Articles

JAMES D. COX: THE SHAREHOLDERS' BEST ADVOCATE

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ABSTRACT

This Article explores the historical development of the academic analysis of corporate law over the past forty years through the scholarship of one of its most influential commentators, Professor James D. Cox of the Duke University School of Law. It traces the ways in which corporate law scholarship changed from the 1970s to the present, including the rise of economic theory and empirical work in the study of corporate law. It shows how Professor Cox's early scholarship shaped and challenged economic orthodoxy, while his later work used empirical analysis to help corporate law become a more dynamic and richer field.

Throughout his career, Professor Cox's scholarship has focused on the protection of shareholder rights. He has rebuffed contractarians' attacks on shareholder protections using a variety of economic, psychological, and empirical techniques. Professor Cox's support for investors has continued in the wake of financial-market crises, corporate scandals, and the challenges of globalization. He provides an outstanding example of how a thoughtful academic can influence theories and market conditions with several decades of valuable insights.

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INTRODUCTION

Over the past forty years, corporate law scholarship has produced wide-ranging, penetrating, and sophisticated analysis on par with any field in the legal academy.[1] Spurred by the law and economics revolution of the 1970s—which prompted varied research, expansive in scale and international in scope[2]—corporate law scholars have joined the vanguard of interdisciplinary analysis within the academy.[3] Even as it has pushed corporate law in new directions, this intellectual revolution has also reinvigorated longstanding questions that corporate law has yet to satisfactorily resolve, questions made all the more pressing by the transformation of the corporate economy over the past forty years: For whom should the corporation be run? Are those who run the corporation sufficiently accountable? How should these answers change as our presumptions about the corporate, economic, and political worlds shift?

This Article examines the development of modern-day corporate law by examining the career of a remarkable man Professor James D. Cox whose scholarship over his forty-five years in the academy has had a profound influence.[4] Cox began as a teaching fellow at Boston University School of Law in 1970 and—after a series of rapid promotions at other law schools—joined the Duke Law faculty in 1979, where he has remained. A central figure in the field of corporate law, Cox's career illuminates the transformation of the field as intellectual, economic, political, and technological changes rendered obsolete old frameworks and demanded new legal responses.

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1. For examples of works addressing the changes in corporate law scholarship over the past four decades, see BRIAN R. CHEFFINS, THE TRAJECTORY OF (CORPORATE LAW) SCHOLARSHIP: AN INAUGURAL LECTURE GIVEN IN THE UNIVERSITY OF CAMBRIDGE OCTOBER 2003, at 38–82 (2004); Matthew T. Bodie, *The Post-Revolutionary Period in Corporate Law: Returning to the Theory of the Firm*, 35 SEATTLE U. L. REV. 1033, 1040–52 (2012); William W. Bratton, Jr., *The New Economic Theory of the Firm: Critical Perspectives from History*, 41 STAN. L. REV. 1471, 1498 (1989); Roberta Romano, *After the Revolution in Corporate Law*, 55 J. LEGAL EDUC. 342, 347, 349–51 (2005).

2. *See, e.g.*, Richard A. Epstein, *Law & Economics: Its Glorious Past and Cloudy Future*, 64 U. CHI. L. REV. 1167, 1172 (1997) ("[T]he rate of intellectual return on relatively straightforward problems was exceedingly high."); *see also* Tracey E. George, *An Empirical Study of Empirical Legal Scholarship: The Top Law Schools*, 81 IND. L.J. 141, 141–42, 145–47, 158 (2006) (tracking the emergence of empiricism across the legal academy).

3. *See generally* Sanjai Bhagat & Roberta Romano, *Events Studies in the Law* (pts. 1 & 2), 4 AM. L. & ECON. REV. 141 (2002) (providing examples and explaining the emergence of corporate law empirical studies).

4. For Professor Cox's biography, see *James D. Cox*, DUKE LAW, https://law.duke.edu/fac/cox [https://perma.cc/E89A-GFZL].

Cox has written on a variety of topics, but a central theme running through his work has been the protection of shareholders. In the 1980s and 1990s, he made his mark as a scholar by challenging the contractarian approach to corporate law, viewing this legal-intellectual innovation as a threat to the protection of shareholders.[5] In the new millennium, he has continued to support shareholder rights in the face of new threats as corporate scandals, globalization, and the global financial crisis posed new problems to traditional means of defending shareholders.[6] Cox's work has been innovative as well as traditional. Although he was often skeptical of some new trends, his scholarship incorporated recent developments in economics, psychology, and later empirical methods, and he drew attention to overlooked issues of organizational culture, while still demonstrating the value of more traditional doctrinal and analytical approaches to legal scholarship. In so doing, he provided a model for how careful legal scholarship can address new ideas and situations.

This Article describes the development of corporate law scholarship from the 1930s to the present and Cox's influence on it. Part I explains the transition from Berle and Means's trust paradigm, to the rise of contractarianism, to the eventual counterreaction against contractarianism. It focuses on four of Cox's articles that responded to the underlying assumptions and implications of contractarianism. Part II evaluates the evolution of legal scholarship as the contractarian battles stalemated. It begins with four of Cox's pieces in which he analyzes the importance of accounting standards and the role of gatekeepers, and then discusses several of his recent empirical legal studies.

I. FROM BERLE AND MEANS TO JENSEN AND MECKLING

A. *Berle and Means and the Trust Paradigm*

Modern corporate law scholarship began with Professors Adolf Berle and Gardiner Means's seminal book, *The Modern Corporation and Private Property*, which identified the central issue of corporate law as the "separation of ownership and control," by which the dispersal of share ownership effectively removed control of the public corporation from its putative owners, the shareholders, and gave it to

5. *See infra* Part I.C.
6. *See infra* Part II.A.

its managers.[7] This development, left unchecked, would have freed managers from oversight and enabled managerial self-dealing.[8] Professor William Bratton explains that the remedy proposed by Berle and Means for such unfettered managerial power is that there "should be a pervasive equitable limitation on power granted to corporate management" under which management's power could only be exercised "for the pro-rata benefit of all shareholders."[9] Following this "trust paradigm" for corporate law, the judge's role in corporate law would be to scrutinize management and use their equitable powers to provide "solutions to problems that demanded a remedy."[10] Although the details of this view changed over time, for forty years, the belief that the power imbalance between shareholders and managers was a problem, and that the solution was increased oversight and regulation of one form or another, constituted the dominant framework for corporate law scholarship.[11]

In the early 1970s, when Cox entered the academy, perhaps the ablest defender of this view was Professor Melvin Eisenberg.[12] Eisenberg's pathbreaking work, *The Structure of the Corporation*, stands as a high-water mark for the trust-paradigm-inspired legal scholarship.[13] In this work, Eisenberg identified the main shortcomings

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7. ADOLF A. BERLE, JR. & GARDINER C. MEANS, THE MODERN CORPORATION AND PRIVATE PROPERTY 4 (1932). On whether or not this prescription was correct, see Brian R. Cheffins & Steven Bank, *Is Berle and Means Really a Myth?*, 83 BUS. HIST. REV. 443, 466–67 (2009).

8. To be clear, the exact stance taken by the authors of *The Modern Corporation and Private Property* is complicated. Although much of the work is an attack on unfettered managerial power, in at least one famous passage, it welcomes such managerial freedom, looking forward to a day when management could evolve into a "neutral technocracy" that would manage the corporation for the interests of multiple constituencies. *See* BERLE & MEANS, *supra* note 7, at 312–13; *see also* William W. Bratton & Michael L. Wachter, *Tracking Berle's Footsteps: The Trail of* The Modern Corporation*'s Last Chapter*, 33 SEATTLE U. L. REV. 849, 861–62 (2010) (explaining Berle's view that, because public opinion directly affected managers, the outside community could impose a "conscience" on the corporation).

9. William W. Bratton, *An Anatomy of Corporate Legal Theory*, 24 RES. L. & ECON. 21, 30 (2009); *see* Adolf A. Berle, *Corporate Powers as Powers in Trust*, 44 HARV. L. REV. 1049, 1049 (1931).

10. *See* Bratton, *supra* note 9, at 31. Of course, the trust paradigm was significantly modified over the years, and even if corporate law's trust paradigm left space for managerial self-interest, it never approximated trust-law doctrine. *See* Bratton, *supra* note 1, at 1498.

11. *See* CHEFFINS, *supra* note 1, at 40–49.

12. Cox would later join Eisenberg in his classic business organizations casebook. *See* MELVIN ARON EISENBERG & JAMES D. COX, BUSINESS ORGANIZATIONS: CASES AND MATERIALS (11th unabr. ed. 2014).

13. MELVIN A. EISENBERG, THE STRUCTURE OF THE CORPORATION (1976). The book expounds upon and refines the work of several of Eisenberg's earlier articles: Melvin Aron

of the existing law as its failure to map the realities of the public corporation[14] and its consequent inability to provide a coherent framework that would "protect the legitimate interests of shareholders" while still ensuring the corporation's efficient management.[15] In some ways, the work was prescient, as when it called for independent monitoring boards and identified institutional investors as potential active players in corporate governance.[16]

That said, its solutions fit comfortably within the existing paradigm, inasmuch as they were to be incorporated into the mandatory framework of corporate law.[17] Eisenberg's solution called for governmental interventions to solve the problems first sketched by Berle and Means, specifically the problem of managerial "wrongdoing or impropriety" and the need to protect shareholders.[18] Eisenberg's specific proposals included improving shareholder access to the proxy machinery, creating mechanisms to preserve and empower certain types of noncontractual private ordering, and regulating the work of auditors and independent directors.[19]

B. The Rise of the Contractarians

As Cox began his career, the "contractarian" revolution in corporate law loomed. The contractarians were a group of corporate law scholars influenced by the spreading law and economics movement, who picked up an ideological baton first carried by Henry Manne.[20] In a series of articles starting in the early 1960s, Manne had

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Eisenberg, *Access to the Corporate Proxy Machinery*, 83 HARV. L. REV. 1489 (1970); Melvin Aron Eisenberg, *Legal Models of Management Structure in the Modern Corporation: Officers, Directors, and Accountants*, 63 CALIF. L. REV. 375 (1975); Melvin Aron Eisenberg, *Megasubsidiaries: The Effect of Corporate Structure on Corporate Control*, 84 HARV. L. REV. 1577 (1971); Melvin Aron Eisenberg, *The Legal Roles of Shareholders and Management in Modern Corporate Decisionmaking*, 57 CALIF. L. REV. 1 (1969); *see also* Bratton, *supra* note 9, at 30–32 (discussing generally the trust paradigm of corporate law advocated by Berle and Means).

14. *See* EISENBERG, *supra* note 13, at 18.

15. *Id*. at 319.

16. *See id*. at 56–63, 156–69.

17. *See id*. at 317–18.

18. David L. Ratner, Book Review, 64 CALIF. L. REV. 1484, 1488 (1976) (reviewing EISENBERG, *supra* note 13).

19. EISENBERG, *supra* note 13, at 317–20.

20. *See* Harwell Wells, *"Corporation Law is Dead": Heroic Managerialism, Legal Change, and the Puzzle of Corporation Law at the Height of the American Century*, 15 U. PA. J. BUS. L. 305, 307 n.3, 355 (2013).

been witheringly critical of Berle and Means.[21] Berle and Means had concluded that, without legal intervention and judicial oversight, the separation of ownership and control would enable managers to self-deal and injure shareholders, often with impunity—a conclusion present as well in Eisenberg's work. Manne vehemently disagreed. Why, he asked, would investors continue to invest in equity markets if managers were as unaccountable as Berle, Means, and their followers claimed?[22] Manne's answer was that shareholders were already well-protected. Existing market constraints—most notably the market for corporate control—served as effective limits on managerial graft and overreach.[23] Good, efficient managers correlated to strong returns for healthy companies, and poor, ineffective managers produced weak returns.[24] Stock prices would reflect whether the managers were good or not, enabling the market for mergers to oust poor managers and shift those underperforming assets into the hands of better managers, with shareholders benefiting from the consolidation.[25] For Manne, the market, not mandatory rules for corporate governance, provided the best protections for shareholders.

Although Manne struggled to be heard in the 1960s and early 1970s, by the late 1970s, his critique gained traction, partially due to the emergence of transaction-cost-based economic scholarship,[26] which in turn was heavily influenced by Professor Ronald Coase. In his classic

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21. *See, e.g.*, Henry G. Manne, *The "Higher Criticism" of the Corporation*, 62 COLUM. L. REV. 399, 399–407 (1962); *see also* Henry G. Manne, *Mergers and the Market for Corporate Control*, 73 J. POL. ECON. 110, 117–20 (1965) [hereinafter Manne, *The Market for Corporate Control*] (addressing Berle's contention that control is a corporate asset); Henry G. Manne, *Some Theoretical Aspects of Share Voting*, 64 COLUM. L. REV. 1427, 1431 n.13 (1964) (stating that the Berle and Means thesis of ownership and control "fits foundations, universities, and other nonprofit organizations far better than it does the large corporation in which it was designed").

22. Henry G. Manne, *The Myth of Corporate Responsibility or Will the Real Ralph Nader Please Stand Up?*, 26 BUS. LAW. 533, 534 (1970). Manne states:

> [I]f things were as Berle believed, it is very difficult to understand why 30 million Americans would continue to put money into the hands of corporate executives . . . . We would have to assume that American investors were either the greatest collection of fools the world had ever seen or that they were charitable to a degree that even saints could not aspire to.

Id.

23. *See* Manne, *The Market for Corporate Control*, *supra* note 21, at 117–20.

24. *See id.*

25. *See id.*

26. *See* Romano, *supra* note 1, at 347, 349–51. *But see* William J. Carney, *The Legacy of "The Market for Corporate Control" and the Origins of the Theory of the Firm*, 50 CASE W. RES. L. REV. 215, 227, 231–33, 238–44 (1999) (arguing that Manne's ideas influenced this field of study and the courts through the late 1960s and early 1970s, before his ideas spread more widely through the academy).

article *The Nature of the Firm*, Coase sought to address the question of "why a firm emerges at all in a specialized exchange economy."[27] Coase presented his theory as a tradeoff between the benefits of market exchanges, in which an entity would choose a contractual relation with an outside party, against internal firm exchanges, in which the hierarchical firm structure was preferred.[28] In showing how contracting costs help explain firm formation, Coase provided legal academics a glimpse inside the "black box" of the firm.[29]

In 1976, Professors Michael Jensen and William Meckling operationalized Coase's views of the "black box" for the legal academy.[30] Using the familiar paradigm from Berle and Means—centered on the separation of ownership from control—Jensen and Meckling provided "systematic economic content" to the earlier observations by couching their studies in marginal utility and introducing agency-cost theory into their analysis.[31] Jensen claimed that this sort of economic analysis would rapidly permeate the field.[32] And as economic theory expanded from market applications to judicial decisionmaking[33] to corporate law scholarship, Jensen's claim seemed accurate.[34]

Undoubtedly the most influential work applying law and economics to corporate law was that of Judge Frank Easterbrook and Professor Daniel Fischel. In a series of articles—and then their classic book *The Economic Structure of Corporate Law*—they effectively founded the contractarian school, blazing a trail for later law and

27. Ronald Coase, *The Nature of the Firm*, 4 ECONOMICA 386, 390 (1937).

28. *Id.*; *see* Jason Scott Johnston, *The Influence of* The Nature of the Firm *on the Theory of Corporate Law*, 18 J. CORP. L. 213, 214 (1993).

29. Johnston, *supra* note 28, at 215–16.

30. Michael Jensen & William Meckling, *Theory of the Firm: Managerial Behavior, Agency Costs & Ownership Structure*, 3 J. FIN. ECON. 305 (1976).

31. *See* CHEFFINS, *supra* note 1, at 44–45; Romano, *supra* note 1, at 347.

32. Michael C. Jensen, *Organization Theory & Methodology*, 58 ACCT. REV. 319, 324 (1983).

33. Richard A. Posner, *Some Uses and Abuses of Economics and Law*, 46 U. CHI. L. REV. 281, 294 (1979).

34. Frank H. Easterbrook & Daniel R. Fischel, *The Proper Role of a Target's Management in Responding to a Tender Offer*, 94 HARV. L. REV. 1161 (1981). Easterbrook and Fischel's work would become the most-cited article of the 1980s and the twenty-fourth most-cited article of all time as of 1996. Fred R. Shapiro, *The Most-Cited Law Review Articles Revisited*, 71 CHI.-KENT L. REV. 751, 761, 765 (1996). Their work trails only Manne's *Mergers and the Market for Corporate Control* amongst corporate works for citations, and is one of only three corporate law pieces in the top one hundred most-cited law review articles. *Id.*

economics scholars.[35] Beginning in 1981 with *The Proper Role of a Target's Management in Responding to a Tender Offer*, Easterbrook and Fischel supplemented legal analysis with an empirical study of stock prices and market mechanisms.[36] They not only showed how certain transactions created value but also how market-based "self-deterring" mirrored and buttressed corporate law.[37] In doing so, their work also presented a powerful presumption that ran counter to much of corporate law scholarship up until that point: rather than require further regulation, corporate entities would, on their own, select their own governance to the point that it was efficient and profitable.[38] As one reviewer of their book noted, in Easterbrook and Fischel's account, corporate law already provided participants in the corporation the protection they needed, and "the need for legal reforms and government regulation goes out the window."[39]

By the mid-1980s, the "prairie fire" of law and economics analysis—particularly its contractarian version, which depicted the corporation as a mere "nexus of contracts"—had swept through the academy.[40] This analysis helped explain existing market-actor behavior,[41] while deemphasizing shareholder protection as a core function of corporate law. In characterizing corporate law as enabling

35. For a more complete accounting of their groundbreaking work, see generally FRANK H. EASTERBROOK & DANIEL R. FISCHEL, THE ECONOMIC STRUCTURE OF CORPORATE LAW (1991); Frank H. Easterbrook & Daniel R. Fischel, *Auctions and Sunk Costs in Tender Offers*, 35 STAN. L. REV. 1 (1982); Frank H. Easterbrook & Daniel R. Fischel, *Close Corporations and Agency Costs*, 38 STAN. L. REV. 271 (1986); Frank H. Easterbrook & Daniel R. Fischel, *Corporate Control Transactions*, 91 YALE. L.J. 698 (1982) [hereinafter Easterbrook & Fischel, *Corporate Control Transactions*]; Frank H. Easterbrook & Daniel R. Fischel, *Limited Liability and the Corporation*, 52 U. CHI. L. REV. 89 (1985); Frank H. Easterbrook & Daniel R. Fischel, *Mandatory Disclosure and the Protection of Investors*, 70 VA. L. REV. 669 (1984); Frank H. Easterbrook & Daniel R. Fischel, *Optimal Damages in Securities Cases*, 52 U. CHI. L. REV. 611 (1985); Frank H. Easterbrook & Daniel R. Fischel, *The Corporate Contract*, 89 COLUM. L. REV. 1416 (1989); Frank H. Easterbrook & Daniel R. Fischel, *Voting in Corporate Law*, 26 J.L. & ECON. 395 (1983).

36. *See supra* notes 34–35 and accompanying text.

37. *E.g.*, Easterbrook & Fischel, *Corporate Control Transactions*, *supra* note 35, at 707.

38. *See, e.g.*, Bratton, *supra* note 9, at 34–35 (discussing the "deregulatory presumption" in modern corporate law and the prevalence of self-regulating strategies).

39. Lyman Johnson, *Individual and Collective Sovereignty in the Corporate Enterprise*, 92 COLUM. L. REV. 2215, 2222 (1992).

40. CHEFFINS, *supra* note 1, at 28 (quoting Douglas Branson, *A Corporate Paleontologist's Look at Law and Economics in the Seventh Circuit*, 65 CHI.-KENT L. REV. 745 (1989)).

41. *See generally* Bhagat & Romano, *supra* note 4 (listing examples of empirical studies that incorporate economic research and explain topics as diverse as the value of minority shareholder voting rights, the emergence of "corporate specialization," the overpayment of bidders, the synergistic gains of corporate-acquiring firms, and the effectiveness of antitakeover amendments).

law that conformed to economic rationality rather than mandatory law that imposed strictures on the self-interested, the contractarian school implicitly validated the present structures of corporate law and pushed for fewer mandatory provisions in the law. By the end of the decade, it was clear that the value judgment presented in Berle and Means's original work—that separation of ownership from control was a problem in need of a solution—was no longer treated as gospel.[42] To some, it just sounded like a plea to retain the status quo.[43]

C. The Response to Contractarianism

Although a majority of academics conceded the general merits of economic and other social-science-based methods of analysis, many sharply disputed the contractarians' conclusions.[44] Eisenberg was one of the most prominent critics. Having been the profession's leading voice for continuing the work started by Berle and Means, he struggled to use the new tools of economics, and his work was sharply challenged by many of the new school of corporate scholars throughout the 1980s.[45]

In important corners of the profession, however, Eisenberg's arguments were being echoed. Authors like William Allen,[46] Victor

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42. William W. Bratton, *The Economic Structure of the Post-Contractual Corporation*, 87 NW. U. L. REV. 180, 190 (1992); *see also* Robert John Schulze, Book Note, *Can This Marriage Be Saved? Reconciling Progressivism with Profits in Corporate Governance Laws*, 49 STAN. L. REV. 1607 (1997) (reviewing PROGRESSIVE CORPORATE LAW (Lawrence E. Mitchell ed., 1995)) (challenging a series of critiques of the corporate law theory paradigm).

43. It should be noted that law and economics approaches need not result in the antiregulatory conclusions reached by Easterbrook and Fischel—hence the need to distinguish between their version of contractarianism and broader approaches to economic theory. For a different take focusing on the theory of the firm, see Bodie, *supra* note 1.

44. *See, e.g.*, John C. Coffee, Jr., *The Mandatory/Enabling Balance in Corporate Law: An Essay on the Judicial Role*, 89 COLUM. L. REV. 1618, 1626 (1989) ("[T]he permissibility of deviations from the traditional standards of corporate law should be judged primarily in terms of the competence of courts or other agencies to monitor these departures and prevent opportunism."); Melvin Aron Eisenberg, *New Modes of Discourse in the Corporate Law Literature*, 52 GEO. WASH. L. REV. 582, 589–90, 595–97 (1984); *id.* at 595 ("[I]t is extremely unlikely that market forces acting alone will produce an optimal solution of agency-cost problems in the context of the publicly held corporation."); Jeffrey N. Gordon, *The Mandatory Structure of Corporate Law*, 89 COLUM. L. REV. 1549, 1585–98 (1989) (highlighting the importance of corporate law legal rules created by the courts and the legislature).

45. For an example of this type of critique, see generally Ralph K. Winter, *The "Race for the Top" Revisited: A Comment on Eisenberg*, 89 COLUM. L. REV. 1526 (1989).

46. William T. Allen, *Our Schizophrenic Conception of the Business Corporation*, 14 CARDOZO L. REV. 261, 278 (1992) ("To approach understanding, we must be able to see legal rules and principles as social constructs, affected by their internal logic, but affected even more profoundly by the social world in which they exist.").

Brudney,[47] and John Coffee[48] raised similar critiques about the lack of normative values presented by those in the law and economics space.[49] These critiques increased when the law and economics school eventually attempted to assert certain normative values by using market discipline.[50] Gradually, these anticontractarian critics challenged the contractarians' assumptions by using the contractarians' own law and economics tools.[51] Some assumptions were questioned on theoretical grounds;[52] others were proven incorrect in practice.[53]

Beginning in the 1980s, Cox joined the challenge to the rapid expansion of contractarianism and its underlying behavioral assumptions. In so doing, he provided new and innovative defenses of the belief that shareholders still needed protection by the mechanisms of corporation law. Here, we briefly outline some of his more important pieces from this period and explain their significance in the debates.

1. *Bias in the Boardroom.* In the pathbreaking article *Bias in the Boardroom*, Cox and his coauthor, Professor Harry Munsinger, draw on psychological research about insider bias to challenge the

47. Victor Brudney, *The Role of the Board of Directors: The ALI and its Critics*, 37 U. MIAMI L. REV. 223, 235 (1983).

48. John C. Coffee, Jr., *The Uncertain Case for Takeover Reform: An Essay on Stockholders, Stakeholders and Bust-Ups*, 1988 WIS. L. REV. 435, 439.

49. For an overview of these debates, see generally Symposium, *The Debate on Contractual Freedom in Corporate Law*, 89 COLUM. L. REV. 1395 (1989).

50. *See* Johnston, *supra* note 28, at 241 (describing the values of the law and economics school). According to Johnston:

> [T]he explanatory power of the economic approach to corporate law . . . derives very largely from the fact that this approach is a theory of what competitive forces should eventually, in the long run, constrain rational economic actors to do. Under such an approach, the pattern of corporate governance structures which we observe at any point in time . . . are presumed to be efficient, equilibrium choices, because in the long run, only such choices will survive.

Id.

51. Lawrence E. Mitchell, *A Theoretical and Practical Framework for Enforcing Corporate Constituency Statutes*, 70 TEX. L. REV. 579, 583–84 (1992).

52. *E.g.*, Nancy Levit, *Listening to Tribal Legends: An Essay on Law and the Scientific Method*, 58 FORDHAM L. REV. 263, 266–72 (1989); Mark V. Tushnet, *Law, Science, and Law and Economics*, 21 HARV. J.L. & PUB. POL'Y 47, 51–52 (1997).

53. *E.g.*, Robert B. Thompson, *Piercing the Corporate Veil: An Empirical Study*, 76 CORNELL L. REV. 1036, 1059 (1991) (noting that, contrary to what law and economics theorists hypothesized, in practice, veil piercing of limited-liability corporations occurred more regularly in contractual rather that tort settings).

contractarians' rational-actor model of human behavior.[54] They focus on a topic that Cox would repeatedly return to: the shareholder derivative action. The article begins by asking how much we can rely upon independent directors to monitor corporate management and each other.[55] The widely accepted, economically oriented-Jensen and Meckling-monitoring model of the corporation had assumed that independent directors would do this, acting in shareholders' best interests.[56]

Drilling into this assumption, Cox and Munsinger questioned its accuracy. They offered "a psychological perspective on a specific application of the monitoring function: the independent directors' assessment [of] whether the corporation's interest is served by a derivative suit against their 'insider' colleagues."[57] In particular, the authors focused on independent directors' ability to perceive and represent the corporation's interests in evaluating a demand on the board or when serving on a special litigation committee (SLC). They concluded that "several psychological mechanisms can be expected to generate subtle, but powerful, biases which result in the independent directors' reaching a decision insulating colleagues on the board from legal sanctions."[58]

The heart of the article lays out the psychological research related to in-group bias, which is especially problematic within the boardroom. The article focuses on uncertainty and director bias,[59] social needs and director service,[60] and self-validation and director bias.[61] The authors apply these concepts to suggest that there is a strong bias in the

54. James D. Cox & Harry L. Munsinger, *Bias in the Boardroom: Psychological Foundations and Legal Implications of Corporate Cohesion*, 48 LAW & CONTEMP. PROBS. 83 (1985).

55. *See id.* at 84 ("We are interested in the independent directors' ability to perceive and represent the corporate interest in evaluating a demand to the board or in serving on a special litigation committee.").

56. *See generally* Michael Jenson & William H. Meckling, *Theory of the Firm: Managerial Behavior, Agency Costs and Ownership Structure*, *in* THE MODERN THEORY OF CORPORATE FINANCE (Michael C. Jensen & Clifford H. Smith Jr. eds., 1984) (laying out the monitoring model of the corporation). In fairness, Eisenberg made almost the same assumption. *See* EISENBERG, *supra* note 13, at 174–77 (noting that independent directors had to be "independent in fact as well as in form").

57. Cox & Munsinger, *supra* note 54, at 84.

58. *Id*. at 85.

59. *Id.* at 85–91.

60. *Id.* at 91–99.

61. *Id.* at 99–108.

boardroom against plaintiff shareholders and that even outside directors cannot be expected to operate impartially.[62]

Bias in the Boardroom then connects its criticism of the academic theory to the problems with then-current doctrine by examining the analytical approaches for SLC reports offered by courts and the American Law Institute's (ALI) Corporate Governance Project.[63] It dissects the leading cases on the appropriate standard of judicial review for SLC reports and rejects each one.[64] The authors advocated both for having court-appointed members of the SLC and for disallowing the committee's recommendation whenever it "implicates a colleague of the directors, be that colleague a fellow director, control person, or a senior executive who associates on a regular basis with the directors."[65] They conclude that SLC should be appointed by the court and should not include any of the defendants' colleagues, past or present, or even those sharing a cultural identity with the defendants.[66]

This key article was widely seen as offering a new and insightful critique of the use of SLCs and their impact on shareholder litigation.[67] By bringing the tools of psychology to bear, Cox and Munsinger offer insights that law and economics scholarship missed. Equally important, they provide a sophisticated critique of the view that market forces and existing corporate law sufficed in providing adequate shareholder protection.

2. *Insider Trading and Contracting: A Critical Response to the "Chicago School."* Nowhere is Cox's resistance to contractarianism more apparent than in his article *Insider Trading and Contracting: A Critical Response to the "Chicago School*,*"* which directly tackles Chicago School arguments that favored legalizing insider trading.[68] The article opens by criticizing the deficient grounds that the Supreme Court had previously offered for condemning insider trading as well as the theories that commentators had offered to fill its jurisprudential

62. *Id.* at 107.

63. *See id.* at 108–31.

64. *See id.*

65. *Id.* at 132.

66. *Id.* at 134.

67. *See, e.g.*, Donald C. Langevoort, *Resetting the Corporate Thermostat: Lessons from the Recent Financial Scandals About Self-Deception, Deceiving Others and the Design of Internal Controls*, 93 GEO. L.J. 285, 286 n.6 (2004) (arguing that SLCs are suspect for multiple reasons).

68. James D. Cox, *Insider Trading and Contracting: A Critical Response to the "Chicago School*,*"* 1986 DUKE L.J. 628.

holes, such as the view that insider trading adversely affects the stock market's allocative efficiency.[69] Its main thrust, though, is a direct response to the Chicago School's claims that insider trading should be permitted and that the law should allow corporations to license their officers and directors to engage in it.[70]

Briefly, the Chicago School academics had argued that there was no empirical evidence that insider trading harms anyone.[71] Cox counters that there was no empirical evidence that it is not harmful either and that, as the challengers to the status quo, the proponents of legalization should be required to make such a showing.[72] A second argument for dropping the ban was that insider trading promotes stock-price adjustments.[73] But, as Cox notes, insider trading is a much less efficient way to disclose information than regular corporate filings, and it could lead to disclosures that harm the corporation's interest in withholding some confidential information to preserve its business advantages.[74]

Chicago School scholars had further claimed that allowing insider trading would avoid periodic and wasteful negotiations between the company and managers over compensation by allowing managers to unilaterally reset their compensation.[75] Cox has several responses to this claim, such as: What are the alternative ways for companies to sell their information?[76] Will managers do this in a way that maximizes shareholder value?[77] And will it encourage the creation of valuable information or just lead to self-dealing transactions?[78]

Finally, the proponents of lifting the ban on insider trading argued that managers and stockholders would like to be able to contract for the right to participate in insider trading because that would benefit both sides.[79] This claim's validity turns on the shareholders' ability to

69. *See id*. at 635–42.

70. *See id*. at 642–55.

71. *Id.* at 642. This view of insider trading was widespread. Among the classic works arguing for it were HENRY G. MANNE, INSIDER TRADING AND THE STOCK MARKET (1966), and Dennis W. Carlton & Daniel R. Fischel, *The Regulation of Insider Trading*, 35 STAN. L. REV. 857 (1983).

72. Cox, *supra* note 68, at 644.

73. *Id.* at 645–48.

74. *Id.* at 648.

75. *Id.* at 649–53.

76. *Id.* at 650–51.

77. *Id.* at 651.

78. *Id.*

79. *Id.* at 653–55.

contract efficiently given their information disadvantage. Cox points out that it is difficult for shareholders to estimate the costs and benefits of insider trading, especially in public companies.[80] In addition, corporations have several interests that would be affected by allowing insider trading, including the need to understand the executives' motives and compensation sources, the need for full information to assess the executives' stewardship, and the shareholders' desire that executives concentrate on the welfare of the company rather than their private investment agenda.[81]

3. *Compensation, Deterrence, and the Market as Boundaries for Derivative Suit Procedures*. Cox returned to shareholder litigation in his article *Compensation, Deterrence, and the Market as Boundaries for Derivative Suit Procedures*, which delves into the purpose of the derivative suit.[82] Deterrence and compensation are often mentioned as the twin goals of derivative litigation, but sometimes, as Cox notes, these goals are in conflict.[83] When they do conflict, he asks, how should the conflict be resolved?

Initially, Cox attacks the contractarians' view that derivative suits are unnecessary because market forces are sufficient to police management wrongdoing. He deploys economic analysis to argue that this view is incorrect for several reasons. First, market monitoring only prevents extreme deviations, and the law should impose fiduciary obligations to establish the parameters of mutually acceptable conduct.[84] Second, although portfolio theory suggests that holding a diversified group of stocks eliminates unsystemic risks, managerial-misconduct levels are a form of systemic risk that can be lowered by the deterrence value of derivative suits.[85] Finally, he contends that the market for corporate control is inadequate because there must be massive misconduct to appreciably drive down the stock price, and most of the time, managerial misconduct is only a "one shot" breach of fiduciary duties.[86]

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80. *Id.* at 654.

81. *Id.* at 658–59.

82. James D. Cox, *Compensation, Deterrence, and the Market as Boundaries for Derivative Suit Procedures*, 52 GEO. WASH. L. REV. 745 (1984).

83. *Id.* at 746.

84. *Id.* at 748.

85. *Id.* at 752.

86. *Id.* at 753.

After he establishes the necessity of derivative suits, Cox addresses limitations on these cases that spring from concerns that such suits would lessen shareholders' incentives to monitor managers or impose liability on directors who engage in legitimate risk-taking activities. Here, Cox argues that shareholder monitoring is only economical to a point and that the derivative suit's enforcement of fiduciary duties is necessary to deter managerial misconduct.[87] Furthermore, it does not inhibit risk-taking if courts treat duty-of-care claims as seriously as duty-of-loyalty claims even though the latter are more frequently upheld.[88] Because the two sets of issues are often intertwined, and even though the duty of care is only violated in egregious cases, the duty of care is a minimal standard of legal performance.[89]

Cox argues that courts had overemphasized compensation as a goal for derivative actions, in some cases allowing it to eclipse deterrence altogether. For example, courts dismissed cases in which there was no corporate injury—even if they involved knowing criminal violations—because the corporation benefited from the managers' actions.[90] Cox argues that courts should consider the deterrence benefits from chastening managers by allowing a modest recovery or by ordering corporate-governance changes that would prevent a reoccurrence, even in cases in which no injury can be shown.[91]

Yet the balance can also tip the other way. Cox argues that, in the ALI's then-proposed *Principles of Corporate Governance*, Drafts 1–3, there was too strong a preference for deterrence as a goal for the derivative suit instead of compensation.[92] This had the adverse effect of ignoring important compensatory issues that derivative suits should also address.[93]

4. *The Social Meaning of Shareholder Suits*. Although Cox maintained his scholarly focus on corporate and securities law issues, his wide-ranging response to law and economics led him to draw on economics and psychology and eventually emerging scholarship around social meaning and social norms. In *The Social Meaning of*

87. *Id.* at 758.
88. *Id.* at 760–61.
89. *Id.* at 761–63.
90. *Id.* at 765 n.97.
91. *Id.* at 775–76.
92. *Id.* at 777–79.
93. *Id.* at 777.

Shareholder Suits, Cox examines the public image of shareholder lawsuits, their "expressive value," to determine if there are particular characteristics of class actions and derivative suits that enhance or detract from people perceiving them as a positive social force. [94] The public image of these suits is critical because it determines whether managers will change their behavior if there is a threat of being a defendant in shareholder litigation.[95] Cox uses Professor Lawrence Lessig's techniques for constructing social meaning to determine which features of shareholder litigation are consistent with the process of establishing business-organization norms.[96]

Here, Cox again considers the interaction between deterrence and compensation as goals in shareholder suits. He concluded that compensation is the "prevailing objective of shareholder suits" with "deterrence [as] its valuable byproduct."[97] He argues that this hierarchy of goals dilutes the social meaning of shareholder suits because compensation is a private matter whereas deterrence is a public good.[98] Emphasizing compensation muddies the suits' expression of social values, he claims, weakening the public perception that shareholder suits reflect society's condemnation of the misconduct.[99] Settlements similarly emphasize the private nature of shareholder suits by breaking those suits' link to the state and speaking to the proportionality of the consideration supporting the contract instead of admonishing the company for violating laws and social norms.[100]

Such framing—placing an emphasis on suits' compensatory function—may adversely affect one's image of the suit because leading academics and other lawyers evaluate the suits' success by whether they result in proper compensation for injured parties.[101] Because suits tend to yield low-percentage recoveries for shareholders, they are assessed by many as a failure.[102] This perception of failure is compounded by the fact that Directors and Officers' (D&O) insurance

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94. James D. Cox, *The Social Meaning of Shareholder Suits*, 65 BROOK. L. REV. 3 (1999).

95. *Id.* at 5.

96. *Id.* at 7–8 (citing Lawrence Lessig, *The Regulation of Social Meaning*, 62 U. CHI. L. REV. 943 (1995)).

97. *Id.* at 8.

98. *Id.* at 11.

99. *Id.*

100. *Id.* at 11–12.

101. *Id.* at 13.

102. *Id.* at 14–16.

carriers pay all settlement amounts, so individual managers and directors do not contribute any personal funds for wrongdoing. This tendency to overemphasize compensation is exacerbated by the fact that deterrence is not easily measureable in economic figures, so it is not heavily weighed.

There are ways to change the social meaning of lawsuits. Cox points out that strong pretrial procedures can help create a positive impression of shareholder suits. For example, the Private Securities Litigation Reform Act of 1995 (PSLRA) had such an effect by adding stricter pleading requirements and a discovery bar for securities-fraud class actions, which helped ensure that stronger suits were filed.[103] In contrast, D&O insurance coverage does little to burnish the suits' social meaning. Even though D&O policies have exclusions for intentional misconduct, shareholder suits almost always settle within the amounts of the D&O insurance coverage without any contribution by individual defendants.

Finally, the use of certain rituals may reinforce the positive social meaning of shareholder suits. For instance, under the terms of the PSLRA's "lead plaintiff" provision, courts appoint the lead plaintiff, creating an "important public connection" that also reinforces "the legitimacy of the suit[]."[104] With derivative suits, however, no such process existed at the time *The Social Meaning of Shareholder Suits* was published (although it has since become more prevalent in Delaware[105]), and the court engaged in the demand-requirement inquiry. Settlements in these cases are also problematic in light of social meaning: they are lawyer and insurance driven and "do not reflect the broader private interest of the class or corporation or . . . the public objective of deterrence."[106]

So what can be done to improve the social image of the shareholder suit? First, as Cox suggests, shareholder suits should explicitly elevate the goal of deterrence over that of compensation and call on individual defendants to make contributions to the settlement to increase the suit's deterrence value.[107] Second, they should

103. Private Securities Litigation Reform Act (PSLRA) of 1995, Pub. L. No. 104-67, 109 Stat. 737 (codified as amended in scattered sections of 15 U.S.C.).

104. *Id.* at 29.

105. *See generally* Randall S. Thomas & Robert B. Thompson, *A Theory of Representative Shareholder Suits and Its Application to Multijurisdictional Litigation*, 106 NW. U. L. REV. 1753 (2012) (detailing Delaware's increased popularity as a forum for shareholder litigation).

106. Cox, *supra* note 94, at 34.

107. *See id.* at 39–40.

reinvigorate the adequacy-of-the-plaintiff requirement in derivative suits to make it more like the PSLRA lead-plaintiff determination and provide standing for nonintervenors to object to the settlement and to appeal.[108] Finally, Cox condemns the corrupting influence of the Supreme Court's decision in *Matsushita Electric Industrial Co. v. Epstein*,[109] which promoted forum shopping by defense firms and "weaken[ed] the ritual of settlement."[110]

II. NEW DIRECTIONS

By the end of the 1990s, the battle over contractarianism had stalemated. Law and economics had, it appeared, become almost universally accepted as the central tool for corporate law. But the nexus-of-contracts model of the corporation—and its implicit devaluation of shareholder protection as a central goal of corporate law—had not won over all of its opponents.[111] Economic analysis, many concluded, could serve as a tool to justify legal conclusions but could not, on its own, definitively answer policy questions surrounding corporate accountability and governance.[112] What intellectual coherence could be found formed instead around a set of less sweeping assumptions about corporate law and governance: that boards serve as monitors instead of managers,[113] that investors and boards contract for certain expectations of protection subject to market-based and regulatory frictions,[114] and that those protections have normative decisions attached to them beyond pure profit-seeking motives.[115]

Quite possibly, changes in the corporate economy over the previous two decades had undermined scholars' faith in a single narrative for corporate law, while redirecting scholarly attention toward specific developments and the construction of empirical tools to better understand them. For instance, shifts in the nature of corporate shareholding led to the reconsideration of once-bedrock assumptions about shareholder powerlessness. Shareholders

108. *See id.* at 41–44.

109. Matsushita Elec. Indus. Co. v. Epstein, 516 U.S. 367 (1996).

110. Cox, *supra* note 94, at 38 (citing *Matsushita*, 516 U.S. at 373); *see also* Thomas & Thompson, *supra* note 105, at 1766–67, 1770 (pointing out how *Matsushita* "stimulated multijurisdictional litigation filings" and led to reverse auctions by defense law firms).

111. CHEFFINS, *supra* note 1, at 29.

112. *See* Bratton, *supra* note 42, at 193–97.

113. *See id.* at 186 n.37.

114. *See id.* at 180, 186–90.

115. *See id.* at 212.

increasingly came in "many sizes and shapes,"[116] and as a result, older models of shareholder behavior that presumed diffuse ownership rapidly lost validity.[117] Similarly, questions reemerged about the value of shareholder primacy and its economic desirability.[118] New criticisms also appeared about the presumption that boards behaved rationally to maximize shareholder value[119] and about the processes by which firms determined their organizational boundaries.[120] All the while, new intellectual developments threw into doubt the economic theories underlying much of this legal analysis as behavioral economics emerged from classical microeconomic modeling as a distinct school of thought.[121]

These developments may explain why Cox's interests and most significant publications moved toward closer studies of new developments in the corporate governance system. In the late 1990s, his attention was drawn to questions such as how globalization and technological change challenged shareholder protections,[122] how gatekeepers like the accounting profession could perform their roles in the aftermath of corporate scandals,[123] and how the new tools of empirical legal research could be deployed to answer pressing questions in corporate law.[124]

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116. Jack B. Jacobs, *Some Legal and Policy Implications of the New Shareholder Paradigm*, 22 CORP. GOVERNANCE ADVISOR, Mar./Apr. 2014, at 1, 2.

117. *Id. See generally* Leo. E. Strine, Jr., *The Inescapably Empirical Foundation of the Common Law of Corporations*, 27 DEL. J. CORP. L. 499 (2002) (advocating for corporate law judges to adapt to changing understandings of the business world).

118. Zhong Xing Tan, *Stewardship in the Interests of Systemic Stakeholders: Re-conceptualizing the Means and Ends of Anglo-American Corporate Governance in the Wake of the Global Financial Crisis*, 9 J. BUS. & TECH. L. 169, 173–79 (2014).

119. *See* Margaret M. Blair & Lynn A. Stout, *Director Accountability and the Mediating Role of the Corporate Board*, 79 WASH. U. L.Q. 403, 406 (2001).

120. *See* Henry Hansmann & Reinier Kraakman, *The Essential Role of Organizational Law*, 110 YALE L.J. 387, 391–93 (2000).

121. *See generally* Donald C. Langevoort, *Behavioral Approaches to Corporate Law*, *in* RESEARCH HANDBOOK ON THE ECONOMICS OF CORPORATE LAW 442 (Claire A. Hill & Brett H. McDonald eds., 2012) (explaining how behavioral economics and psychology can be applied to understanding corporate law structures).

122. *See, e.g.*, James D. Cox, *The Fundamentals of an Electronic-Based Federal Securities Act*, 75 WASH. U. L.Q. 857, 873–75 (1997); James D. Cox, *Regulatory Duopoly in U.S. Securities Markets*, 99 COLUM. L. REV. 1200, 1244–52 (1999) [hereinafter Cox, *Regulatory Duopoly*].

123. *See infra* Part II.A.

124. *See infra* Part II.B.

A. Standards and Gatekeepers

Some of Cox's most insightful and prescient writings during this period focused on accounting—long an area of particular expertise for him[125]—as he examined both the growing battle over U.S. corporations' accounting standards and the changing nature of the accounting profession in the United States. Starting in the late 1990s, Cox wrote a series of key articles on the evolution of accounting standards and the accounting profession, examining the challenges that each posed to the U.S. securities markets and corporate governance systems. This Section highlights three of his best-known pieces that responded to globalization, regulatory competition, and financial collapses, each implicating the role of accounting standards and the accounting profession.

1. *Regulatory Duopoly in U.S. Securities Markets*. Cox opens his 1999 article *Regulatory Duopoly in U.S. Securities Markets* by observing that globalization and technological advances had "nurture[d] an environment of regulatory competition among nations." He then focuses his attention on recent debates over whether the SEC should allow issuers to reconcile their financial statements using International Accounting Standards (IAS) instead of the U.S.-generated Generally Accepted Accounting Principles (GAAP).[126] Although giving due weight to the technical differences between the standards, Cox uses the issue to engage with larger questions about the dubious benefits promised by regulatory competition.

The article situates the specific standards under consideration in their larger institutional and cultural contexts. GAAP was developed by the Financial Standards Accounting Board (FASB), a robust U.S. organization significantly insulated from government and private sector pressures that possesses notable expertise. The International Accounting Standards Committee (IASC), overseer of IAS (and later IAS's successor, the International Financial Reporting Standards (IFRS)), lacked these qualities.[127] Thus, the decision to allow U.S.

125. *See, e.g.*, JAMES D. COX, FINANCIAL INFORMATION, ACCOUNTING, AND THE LAW: CASES AND MATERIALS (1980).

126. Cox, *Regulatory Duopoly*, *supra* note 122, at 1201. For descriptions of the ongoing attempt to import international accounting standards, see generally Lawrence A. Cunningham, *The SEC's Global Accounting Vision: A Realistic Appraisal of a Quixotic Quest*, 87 N.C. L. REV. 1 (2008); Martin Gelter & Zehra G. Kavame Eroglu, *Whose Trojan Horse? The Dynamics of Resistance Against IFRS*, 36 U. PA. J. INT'L L. 89 (2014).

127. *See* Cox, *Regulatory Duopoly*, *supra* note 122, at 1206–08.

issuers to adopt IAS involved not just a choice between two standards but between two organizational frameworks. This change would require the SEC, assuming the SEC wanted to maintain its dominant role in regulating U.S. markets, to "assure itself that the IASC has a governance structure and operating processes sufficient to assure it can continually establish high-quality financial reporting standards,"[128] and it would also require the SEC to evaluate other nations' accounting cultures to decide whether they sufficiently tracked those of the United States.[129] There may, Cox concedes, be benefits from the SEC allowing U.S. issuers to use IAS: issuers could for instance benefit if cross-listing in foreign markets reduced their cost of capital.[130] But it is difficult to determine if those benefits outweighed the costs.[131]

Cox then deepens his focus by taking on advocates for regulatory competition in securities markets. Here he continues his fight against a knee-jerk adoption of the contractarian approach. In particular, Cox challenges arguments in favor of allowing accounting standards to be set by an issuer's domicile or allowing an issuer to choose any regime's disclosure requirements.[132] He argues that "[u]nderlying each of these proposals is the belief that regulatory competition . . . is more likely to result in disclosure standards that are optimal for investors and issuers."[133] Cox points out the many flaws to these arguments: there are not many competing regulators, there is not perfect information that discounting between different jurisdictions based on jurisdiction-specific disclosure requirements actually occurs, and there may be staggering enforcement difficulties if corporations could indeed choose which standard to follow.[134] In contrast, he contends, that there are benefits to be derived from a single or lead standard-setter, such as the SEC, developing and overseeing these standards.[135]

In the end, although Cox rejects more radical arguments for regulatory competition, he acknowledges that there is still a lack of "hard evidence bearing on the intrinsic merits of the exclusivity of U.S. GAAP."[136] Given the political pressures placed on the SEC at that

128. *Id.* at 1210.
129. *See id.* at 1211.
130. *See id.* at 1219–21.
131. *See id.* at 1219–23.
132. *See id.* at 1229–33.
133. *Id.* at 1230.
134. *Id.* at 1232–33, 1239.
135. *See id.* at 1237–44.
136. *Id.* at 1244.

time, it seemed that the adoption of IAS was inevitable.[137] The SEC's best approach, he concludes, was to take an active role in overseeing measured acceptance of IAS: "Experience gained by the SEC's incremental embrace of IAS . . . will surely provide experience that the SEC can apply when considering foreign-based disclosure standards in the future."[138] In sum, Cox doubts the value of the IAS but saw its adoption as unavoidable, so he charted a path forward that leaves a strong role for the SEC to maintain its oversight of public companies.[139]

Cox's focus on the SEC's important role as overseer of accounting standards leads him into a careful analysis of the accounting profession itself.[140] His analysis became urgent with the bursting of the Internet bubble in 2000 and the series of corporate scandals that began with Enron in 2001, events in which the accounting profession played a major role.

2. *Reforming the Culture of Financial Reporting: The PCAOB and the Metrics for Accounting Measurements*. After the corporate debacles of 2000–2002, widespread criticism was leveled at the accounting profession for allowing the disasters to occur. In his article *Reforming the Culture of Financial Reporting: The PCAOB and the Metrics for Accounting Measurements*, Cox surveys a number of responses to this crisis, from calls for principles-based accounting to the various reforms bundled together in the Sarbanes-Oxley Act of 2002 (Sarbanes-Oxley). But he asks whether more basic features of accounting relationships contributed to accounting's apparent failure and what changes might be needed to restore investors' faith in public companies.[141]

For Cox, the underlying problem in the accounting profession is that too many of its members are willing to abandon their public-overseer role and compromise their independence to help clients.[142] Like other observers, he blames the erosion of independence in large part on the growing importance of nonaudit services for accounting

137. *Id.* at 1247. This adoption did not ultimately happen, due in part to the aftermath of the 2008 financial crisis.

138. *Id.* at 1252.

139. *Id.* at 1244–50.

140. *Id.* at 1228–52.

141. James D. Cox, *Reforming the Culture of Financial Reporting: The PCAOB and the Metrics for Accounting Measurements*, 81 WASH. U. L.Q. 301 (2003).

142. *See id.* at 308–10.

firms.[143] In 1976, "audit fees constituted [70] percent of accounting firm revenues; by 1998 audit fees had fallen to [31] percent of their revenues."[144] Why this eroded independence was unclear: perhaps accounting firms treat accounting fees as "loss leader[s]"[145] to enter more competitive consulting fields, or perhaps management uses the threat of lost consulting fees to obtain more favorable treatment from auditors.[146] Whatever the mechanism, accountants' professional judgment appears compromised by the changing nature of their firms' businesses.[147]

What to do? Cox refuses to blame the rule-oriented nature of GAAP for the problem. Some had claimed that this approach made it "too easy for the accountant to rationalize that if a specific treatment is not prohibited, then it must be permissible."[148] If anything, Cox points out, accounting trickery would be easier under an approach that abandoned rules in favor of broad principles that gave auditors greater discretion as to how to apply them.[149] Furthermore, current law already incorporated elements identified with a principles-based approach. A leading case, for example, required disclosures to provide a "fair presentation of the company's assets, liabilities, revenues, and expenses."[150] And this approach was reinforced in Sarbanes-Oxley's "strengthened requirements of the audit committee and the executive certifications [intended] to drive reporting toward principles, or at least a single principle, of fair presentation, and away from a more technical orientation toward rules."[151]

The reference to Sarbanes-Oxley points to a different approach that was embodied in its provisions, strengthening the audit committee and "anchor[ing] the accountant's relationship in the audit committee and not in management."[152] To this end, Sarbanes-Oxley tightens the

143. *See id.* at 309–10.

144. *Id.* at 310.

145. *Id.* at 312.

146. *Id.* at 313.

147. *Id.* at 314. Cox noted that (at least in 2002) there was no "solid empirical support that nonaudit services . . . systematically compromise[d] the quality of the outside accountant's audit." *Id.* at 313. It would be foolish, however, to ignore the intuitions and less systematic evidence that such influence occurred. *Id.* at 314–15.

148. *Id.* at 303.

149. *Id.* at 309.

150. *Id.* at 320 (citing United States v. Simon, 425 F.2d 796 (2d Cir. 1969), *cert. denied*, 397 U.S. 1006 (1970)).

151. *Id.* at 321.

152. *Id.* at 307.

definition of independence for audit committee members, creates strong pressure to make one member a "financial expert,"[153] empowers the committee to engage its own independent experts, and—crucial in Cox's view—"impose[s] a dialogue between the audit committee and the outside accountants."[154]

Yet even this is not enough, and here we see again Cox's sensitivity to the larger contexts within which laws and rules operate. For all the legal changes made, "there is good cause for concern that the culture of accounting has not yet moved forward to reflect these changes."[155] The auditor's independence requires the auditor to operate independently from management, and yet there was little evidence of this. Hence the article's closing, in which Cox calls for the new Public Company Accounting Oversight Board (PCAOB) to reinvigorate accounting's social role and "foster[] an environment for auditors to perform their vocation as professionals."[156] In this way, the new body would have a "significant contribution to making audit committees effective guardians of stockholders' interests."[157]

3. *The Oligopolistic Gatekeeper: The U.S. Accounting Profession*. In the book chapter *The Oligopolistic Gatekeeper: The U.S. Accounting Profession*, written a few years after the previous article, Cox returns to the problems with the accounting industry, focusing on how its structure helped cause the industry's transformation "from a profession to a business" and asking what further reforms could mitigate still-existing problems within the field.[158] He begins with startling facts driving home the existence of a "tight oligopoly" in accounting: accounting is now so concentrated that, at the time the chapter was written, the "Big Four" firms performed 97 percent of all public-company audits for companies with sales over $250 million. In some industries, accounting was effectively dominated by a single firm.[159] Despite this contention, there was little evidence that the Big

153. *Id.*

154. *Id.* at 308.

155. *Id.* at 323.

156. *Id.* at 327.

157. *Id.*

158. James D. Cox, *The Oligopolistic Gatekeeper: The US Accounting Profession*, *in* AFTER ENRON: IMPROVING CORPORATE LAW AND MODERNISING SECURITIES REGULATION IN EUROPE AND THE US 294, 296 (John Armour & Joseph A. McCahery eds., 2006).

159. *Id.* at 297, 298 (quoting U.S. GOV'T ACCOUNTABILITY OFFICE, GAO-03-864, PUBLIC ACCOUNTING FIRMS: MANDATED STUDY ON CONSOLIDATION AND COMPETITION 16 (2003)).

Four had colluded to raise prices for accounting work, likely due to obstacles to collusion including a lack of transparency in accounting fees, which makes monitoring any kind of explicit or implicit agreement tough, and a lack of an effective means for punishing defectors from an explicit or implicit agreement.[160]

But, strangely enough, neither is there any evidence of vigorous competition in the accounting field—what competition that does occur between big accounting firms is for nonaudit services.[161] Accounting firms had apparently concluded that "profits could better be obtained through expanding their consulting operations than to expend efforts to wrest audit clients from their competitors."[162] For Cox, this lack of competition is particularly harmful to investors. Financial theory predicts that in such a concentrated industry an accounting firm would seek a competitive edge by offering "superior" accounting services to clients and foreswearing nonaudit services. It also predicts that public companies eager to impress capital markets with the stringency of their financial statements would hire these independent accounting firms. This prediction has not come true, in large part because of the attractiveness of charging consulting (nonaudit) fees: Each firm "pursued the same parallel behavior of leveraging their audit relationship to expand their profits through the rapid growth of consulting. . . . [E]ach firm's pursuit of this parallel strategy was made possible by the industry's concentration."[163] What results is today's unsatisfactory situation, in which audits are dominated by the Big Four, but each firm is reliant on nonaudit fees that reduce their independence and the reliability of their attestations. Industry structure, not greed alone, produces this problematic situation.

Sarbanes-Oxley improved what came before it, but it left the basic industry structure in place. And such reforms as were adopted had begun eroding by the time this chapter appeared in 2006, as evidenced by Congress's intervention to block proposals that would have required the expensing of stock options and the SEC's approval of amendments to disclosure requirements that obscured the distinction between some audit and nonaudit fees.[164]

For example, "76.4 per cent of total assets of the petroleum and coal products industry were audited by Pricewaterhouse Coopers." *Id.* at 298.

160. *Id.* at 301–03.

161. *See id.* at 307–08.

162. *Id.* at 308.

163. *Id.* at 316.

164. *See id.* at 328.

Cox concludes the piece with several proposals designed to ameliorate this problem, such as increased, more accurate disclosure of audit and nonaudit payments—which would give the market a better sense of the auditor's dependence on the client[165]—and requiring 8-K reporting when a client terminates an auditor's nonaudit consulting relationship—which may cast a harsh light on management's manipulation of the nonaudit fees.[166] The availability of PCAOB reports on auditors may also improve the situation, allowing audit committees to measure the quality of auditors.[167] Most radically, Cox proposes mandatory periodic rotation of auditors, a move that might finally shake up this oligopoly and reignite competition in the field.[168]

4. *Coping in a Global Marketplace: Survival Strategies for a 75-Year-Old SEC*. Cox also kept an eye on the larger currents of globalization and technological change that were transforming U.S. securities markets and asked how the SEC should respond. Cast in broader terms, he asks: "[C]an an agency created and operating through most of its years in the internationally insulated environment of U.S. capital markets survive in a world without borders[?]"[169] As he had done before, he focuses on accounting standards, particularly the recent SEC decision to allow foreign issuers to reconcile their financial reports to IFRS rather than GAAP.[170] But his real goal is to reveal how "globalization forces us to rethink the ultimate role of securities regulation in an environment of global trading and offerings."[171] The article also offers Cox another opportunity to challenge opponents of mandatory disclosure.

The SEC's limited acceptance of the IFRS seemed to portend that it would soon allow all issuers—from the United States or otherwise—to choose which standard to adhere to (a development

165. *See id.* at 332 (recommending "enhanced disclosure of those relationships" that "might compromise the accountant's independence").

166. *See id*.

167. *See id.* at 336.

168. *See id.* at 335 ("[I]f all firms were required to rotate auditors every ten years . . . the number of changes in any single year would be roughly double the number that occurred in 2003. Such rotation can be expected to lead to much less concentration within industries.").

169. James D. Cox, *Coping in a Global Marketplace: Survival Strategies for a 75-Year-Old SEC*, 95 VA. L. REV. 941, 941 (2009).

170. *Id.* at 943–44, 946–51.

171. *Id.* at 946.

subsequently derailed by the 2008 financial crisis).[172] In challenging this, Cox returns to first principles and argues that there are "four well-recognized interrelated objectives sought to be achieved by mandatory disclosure requirements"[173]: to provide investors with sufficient information to make informed, intelligent investment choices; to enhance the allocational efficiency of securities markets; to reduce fraudulent offerings and manipulation; and to "empower[] stockholders vis-à-vis the firm's managers and restrain[] opportunistic behavior by company managers."[174] Given the weaknesses of the IFRS—their lack of precision, their deference to management, and their openness to political manipulation—only the first objective would be satisfied under mutual recognition of both standards; the other three would be harmed. Nor would investors be able to mitigate the risks of fraudulent offerings through a properly diversified portfolio.[175]

Yet it does not seem possible to return to a world in which all issuers touching U.S. markets are required to adhere to GAAP because the forces of globalization are so powerful that "each country's securities regulations regime [cannot act as] an island unto itself."[176] In the global marketplace, Cox counsels, the best approach is for the SEC to engage with foreign regulators and authorities to raise standards around the globe through "engagement, persuasion, and perseverance,"[177] developing capacities to evaluate proposed foreign standards in the process. Neither isolationism nor heedless acceptance of competing standards would serve the American investor.

B. Empirical Research Comes to the Fore in the Legal Academy

Cox's scholarship over the past forty years displays remarkable range, flexibility, and curiosity. Most recently, he has engaged with what some see as the most exciting development in current corporate

172. Emily Chasan, *SEC's New Strategic Plan Backs Away from IFRS*, WALL STREET J. (Feb. 4, 2014, 1:37 AM), http://blogs.wsj.com/cfo/2014/02/04/secs-new-strategic-plan-backs-away-from-ifrs [https://perma.cc/FP5T-THHS].

173. Cox, *supra* note 169, at 959.

174. *Id.* at 961.

175. *See id.* at 969 (demonstrating that the risk of purchasing a fraudulent offering "is systematic so that it cannot be diversified away; the larger and more diverse one's portfolio, the closer the portfolio's overall risk . . . will be to the risk of fraud in the market as a whole").

176. *Id.* at 983.

177. *Id.* at 985.

legal scholarship: empirical legal studies.[178] Cox (in conjunction with one of the authors of this Article) has played a significant role in this new scholarship, writing extensively about the empirical dimensions of private and public enforcement of the federal securities laws and showing the value of how lawyers analyze problems. His work in this area shows a continued focus on the key role that shareholders play in modern corporate governance, combining careful doctrinal and theoretical analysis with the tools of modern econometrics to reinforce his arguments.

1. *Letting Billions Slip Through Your Fingers: Empirical Evidence and Legal Implications of the Failure of Financial Institutions to Participate in Securities Class Action Settlements*. In his widely cited article *Letting Billions Slip Through Your Fingers: Empirical Evidence and Legal Implications of the Failure of Financial Institutions to Participate in Securities Class Action Settlements*,[179] Cox and one of the authors of this Article document that many institutional investors, perhaps as much as 70 percent, do not file claims to recover damages that they are entitled to receive in settlements of securities class actions.[180] For those institutions that do file settlement claims, their "average recovery rates are about one-third of losses" and the dollar amounts of their mean and median recoveries are "substantial."[181]

The reasons why these investors leave significant amounts of money on the table are numerous. First, some institutional investors accord a low priority to filing claims because they do business with some of the settling companies and do not wish to ruffle their feathers.[182] Second, a lot of time passes between the commission of the fraud, the filing of the suit, the final settlement, and the disbursement

178. *See generally* Randall S. Thomas, *The Increasing Role of Empirical Research in Corporate Law Scholarship*, 92 GEO. L.J. 981 (2004) (defending an analytic approach to corporate law that withstands rigorous testing while capturing the broad influences of politics and economics).

179. James D. Cox & Randall S. Thomas, *Letting Billions Slip Through Your Fingers: Empirical Evidence and Legal Implications of the Failure of Financial Institutions to Participate in Securities Class Action Settlements*, 58 STAN. L. REV. 411 (2005) [hereinafter Cox & Thomas, *Letting Billions Slip Through Your Fingers*]. A pilot version of this study was published earlier. James D. Cox & Randall S. Thomas, *Leaving Money on the Table: Do Institutional Investors Fail to File Claims in Securities Class Actions?*, 80 WASH. U. L.Q. 855 (2002).

180. Cox & Thomas, *Letting Billions Slip Through Your Fingers*, *supra* note 179, at 425.

181. *Id.* at 424–25.

182. *Id.* at 425–29.

of money.[183] During that period, institutions may change advisors or custodian banks and the claims and supporting documentation may get lost.[184] Third, institutions and advisors worry about their trading profits a lot, and they fret about their returns from filing claims very little. After all, they are evaluated on the trading profits, not the returns from filing claims.[185] Fourth, the company thinks that their custodian is filing the claims while the custodian thinks the company is doing it, so neither checks the other.[186]

These observations are supported by two surveys of institutional investors about their practices.[187] According to these surveys, institutions largely rely on custodian banks to handle the filing of their claims and hardly monitor the filing themselves.[188] Custodians do not charge separate fees for filing claims and therefore have little incentive to do much work on them. Furthermore, the liability rules that apply in this area for failing to file claims are weak: only abject failure to file or monitor in the face of bad news is enough to establish liability for institutional investors.[189] Custodians can face contractual liability for breaching any claim-filing obligation, but, again, institutions do not actively monitor them.[190]

Having established the problem, Cox offers some policy recommendations to deal with it. First, he proposes that the courts establish a central clearinghouse for information about settlements and claims.[191] They should also standardize claim-filing documentation and

183. *See id.* at 429 (estimating that "four years or more can elapse between the date of a trade that occurred during the front end of the class action period and the publication of notice of a settlement").

184. *See id.* (stating that "institutions and their advisors . . . change their custodian banks" frequently, and that the "departing investment advisor or custodian bank does not customarily forward to the institution, or its successors, the trading records for the portfolio it had previously handled").

185. *Cf. id.* at 431 (suggesting that institutional "managers who view their objective as being well-performing traders" do "not value submitting claims because the expected gains of doing so" are typically "dwarfed by both the size of the fund's assets and the average yearly returns by the fund").

186. *See id.* at 432.

187. *See id.* at 432–38.

188. *See id.* at 445.

189. *See id.* at 441 ("[U]nless a fund was aware that its custodian was performing its claims filing duties badly *and* the fund's trustees consciously decided to do nothing about it, the current practice would likely be sufficient to protect fund trustees from liability.").

190. *See id.* at 442, 445.

191. *Id.* at 446.

forms.[192] Institutional investors need to monitor their custodians' claim-filing practices. Finally, the SEC should improve institutional investors' 13F filing requirements and make this data more easily available.[193]

More generally, Cox discusses the allocation rules that institutions use for distributing proceeds that they collect.[194] He shows that the proceeds do not directly benefit the beneficiaries that lost money, but rather they usually go into the institution's general funds for the benefit of all plan beneficiaries. This means that the losers from securities fraud are not fully compensated for their losses. From a theoretical perspective, these findings constitute an argument against justifying securities class actions on the basis of compensation. Instead, justifications should focus more on the class actions' deterrence value. This consideration reflects the earlier theme found in much of his work on derivative suits: representative suits are best understood and evaluated in terms of deterrence and not compensation.

2. *Does the Plaintiff Matter? An Empirical Analysis of Lead Plaintiffs in Securities Class Actions*. The PSLRA[195] was passed by the U.S. Congress in 1995 and had a dramatic impact on private-securities-fraud class actions.[196] One of its most innovative provisions was the lead-plaintiff provision,[197] which created a rebuttable presumption that the shareholder with the largest financial interest should be the named plaintiff in securities fraud class actions.[198] The theory was that large institutional investors would have the best financial incentives to monitor the plaintiffs' attorneys who file these class actions. The hope was that the institutional investors would negotiate lower fees, supervise the filing of suits and litigation documents, and monitor class counsel.

Institutional investors, however, were slow to answer the call to arms. It turned out that becoming a lead plaintiff imposed significant

192. *Id.* at 445.

193. *Id.* at 446–48.

194. *Id.* at 449–53.

195. Private Securities Litigation Reform Act (PSLRA) of 1995, Pub. L. No. 104-67, 109 Stat. 737 (codified as amended in scattered sections of 15 U.S.C.).

196. *See* James D. Cox & Randall S. Thomas, *Does the Plaintiff Matter? An Empirical Analysis of Lead Plaintiffs in Securities Class Actions*, 106 COLUM. L. REV. 1587, 1588 (2006).

197. 15 U.S.C. §§ 77z-1(a)(3), 78u-4(a)(3) (2012).

198. Cox & Thomas, *supra* note 196, at 1588–89.

costs on institutions.[199] These costs included discovery into the institution's business practices; the time needed to manage the litigation, which was often uncompensated; the risk of disclosing proprietary business information through discovery; and the threat of suit by other plaintiffs who were disappointed at not being appointed lead plaintiff.[200] The institution would also face significant opportunity costs as it was forced to give up the option of pursuing an individual recovery.[201]

In the article *Does the Plaintiff Matter? An Empirical Analysis of Lead Plaintiffs in Securities Class Actions*, Cox and one of the authors of this Article assess the impact of the lead-plaintiff provision, finding that the presence of an institutional investor as the lead plaintiff leads to a higher recovery for defrauded shareholders.[202] The empirical analysis also documents that courts prefer to select institutional investors in the lead-plaintiff beauty contests. Lead plaintiffs choose the biggest cases to seek appointment as lead plaintiffs, and the percentage of losses recovered in securities class actions seemingly declined after the passage of the PSLRA.[203]

Although most of these findings support Congress's decision to enact the lead-plaintiff provision, Cox sees room for improvement. He suggests that courts should allow reimbursement of all the institutions' expenses for being a lead plaintiff and ignore the statutory restrictions on the number of cases in which a prominent institutional investors can act as lead plaintiff.[204]

3. *The Emperor Has No Clothes: Confronting the D.C. Circuit's Usurpation of SEC Rulemaking Authority*. Cox's embrace of economic and empirical approaches does not signal an abandonment of more traditional tools of legal analysis. In *The Emperor Has No Clothes: Confronting the D.C. Circuit's Usurpation of SEC Rulemaking*

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199. *See id.* at 1602–10 (discussing the costs of serving as lead plaintiff).

200. *See id.* at 1602.

201. *Id.* at 1604–05.

202. *Id.* at 1630–34. A related article is James D. Cox, Randall S. Thomas & Lynn Bai, *There Are Plaintiffs and . . . There Are Plaintiffs: An Empirical Analysis of Securities Class Action Settlements*, 61 VAND. L. REV. 355 (2008).

203. *Id.* at 1619–27, 1627 tbl.8.

204. Cox & Thomas, *supra* note 196, at 1637 ("[C]ourts should be more willing, indeed activist, in awarding costs to institutional lead plaintiffs for *all* expenses related to an institution's participation as a lead plaintiff."); *id.* at 1638 ("Furthermore, we believe courts generally should follow the lead of the few judges that have been willing, in the right circumstances, to excuse the 'professional plaintiff' restrictions of the PSLRA.").

Authority, Cox and Professor Benjamin Baucom analyze[205] the D.C. Circuit's decision in *Business Roundtable v. SEC*,[206] which invalidated the SEC's recently adopted Rule 14a-11.[207] This rule provided certain shareholders access to a corporation's proxy so that they could nominate their own candidates for director positions.[208] In this article, Cox and Baucom challenge both the decision that struck down the rule and the court's new approach to regulations that promised to strangle much SEC rulemaking.

In *Business Roundtable*, the court insisted that the SEC was required to apply a cost-benefit analysis to justify the proposed regulation.[209] Here, Cox and Baucom closely examine the relevant legislative history before concluding that the court applied a level of judicial review inconsistent with what Congress had mandated in the securities acts.[210] They then offer a new approach to justify the adoption of regulations that would allow future SEC rulemaking to better fit the more exacting scrutiny that new rules will seemingly have to survive.

According to Cox and Baucom, the main flaw in the D.C. Circuit's analysis is its conclusion that the SEC, in adopting Rule 14a-11, was required to produce "an accurate cost-benefit determination" and failed to do so.[211] For most of its history, the SEC merely had to determine whether a rule was "in the public interest" and would further "the protection of investors."[212] In 1996, however, the National Market Securities Improvement Act (NMSIA)[213] added a requirement

205. James D. Cox & Benjamin J.C. Baucom, *The Emperor Has No Clothes: Confronting the D.C. Circuit's Usurpation of SEC Rulemaking Authority*, 90 TEX. L. REV. 1811 (2012).

206. Bus. Roundtable v. SEC, 647 F.3d 1144 (D.C. Cir. 2011).

207. *Id.* at 1156.

208. *See* Facilitating Shareholder Director Nominations, 75 Fed. Reg. 56,668, 56,677 (Sept. 16, 2010) (amending 17 C.F.R. pts. 200, 232, 240, 249), *invalidated by Bus. Roundtable v. SEC*, 647 F.3d 1144 (D.C. Cir. 2011).

209. *See Bus. Roundtable*, 647 F.3d at 1148–49 (holding that the SEC's "failure to 'apprise itself . . . of the economic consequences of a proposed regulation' makes promulgation of the rule arbitrary and capricious" (citing Chamber of Commerce v. SEC, 412 F.3d 133, 144 (D.C. Cir. 2005))).

210. Cox & Baucom, *supra* note 205, at 1818–21 (concluding that the "triple considerations of efficiency, competition, and capital formation" in the statute are subordinate to the SEC's primary goal of investor protection (citing the review standard set out in Securities Exchange Act of 1934 § 3(f), 15 U.S.C. § 78c(f) (2012))).

211. *Id.* at 1813.

212. *Id.* at 1818 (quoting 15 U.S.C. § 77b(b)).

213. National Securities Markets Improvement Act of 1996, Pub. L. No. 104-290, 110 Stat. 3416 (codified in scattered sections of 15 U.S.C.).

that the SEC also consider whether a proposed rule "promote[s] efficiency, competition, and capital formation."[214] The legislative history of the NMSIA shows, though, that Congress did not intend to require a rule always be found to promote "efficiency, competition, and capital formation," nor did Congress intend to mandate cost-benefit analysis for every rule.[215] Legislative history did, to be sure, suggest that "rigorous analysis"[216] would be demanded when weighing a proposed rule, but this suggestion did not mean that each rule had to advance "efficiency, competition, or capital formation."[217] Nor did there exist any requirement that a rule yield a quantifiable net benefit. In sum, the new language in the NSMIA was not intended to change the criteria by which courts should weigh SEC rulemaking. This fact is shown all the more through Congress's addition of a mandate that requires the U.S. Commodities Future Trading Commission to consider a rule's costs and benefits in other legislation.[218]

So *Business Roundtable*, Cox and Baucom conclude, is simply wrong when it says the SEC has to determine that a rule yields a "*net* benefit" or promotes efficiency, competition, and capital formation.[219] Courts may have to consider these three factors, but not every rule must promote them.[220] It is also possible, they note, that the SEC shot itself in the foot by specifically finding that Rule 14a-11 would enhance "efficiency, competition, and capital formation" even though it was not necessary.[221]

Cox and Baucom recommend that, going forward, the SEC reenact the rule so that it and future rules meet the review standard and satisfy the language of the statute. They recommend taking three specific steps. First, the SEC should stop "concluding" that a proposed rule promotes all of the abovementioned factors: if the statute only requires that the SEC "consider" the rule's impact on the factors, then

214. 15 U.S.C. § 77b(b).

215. Cox & Baucom, *supra* note 205, at 1820 (quoting H.R. REP. NO. 104-622, at 39 (1996) (emphasis added)).

216. *Id.* (emphasis omitted).

217. 15 U.S.C. § 77b(b).

218. 7 U.S.C. § 19(a); *see* Cox & Baucom, *supra* note 205, at 1823.

219. Cox & Baucom, *supra* note 205, at 1822.

220. *See id.* at 1837 (maintaining that Congress only mandated that the SEC "consider"—not "*find*" or "*ensure*"—that a proposed rule satisfies the triple aims of efficiency, competition, and capital formation).

221. *See id.* at 1840 (suggesting that the "SEC appears to have blindly walked into a trap it has set for itself . . . find[ing] itself hoisted by its own petard").

that is all it should do.[222] Second, it should defend its conclusions rigorously but not in the language of econometrics. A strong qualitative case can be made for rules whose benefits are impossible to precisely quantify. It may also be better if the SEC promulgated its rule in a different way. It should, Cox and Baucom propose, consider "staging" such regulatory changes to allow for a "natural experiment" on a rule, creating data about the rule's impact and success before its widespread adoption.[223] Third, because the burdens imposed by "one size fits all" regulations can be disproportionately great for smaller companies, the SEC should consider scaling regulation so that smaller issuers would initially enjoy less-stringent regulation until a rule's impact could be measured.[224]

CONCLUSION

Over the past forty years, corporate law scholarship has moved through a series of stages, from wrestling with the traditional problems Berle and Means set out, to the attack on accepted verities launched by the contractarians, to a theoretical stalemate offset by new developments that led to the application of empirical methods. Through all these shifts, Jim Cox has produced an enviable body of scholarship and has provided a model for what a corporate law scholar can accomplish. He has fought tenaciously to defend shareholders when he believed they were threatened by new developments. He has kept his roots in traditional scholarship, yet has judiciously applied the latest tools and developments when warranted. Through his labors, he has moved the needle in corporate law scholarship away from contractarianism and toward a more open-ended paradigm. For those of us who are his contemporaries, we can only wish that we have as great an impact on the field as he has had.

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222. *Id.*

223. *Id.* at 1843.

224. *Id.* at 1845–46.