuers and Maintaining the Vitality of U.S. Markets*, 16 TRANSNAT'L LAW. 439, 454–55 (2003) ("The United Kingdom drafted . . . the Combined Code . . . out of concern for maintaining integrity in financial reporting and boosting investor confidence." (citation omitted)); Shirley, *supra* note 71, at 508.

73. *See* BROOKS CARDER & PATRICK RAGAN, MEASUREMENT MATTERS: HOW EFFECTIVE ASSESSMENT DRIVES BUSINESS AND SAFETY PERFORMANCE 124 (2005) ("Audited financial statements indicated that Enron, WorldCom, and Health South were making substantial profits at a time when they were in fact losing large amounts of money.").

74. ANDREW D. CROCKETT, CONFLICTS OF INTEREST IN THE FINANCIAL SERVICES INDUSTRY: WHAT SHOULD WE DO ABOUT THEM? 36 (2003).

75. *Compare* 15 U.S.C. § 78j-1(m)(3)(A) (Supp. V 2005) ("Each member of the audit committee of the issuer . . . shall otherwise be independent."), *with* COMBINED CODE, *supra* note 20, § C.3.1 (stating that the members of the audit committee "should all be independent non-executive directors").

they approach this goal in different ways. The Combined Code showcases its flexibility in regulating corporations, stating that "[t]he board should *satisfy itself* that at least one member of the audit committee has recent and relevant financial experience."[76] Thus, even if the board decides to bring someone onto its audit committee whose financial expertise is limited to balancing a personal checkbook, the Combined Code only requires that the board feel satisfied that the experience is both recent and relevant. No one else must be satisfied. Under such a permissive standard, even if a corporation fails to put anyone with a moderate amount of financial experience on its audit committee, as long as it satisfies itself, no disclosure is required in the annual report.

Moreover, shareholder discretion is the only policing mechanism provided by the Combined Code. No government or industry watchdog has authority to assess the extent of a financial expert's expertise. Indeed, even if a provision bestowed such authority on an industry watchdog, it would have no objective standard for measuring whether a board member's financial expertise was sufficient. All the Combined Code requires is that the corporation "satisfy itself." This implies that the corporation must satisfy not only its directors, but also its owners—the shareholders—whom the Combined Code envisions as the real watchdogs of corporation. Because all shareholders have access to reports detailing the composition of the company's audit committee,[77] the Combined Code anticipates that these shareholders will regulate company behavior by either pressuring corporations to appoint someone with bona fide financial expertise to the audit committee or by moving their money elsewhere.

3. *Financial Expertise under the U.S. Regulations*. The numerous requirements and regulations imposed by Sarbanes-Oxley, the SEC rules, and the mandatory listing requirements of the major U.S. securities exchanges contrast sharply with the Combined Code's flexible, principles-based and shareholder-regulated model. Because Sarbanes-Oxley directs SEC rulemaking with regard to audit committee financial experts, Sarbanes-Oxley and the SEC rules are

76. COMBINED CODE, *supra* note 20, § C.3.1 (emphasis added).

77. *Id.* § A.1.2 ("The annual report should identify the chairman, the deputy chairman (where there is one), the chief executive, the senior independent director and the chairmen and members of the nomination, audit, and remuneration committees.").

discussed together in the next Section. A description of the New York Stock Exchange (NYSE) and NASDAQ listing requirements for financial experts follows.

a. Sarbanes-Oxley and Associated SEC Regulations. Sarbanes-Oxley directs the SEC to enact rules defining the qualifications of an "audit committee financial expert."[78] Sarbanes-Oxley also requires each corporation to disclose in either its annual report or its annual shareholder proxy statement whether any member of its audit committee meets these qualifications.[79] If a corporate audit committee has no financial expert, the company must explain why.[80] If it does have an expert, the company must disclose the name of that expert.[81]

Although on their surface the Sarbanes-Oxley and SEC provisions appear quite similar to the Combined Code provisions in that they both require companies to comply or explain their reasons for noncompliance, two key differences make the American rule-based scheme more onerous on the companies it regulates. First, finding an audit committee member who meets the SEC's high bar for financial expertise[82] is much more difficult than finding one who meets the Combined Code's simple "board should satisfy itself" requirement.[83] Although the SEC has broadened the definition of financial expertise somewhat since its first draft, which would have excluded even former Federal Reserve Chairman Alan Greenspan

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78. 15 U.S.C. § 7265(a) (Supp. V 2005); Lawrence E. Mitchell, *The Sarbanes-Oxley Act and the Reinvention of Corporate Governance?*, 48 VILL. L. REV. 1189, 1199 (2003). The SEC's elaborate definition spans seventy-five pages. Ascarelli, *supra* note 10.

79. 15 U.S.C. § 7265(a).

80. Adam O. Emmerich et al., *Composition of the Audit Committee: Ensuring Members Meet the New Independence and Financial Literacy Rules*, 2 INT'L J. DISCLOSURE & GOVERNANCE 67, 69 (2005).

81. *Id.*

82. The SEC's corrected final rule implementing Sarbanes-Oxley section 407 requires that a financial expert have (i) an understanding of generally accepted accounting principles and financial statements; (ii) experience applying such principles in connection with the accounting for estimates, accruals, and reserves that are generally comparable to the estimates, accruals and reserves used in the registrant's financial statements; experience preparing or auditing financial statements that present accounting issues that are generally comparable to the breadth and complexity of issues expected to be raised by the registrant's financial statements; (iii) experience with internal controls and the procedures for financial reporting; and (iv) an understanding of audit committee functions. Disclosure Required by Sections 406 and 407 of the Sarbanes-Oxley Act of 2002, Securities Act Release Nos. 33-8177, 34-47235, 68 Fed. Reg. 5110 (Jan. 23, 2003).

83. COMBINED CODE, *supra* note 20, § C.3.1.

and investing luminary Warren Buffett from qualifying as experts,[84] corporate chiefs continue to complain that recruiting qualified financial experts is a time-consuming hassle accompanied by high "explicit and implicit costs [that] arise in attracting and retaining such experts."[85] The SEC's rules are "strict enough that even a highly competent person with a financial background might fail to qualify."[86] Given that most of the Fortune 500 companies have already recruited qualified experts, a substantial part of the problem may be that the limited pool of qualified talent is drying up.

Finally, Sarbanes-Oxley's requirement that each company must disclose the name of its financial expert has created its own unique set of problems. Many have questioned whether characterizing someone on the audit committee as an "expert" will bestow on that individual a higher standard of care than is assumed by other directors, thereby exposing the expert to increased liability. The SEC has attempted to assuage these anxieties by assuring financial experts that they are not subject to any liability, duties, or obligations above those traditionally assumed by other directors.[87] The SEC even adopted a safe harbor to shield audit committee financial experts from liabilities arising under federal securities laws.[88]

This safe harbor however, provides no refuge from plaintiffs filing suit under *state* securities laws, and such plaintiffs have already enjoyed a significant measure of success. For example, in *In re Emerging Communications, Inc., Shareholders Litigation*,[89] shareholders brought suit claiming the directors of the corporation had breached their fiduciary duty in connection with a merger negotiation.[90] Because fiduciary duties are matters of state law and

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84. Geoffrey Colvin, *Sarbanes & Co. Can't Want This*, FORTUNE, Dec. 30, 2002, at 66, 66. ("Based on the language in [Sarbanes-Oxley], Alan Greenspan would not qualify as a financial expert. Warren Buffet apparently would not qualify either. The reason, essentially, is that neither man has been an accountant, an auditor, or a CFO, though it's hard to imagine either man failing to lead an audit committee quite effectively.").

85. Alan Reinstein, *To the Rescue: The ACFE: Is it a Bird? A Plane? Alan Greenspan?*, RMA J., Oct. 2004, at 62.

86. Bradley P. Cost & Daniel M. Miller, Emerging Communications*: Enhanced Director Liability for Experts?*, METROPOLITAN CORP. COUNS., Jan. 2005, at 26, *available at* http://www.metrocorpcounsel.com/pdf/2005/January/26.pdf.

87. Disclosure Required by Sections 406 and 407, *supra* note 82.

88. *Id.*

89. *In re* Emerging Commc'ns, Inc., S'holders Litig., No. Civ. A. 16415, 2004 WL 1305745 (Del. Ch. May 3, 2004).

90. *Id.* at *1.

not federal law, the SEC safe harbor was inapposite.[91] The Delaware Chancery Court held one director to a higher standard of care than all the other directors because he was a financial expert, having gained specialized experience in both securities and the telecom industries.[92] This case has effectively put all other financial experts on notice that state courts may interpret the fiduciary obligations of experts to be greater than those of the other audit committee members.

b. NYSE and NASDAQ Listing Requirements. The listing requirements of the NYSE and NASDAQ likewise offer corporations less flexibility than the Combined Code, and in some respects they are even more restrictive than Sarbanes-Oxley. To be listed on either of these exchanges, a corporation must have a financial expert on its audit committee. There is no exception to this rule.[93] In other words, the rule is not "comply or explain," it is "comply or list elsewhere." All issuers who list on the NYSE must have an independent director who serves on the audit committee as a financial expert, and the expert must possess "accounting or related financial management expertise."[94] A qualified financial expert must possess sufficient expertise to understand the most complex finance and accounting issues a company might encounter during the course of its business.[95]

Similarly, the NASDAQ listing rules require company audit committees to have at least one member with "past employment experience in finance or accounting, requisite professional certification in accounting, or any other comparable experience or background" that elevates that individual to a level of financial sophistication, such as experience as a chief executive officer or chief

91. *See* Cost & Miller, *supra* note 86 ("The safe harbor is meant to protect directors from extra liability under the federal securities laws. However, it is state law that imposes fiduciary duties upon directors . . . .").

92. *In re Emerging Commc'ns, Inc.*, 2004 WL 1305745, at *40 (finding a financial expert culpable because he "possessed a specialized financial expertise, and an ability to understand ECM's intrinsic value, that was unique to ECM board members").

93. Emmerich et al., *supra* note 80, at 68 (noting that although the New York Stock Exchange does require at least one member of the committee to be financially literate, it also permits a corporation to be listed on the exchange even without such a member if the "audit committee member . . . become[s] financially literate within a reasonable period of time after being appointed to the audit committee").

94. NYSE, Inc., Listed Company Manual § 303A.07(a), http://www.nyse.com/regulation/listed/1182508124422.html (last visited Jan. 27, 2008).

95. Emmerich et al., *supra* note 80, at 68.

financial officer.[96] A company whose audit committee financial expert qualifies under the SEC rules also qualifies for purposes of the NASDAQ listing requirements.[97]

When juxtaposed against the principles-oriented Combined Code, the NYSE and NASDAQ listing rules bring to light another important ideological principle that distinguishes U.S. corporate governance from its U.K. counterpart. Listing rules are essentially protective intermediaries. They stand at the gateway of the major exchanges to bar companies deemed most likely to harm investors.[98] For the NYSE and NASDAQ, those companies that do not have a qualified financial expert on their audit committee are barred from issuing securities. Conversely, the Combined Code allows *any* issuer to market its securities as long as it reports what is happening behind closed doors. The state ultimately places trust in shareholders and investors, who are empowered to look after their own interests, to do their own research, and to make investment decisions without intermediary gatekeepers.

III. UNITED STATES AND UNITED KINGDOM CORPORATE GOVERNANCE REGIMES IN CONTEXT

The ultimate question this Note seeks to address, and the one posed by many U.S. political and financial leaders, is whether it is feasible to transplant into U.S. law a more principles-based regulatory approach to corporate governance that is similar to and perhaps patterned after the Combined Code. To understand whether such dramatic changes in U.S. law are feasible—and if feasible, what they would look like in a legal and political system that has long been predominantly rules-based—it is useful to examine the genesis and evolution of the U.S. regulatory framework. It is likewise useful to assess the impact American culture has had and continues to have on U.S. corporate regulation.

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96. NASDAQ Manual Online, Marketplace Rule 4350(d)(2)(A), http://nasdaq.complinet.com/nasdaq/display/display.html?rbid=1705&element_id=1014 (last visited Jan. 27, 2008); *accord* Emmerich et al., *supra* note 80, at 69.

97. NASDAQ Manual Online, Marketplace Rule IM-4350-4, http://nasdaq.complinet.com/nasdaq/display/display.html?rbid=1705&element_id=1014 (follow the "IM-4350-4 Board Independence and Independent Committees" hyperlink) (last visited Jan. 27, 2008).

98. *See* 13 INTERNATIONAL ENCYCLOPEDIA OF COMPARATIVE LAW 22 (1981) (labeling the listing requirements of the securities exchanges the "gatekeepers of the path along which securities move to the public").

However, because "culture can mean so many things,"[99] and is susceptible to being "everywhere invoked and nowhere explained,"[100] it is first necessary to briefly define the meaning of "culture" used here. Borrowing from "the dominant paradigm" of culture that has emerged from cultural studies,[101] this Note defines "culture" as "both the meanings and values which arise amongst distinctive social groups and classes, [based on] their given historical conditions and relationships . . . and as the lived traditions and practices through which those 'understandings' are expressed and . . . embodied."[102] As Gunther Teubner points out, cultural differences between nations complicate legal transfer and may lead to its failure, for "legal transfer is not smooth and simple but has to be assimilated to the deep structure of the new law, to the social world constructions that are unique to the different legal culture."[103] This Note argues that the uniquely American culture that has fostered rules-based corporate governance will resist and spurn the adoption of a soft law, principles-based regime to regulate corporate behavior.

This Part assesses the respective roles of both history and culture in the formation and perpetuation of U.S. rules-based corporate regulation. It then draws several comparative connections with the development of the United Kingdom's principles-based scheme.

A. Historical Influences

Early American colonists arrived in the New World feeling a tremendous sense of distrust for corporate enterprise.[104] Since early in the eighteenth century, the English middle and lower classes had been subject to widespread abuse and degradation at the hands of profit-thirsty corporations that emerged during the Industrial

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99. Naomi Mezey, *Law as Culture*, 13 YALE J.L. & HUMAN. 35, 35 (2001) (explaining that culture can mean "collective identity, nation, race, corporate policy, civilization, arts and letters, lifestyle, mass-produced popular artifacts, [and] ritual").

100. *Id.*

101. Stuart Hall, *Cultural Studies: Two Paradigms*, *in* CULTURE/POWER/HISTORY: A READER IN CONTEMPORARY SOCIAL THEORY 520, 527 (Nicholas B. Dirks, Geoff Eley & Sherry B. Ortner eds., 1994) (emphasis omitted).

102. *Id.* (emphasis omitted).

103. Gunther Teubner, *Legal Irritants: Good Faith in British Law or How Unifying Law Ends Up in New Divergences*, 61 MOD. L. REV. 11, 19 (1998).

104. JOHN DAVID ROSE, RESCUING CAPITALISM FROM CORPORATISM: GREED AND THE AMERICAN CORPORATE CULTURE 9 (2005).

Revolution.[105] Poor children were often delivered in batches of fifty to one hundred to factory owners who whipped them, imprisoned them in irons, and forced them to work up to eighteen hours a day.[106]

Even after arriving in the colonies, British settlers were frequently exposed to the excesses of industrialist corporate greed. The Crown routinely exploited the American colonies by making them a nonconsenting market for English goods. It forced the colonists to buy more than they were able to sell, thereby exacerbating the deep recession and concomitant unemployment crisis that already plagued the colonial economy.[107] Bereft of any means of stemming or regulating these inequities, the colonial merchant, manufacturer, farmer, and planter were bonded together in loathing British market manipulation.[108]

Thus, not surprisingly, the Founding Fathers viewed corporations as dangerous organizations that, if not heavily regulated, would threaten the very freedom of their fledgling nation.[109] Fearing such a threat, the original thirteen states adopted constitutional provisions that placed strong restrictions on businesses, especially those with the greatest potential to capture significant market, economic, and political power.[110] The Pennsylvania Legislature justified its heavy regulation of industry, stating, "A corporation in law is just what the incorporating act makes it. It is the creature of the law, and may be moulded to any shape or for any . . . purpose that the Legislature may deem most conducive to the general good."[111] Hence, from the early days of the young republic, corporations were perceived with a wariness that prompted and justified aggressive corporate regulation.

Such wariness and a consequent desire to check corporate ambition are not isolated relics of colonial times long past. Near the beginning of the twentieth century, even greater social acceptance of

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105. *Id.*

106. 2 MIRIAM BEARD, A HISTORY OF BUSINESS: FROM THE MONOPOLISTS TO THE ORGANIZATION MAN 127 (1938).

107. HERBERT APTHEKER, THE AMERICAN REVOLUTION: 1763–1783, at 34 (1960).

108. *Id.* at 34–35.

109. ROSE, *supra* note 104, at 9.

110. *Id.*

111. REPORT OF THE COMMITTEE OF THE SENATE OF PENNSYLVANIA UPON THE SUBJECT OF THE COAL TRADE 46 (1834).

broad regulations of corporate affairs[112] emerged in the United States following the failure of the Reading Railroad and the subsequent failures of hundreds of banks.[113] These sudden and calamitous economic disasters "shifted the psyche of the American public" toward an even greater distrust of corporate behemoths in a way that would continue to drive twentieth-century policy and lawmaking decades later.[114] In 1927, Supreme Court Justice Oliver Wendell Holmes, Jr., proclaimed a sentiment representative of his era, stating, "[T]he notion that a business is clothed with a public interest and has been devoted to the public use is little more than a fiction intended to beautify what is disagreeable to the sufferers."[115]

Several years later, after plummeting stock prices on Wall Street had signaled the onset of the Great Depression, President Franklin Delano Roosevelt and the U.S. Congress completely reshaped the federal government's role in the U.S. economy by introducing the New Deal.[116] Historian Ronald Edsforth observes, "At the heart of the New Deal reform program was a liberal commitment to make federally guaranteed economic security a political right for every American citizen."[117] It was envisioned that this security would be permanently established through the creation of a broad series of regulatory programs and agencies, including the Securities and Exchange Commission.[118] Because many of these programs and agencies continue to play a prominent role in the twenty-first century's American corporate governance regime, political leaders

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112. CRANE BRINTON, II A HISTORY OF CIVILIZATION 239 (1984) ("By the early twentieth century public opinion was ready for increased participation by the national government in the regulation of economic life.").

113. Frederic S. Mishkin, *Asymmetric Information and Financial Crises: A Historical Perspective*, *in* FINANCIAL MARKETS AND FINANCIAL CRISES 69, 86 (R. Glenn Hubbard ed., 1991); Lee I. Niedringhaus, *The Panic of 1893*, FIN. HIST., Winter 1998, at 16, 19.

114. Niedringhaus, *supra* note 113, at 19.

115. Tyson & Bro.-United Theatre Ticket Offices, Inc. v. Banton, 273 U.S. 418, 446 (1927) (Holmes, J., dissenting).

116. RONALD EDSFORTH, THE NEW DEAL: AMERICA'S RESPONSE TO THE GREAT DEPRESSION 1 (2000) ("'The New Deal' is what [Franklin Delano Roosevelt], the press, and everyone else in the country called the laws Congress began enacting just days after FDR took office in the first week of March 1933.").

117. *Id.* at 2.

118. *See generally* Edwin C. Rozwenc, THE NEW DEAL: REVOLUTION OR EVOLUTION, at v (1949), *reprinted in* 8–10 PROBLEMS IN AMERICAN CIVILIZATION (Earl Latham, George Rogers Taylor & George F. Whicher eds., 1959) ("The Roosevelt New Deal was a period of unparalleled legislative activity . . . [marked] by an unprecedented multiplication of administrative rules and regulations.").

calling for a more principles-based approach have condemned that regime as an antiquated relic, rooted in a New Deal era that was closer in time to the Civil War than to the corporate scandals that fueled the creation of Sarbanes-Oxley.[119]

Nevertheless, from a purely historical perspective, it appears that the greatest economic harm done to U.S. issuers, shareholders, and investors actually resulted from the government's surrender of portions of its regulatory power in the days since the New Deal, not from its continued imposition of onerous rules-based regulations on corporations. For example, in 1983—a half-century after the New Deal was instituted—banking institutions successfully lobbied for the abrogation of certain government regulations, including restrictions blocking their entry into stock brokerage activities.[120] This deregulation was heralded as a grand leap forward for business and investors until just three years later, in 1986, when it led to the greatest collapse of U.S. financial institutions since the Great Depression.[121] From 1986 to 1995, 1,043 savings and loan institutions, with combined holdings of over $500 billion, failed.[122] The cost of resolving this crisis eventually surpassed $190 billion, most of which was paid for by taxpayers.[123] In this instance, deregulation only catalyzed economic growth for a short period before it contributed to a devastating economic collapse.

Still, the savings and loan crisis did not put an end to deregulation. In 1999, President Bill Clinton signed the Gramm-Leach-Bliley Act,[124] which removed the regulatory barriers erected after the market crash of 1929 that had segregated banking and stock brokering.[125] Within months of this deregulation, a feverish outbreak of fraudulent mismanagement scandals infected such reputable firms as CitiCorp, Merrill Lynch, Goldman Sachs, Solomon Barney, and

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119. COMM'N ON THE REGULATION OF U.S. CAPITAL MKTS. IN THE 21ST CENTURY, *supra* note 17, at 2.

120. ROSE, *supra* note 104, at 64.

121. Timothy Curry & Lynn Shibut, *The Cost of the Savings and Loan Crisis: Truth and Consequences*, FDIC BANKING REV., Dec. 2000, at 26, 26–27 (2000).

122. *Id.* at 26.

123. JAMES R. BARTH, SUSANNE TRIMBATH & GLENN YAGO, THE SAVINGS AND LOAN CRISIS: LESSONS FROM A REGULATORY FAILURE, at xi (2004).

124. Gramm-Leach-Bliley Act, Pub. L. No. 106-102, 113 Stat. 1338 (1999) (codified as amended in scattered sections of 12 and 15 U.S.C.).

125. ROSE, *supra* note 104, at 210.

Credit Suisse.[126] Some have argued that the spectacular failures of Enron and WorldCom, among others, can be traced directly back to the deregulation of 1999.[127] Whether or not that is the case, a substantial historical record documents the negative economic fallout from periods of significant deregulation.

What relevant principles can be drawn from this history? Although historical attitudes and events are unlikely to serve as dispositive indicators of how well the U.S. legal system would accommodate a more principles-based approach to corporate governance, they provide several important guideposts for comparison. First, Americans' longstanding apprehension of corporate abuses, which has persisted since the earliest days of the colonial era, suggests that rules are preferable to principles in American corporate governance.[128] Rules serve as external legal safeguards—as intermediaries at the gates of the market to prevent corporate abuses[129]—and therefore function to assuage individual anxieties about prospective abuses. Conversely, soft law principles rely on corporate self-regulation. This trust in corporations to govern themselves is anathema to U.S. historical attitudes and experiences that persist into the twenty-first century:[130] nearly three of every four Americans reported in 2002 that "business has too much power over too many aspects of American life."[131]

Additionally, history has shown that U.S. legislators have consistently responded to manifestations of corporate fraud and failure with heavy-handed rules and regulation. Such was true at the beginning of the twentieth century after the Reading Railroad collapse and resultant banking collapses,[132] after the market crash of 1929,[133] and at the beginning of the twenty-first century after the

126. *Id.* at 210–11.

127. *Id.* at 211.

128. *Id.* at 9.

129. 13 INTERNATIONAL ENCYCLOPEDIA OF COMPARATIVE LAW, *supra* note 98, at 22.

130. *See* GEORGE HORACE GALLUP, THE GALLUP POLL: PUBLIC OPINION 2002, at 33 (2003) (noting that a Gallup review of Americans' attitudes toward corporations revealed that "the public has historically held lukewarm feelings toward big business" and a substantial "48% say corporations can be trusted 'only a little' or 'not at all'").

131. OTTO LERBINGER, CORPORATE PUBLIC AFFAIRS: INTERACTING WITH INTEREST GROUPS, MEDIA, AND GOVERNMENT 352 (2006) (reporting the results of a July 2002 survey).

132. Niedringhaus, *supra* note 113, at 19.

133. ROSE, *supra* note 104, at 209.

Enron and WorldCom collapses.[134] Therefore, even *if* a soft law principles-based regime were adopted into U.S. law, it seems highly probable that were another large-scale corporate scandal to emerge and rekindle the frantic flames of anxiety in a spooked American populace, the legislative response would be aggressively regulatory and unequivocally rules based. Thus, even if some legislative attempt were made to institute a soft law corporate governance regime into U.S. law, its longevity would appear dubious at best.

Moreover, soft law has blossomed in the United Kingdom under completely different circumstances than those that exist in the United States. As one observer has noted, in Europe, "the very idea of soft law mechanisms as alternatives or complements to traditional hard law arose a decade ago from the acknowledgement that European integration had created a fundamental asymmetry between policies promoting market efficiency and policies aimed at social protection."[135] During the genesis of the European Union, soft law was championed as an effective way of unifying divergent national perspectives and political systems.[136] In the United States, where the political system is symmetrical, soft law would offer no such benefit.

Furthermore, the United Kingdom emerged as a soft law pioneer during the early period of European Union formation. In 1992, the Bank of England and the London Stock Exchange instituted the first corporate governance code of the modern era, which was developed under the supervision of U.K. corporate luminary Sir Adrian Cadbury.[137] In effect it was business, not government, that was regulating business.[138]

Therefore, while the Combined Code traces its history to this pivotal time in U.K. and European legal and political history, no analogue exists in the modern U.S. experience. The United States has never allowed corporate luminaries like Sir Cadbury to form and

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134. *See* David S. Hilzenrath, *Accounting Bill Advances; Senate Panel Backs Broad Measure with GOP Help*, WASH. POST, June 19, 2002, at E1.

135. Robilant, *supra* note 32, at 505.

136. *Id.* at 501–02.

137. ROBERT A.G. MONKS & NELL MINOW, CORPORATE GOVERNANCE 297 (3d ed. 2004). The committee that drafted the code is known as the "Cadbury Committee," and several additional governance committees, each chaired by United Kingdom corporate leaders, have met to draft and revise governance codes. *Id.* at 297–98.

138. *See* ACCOUNTING ETHICS: CRITICAL PERSPECTIVES ON BUSINESS AND MANAGEMENT, 184 (J. Edward Ketz ed., 2006) (interpreting the Cadbury norms to mean that business in the United Kingdom is "largely of a self-regulatory nature").

reform its law. Congressional committees may seek advice and insight from such luminaries, but ultimately the rules and regulations come from government, principally state governments, and not from chief executive officers and boards of directors.[139] Because this pattern is so well established in U.S. law, and because U.S. shareholders and investors are undoubtedly still smarting from the billions of dollars lost in corporate abuses since the turn of the century, a soft law approach that places code-fashioning authority in the hands of corporate luminaries would very likely meet insurmountable public opposition.

B. Cultural Influences

Just as American history has played a dominant role in shaping and preserving U.S. rules-based regulation of business, deep-seated and uniquely American cultural values have likewise had a significant effect. In particular, the interplay of two American values makes the wholesale adoption of a principles-based code almost un-American. These values are (1) a fervent belief that corporations are capable of moral or immoral action, and (2) an impassioned desire to uphold justice, including harsh retributivist justice, as a means of securing rightness and fairness.

Behavioral and sociological research has shown that Americans believe corporations are capable of immoral acts.[140] Although Americans generally support business, they have a strong, distinctly negative reaction to corporate misbehavior.[141] Public opinion surveys witness that Americans view corporate collapse as a byproduct of "executives' greed for money and power and an overall, societal weakening of personal values."[142] At the time Enron and WorldCom were imploding, a majority of Americans spoke of the crumbling corporate culture in moral terms, believing that former President Bill

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139. *See* Christopher Cox, Chairman, Sec. Exch. Comm'n, Keynote Address to the 2007 US-EU Corporate Governance Conference (Oct. 9, 2007) (transcript on file with the *Duke Law Journal*) ("In America, our system of federal regulation has been built upon a foundation of laws and rules established by 50 state governments as well as U.S. territories and their respective courts of law.").

140. *See* Valerie P. Hans & M. David Ermann, *Responses to Corporate Versus Individual Wrongdoing*, 13 LAW & HUM. BEHAV. 151, 152 (1989) (citing research showing that the public viewed corporate crime as widespread and deserving of punishment).

141. *Id.* at 152, 162.

142. Diane Stafford, *We May Be Closer Than We Think*, KAN. CITY STAR, Mar. 11, 2004, at C1.

Clinton was "at least partially responsible [for the scandals] because of the climate he set in office with his moral failings."[143] Importantly, empirical studies also show that even when corporate and individual misdeeds are identical, Americans hold corporations to a higher standard, judge them to be more reckless and more morally wrong in their behaviors, and wish to see them punished more severely.[144]

This strong negative response to corporations may be partly explained by Americans' perception of corporations as independent actors, capable of making moral choices but possessing more money and power than an everyday individual. In 1790, James Wilson, an early U.S. statesman and signatory of the Declaration of Independence and the Constitution, declared that corporations are "moral persons" though "not in a state of natural liberty, because their actions are cognizable by the superior power of the state."[145] Several years later, the Supreme Court of the United States echoed similar sentiments in the pivotal case *Trustees of Dartmouth College v. Woodward*.[146] The Court opined, "A corporation is an artificial being . . . [which] possesses only those properties which the charter of its creation confers upon it . . . . Among the most important [of these is] . . . individuality . . . ."[147] Thus, a belief that corporations are persons, capable of moral and immoral acts, has been preached by important legal and political leaders in formative eras of U.S. history.

Other sources offer further evidence of this uniquely American value. Authorities in business and industry have also attributed personhood and morality to the corporation. Indeed, the notion that the "corporation [is] a moral agent and [a] fit subject for punishment"[148] pervades American "textbooks and syllabi of courses in business management . . . marketing, and public policy . . . [and] controls the thinking in the majority of many business ethics centers."[149] Business expositor John David Rose observes in unmistakably moral terms that "the Ten Commandments could be

143. David W. Moore, *Little Political Fallout from Business Scandals*, GALLUP NEWS SERVICE, July 8, 2002, http://www.gallup.com/poll/6340/Little-Political-Fallout-From-Business-Scandals.aspx?version=print.

144. Hans & Ermann, *supra* note 140, at 162.

145. 2 THE ANNALS OF AMERICA, GREAT ISSUES IN AMERICAN LIFE 173 (1968).

146. Trs. of Dartmouth Coll. v. Woodward, 17 U.S. (4 Wheat.) 518 (1819).

147. *Id.* at 636.

148. Donna Card Charron, *Stockholders and Stakeholders: The Battle for Control of the Corporation*, 27 CATO J. 1, 9 (2007).

149. *Id.* at 1.

considered the final word of what is right and wrong in business as in life."[150] American CEO Charles Fulweiler describes the abusive way corporations have treated the American public thus: "It is a never-ending source of amazement to me that we are cheated, lied to, murdered and, in general, treated like mindless supplicants . . . ."[151]

Contrast Fulweiler's words with these words of the profoundly influential English jurist Sir Edward Coke: corporations "cannot commit treason nor be outlawed, or excommunicated, for they have no souls."[152] Other eminent English jurists and state executives have agreed.[153] Perhaps Fulweiler's strong diction and the words of the American judges, statesmen, and business leaders cited in this Section are thus evidence not only of a fervent cultural belief that corporations are akin to individuals and capable of immoral acts, but also of a purely American phenomenon that was not inherited from Britain.

Indeed, more than any other nation, the United States relies on lawyers, legal threats, and courts of justice to implement public policies and to resolve business disputes.[154] The range of matters that can be resolved in U.S. courts is "broader than in other nations and growing each year."[155] American culture has also long been imbued with a strong sense that punishment must be exacted in the U.S. courts,[156] which are plaintiff-friendly by design[157] and offer a breadth

150. ROSE, *supra* note 104, at 71.

151. *Id.* at 2.

152. PAUL R. EHRLICH & ANNE H. EHRLICH, ONE WITH NINEVEH: POLITICS, CONSUMPTION, AND THE HUMAN FUTURE 295 (2004).

153. Roger Manwood, Lord Chief Baron of the Exchequer under appointment from Queen Elizabeth I, opined that corporations "were invisible, immortal, and . . . had no soul, and therefore no subpoena lieth against them, because they have no conscience . . . ." FRANKLIN FISKE HEARD, CURIOSITIES OF THE LAW REPORTERS 79 (1871) (quoting from a description of Manwood's opinion in an English Law Reporter). Edward, First Baron Thurlow, attorney and Lord Chancellor of Great Britain under four prime ministers in the eighteenth century, argued that "[c]orporations have neither bodies to be punished, nor souls to be condemned . . . ." OXFORD DICTIONARY OF QUOTATIONS 550 (1979). Thurlow also famously said, "Did you ever expect a corporation to have a conscience, when it has no soul to be damned, and no body to be kicked?" MERVYN KING, PUBLIC POLICY AND THE CORPORATION 1 (1977).

154. THOMAS F. BURKE, LAWYERS, LAWSUITS, AND LEGAL RIGHTS: THE BATTLE OVER LITIGATION IN AMERICAN SOCIETY 3–4 (2002); ROBERT A. KAGAN, ADVERSARIAL LEGALISM: THE AMERICAN WAY OF LAW 3 (2001).

155. BURKE, *supra* note 154, at 3.

156. *See id.* ("[S]ome studies suggest that those supposedly stoic pioneers of frontier America were far more inclined to sue than their allegedly litigation-loving descendants.").

of procedural advantages unmatched in the courts of many other nations because they include civil juries, broad discovery privileges, broader access to courts and lawyers, contingent fee arrangements, and the absence of "loser-pays" cost-shifting rules.[158] American legal culture is likewise rich in constitutional, statutory, and common law jurisprudence that generates an abundance of personal rights and facilitates the litigation necessary to protect them.[159] Perhaps this explains why approximately 92 million lawsuits are filed each year in the United States.[160] Nearly 70,000 of these are liability suits, whereas—for the sake of comparison—only 200 liability suits are filed annually in the United Kingdom.[161]

The U.S. legal culture, however, is not merely preoccupied with providing plaintiffs access to the courts. It is also deeply concerned with the aggressive punishment of convicted wrongdoers. As Marie Gottschalk explains, "[T]he United States . . . has built a carceral state that is unprecedented among Western countries[,] . . . distinguish[ed] [by] the sheer size of its prison and jail population; its reliance on harsh, degrading sanctions; and the persistence and centrality of the death penalty."[162] The proportion of adults behind bars is higher in the United States than in any other nation of the world.[163] And as James Whitman notes, relative to the legal systems of Europe, "America's legal system is harsher . . . in all respects [because]

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157. *See* SARAH JOSEPH, CORPORATIONS AND TRANSNATIONAL HUMAN RIGHTS LITIGATION 16 (2004) (noting the many "unique causes of action available in [the United States], as well as the distinctive plaintiff-friendly nature of the US legal system").

158. Linda J. Silberman, *Developments in Jurisdiction and Forum Non Conveniens in International Litigation: Thoughts on Reform and a Proposal for a Uniform Standard*, 28 TEX. INT'L L.J. 501, 502 (1993).

159. Rogers M. Smith, *Rights*, *in* A COMPANION TO AMERICAN THOUGHT 595, 595–98 (Richard Wrightman Fox & James T. Kloppenberg eds., 1995) (observing that the United States began as the culmination of claims for British recognition of individual and collective American rights, that Americans have made many rights claims through much of U.S. history, and that American courts and legislatures continue to play an essential role in securing those rights).

160. DAVID W. NEUBAUER, AMERICA'S COURTS AND THE CRIMINAL JUSTICE SYSTEM 411 (2004).

161. PETER W. HUBER & ROBERT E. LITAN, THE LIABILITY MAZE: THE IMPACT OF LIABILITY LAW ON SAFETY AND INNOVATION 47 (1991).

162. MARIE GOTTSCHALK, THE PRISON AND THE GALLOWS: THE POLITICS OF MASS INCARCERATION IN AMERICA 1 (2006). Gottschalk continues: "Nearly one in fifty people in the United States, excluding children and the elderly, is behind bars today." *Id.* Gottschalk argues that America's punitive penal policy is the product of several forces, including uniquely American historical events. *Id.* at 4.

163. *Id.* at 1. The incarceration rate in the United States has increased more than five-fold since 1973. *Id.*

America criminalizes a wider variety of conduct than Europe does[,] . . . subjects more classes of people to potential criminal liability[,] . . . [and] the punishments it imposes are far less flexible and less individualized . . . ."[164] Additionally, American laws are more detailed, complex, and prescriptive than those of many countries, and U.S. legal penalties are often more severe.[165] The rate of incarceration in the United States is the highest in the industrialized world, and public opinion polls indicate that Americans are becoming increasingly likely to support punitive measures like "three strikes" sentencing laws.[166] Relative to the laws of many other nations, U.S. law has trended toward ever-increasing harshness in its criminal policies.[167]

For example, in *Roper v. Simmons*,[168] Justice John Paul Stevens opined on "the stark reality that the United States is the only country in the world that continues to give official sanction to the juvenile death penalty."[169] Although the Supreme Court went on to hold that the execution of individuals who were under the age of eighteen when they committed capital crimes is unconstitutional,[170] the U.S. legal culture continues to be infused with retributivist justifications for criminal punishment.[171]

Less severe forms of punishment than the death penalty likewise characterize a brand of retribution that is unmistakably American. It has been estimated that the amount of taxpayer dollars paid in tort punitive damages is 2.5 percent of the gross national product in the

164. Daniel Statman, *The Historical and Cultural Roots of Harsh Punishment*, 17 YALE J.L. & HUMAN. 299, 299–300 (2005) (reviewing JAMES Q. WHITMAN, HARSH JUSTICE: CRIMINAL PUNISHMENT AND THE WIDENING DIVIDE BETWEEN AMERICA AND EUROPE (2003)).

165. KAGAN, *supra* note 154, at 3.

166. *Id.*

167. WHITMAN, *supra* note 164, at 3.

168. Roper v. Simmons, 543 U.S. 551 (2005).

169. *Id.* at 575.

170. *Id.* at 574.

171. *See, e.g.*, Spaziano v. Florida, 468 U.S. 447, 461 (1984) (noting retributivism is the "primary justification for the death penalty"); Guyora Binder & Nicholas J. Smith, *Framed: Utilitarianism and Punishment of the Innocent*, 32 RUTGERS L.J. 115, 117 (2000) (attributing the decline of probation and parole in the American justice system to retributivism); Robert J. Cottrol, *Hard Choices and Shifted Burdens: American Crime and American Justice at the End of the Century*, 65 GEO. WASH. L. REV. 506, 507–08 (1997) (book review) ("[S]ince the mid-seventies retribution has come back with a vengeance, enjoying today a greater prominence in public discourse over crime and punishment than at any other time in post-war America.").

United States, compared to 0.5 percent in the United Kingdom.[172] Additionally, although "three-strikes" laws, mandatory minimum sentences, and "truth in sentencing" laws are often criticized for being excessively punitive, U.S. lawmakers have been undeterred from making them available to courts across the United States.[173]

In light of these distinctively American notions of rights, adequate due process in the courts, and retributive punishment, a soft law system built solely on principles and "best practices" appears completely incompatible with American legal culture. Under a principles-based regime like the Combined Code, shareholders may only punish the corporation by moving their assets elsewhere. But if the corporation is viewed through the lens of American culture as an immoral "person" that has committed fraud or gross negligence leading to significant losses in shareholder investments, then the corporation must be punished directly. Once a shareholder's funds are lost, punitive justice will not be served by transferring the remainder of that shareholder's shares elsewhere. Hence, without rules, without hard law that prohibits transgression and justifies its reprimand, no punishment that satisfies the American cultural sense of retributivist justice can be meted out. Principles-based regulation is therefore anathema to deeply seated and quintessentially American notions of retributivist punishment for immoral acts.

CONCLUSION

American financial and political leaders have assessed the feasibility of overhauling the U.S. regulatory framework of corporate governance by adopting a more principles-based approach. Many of these leaders believe this overhaul would create something similar to and perhaps patterned after the United Kingdom's Combined Code. This Note has argued that this aspiration is fundamentally flawed and patently impractical. America's longstanding, firmly fixed fear of corporate excesses, combined with its strong cultural disdain for corporate misbehavior and its espousal of just deserts punishment, make it highly unlikely the American public and their representatives in Congress would ever replace legislative rules with "best practices"

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172. *Punitive Damages: Tort Reform & FDA Defense: Hearing on S. 671 and S. 672 Before the S. Comm. on the Judiciary*, 104th Cong. 112 (1995) (statement of Theodore Olson).

173. HENRY M. WROBLESKI & KAREN M. HESS, INTRODUCTION TO LAW ENFORCEMENT AND CRIMINAL JUSTICE 467 (8th ed. 2006).

principles. Moreover, even if principles were to find a foothold in U.S. corporate regulation, the consistent history of aggressive congressional responses to corporate misdeeds and collapses suggests that once the first corporate crisis surfaced, Congress would eradicate those principles with aggressive and prophylactic rules-based regulation.