ARTICLE

DEBUNKING THE “END OF HISTORY” THESIS FOR CORPORATE LAW

Leonard I. Rotman

[pages 219–272]

Abstract: In their article, “The End of History for Corporate Law,” Henry Hansmann and Reinier Kraakman proclaimed the triumph of the shareholder primacy norm over competing progressive theories of the corporation. This Article debunks Hansmann and Kraakman’s “end of history” thesis on both U.S. and Canadian corporate law grounds. A critical examination of high-profile U.S. corporate law jurisprudence indicates that the shareholder primacy norm cannot be supported, even by cases such as *Dodge v. Ford* and *Revlon, Inc. v. MacAndrews & Forbes Holdings, Inc.*, which exist at the foundation of shareholder primacy arguments. Further, Canadian corporate law jurisprudence and the structure of Canadian corporate law statutes reveal the complete lack of support for shareholder primacy arguments north of the forty-ninth parallel, further impeding Hansmann and Kraakman’s claim. This state of affairs demonstrates that Hansmann and Kraakman’s “end of history” thesis is, at best, premature and, at worst, incorrect.

NOTES

PIRACY LAWS AND THE EFFECTIVE PROSECUTION OF PIRATES

Diana Chang

[pages 273–288]

Abstract: This Note analyzes the current international legal framework for the punishment and prosecution of maritime piracy. Piracy is an international problem that disrupts global maritime trade and endangers the safe-
ty and security of crewmen and ship owners. Although it is a well-recognized principle that each state has universal jurisdiction to prosecute pirates, the conflicting international definitions of piracy and the preponderance of attacks near states that lack resources to effectively prosecute pirates create a gap in enforcement within the international legal framework. This Note proposes that cooperating states should establish regional international piracy tribunals that can apply an appropriate, uniform definition of piracy while providing the judicial resources to enforce international piracy laws.

**FROM “PERSONAL AUTONOMY” TO “DEATH-ON-DEMAND”: WILL PURDY v. DPP LEGALIZE ASSISTED SUICIDE IN THE UNITED KINGDOM?**

*Carol C. Cleary*

[pages 289–304]

**Abstract:** Debates over end-of-life issues and the “right to die” are becoming increasingly prevalent in many modern societies. In July 2009 the House of Lords addressed the question of whether the legal framework governing assisted suicide in the United Kingdom constitutes an unjustifiable infringement on privacy rights. The court decided that question in the affirmative, and this Note discusses the implications of *Purdy v. Director of Public Prosecutions* for the legality of assisted suicide in the United Kingdom. This Note uses evidence of legal developments in other jurisdictions that have grounded the right to assisted suicide in personal autonomy to argue that the Purdy court’s reasoning and the Director of Public Prosecution’s response to the decision paves the way for a gradual breakdown in restrictions on the practice.

**CHINA’S ANTI-MONOPOLY LAW: PROTECTIONISM OR A GREAT LEAP FORWARD?**

*Britton Davis*

[pages 305–322]

**Abstract:** Thirty years since China’s markets opened to the world, the People’s Republic has seen impressive growth, in large part due to an openness to foreign investment. In 2009, China was one of few nations to experience GDP growth. With a market based on competition for the first time in decades, China has begun to promulgate antitrust legislation to curb anticompetitive behavior. The creation of an Anti-Monopoly Law in 2008 has
prompted concern from outside China that the law will be used to promote a protectionist agenda, shielding Chinese domestic industry from foreign competition or investment. This Note examines the root cause of such concerns using a recent decision by Chinese antitrust authorities to prevent a merger between a domestic Chinese fruit juice company and Coca-Cola. This Note recommends an implementation of merger guidelines by the Chinese government in order to provide more transparency in its antitrust regime.

TAMING THE PERFECT POISON: A COMPARATIVE ANALYSIS OF THE EMEA’S EPAR SYSTEM AND THE FDA’S IMPROVED WARNING PROTOCOL

Nicholas R. Kennedy

[pages 323–338]

Abstract: In Europe and the United States, regulatory agencies responsible for monitoring drug safety have struggled to address the health concerns raised by the burgeoning market for minimally invasive cosmetic procedures utilizing botulinum toxins, the active ingredients in Botox. A 2005 study published in the Journal of the American Academy of Dermatology drew attention to these shortcomings after an analysis of adverse event reports submitted to the Food and Drug Administration (FDA) linked twenty-eight patient deaths to Botox-induced respiratory arrest and myocardial infarction. After an independent review of adverse effects reports submitted to the European Medicines Agency (EMEA) revealed similar findings in Europe, the FDA and EMEA implemented bolstered product warnings aimed at increasing patient awareness of the drug’s health risks. This Note compares the FDA and EMEA’s heightened warning protocols and argues that the agencies’ recent efforts are unlikely to reduce the number of serious adverse events linked to botulinum toxins.

“WHERE IS MY VOTE?”: DEMOCRATIZING IRANIAN ELECTION LAW THROUGH INTERNATIONAL LEGAL RECOURSE

Tanya Otsuka

[pages 339–356]

Abstract: In 2009, massive demonstrations ensued in response to the allegedly fraudulent reelection of Iranian president Mahmoud Ahmadinejad. The Iranian government met these protests with violence, imprison-
ment, and death. Yet, given the Iranian government’s structure and election law, the ability to resolve election disputes through domestic legal means is virtually non-existent. Many provisions of Iranian election law are democratically flawed, even though Iran is a party to numerous international agreements requiring free and fair elections. This Note examines the availability of international legal recourse for the provisions of Iran’s election law that fail to live up to these standards. The Note suggests that the international community apply multi-lateral political pressure to encourage Iranian election reform.

**Carrot or Stick?: The Balance of Values in Qualified Intermediary Reform**

*Steven Nathaniel Zane*

[pages 357–374]

**Abstract:** The qualified intermediary program allows foreign financial institutions to assume certain tax responsibilities ordinarily borne by U.S. withholding agents. The purpose of the program is to collect more foreign taxpayer information by creating a more direct link between the I.R.S. and recipients of foreign income payments. By accepting more responsibility, qualified intermediaries are provided numerous benefits that make business less costly. Nevertheless, the program has recently come under attack due to perceived abuse by wealthy U.S. citizens who use the system to evade income taxes. In response, the Obama Administration proposes numerous changes to the program, intended to strengthen it. But these changes fail to appreciate the balance of values at stake in reforming the qualified intermediary system. This Note argues that until more benign changes are made, the unique jurisdictional dilemma created by the U.S. international income tax system should not be solved by shifting from a “carrot” to a “stick” approach for foreign intermediaries.
DEBUNKING THE “END OF HISTORY” THESIS FOR CORPORATE LAW

LEONARD I. ROTMAN*

Abstract: In their article, “The End of History for Corporate Law,” Henry Hansmann and Reinier Kraakman proclaimed the triumph of the shareholder primacy norm over competing progressive theories of the corporation. This Article debunks Hansmann and Kraakman’s “end of history” thesis on both U.S. and Canadian corporate law grounds. A critical examination of high-profile U.S. corporate law jurisprudence indicates that the shareholder primacy norm cannot be supported, even by cases such as *Dodge v. Ford* and *Revlon, Inc. v. MacAndrews & Forbes Holdings, Inc.*, which exist at the foundation of shareholder primacy arguments. Further, Canadian corporate law jurisprudence and the structure of Canadian corporate law statutes reveal the complete lack of support for shareholder primacy arguments north of the forty-ninth parallel, further impeding Hansmann and Kraakman’s claim. This state of affairs demonstrates that Hansmann and Kraakman’s “end of history” thesis is, at best, premature and, at worst, incorrect.

Introduction

In their provocative article, *The End of History for Corporate Law*, Hansmann and Kraakman asserted that as a result of their view of the profound dominance of the shareholder primacy model of corporate governance, society had witnessed the “end of history” for corporate law.1 They boldly proclaimed that “[t]he triumph of the shareholder-oriented model of the corporation over its principal competitors is now assured,”2 echoing Bainbridge’s earlier claim that “[o]ver the last few

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2 Id. at 468.
decades, law and economics scholars have mounted a largely successful hostile takeover of the corporate legal academy.”

Hansmann and Kraakman contended that the triumph of the shareholder primacy model was part of a worldwide convergence toward a unitary vision of corporate purpose premised upon a shareholder-centered ideology. Their view was that progressive notions of corporate governance had failed to sustain a serious threat to the shareholder primacy model. This “failure” effectively ended the struggle for dominance between these competing approaches to corporate governance, a struggle that may be traced back to the debate between Adolf Berle of Columbia University and Merrick Dodd of Harvard in the 1930s. The primary implication of this “end of history” caused by the hostile takeover of the corporate legal academy was that the shareholder primacy model had supplanted alternative theories of the corporation that did not ascribe to the former’s characterization of corporate governance.

Hansmann and Kraakman’s assertion of the end of history for corporate law, which provided a particular perspective on the function of corporate management, was published in the same year that Enron collapsed and left large-scale corporate scandals in its wake. By asserting

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3 See Stephen M. Bainbridge, Community and Statism: A Conservative Contractarian Critique of Progressive Corporate Law Scholarship, 82 Cornell L. Rev. 856, 857, 859 (1997) (“The law and economics movement remains the most successful example of intellectual arbitrage in the history of corporate jurisprudence.”).

4 See Hansmann & Kraakman, supra note 1, at 443.

5 Id. at 439–40, 443–44, 454 (discussing how the shareholder-oriented model of the corporate form is more commonly accepted than alternative models such as the manager-oriented, labor-oriented, and state-oriented models).


7 The use of the term “management” here denotes both directors and officers. Although there is little uniformity in the obligations of directors and officers under U.S. corporate statutes, Canadian corporate statutes hold directors and officers to virtually the same obligations regarding duties of care and fiduciary obligations. See Gantler v. Stephens, 965 A.2d 695, 708–09 (Del. 2009); see also Lyman P.Q. Johnson & David Millon, Recalling why Corporate Officers Are Fiduciaries, 46 WM. & MARY L. Rev. 1597, 1600–01 (2005). Further, in spite of the differences that exist among various U.S. state corporate statutes and between these U.S. state statutes and Canadian corporate statutes, it appears that officers are now being held to standards more akin to those of directors in U.S. law. See Gant-
that the end of history for corporate law had arrived, Hansmann and Kraakman attempted to subsume the lengthy and vigorous debate over the role of the corporation and the place of corporate management to their own vision of the corporate world.\textsuperscript{8} They articulated their thesis without substantive evidence indicating the triumph of the shareholder primacy model over competing progressive visions of corporate activity.\textsuperscript{9} In so doing, they ignored the very real conclusion that, in 2001, many of the issues that plagued corporate law were the same as those that had hampered it years before.\textsuperscript{10}

In 1934, then-Yale law professor and future U.S. Supreme Court Justice William O. Douglas wrote a scathing attack on corporate management for its misuse, non-use, and abuse of corporate powers. The following passage captures the essence of his critique:

\begin{quote}
[T]he criticism [levied at corporate practices] has been symptomatic of indignation and disapproval of many different abuses and malpractices disclosed in recent years [including] . . . secret loans to officers and directors, undisclosed profit-sharing plans, timely contracts unduly favorable to affiliated interests, dividend policies based on false estimates, manipulations of credit resources and capital structures to the detriment of minority interests, pool operations, and trading in securities of the company by virtue of inside information, to mention only a few. These are not peculiar to recent times. They are forms of business activity long known to the law. . . . [B]usiness, and its legal advisors, have shown great ineptitude in appreciating and appraising the social importance and significance of many of their activities.\textsuperscript{11}
\end{quote}

Such descriptions are now commonplace in the post-Enron era. Yet, Douglas’s seventy-five-year-old critique clearly and crisply indicates that some of the most pressing issues in contemporary corporate law involving the actions of management are not new, but are merely recent incarnations of long-disputed matters.\textsuperscript{12} These matters continue to

\begin{itemize}
\item \textsuperscript{8} See Hansmann & Kraakman, supra note 1, at 449–68.
\item \textsuperscript{9} See id.
\item \textsuperscript{10} See id.
\item \textsuperscript{11} William O. Douglas, Directors Who Do Not Direct, 47 Harv. L. Rev. 1305, 1306 (1934).
\item \textsuperscript{12} See id.
\end{itemize}
arise precisely because of the ongoing debate over the proper characterization of the function of corporate governance.

As vigorously as Hansmann and Kraakman have propounded their view of the dominance of the shareholder primacy model, other prominent commentators have opposed this assertion and continue to do so. The latter have promoted a broader vision of corporate management’s duties that includes not only shareholders, but also bondholders, creditors, employees, and communities. Indeed, a recently published tête-à-tête between Greenfield and Smith intentionally harkens back to the Berle-Dodd debate. The continuation of this debate shows that the end of history for corporate law has not yet been reached—at least not in the manner or with the result Hansmann and Kraakman postulated.

This Article debunks the “end of history” thesis Hansmann and Kraakman espouse and provides a critical and comparative assessment of the foundational basis of their claim. In the process of addressing their claim, this Article engages both domestic and Canadian corporate jurisprudence. The scholarly and jurisprudential discussion about corporate purpose has been a largely U.S.-driven phenomenon to date. Two recent decisions of the Canadian Supreme Court should change this outlook, however. Peoples Department Stores Inc. v. Wise (“Peoples”) and BCE Inc. v. 1976 Debentureholders (“BCE Inc.”) will have a profound impact on the appropriate characterization of contemporary corporate governance and the “end of history” claim.


14 Greenfield & Smith, supra note 13, at 948–1010.

15 See [2004] 3 S.C.R. 461, 477, 482–83 (Can.) (standing for the position that directors of a corporation owe a fiduciary duty to the corporation itself, not to individual stakeholders (such as creditors), whose interests are protected by the honest and good faith obedience to the fiduciary duties owed to the corporation itself).

I. Background

A. The “Beginning of History”: Historical Understanding of Corporate Personality

Academic commentators in various jurisdictions consistently articulate that management owes duties to “the corporation.” This understanding is, however, merely a preliminary point of agreement. It is accepted that managers owe duties to the “corporation.” It is far less clear, however, how this managerial responsibility impacts corporate stakeholders. Are duties owed to the corporation as an entity with interests independent of those of its constituents? Alternatively, is the

17 Adolf A. Berle, Jr. & Gardiner C. Means, The Modern Corporation and Private Property 201 (Transaction Publishers 1991) (1932) (“[A]ny fair statement of the law would have to be based on the theory that the fiduciary duties of the director were limited to the corporation.”); Paul L. Davies with Daniel D. Prentice, Gower’s Principles of Modern Company Law 599 (6th ed. 1997) (“[T]he fiduciary duties are owed to the company and to the company alone.”); John Glover, Commercial Equity: Fiduciary Relationships 187 (1995) (“[T]he company ‘as a whole’ is unquestionably a proper beneficiary of its directors’ fiduciary obligations.”) (quoting Re Horsley & Weight Ltd. [1982] Ch. 442, 453–54 (U.K.); Bruce Welling, Corporate Law in Canada: The Governing Principles 377–78 (3d ed. 2006) (“It is absolutely clear in Canadian law that the person to whom corporate managers owe their duty is the corporation: not the shareholders, not the creditors, not the general public, but the corporate entity itself. There is no authority contrary to this well-entrenched principle.”).

18 While directors and officers are not the only corporate actors who have been found to owe fiduciary duties in corporate fiduciary jurisprudence, they have been the primary focus. Indeed, corporate jurisprudence contains many examples of shareholders’ fiduciary duties, particularly duties of majority shareholders to minority shareholders. Two of the most notorious of these are Pepper v. Linton, 308 U.S. 295 (1939) and Perlman v. Feldmann, 219 F.2d 173 (2d Cir. 1955). The rationale for holding majority shareholders to fiduciary duties to minority shareholders is expressed in Southern Pacific Co. v. Bogart, 250 U.S. 483, 487–88 (1919) (“The majority has the right to control; but when it does so, it occupies a fiduciary relation toward the minority, as much so as the corporation itself or its officers and directors.”). In opposition to domestic jurisprudence, shareholder fiduciary duty arguments are not as prevalent in Canada or in the United Kingdom. See Jeffrey G. McIntosh et al., The Puzzle of Shareholder Fiduciary Duties, 19 Can. Bus. L.J. 86, 86 (1991) (“In England and Canada the courts have in the main clung steadfastly to the notion that controlling shareholders owe no fiduciary duties, either to the company, or to fellow shareholders.”). In this Article, the Canada Business Corporations Act (CBCA), R.S.C., ch. C-44 (1985), will be used to represent all Canadian “division of powers” corporations statutes. The CBCA is the predominant model referring to the statutory division of corporate powers between management and various stakeholders. This structure differs from the “contractarian” model adopted from the United Kingdom that had previously existed in most Canadian jurisdictions. The “contractarian” model regarded shareholders as the fountain of corporate power and dictated that management possessed only those powers shareholders delegated to it.

19 Constituents include shareholders, bondholders, creditors, and employees, for example.
corporation to be regarded as an aggregate of these constituents, or as a representation of only some of these parties? This is where agreement among corporate scholars and jurists ends, resulting in one of the most contentious issues in contemporary corporate law.

The debate over whose interests corporate management must serve has existed almost as long as the modern corporation itself. One of the first cases to consider this issue was Charitable Corporation v. Sutton, 20 in which the directors of a charitable organization were held liable for breach of trust by failing to adequately monitor the charity. In Sutton, the English Court of Chancery held that management owed duties to the corporate entity. 21 In more modern corporate law, this same principle is readily observed across jurisdictions, in such cases as Carpenter v. Danforth in the United States, 22 Percival v. Wright in the United Kingdom, 23 and Clarkson v. Davies in Canada. 24 There is little, if any, contemporary debate over the corporation’s existence as a legal person separate and apart from the personality of its shareholders. 25

20 See (1742) 26 Eng. Rep. 642, 642–45 (Ch.) (U.K.) (holding the directors’ liability for the loss was based on their failure to monitor the charity, which in turn was partially responsible for a significant loss to the charity arising from fraud).

21 Id.

22 See 52 Barb. 581, 584 (N.Y. App. Div. 1868). The prominent precursor to Carpenter v. Danforth is the decision in Trustees of Dartmouth College v. Woodward. 17 U.S. 518 (1819). In Woodward, Chief Justice Marshall gave the following description of the corporation as an artificial entity:

A corporation is an artificial being, invisible, intangible, and existing only in contemplation of law. Being the mere creature of law, it possesses only those properties which the charter of its creation confers upon it, either expressly or as incidental to its very existence. . . . Among the most important are immortality, and, if the expression be allowed, individuality; properties by which a perpetual succession of many persons are considered as the same, and may act as a single individual.

Id. at 636.

23 (1902) 2 Ch. 421, 421 (U.K.).


25 A.V. Dicey articulated this principle in The Combination Laws as Illustrating the Relation Between Law and Opinion in England During the Nineteenth Century, 17 Harv. L. Rev. 511, 513 (1904). Dicey stated:

When a body of twenty or two thousand or two hundred thousand men bind themselves together to act in a particular way for some common purpose, they create a body which, by no fiction of law, but from the very nature of things, differs from the individuals of whom it is constituted.

Id. Within the realm of corporate law, this notion is most famously discussed in Salomon v. Salomon, [1897] A.C. 22, 38 (H.L.) (U.K.); see also Dodd, For Whom Are Corporate Managers Trustees?, supra note 6, at 1160.
Prominent examples of judicial interpretation regarding the effects of the statutory creation of corporations are the U.S. Supreme Court’s decision in *Louisville, Cincinnati & Charleston Railroad Co. v. Letson*, and the English House of Lords’ decision in *Salomon v. Salomon*. The implications of the statements made by the two courts are remarkably similar. The U.S. Supreme Court stated in *Letson*:

A corporation created by a state . . . though it may have members out of the state, seems to us to be a person, though an artificial one, inhabiting and belonging to that state, and therefore entitled, for the purpose of suing and being sued, to be deemed a citizen of that state.

Meanwhile, in *Salomon*, the House of Lords stated that “once the company is legally incorporated it must be treated like any other independent person with its rights and liabilities appropriate to itself . . . .”

How does this historical understanding of corporate personality mesh with Hansmann and Kraakman’s “end of history” thesis? Is the corporation merely a funnel through which profit maximization for shareholders is the ultimate goal? Alternatively, are shareholders merely one of a number of stakeholder groups whose interests must be accounted for in the conduct of corporate management? These questions must be addressed before the application of corporate management’s duties can be meaningfully considered.

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26 See 43 U.S. 497, 558 (1844).
27 See [1897] A.C. at 22. Even prior to *Salomon*, the notion that the separate legal existence of the corporation from that of its stakeholders was said to reside at the “root” of corporate law in *Farrar v. Farrars*, [1888] Ch.D. 395, 409–10 (U.K.).
28 *Letson*, 43 U.S. at 555. The Court further stated that “a corporation created by and doing business in a particular state, is to be deemed to all intents and purposes as a person, although an artificial person . . . capable of being treated as a citizen of that state, as much as a natural person.” *Id.* at 558. This judgment overturned the aggregate theory of the corporation established in *Bank of the United States v. Deveaux*, where Chief Justice Marshall said “[t]hat invisible, intangible, and artificial being, that mere legal entity, a corporate aggregate, is certainly not a citizen; and consequently cannot sue or be sued in the courts of the United States . . . .” 9 U.S. 61, 86 (1809). The Court continued:

[A corporate] name, indeed, cannot be an alien or a citizen; but the persons whom it represents may be the one or the other; and the controversy is, in fact and in law, between those persons suing in their corporate character . . . and the individual against whom the suit may be instituted.

*Id.* at 87.
B. The Berle-Dodd Debate

With deference to the significant contributions of others, the debate between Adolf Berle and Merrick Dodd initiated a longstanding discourse between shareholder primacy theorists and communitarians in legal literature concerning corporate duties. Berle and Dodd, like others, framed their discussion in fiduciary terms. Nevertheless, it is readily observed that their characterizations of the goals of management’s responsibilities differ. In Berle’s view, the exclusive beneficiaries of these duties are the shareholders. Thus, “all powers granted to a corporation or to the management of a corporation, or to any group within the corporation . . . are necessarily and at all times exercisable


31 See generally Berle, Corporate Powers as Powers in Trust, supra note 6, at 1049; Berle, For Whom Corporate Managers Are Trustees: A Note, supra note 6, at 1365; Dodd, For Whom Are Corporate Managers Trustees?, supra note 6, at 1146–47; Dodd, Is Effective Enforcement of the Fiduciary Duties of Corporate Managers Practicable?, supra note 6, at 194. For an interesting and in-depth discussion of the Berle-Dodd debate, see Bratton & Wachter, supra note 6, at 122–35; C.A. Harwell Wells, The Cycles of Corporate Social Responsibility: An Historical Retrospective for the Twenty-First Century, 51 U. Kan. L. Rev. 77, 82–99 (2002). On a related point, see also David Millon, Theories of the Corporation, 190 Duke L.J. 201, 216–25 (discussing Dodd’s theory that the natural entity model provided a basis for corporate social responsibility and Berle and Means rejection of the natural entity in favor of a shareholder-centered privatized conception of corporate law).

32 See, e.g., Douglas, supra note 11, at 1306; I. Beverly Lake, The Use for Personal Profit of Knowledge Gained While a Director, 9 Miss. L.J. 427, 427–28 (1937); Chester Rohrlich, The New Deal in Corporation Law, 35 Colum. L. Rev. 1167, 1192 (1935); Chester Rohrlich & Edith Rohrlich, Psychological Foundations for the Fiduciary Concept in Corporation Law, 38 Colum. L. Rev. 432, 432–34 (1938); Note, Clash of Personal and Corporate Interest as Affecting Business Activities of Officers and Directors, 84 U. Pa. L. Rev. 1008, 1008–09 (1935–36); Note, The Director of a Corporation as a Fiduciary, 20 Iowa L. Rev. 808, 808–12 (1935).

33 Berle, Corporate Powers as Powers in Trust, supra note 6, at 1049 (“[I]n every case, corporate action must be . . . tested . . . by equitable rules somewhat analogous to those which apply in favor of a cestui que trust to the trustee’s exercise of wide powers granted to him in the instrument making him a fiduciary.”); Dodd, For Whom Are Corporate Managers Trustees?, supra note 6, at 1147 n.6 (“That directors are fiduciaries for their corporations is indisputable.”).

34 Berle, For Whom Corporate Managers Are Trustees: A Note, supra note 6, at 1365 (“Historically, and as a matter of law, corporate managements have been required to run their affairs in the interests of their security holders.”).
only for the ratable benefit of all the shareholders as their interest appears.”  

35 Dodd disagreed with this assessment.  

36 He contended that corporations have a much larger constituency to whom their duties are owed, including, \textit{inter alia}, shareholder interests,  

37 the interests of corporate employees,  

38 and broader social goals.  

39 The rationale for this broader constituency was premised upon his assertion that corporate managers “are guardians of all the interests which the corporation affects and not merely servants of its absentee owners.”  

40 Although in later years Berle conceded that Dodd’s broader vision of the scope of the responsibilities of commercial enterprise—as well as that of management’s duties—had prevailed over his own,  

41 the debate over their formerly entrenched positions persisted. The debate between Berle and Dodd foreshadowed the contemporary controversy as to the proper beneficiaries of management’s duties. This modern-day debate pits shareholder primacy model advocates against progressives championing a broader constituency to whom management’s duties are owed.  

42 This “broader constituency” may include any or all of

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36 Dodd, \textit{Is Effective Enforcement of the Fiduciary Duties of Corporate Managers Practicable?}, supra note 6, at 205 (“The proposition that the sole function of business organizations is to produce the maximum profit for absentee owners is not only one which cannot, in the nature of things, appeal strongly as a code of professional ethics to the managers; it is also one which no longer appeals strongly to the community as a social policy.”).

37 Berle, \textit{For Whom Are Corporate Managers Trustees?}, supra note 6, at 1152 (“It may, however, be forcibly urged that all these and other past, present, and possible future limitations on the pursuit of stockholder profit in no way alter the theory that the sole function of directors and other corporate managers is to seek to obtain the maximum amount of profits for the stockholders as owners of the enterprise.”).

38 \textit{Id.} at 1151–52. Berle asserts that “managers . . . may easily come to feel as strong a community of interest with their fellow workers as with a group of investors whose only connection with the enterprise is that they or their predecessors in title invested money in it . . . .” \textit{Id.} at 1157.

39 \textit{Id.} at 1153–57, 1161.

40 \textit{Id.} at 1157. Berle explains:

\begin{quote}
If we think of [the corporation] as an institution which differs in the nature of things from the individuals who compose it[,] . . . [the corporation] is affected not only by the laws which regulate business but by the attitude of public and business opinion as to the social obligations of business.
\end{quote}

\textit{Id.} at 1161.


42 See Kent Greenfield, \textit{New Principles for Corporate Law}, 1 HASTINGS BUS. L.J. 89, 91 (2005) (“For most people honestly wrestling with issues of corporate governance, however,
shareholders, bondholders, general creditors, employees, and social interests at large.\footnote{See generally Progressive Corporate Law 37–59 (Lawrence Mitchell ed., 1995) (discussing various challenges to the prevailing shareholder primacy and shareholder wealth maximization views). Although a discussion of corporate social responsibility is beyond the scope of this Article, it directly affects the fiduciary characterization of corporate bodies and the obligations that result from that characterization. The idea that private corporations have responsibilities to the public at large, for example, has a direct impact on corporations’ duties of disclosure and their method of reporting their financial affairs, as well as the level of detail that ought to be required. Indeed, as Justice J.T. Walsh suggests, recent corporate scandals, such as the collapse of energy giant Enron Corp. as a result of faulty or misleading financial reporting, “may cause us to reexamine our traditional notions of the public responsibility of private corporations and, in particular, to whom corporate directors owe a fiduciary duty of disclosure.” Walsh, supra note 41, at 339.}

Despite the fact that the foundational debate over corporate purpose has ebbed and flowed over the years, shareholder primacy theorists and progressives have continued to jockey for position and influence. This struggle is evidenced through the writings of an ever-changing list of corporate law commentators, statutory reforms, and jurisprudential developments.\footnote{See Mitchell, supra note 13, at 3; Blair & Stout, supra note 13, at 300–01; Dallas, supra note 13, at 217; Greenfield & Smith, supra note 13, at 965–66; Johnson, supra note 13, at 1716–17 (1993); Millon, supra note 13, at 1376–77.} Thus, the classic Berle and Dodd debate over corporate governance remains alive and well. Even Hansmann, in revisiting The End of History for Corporate Law some eight years later, admitted that the paper “was written to capture, a bit provocatively, a particular perspective in a debate on convergence in corporate law that was just then gathering steam.”\footnote{Henry Hansmann, How Close Is the End of History?, 31 J. Corp. L. 745, 745, 749 (2006) (stating that one’s faith in reaching the end of history for corporate law may be closely tied to one’s faith in achieving Fukuyama’s original End of History thesis in politics). Curiously, Hansmann’s commentary could be seen to parallel that expressed in Francis Fukuyama, The End of History and the Last Man (1992), which served as the inspiration for the title of Hansmann and Kraakman’s article, The End of History for Corporate Law. See Hansmann & Kraakman, supra note 1, at 439. Francis Fukuyama, Our Posthuman Future: Consequences of the Biotechnology Revolution (2002), qualifies Fukuyama’s original “end of history” thesis, much like Hansmann may be seen to have qualified the strength of the original “end of history for corporate law” prediction that he and Kraakman made in 2001. Hansmann & Kraakman, supra note 1, at 439.} Hansmann conceded that “[t]here will probably never be perfect homogeneity in the approaches taken to these issues.”\footnote{Hansmann, supra note 45, at 750.} Arguably, the same conclusion is equally appro-
Debunking the “End of History” Thesis for Corporate Law

II. Analysis

A. Debunking U.S. Corporate Law Foundations of the “End of History” Thesis

Despite claims of the “end of history” of corporate law or assertions that U.S. corporate law was the subject of a successful hostile takeover by shareholder primacy theory, it is not clear that U.S. law wholly ascribes to the shareholder primacy norm. Blair and Stout have shown that “a series of mid- and late-twentieth-century cases . . . have allowed directors to sacrifice shareholders’ profits to stakeholders’ interests when necessary for the best interests of ‘the corporation.’” As evidenced in the cases that follow, U.S. corporate law jurisprudence would appear to be far more muted in its support of shareholder primacy and shareholder wealth-maximization arguments than Hansmann and Kraakman or Bainbridge have suggested.


A closer examination of the landmark 1919 Dodge v. Ford Motor Co. case, which has long been associated with the idea of shareholder primacy, indicates that the decision shares more in common with pro-

47 See id. (“[I]t might be said that this leaves most of the important and interesting debates within corporate law today untouched by our thesis. And, admittedly, that’s not an unreasonable thing to say.”).


50 Id.
gressive analyses of corporate law than with Hansmann and Kraakman’s “end of history” claim. In particular, the noted *Dodge v. Ford* judgment, long considered to be the beacon for shareholder primacy advocates, is not as absolutely dedicated to the advancement of shareholder wealth maximization as observers have generally posited. *Dodge v. Ford* is far more complicated and nuanced than most corporate law scholars have tended to suggest. Thus, although even noted progressive scholars have conceded that the judgment in *Dodge v. Ford* ran roughshod over broader notions of stakeholder protection as the basis of corporate function, a thorough analysis suggests that they may well have given their concessions too freely.

In *Dodge v. Ford*, the Dodge brothers, holders of 10% of the shares of Ford Motor Co. (FMC), commenced a lawsuit against FMC’s management for its failure to distribute an appropriate amount of FMC’s earnings to its shareholders. At the time, FMC was a hugely successful enterprise. It held property and receivables in the amount of some $78 million as of July 1916, as well as $54 million in cash or cash equivalents. In addition, FMC had paid some $41 million in special dividends to its shareholders between December 1911 and October 1915, on top of the $1.2 million that it paid annually in regular dividends.

In November 1916, FMC declared a special dividend of $2 million. FMC’s board of directors subsequently decided to cease paying such large special dividends to shareholders and instead use the bulk of FMC’s profits for other purposes. The directors sought to use some of FMC’s profits to construct a smelter and steel manufacturing plant to produce steel for car production, as well as to create a new, state-of-the-art manufacturing facility. Moreover, FMC’s directors decided to con-
tinue the corporation’s longstanding policy of manufacturing cars at a lower cost by reducing the unit price of its vehicles from $440 to $360.\(^6^1\)

The Dodge brothers regarded these plans as designed “to continue the corporation henceforth as a semi-eleemosynary [charitable] institution and not as a business institution.”\(^6^2\) They sought a special dividend of not less than 75% of FMC’s accumulated cash surplus,\(^6^3\) injunctions to prevent the construction of the smelter and manufacturing facilities, and the reduction in the per-unit cost of Ford cars.\(^6^4\)

Henry Ford, chairman and founder of FMC, as well as the owner of 58% of FMC shares, maintained that FMC had a responsibility to benefit the general public, and that the plans were consistent with that responsibility.\(^6^5\) When questioned about his stance at trial, Ford maintained that FMC took into consideration a wide range of stakeholder interests, not only the interests of its shareholders.\(^6^6\) During the proceedings, when asked for what purpose besides profit-making FMC was organized, Ford replied, “[FMC is] organized to do as much good as we can, everywhere, for everybody concerned . . . and incidentally to make money.”\(^6^7\) Ultimately, the Dodge brothers’ suit was successful at trial.\(^6^8\) The trial court ordered the declaration of a dividend in excess of $19 million and granted an injunction to halt construction of new manufacturing and smelting facilities.\(^6^9\) The decision to reduce the price of Ford vehicles was upheld.\(^7^0\)

On appeal, the Michigan Supreme Court determined that FMC’s plan and spending

[.] not call for and [was] not intended to produce immediately a more profitable business but a less profitable one; not only less profitable than formerly but less profitable than it

\(^6^1\) The per-unit cost of Ford vehicles had decreased from an initial cost in excess of $900 to a cost of $440 in July, 1916, with a plan to further reduce it to $360 beginning August 1, 1916. *Dodge*, 170 N.W. at 670.

\(^6^2\) *Id.* at 683.

\(^6^3\) *Id.* at 673.

\(^6^4\) *Id.*

\(^6^5\) *See id.* at 684.

\(^6^6\) *See id.*


\(^6^8\) *See Dodge.*, 170 N.W. at 677.

\(^6^9\) *See id.* at 677–78.
[was] admitted it might [have been] made. The apparent immediate effect [would] be to diminish the value of shares and the returns to shareholders.  

The court further found that “certain sentiments, philanthropic and altruistic, creditable to Mr. Ford, had large influence in determining the policy to be pursued by the Ford Motor Company . . . .”  

Notwithstanding the FMC board’s determination that the best interests of the corporation were served by eliminating the large special dividends and reinvesting profits in the business, the court stated that “[t]here should [have been] no confusion (of which there was evidence) of the duties which Mr. Ford conceive[d] that he and the stockholders owe[d] to the general public and the duties which in law he and his codirectors owe[d] to protesting, minority shareholders.”  

The court then famously distilled its vision of the essential purpose of the for-profit corporation:

A business corporation is organized and carried on primarily for the profit of the stockholders. The powers of the directors are to be employed for that end. The discretion of directors is to be exercised in the choice of means to attain that end, and does not extend to a change in the end itself, to the reduction of profits, or to the nondistribution of profits among stockholders in order to devote them to other purposes. 

The court also held that courts may interfere with business decisions where profit maximization is not the primary motivation of directors.  

These conclusions have been used to support the notion that Dodge v. Ford is properly viewed as supporting the shareholder primacy model of corporate governance.  

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71 Id. at 683.  
72 Id. at 684.  
73 Id.  
74 Id.  
75 Dodge, 170 N.W. at 684. The court explained:  

[I]t is not within the lawful powers of a board of directors to shape and conduct the affairs of a corporation for the merely incidental benefit of shareholders and for the primary purpose of benefitting others, and no one will contend that, if the avowed purpose of the defendant directors was to sacrifice the interests of shareholders, it would not be the duty of the courts to interfere.  

Id.  

76 See id.
premature Court had said, then such a conclusion would be logical. The court did not stop there, however. While it ordered the payment of significant dividends against the wishes of FMC’s directors, it also vacated the injunction imposed by the trial court on the construction of FMC’s new manufacturing and smelting facilities. Further, the court did not enjoin the corporation’s plan to lower the price of its vehicles from $440 to $360, even though that action would have reduced FMC’s sales figures by a minimum of $48 million in the first year alone. As the court explained, “[i]t is recognized that plans must often be made for a long future, for expected competition, for a continuing as well as immediately profitable venture.”

The decision of FMC’s board to invest in infrastructure development and to reduce the price of its vehicles cannot be properly assessed outside of the context in which those decisions were made. FMC had faced significantly increased competition during the period in question. The previously volatile automobile manufacturing industry that had been characterized by numerous small, independent operators who generally manufactured modest numbers of vehicles had become dominated by larger and more sophisticated corporations. The Dodge brothers themselves began manufacturing their own complete automobiles in 1914 in competition with FMC. General Motors Corporation (GMC) was formed in 1908 by the merging of the Buick and Oldsmobile companies, expanded in 1909 by adding the Oakland Motor Company (later Pontiac) and Cadillac, and was merged with the Chevrolet Motor Company in 1916. Consequently, it was prudent for the directors of FMC to seek to entrench or improve FMC’s position in the automotive market, as well as to attempt to impede competitors’ inroads into their market share, which would reduce FMC’s long-term profitability.

Thus, in order to sustain the level of profits earned prior to

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77 See id. at 683.
78 Id. (doing so on the basis that the board’s refusal to pay special dividends “appear[ed] to be not an exercise of discretion on the part of the directors, but an arbitrary refusal to do what the circumstances required to be done”).
79 See id. at 683–85 (basing estimates on FMC’s annual production capacity of 600,000 cars, not reflecting increase in manufacturing capacity anticipated by $24 million infrastructure enhancement plan).
80 Id. at 684.
81 Dodge, 170 N.W. at 683–84.
83 Dodge, 170 N.W. at 684; see also Lawrence E. Mitchell, A Theoretical and Practical Framework for Enforcing Corporate Constituency Statutes, 70 Tex. L. Rev. 579, 602 (1992) (suggesting that “[h]ad Ford testified to a desire to restrain the Dodges’ competition, rather
1916 and the market position of the company, FMC’s board of directors looked beyond the immediate satisfaction of its shareholders.\textsuperscript{84}

In addition to the infrastructure improvements and price reductions designed to ensure FMC’s competitiveness, the benefits that FMC conferred on other stakeholders, such as employees and the public at large, were not entirely selfless, but ultimately enured to FMC’s benefit.\textsuperscript{85} Such actions were, therefore, consistent with the fulfillment of directors’ fiduciary duties owed to their corporations.\textsuperscript{86} Increased wages for employees, notably in the form of the “five-dollar-day,” brought more potential customers for Ford vehicles,\textsuperscript{87} especially when the loyalty and pride of employees—particularly extant in the automotive sector—is considered. Similarly, reducing the price of Ford vehicles allowed more people to purchase Ford cars.\textsuperscript{88} Although this strategy might have resulted in less profit per vehicle, it was designed to create greater long-term profitability because of the larger volume of vehicles sold and the reduction in the costs of production envisaged by FMC’s infrastructure plan.\textsuperscript{89}

By not requiring FMC to abandon its infrastructure improvement and vehicle cost reduction plans, even though the former considerably reduced firm cash reserves and the latter had the effect of significantly reducing profits, the court deferred to the business judgment exercised by FMC’s board.\textsuperscript{90} In doing so, the court effectively sanctioned its ability to not only look beyond immediate shareholder interests, but to ignore those interests in favor of broader objectives.\textsuperscript{91} Therefore, \textit{Dodge v. Ford} is

\textsuperscript{84} See \textit{Dodge}, 170 N.W. at 684.
\textsuperscript{85} See \textit{id.} at 683.
\textsuperscript{86} See \textit{id.} at 683–84.
\textsuperscript{87} The company’s financial statement for the fiscal year ending July 31, 1916 showed 36,626 employees earning at least five dollars a day. \textit{Id.} at 670. To put this into perspective, the five-dollar-a-day wage more than doubled the previous wage when the one-hour reduction in the length of the work day is factored into the equation. See \textit{Mich. Dep’t of Nat’l Res. & Env’t, The Assembly Line and the $5 Day, Background Reading} (2003), http://www.michigan.gov/dnr (search article title; follow hyperlink). At the time that Ford introduced its five-dollar-day in 1914, the average daily wage of factory workers was one dollar a day. See \textit{The Museum of Am. Heritage, A Sense of Wonder: The 1915 San Francisco World’s Fair, June 7, 2002–Sept. 22, 2002} (2003), http://www.moah.org/exhibits/archives/1915.
\textsuperscript{88} See \textit{Dodge}, 170 N.W. at 683.
\textsuperscript{89} See \textit{id.} at 683–84.
\textsuperscript{90} \textit{Id.} at 684.
\textsuperscript{91} See \textit{id.} In any event, it is difficult to accept that shareholders’ interests were being ignored when they had received some $41 million in special dividends between December
inconsistent with the shareholder primacy norm that it is generally said to represent.\textsuperscript{92} Indeed, although \textit{Dodge v. Ford} is often juxtaposed against cases such as \textit{Shlensky v. Wrigley},\textsuperscript{93} which emphasize broader, communitarian interests, the decision is, in fact, more consistent with the view articulated in \textit{Shlensky} than it is with the pro-shareholder primacy model.


\textit{Shlensky v. Wrigley}\textsuperscript{94} represents another prominent case that rejects the shareholder primacy model of corporate governance.\textsuperscript{95} Shlensky was a minority shareholder of the Chicago National League Ball Club, Inc. (CNLBC), which operated the Chicago Cubs professional baseball team.\textsuperscript{96} He sued the directors of CNLBC for refusing to install lights in Wrigley Field, the Cubs’ home ballpark, in order to allow for night baseball games.\textsuperscript{97} From 1961 to 1965, the Cubs had sustained operating losses from their baseball operations.\textsuperscript{98} Shlensky maintained that the

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\textsuperscript{92} See id. at 684; see also Einer Elhauge, \textit{Sacrificing Corporate Profits in the Public Interest}, 80 N.Y.U. L. Rev. 733, 775 (2005) (“So even \textit{Dodge}, the high-water mark for the supposed duty to profit-maximize, indicates that no such enforceable duty exists. Nor does there appear to be any other case that has ever actually restrained a management decision to sacrifice corporate profits in the public interest.”); Henderson, \textit{supra} note 60, at 34 (“The \textit{Dodge} case is often misread or mistaught as setting a legal rule of shareholder wealth maximization. This was not and is not the law.”); Lynn A. Stout, \textit{Why We Should Stop Teaching \textit{Dodge v. Ford}}, 3 Va. L. & Bus. Rev. 163, 166 (2008) (“\textit{Dodge v. Ford} is indeed bad law, at least when cited for the proposition that the corporate purpose is, or should be, maximizing shareholder wealth. \textit{Dodge v. Ford} is a mistake, a judicial ‘sport,’ a doctrinal oddity largely irrelevant to corporate law and corporate practice.”).


\textsuperscript{94} 237 N.E.2d at 776.

\textsuperscript{95} Id. at 780–81.

\textsuperscript{96} Id. at 777.

\textsuperscript{97} Id. At the time of the \textit{Shlensky} decision, Wrigley Field was the only stadium in Major League Baseball that was not equipped for night games, having remained so long after all other teams had outfitted their ballparks for night baseball. Baseball Almanac, Famous First Night Games, http://www.baseball-almanac.com/firsts/first10.shtml (last visited Apr. 25, 2010). Night baseball was first played in 1935 in Cincinnati’s Crosley Field and was played in every major league ballpark by the late 1960s, with subsequent expansion teams beginning night baseball immediately upon joining Major League Baseball. See id.

\textsuperscript{98} \textit{Shlensky}, 237 N.E.2d at 777.
lack of night baseball games diminished the value of the company and its shares by reducing its profitability.99

Shlensky alleged that Philip K. Wrigley, President of CNLBC and holder of approximately 80% of its shares, had admitted that he was unconcerned whether the Cubs would become more profitable if they played night games.100 Wrigley’s reluctance to retrofit his ballpark with lights was said to have stemmed from his belief “that baseball [was] a ‘daytime sport’ and that the installation of lights and night baseball games w[ould] have a deteriorating effect upon the surrounding neighborhood.”101 Shlensky charged that the other directors of CNLBC acquiesced in the policy Wrigley had dictated, that the policy clearly concerned matters other than maximizing shareholder value, and that the directors’ “arbitrary and capricious acts constitute[d] mismanagement and waste of corporate assets.”102

The Illinois Court of Appeal rejected Shlensky’s allegations and determined that the directors’ decision to not play night games was, in fact, consistent with their duties owed to CNLBC.103 The court concluded that the directors need not have the corporation engage in the most immediately profitable course of action, but could base their decisions on the longer-term interests of the corporation and its shareholders.104 The court agreed with the defendant’s claim that the scheduling of night games could result in the deterioration of the surrounding neighborhood, which might reduce the long-term profitability of the corporation and detrimentally affect share value.105 In dismissing the suit, the court deferred to the directors’ exercise of their business judgment. As the court stated:

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99 Id. This lack of profitability is arguably not solely attributable to the absence of night baseball, but also to the fact that the Cubs finished seventh twice, eighth twice, and ninth once between 1961 and 1965. Id.
100 Id. at 778.
101 Id.
102 Id.
103 Id. at 780.
104 Shlensky, 237 N.E.2d at 780.
105 Id. Interestingly, in 1988, lights were installed at Wrigley Field, and night baseball is now a regular event at the stadium. Not only has the surrounding neighborhood not deteriorated as a result, but it has experienced a resurgence with the addition of new businesses tapping into the increased attendance generated by the ballpark. Peak attendance at Wrigley Field before the introduction of night baseball came in 1985, when 2,161,534 fans attended baseball games. In the first full year of night baseball in 1989, 2,491,942 fans were in attendance, while attendance since 1998 has consistently been in excess of 2.6 million (and in excess of the National League’s average attendance), reaching a peak of 3.3 million in the 2008 season. Baseball Almanac, Chicago Cubs Attendance Records, http://www.baseball-almanac.com/teams/cubsatte.shtml (last visited Apr. 25, 2010).
[W]e do not mean to say that we have decided that the decision of the directors was a correct one. That is beyond our jurisdiction and ability. We are merely saying that the decision is one properly before directors and the motives alleged . . . showed no fraud, illegality or conflict of interest in their making of that decision.\(^\text{106}\)

The court’s words thus served as yet another clear invalidation of the shareholder primacy model.


a. Unocal v. Mesa Petroleum Corp. (1985):\(^\text{107}\) *The “Corporate Enterprise” Above All*

The shareholder primacy model did not achieve much traction, if any, in U.S. corporate law jurisprudence in the 1980s. For example, 1985 yielded one of the clearest examples of the subordination or rejection of the model. The landmark case *Unocal v. Mesa Petroleum Co.* concerned the actions of Unocal’s board of directors in resisting a hostile takeover bid by Mesa.\(^\text{108}\) Unocal’s board alleged that this bid would have been detrimental to the corporation.\(^\text{109}\) The Delaware Supreme Court explicitly recognized the potential for a conflict of interest where a sitting board was in a position to thwart a takeover bid.\(^\text{110}\) In such a circumstance, directors might be tempted to resist a takeover bid solely to maintain their incumbency.\(^\text{111}\) Directors’ ability to resist a takeover bid through defensive tactics designed to solidify their positions created at least the possibility that directors might choose to favor their own interests over those of a corporation’s shareholders and over those of other stakeholders.\(^\text{112}\)

As the potential for this type of action posed a significant risk to stakeholder—and especially shareholder—interests, the *Unocal* court held that the actions of directors in opposing a hostile takeover would be subjected to an increased level of scrutiny beyond the more relaxed

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106 Shlensky, 237 N.E.2d at 780.
107 493 A.2d 946 (Del. 1985).
108 Id. at 955–56.
109 Id. at 953.
110 Id. at 955.
111 Id.
business judgment standard. Directors in such circumstances would be required to demonstrate that their actions were precipitated by their belief that a threat to the corporation as an entity existed, and that their defensive tactics were reasonable in relation to the perceived threat.

This response by the *Unocal* court marked a significant departure from existing Delaware jurisprudence, which tended to defer to directors’ exercise of business judgment. In the process of protecting against directorial self-interest, the *Unocal* decision created an entirely different effect by sanctioning the idea that a board of directors had to consider the impact of a takeover bid on “the corporate enterprise.” In particular, the court determined that, in the context of ascertaining whether a threat to a corporation existed, which was necessary in order to claim the protection of the business judgment rule in resisting a hostile takeover bid, directors could consider “the impact on . . . creditors, customers, employees, and perhaps even the community generally.” This conclusion, although perhaps necessary to curb director conflicts of interest, subordinates the shareholder primacy model to the constituency model of the corporate form.


*Revlon, Inc. v. MacAndrews & Forbes Holdings, Inc.*, like *Dodge v. Ford*, appears to be a case that affirms the shareholder primacy model. Nevertheless, a closer inspection of the case reveals its limitations for supporting shareholder primacy in a manner similar to *Dodge*.

In *Revlon*, the corporation’s directors engaged in defensive tactics to forestall a hostile takeover bid and instead negotiated the sale of the company to a friendly buyer at a lower price. Part of the rationale for choosing the friendly bid was a desire to protect certain creditors’ in-

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113 *Unocal*, 493 A.2d at 954.
114 Id. at 955.
115 Mitchell, supra note 83, at 611 (“The *Unocal* court . . . follow[ed] a conceptual approach quite at odds with the acknowledged formalism of Delaware corporate jurisprudence.”).
117 Id. at 955.
118 Id.
119 506 A.2d 173 (Del. 1986).
120 Id.
121 Id. at 182; *Dodge*, 170 N.W. at 684.
122 See *Revlon*, 506 A.2d at 180–83; *Dodge*, 170 N.W. at 684.
123 See *Revlon*, 506 A.2d at 176–79.
The Delaware Supreme Court held that the directors had wrongfully engaged in selective dealing to stave off the hostile bidder when “obtaining the highest price for the benefit of the stockholders should have been the central theme guiding director action.” The court determined that once the break-up of Revlon was inevitable,

[t]he duty of the board . . . changed from the preservation of Revlon as a corporate entity to the maximization of the company’s value at a sale for the stockholders’ benefit. . . . The directors’ role changed from defenders of the corporate bastion to auctioneers charged with getting the best price for the stockholders at a sale of the company.

Subsequently, the directors were found to have breached their duties of care to the shareholders for failing to maximize the value of their share holdings.

This shift in director duties became known as “Revlon duties.” Thus, where the break-up of a company becomes inevitable, the directors’ duties, which are normally owed to the corporation, shift to its shareholders and become focused on the sole purpose of maximizing shareholder value. The holding in Revlon was subsequently clarified by the Delaware Supreme Court in Paramount Communications, Inc. v. Time Inc. and Paramount Communications, Inc. v. QVC Network. Nev-

124 Id. Additionally, the white knight in Revlon had agreed to allow the incumbent management to operate the company, subject to its agreement to sell off certain divisions and to remain capable of servicing its debts. Id. at 178–79.
125 Id. at 182.
126 Id.
127 Id. at 185.
128 See id. at 182.
129 Curiously, although the Delaware Supreme Court held that the Revlon directors had breached their duties of care to the shareholders, the Delaware Court of Chancery had found that the directors had breached their duties of loyalty. MacAndrews & Forbes Holdings, Inc. v. Revlon, Inc., 501 A.2d 1239, 1250 (Del. Ch. 1985). Even in the Supreme Court’s judgment, it confused the matter, first stating that the Court of Chancery had found that the directors had breached their duties of care and subsequently characterizing the Chancery Court’s finding as one of a breach of duty of loyalty. Revlon, 506 A.2d at 175–76, 179. The Delaware Supreme Court’s haphazard characterization seems to be the simple result of carelessness rather than having any substantive reason. See id.
130 Revlon, 506 A.2d at 182.
131 See 571 A.2d 1140, 1150 (Del. 1989). The court determined that there were generally two circumstances that resulted in Revlon-type duties, both of which focused on the break-up of the target: when “a corporation initiates an active bidding process seeking to sell itself or to effect a business reorganization involving a clear break-up of the company” or when “in response to a bidder’s offer, a target abandons its long-term strategy and seeks an alternative transaction involving the breakup of the company.” Id.
ertheless, dissecting the logic of the shift required by the *Revlon* duties reveals that the shift is inconsistent with the shareholder primacy model of corporate governance.\(^{133}\) The *Revlon* duty shift required that the fiduciary duty of directors become a duty to maximize shareholder value.\(^{134}\) Shareholder primacy theory interprets the normal operation of directors’ fiduciary duties as being primarily aimed at benefitting shareholders.\(^{135}\) Yet, if the duty in *Revlon* results in a shift in directors’ focus toward shareholder interests from that which it usually is, the indication is that the duties owed under non-*Revlon* circumstances (i.e. “normal” or “usual” circumstances) would not be directed toward the shareholders’ benefit.\(^{136}\) In this sense, *Revlon* appears inconsistent with the shareholder primacy model.\(^{137}\)

If directors’ usual fiduciary duty is not owed to shareholders, as a logical construction of the *Revlon* judgment would indicate, then the judgment is both inconsistent with shareholder primacy theory and brings Hansmann and Kraakman’s assertion of the “end of history” for corporate law into question.\(^{138}\) It also provides an interesting twist on Stout’s contention that “*Revlon* thus defines the one context in which Delaware law mandates shareholder primacy.”\(^{139}\) Using the logic above, Stout’s contention would dictate that shareholder primacy is only mandated when there is a required shift in directors’ fiduciary duties, as the *Revlon* precedent requires.\(^{140}\) Although this outcome is not consistent

\(^{132}\) 637 A.2d 34, 46 (Del. 1994). In this case, the Delaware Supreme Court stated that it was not necessary for an inevitable break-up of the corporation to occur before *Revlon*-type duties were triggered; the key to the application of those duties was the pending sale of corporate control. *Id.* at 37. Thus, the court concluded that directors owed fiduciary duties to maximize shareholder value where a corporation engaged in a transaction that either caused a change in corporate control or resulted in the break-up of the corporation. *Id.* at 47–48.

\(^{133}\) Although the existence of *Revlon* duties may have been weakened by subsequent developments, this does not affect the impact of those shifting duties on Hansmann and Kraakman’s assertion of the triumph of the shareholder primacy model. See, e.g., Sean J. Griffiths, *Good Faith Business Judgment: A Theory of Rhetoric in Corporate Law Jurisprudence*, 55 Duke L.J. 1, 66–67 (2005); Lynn A. Stout, *Bad and Not-So-Bad Arguments for Shareholder Primacy*, 85 S. Cal. L. Rev. 1189, 1204 (2002).

\(^{134}\) *Revlon*, 506 A.2d at 182.

\(^{135}\) Berle, *Corporate Powers as Powers in Trusts*, supra note 6, at 1049.

\(^{136}\) See *Revlon*, 506 A.2d at 182.

\(^{137}\) See *id.*; Berle, *Corporate Powers as Powers in Trusts*, supra note 6, at 1049.


\(^{139}\) Stout, *supra* note 133, at 1204.

\(^{140}\) See id.
with Stout’s original meaning, she would likely find it a preferable basis for arguing against shareholder primacy theory.\textsuperscript{141}

c. Paramount Communications, Inc. v. Time Inc. (1989):\textsuperscript{142} Reaffirming the Primacy of the Corporate Entity

The 1989 case \textit{Paramount Communications, Inc. v. Time Inc.} further questions the legitimacy of Hansmann and Kraakman’s shareholder primacy claim.\textsuperscript{143} In that case, Time Inc. (Time), which had already approved a merger with Warner Communications Inc. (Warner), became the target of a surprise takeover bid by Paramount Communications, Inc. (Paramount).\textsuperscript{144} Time resisted Paramount’s bid on the basis that it posed a threat to Time’s control over its own destiny and long-term welfare.\textsuperscript{145} Time’s management contended that the merger with Warner would allow Time to retain its control and culture. It acknowledged, however, that the deal would result in Time’s shareholders becoming minority shareholders in the newly-merged company and would saddle the company with significant debt.\textsuperscript{146} The Delaware Supreme Court accepted Time’s arguments and denied Paramount’s request for an injunction to halt Time’s merger with Warner.\textsuperscript{147}

The judgment in \textit{Paramount} allowed Time’s directors to refuse to put Paramount’s tender offer to a shareholder vote, even though the offer would have maximized shareholder value, because Time’s directors deemed the sale to Paramount to be against Time’s best interests.\textsuperscript{148} Time’s management asserted that the sale of Time to Paramount would have meant the sacrifice of Time’s control over its future, as well as the distinct “Time Culture” of “journalistic integrity” that had been built up within the corporation’s operations.\textsuperscript{149}

The most important element of \textit{Paramount}, for present purposes, is the court’s acceptance that the interests of the Time Corporation as an entity, or the interests of the corporation’s employees, are to be regarded as paramount over the interests of any particular corporate

\begin{footnotes}
\item[141] See \textit{id.}.
\item[142] 571 A.2d at 1140.
\item[143] See \textit{id.} at 1150.
\item[144] \textit{Id.} at 1146–47.
\item[145] \textit{Id.} at 1148.
\item[146] \textit{Id.} at 1153.
\item[147] \textit{Id.} at 1154–55.
\item[148] \textit{Paramount}, 571 A.2d at 1148.
\item[149] \textit{Id.}.
\end{footnotes}
stakeholder, including shareholders.\textsuperscript{150} In this sense, the judgment is inconsistent with the position Hansmann and Kraakman advanced.\textsuperscript{151} As Professor Allen has stated, \textit{Paramount} “might be interpreted as constituting implicit judicial acknowledgement of the social entity conception [of the corporation],” as clearly as \textit{Dodge} reflects the alternative property conception of the corporation.\textsuperscript{152}

\textbf{B. Canadian Corporate Law and the “End of History” Claim}

1. A Comparison of U.S. and Canadian Characterizations of Corporate Governance

In comparing U.S. and Canadian characterizations of corporate governance, some obvious distinctions between the jurisdictions ought to be noted. First, share ownership in Canadian corporations has historically been far more concentrated than that existing in U.S. corporations. Second, the duties and restrictions imposed on Canadian corporate management appear more onerous than those established by U.S. law. It might be said that the breadth of management’s duties in Canada is justified because of a greater need to prevent Canadian corporate management from having its duties to the corporation be corrupted or improperly influenced by more concentrated voting rights or financial might. There are other potential explanations of this situation, however.

Despite the fact that greater concentrations of share ownership could justify the broader and more onerous regulation of Canadian corporate management activity, this increased oversight could also be explained by another significant distinction: the more pervasive governmental regulation of private relations in Canada than what generally exists in the United States. The enhanced scrutiny given to private interactions by Canadian governmental bodies has profound effects on Canadian corporate law. Additionally, increased concentrations of financial power and influence in Canada could lead to the existence of greater conflicts of interest,\textsuperscript{153} which could also rationalize the need for

\textsuperscript{150} Id. at 1154–55.
\textsuperscript{151} See Hansmann & Kraakman, supra note 1, at 468.
\textsuperscript{153} Indeed, fewer investors and lenders could easily translate into more incestuous relations in the Canadian corporate realm than those existing in the United States. Historically, this has been the norm; however, increased globalization potentially results in reduced concentrations of investment and more widespread financial dealings between
stronger regulation of corporate management. Although these matters will not be discussed directly herein, they provide a context for appreciating the comparisons that do appear below.

As indicated above, it is unclear why explicit discussion of corporate purpose was far less noticeable in Canadian corporate law than it was in the United States until quite recently. This situation changed, however, with the Canadian Supreme Court’s judgment in *Peoples Department Stores Inc. v. Wise*.155 *Peoples* was the first modern Canadian case to expressly discuss management’s duties in corporate governance. It also generated a wealth of commentary, the breadth of which was as new to Canadian law as the character of the *Peoples* decision itself.156 The Canadian Supreme Court’s subsequent decision in *BCE Inc. v. 1976 Debentureholders*157 provided an opportunity for the court to clarify and amplify some of the principles that it had established in *Peoples*.

Before venturing into a discussion of the *Peoples* and *BCE Inc.* cases, a preliminary note on Canadian corporate law is appropriate. Canadian corporate law shares certain commonalities with U.S. law, but draws upon both British and U.S. corporate principles, which it combines with some unique innovations of its own. Unlike U.S. corporate law, Canadian corporate law falls under both federal and provincial jurisdiction. Additionally, unlike the United States, where the state of Dela-

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Ware is readily acknowledged as the primary source of domestic corporate law, there is no undisputed jurisdictional leader in Canadian corporate law. For this reason, corporate law decisions of the Canadian Supreme Court, although few and far between, hold particular prominence in Canadian corporate law.

The *Peoples* and *BCE Inc.* judgments advance the broader understanding of corporate purpose and the function of corporate management that is suggested by the structure of most Canadian corporate law statutes. This is particularly evidenced by the physical and conceptual separation of management’s fiduciary duties from its duty of care, the broader range of individuals granted standing to bring derivative actions on behalf of corporations in Canada than in the United States, and the existence of a statutory oppression remedy that provides significant relief for a broad range of aggrieved corporate stakeholders.

2. Rejection of the Shareholder Primacy Model in Canadian Supreme Court Jurisprudence

a. Peoples Department Stores Inc. v. Wise (2004): Management Owes Fiduciary Duties to the Corporation

The *Peoples* case concerned corporate management’s duties to creditors upon or in the vicinity of corporate insolvency. Unlike the jurisprudence in other countries, including Australia, New Zealand, the United Kingdom, and the United States, all of which had sanctioned the notion that management held fiduciary duties to creditors

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when a corporation was near insolvency, Canadian law remained unsettled on the issue when the *Peoples* action commenced.

In the *Peoples* case, the Wise brothers were the sole directors of the Wise Stores department store chain. In 1992, Wise Stores purchased all of the shares in a troubled competitor chain, Peoples Department Stores Inc. (*Peoples*) pursuant to a highly-leveraged purchase agreement. Following its purchase of Peoples, Wise Stores sought to improve the efficiency of its expanded operations by implementing a new inventory procurement policy. Under this policy, Peoples purchased all inventory for the two chains from North American suppliers, and Wise Stores bought all inventory from international suppliers. As North American goods constituted 82% of both chains’ inventory purchases, Peoples became heavily indebted for inventory from which profits were primarily retained by Wise Stores.

Less than a year after implementing this inventory procurement policy, Peoples and Wise Stores were both petitioned into bankruptcy. Although the financing bank was paid in full and the vendor of Wise Stores suffered only a 1% loss on the purchase price, trade creditors were still owed approximately $21.5 million. Peoples’ trustee in bankruptcy commenced an action on behalf of Peoples’ unsecured creditors.

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166 One of the only cases on point prior to the trial judgment in *Peoples* was *Re Trizec Corp.*, [1994] 10 W.W.R. 127, 139 (Can.), in which the Alberta Court of Queen’s Bench said:

> A specific duty to shareholders becomes intermingled with a duty to creditors when the ability of a company to pay its debts becomes questionable. However, a wholesale transfer of fiduciary duty to creditors likely does not occur at the stage of proceedings where an arrangement is sought as opposed to a case where liquidation occurs.

*Id.* After the trial judgment in *Peoples* was released, the Ontario Superior Court of Justice released a judgment that supported the existence of management’s fiduciary duties to creditors upon or in the vicinity of insolvency. *Canbook Distrib. Corp. v. Bornis*, [1999] 45 O.R.3d 565, 574 (Can.). After the Quebec Court of Appeal reversed the trial judgment in *Peoples* and found no fiduciary duty owed by Peoples’ management to its creditors, the Ontario Superior Court of Justice again indicated that fiduciary duties could be owed by management to creditors in a manner essentially similar to what it had previously stated in *Canbook*. See *Peoples*, [2004] 3 S.C.R. at 485–86; *Dylex Ltd. v. Anderson*, [2003] 63 O.R.3d 659, 669–70 (Can.).

against the Wise brothers in their capacities as directors of Peoples. The action claimed that the Wise brothers had breached their fiduciary duties and duties of care under section 122(1) of the Canada Business Corporations Act (CBCA).\textsuperscript{168}

In the Canadian Supreme Court’s unanimous judgment, Justices Major and Deschamps held that Peoples’ directors had not violated either their fiduciary duties or duties of care under section 122(1). The court took care to distinguish between these duties, however. As the court indicated, the fiduciary duty, or duty of loyalty, “require[ed] directors and officers to act honestly and in good faith with a view to the best interests of the corporation,” while the duty of care imposed a duty of diligence on management in supervising and managing a corporation’s affairs.\textsuperscript{169} The court expressly noted that the trial judge in Peoples had not separately considered these duties in his judgment; moreover, it emphasized that those duties “are, in fact, distinct and are designed to secure different ends.”\textsuperscript{170}

The court’s emphasis on the distinction between management’s fiduciary duties and its duty of care is reflected in most Canadian corporate law statutes. Section 122(1) of the CBCA is reflective of the structure and, for the most part, the wording of most provincial corporations statutes:

\[
\begin{align*}
(1) & \text{ Every director and officer of a corporation in exercising their powers and discharging their duties shall} \\
& \hspace{1cm} (a) \text{ act honestly and in good faith with a view to the best interests of the corporation; and} \\
& \hspace{1cm} (b) \text{ exercise the care, diligence and skill that a reasonably prudent person would exercise in comparable circumstances.}\textsuperscript{171}
\end{align*}
\]

This physical and conceptual separation of management’s fiduciary duties and duties of care in Canadian law is a notable distinction from U.S. corporate law jurisprudence, particularly in Delaware, which has tended to conflate these duties.\textsuperscript{172}


\textsuperscript{169} See Peoples, [2004] 3 S.C.R. at 476.

\textsuperscript{170} Id. at 476–77.

\textsuperscript{171} CBCA § 122. Subsection 122(1)(a) is the statutory embodiment of management’s fiduciary duties, while subsection 122(1)(b) outlines the duties of care owed by management. Id.

Despite the fact that corporate fiduciaries owe each of these duties, not all are fiduciary duties. Although a fiduciary may owe a duty of care or a duty of good faith, those duties do not become fiduciary duties simply because a fiduciary owes them. Fiduciary duties pertain to conflicts of interest such as self-dealing, and the duty to act on behalf of one’s beneficiaries rather than in one’s own interest or on behalf of the interests of third parties. The duty of care is a tort duty under which a party is obliged to exercise the same level of care on behalf of others that would be expected of ordinarily prudent persons in the conduct of their own affairs.\textsuperscript{173} Meanwhile, the duty of good faith is a contractual standard of honesty in the discharge of one’s obligations and is limited to the range of duties outlined in the contract.\textsuperscript{174}

In dismissing the creditors’ claim, the Canadian Supreme Court held that the directors are obliged to “serve the corporation selflessly, honestly and loyally,”\textsuperscript{175} but it also emphasized that “[a]t all times, directors and officers owe their fiduciary obligation to the corporation.”\textsuperscript{176} The court further explained that “[t]he interests of the corporation are not to be confused with the interests of creditors or those of any other stakeholders.”\textsuperscript{177} The court stressed that management’s fiduciary duties do not change when a corporation is in the vicinity of insolvency.\textsuperscript{178} Consequently, in assessing the nature of the claim before it,

\textsuperscript{173} Although, curiously, the Revised Uniform Partnership Act expressly states that the duty of care is a fiduciary duty owed by partners. REVISED UNIF. P’SHIP ACT § 404(a), 6 U.L.A. 143 (1997).

\textsuperscript{174} Id. cmt. 4.

\textsuperscript{175} Peoples, [2004] 3 S.C.R. at 477.

\textsuperscript{176} Id. at 482–83.

\textsuperscript{177} Id.

\textsuperscript{178} Id. at 483. Note also the court’s comments that “that phrase [vicinity of insolvency] has not been defined; moreover, it is incapable of definition and has no legal meaning.” Id.
the Canadian Supreme Court suggested that the creditors ought to have sought an oppression remedy rather than relief for breach of fiduciary duty.\textsuperscript{179}

The Canadian Supreme Court’s contention in \textit{Peoples} that there was no need for management to owe fiduciary duties to creditors on the eve of insolvency because of the existence of the statutory oppression remedy, notwithstanding its breadth,\textsuperscript{180} is neither logical nor appropriate.\textsuperscript{181} In many situations in law, concurrent or overlapping duties or obligations exist, as evidenced by the concurrent duties present in contract and tort. Yet, the fact that some claims may be brought in either contract or tort does not warrant the insistence that one or the other is, \textit{a priori}, denied applicability. Matters ought not be any different for claims of a breach of fiduciary duty in the face of overlapping oppression claims.\textsuperscript{182} It is not the proper function of a court to decide

\textsuperscript{179} See \textit{id.} at 483–84. Indeed, the Canadian Supreme Court stated that “[i]f the stakeholders cannot avail themselves of the statutory fiduciary duty (the duty of loyalty, \textit{supra}) to sue the directors for failing to take care of their interests, they have other means at their disposal.” \textit{Id.} Specifically, the court indicated that “[t]he oppression remedy of s. 241(2) of the CBCA and the similar provisions of provincial legislation regarding corporations grant the broadest rights to creditors of any common law jurisdiction.” \textit{Id.} at 484. Importantly, however, the creditors in \textit{Peoples} did not seek an oppression remedy against Peoples’ management. \textit{Id.} at 481–82.

\textsuperscript{180} \textit{Id.} at 483. The breadth of the oppression remedy, which is considered \textit{infra} Part II.B.3.b, has sometimes led Canadian courts to inappropriate conclusions which suggest that the oppression remedy has overtaken or absorbed other causes of action. \textit{See, e.g.,} Brant Invs. Ltd. v. KeepRite Inc., [1991] 80 D.L.R.4th 161, 172 (Can.) (discussing the breadth of the statutory oppression remedy). The purpose of the oppression remedy is not to remove existing bases of legal or equitable claims but to provide a method for relief against oppressive conduct. Where such conduct also fits within the scope of other legal claims, such as breach of fiduciary duty, the breadth of the oppression remedy should not be understood to supersede any other appropriate basis of legal action.

\textsuperscript{181} \textit{Peoples} was not the first Canadian case to have ventured down this path. \textit{See Brant Invs.}, 80 D.L.R.4th at 172. In \textit{Brant Investments}, the Ontario Court of Appeal held that it was “unnecessary and . . . inappropriate” to saddle directors or majority shareholders with fiduciary duties towards minority shareholders in light of the existence of the broad statutory oppression remedy. \textit{Id.} This statement was made, at least in part, because the court held that “the evidence necessary to establish a breach of fiduciary duty would be subsumed in the broader range of evidence which would be appropriately adduced on an application under the section.” \textit{Id.}

\textsuperscript{182} As suggested in \textit{Leonard I. Rotman, FIDUCIARY LAW} 503–04 (2005):

It matters not a wit to the lawful determination of a plaintiff’s claim whether that plaintiff had other causes of action available that were not pleaded; rather, what is relevant is simply whether the cause of action pleaded may be properly made out on the facts. This is clearly indicated by Viscount Haldane in \textit{Nocton v. Lord Ashburton}.
how a plaintiff ought to frame his or her claim in an action. All a court is entrusted to do is to assess the relative merits of the claims advanced by the plaintiff once they are asserted.

To further entrench the idea that management’s duties are owed to “the corporation,” the Canadian Supreme Court in Peoples emphasized that “the phrase ‘the best interests of the corporation’ should be read not simply as the ‘best interests of the shareholders.’”\(^{183}\) In so doing, the Supreme Court’s rejection of the shareholder primacy model is quite clear. The court placed all stakeholder interests on the same level in the context of assessing a corporation’s best interests, stating:

\[
\text{[I]n determining whether they are acting with a view to the best interests of the corporation, it may be legitimate, given all the circumstances of a given case, for the board of directors to consider, inter alia, the interests of shareholders, employees, suppliers, creditors, consumers, governments and the environment.}^{184}\]

Unlike the situation with management’s fiduciary duties, the court held that its duties of care were not restricted to the corporation but could directly apply to stakeholders such as creditors.\(^{185}\) Nonetheless, it

\[\text{It did not matter that the client would have had a remedy in damages for breach of contract. Courts of Equity had jurisdiction to direct accounts to be taken, and in proper cases to order the solicitor to replace property improperly acquired from the client, or to make compensation if he had lost it by acting in breach of a duty which arose out of his confidential relationship to the man who had trusted him.}\]

Justice La Forest acknowledges this same idea in his own judgment in \(M.(K.) v. M.(H.)\), where he expressly states that “a breach of fiduciary duty cannot be automatically overlooked in favour of concurrent common law claims.” Similarly, in Hodgkinson \(v. Simms\), La Forest J. states that “the existence of a contract does not necessarily preclude the existence of fiduciary obligations between the parties . . . .” For these reasons, the rationale behind the Supreme Court’s judgment in Peoples has no sound basis in law.

\[\text{Id. (citations omitted).}\]

\(^{183}\) Peoples, [2004] 3 S.C.R. at 481. Although the court conceded, that, from an economic perspective, “the ‘best interests of the corporation’ means the maximization of the value of the corporation,” it held that various other factors were relevant when directors considered how to manage the corporation with a view to its best interests. \textit{Id.} These considerations included the interests held by the various stakeholders of the corporation. \textit{Id.}\(^{184}\)

\(^{185}\) \textit{Id.} at 488 (“[U]nlike the statement of the fiduciary duty in s. 122(1)(a) of the CBCA, which specifies that directors and officers must act with a view to the best interests of the corporation, the statement of the duty of care in s. 122(1)(b) of the CBCA does not specifically refer to an identifiable party as the beneficiary of the duty.”).
concluded that Peoples’ directors had not breached their duty of good faith to the creditors in implementing the new inventory procurement policy, as that was deemed a valid exercise of management’s business judgment.

Although the Peoples judgment stands for the proposition that corporate management owes fiduciary duties to the corporation and not to any particular stakeholder, it articulates a rather broad vision of the stakeholders whose interests may be considered by corporate management in discharging its fiduciary duties to the corporation. Indeed, the potential stakeholder interests that are recognized as a result of the Canadian Supreme Court’s analysis in Peoples—particularly government and the environment—are likely broader than the range of corporate stakeholders generally contemplated by most progressive scholars.

The Peoples case was a watershed in Canadian corporate jurisprudence as the first Supreme Court case to overtly consider and reject the shareholder primacy model in ascertaining the object of management’s fiduciary duties. Nonetheless, Peoples did not usher in a new manner of thinking about the recipients of corporate management’s fiduciary duties, whether in Canada or elsewhere.186 Despite the fact that the Peoples case may not have carved out a new way of thinking about the beneficiaries of corporate management’s duties, it did broadcast its conclusions much more broadly than had previously been communicated in Canadian corporate law.


In BCE Inc., the Canadian Supreme Court had an opportunity to revisit its comments about corporate management’s duties in Peoples in the context of a going-private transaction involving the leveraged buyout (LBO) of telecom giant BCE Inc. The $52 billion transaction, at the time the largest private equity deal in history,188 offered a premium of more than 40% to BCE Inc.’s common shareholders, or approxi-
mately $10 billion over the value of the shares prior to the time they were put in play. The deal would also have resulted in the assumption of $30 billion in debt by BCE’s wholly owned subsidiary, Bell Canada.

BCE Inc. sought court approval of the LBO as required under section 192 of the CBCA. The plan of arrangement was approved by 97.93% of BCE Inc.’s common shareholders, but opposed by certain Bell Canada debentureholders, who claimed that Bell Canada’s assumption of the $30 billion debt would reduce the value of their bonds by an average of 20% and lower their trade value from their “investment grade” rating. Consequently, the debentureholders sought an oppression remedy pursuant to section 241 of the CBCA. They also opposed the trial court’s approval of the arrangement under section 192 as not being “fair and reasonable” due to the negative effect on their economic interests.

In determining the merits of the debentureholders’ claim, the Canadian Supreme Court examined the actions of BCE Inc.’s directors in accepting the purchase arrangement. As no duty of care claim arose, the court’s focus was solely on the directors’ fiduciary duty. The Supreme Court affirmed that the directors owed a fiduciary duty to “the corporation,” as it had concluded in Peoples, and that directors may consider the impact of corporate decisions on stakeholders other than shareholders. The court held that the content of management’s duty

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189 CBCA § 192. Subsection 192(3) reads as follows:

Application to court for approval of arrangement—Where it is not practicable for a corporation that is not insolvent to effect a fundamental change in the nature of an arrangement under any other provision of this Act, the corporation may apply to a court for an order approving an arrangement proposed by the corporation.

Id.

190 See BCE Inc., [2008] 3 S.C.R. at 577. In addition, the debenture downgrade could have forced debentureholders with credit rating restrictions to sell their debentures at a loss. See id.

191 See id. at 578. Initially, the debentureholders also brought motions for declaratory relief under the terms of the trust indentures, although that issue was not before the Canadian Supreme Court. See id.

192 See id. at 605. For the purpose of the appeal, the Canadian Supreme Court held that it did not need to distinguish between the conduct of the directors of BCE and the directors of Bell Canada, since the same directors served on the boards of both corporations. See id. at 582.

193 See id. at 584. The court reaffirmed its finding in Peoples that the stakeholders whose interests may be considered included “inter alia, shareholders, employees, creditors, consumers, governments and the environment.” See id. at 585.
was not limited to fostering short-term profit or increasing share value, but extended to the corporation’s long-term interests.\footnote{194}

The remainder of the judgment in \textit{BCE Inc.} considered the application of the oppression remedy to the alternative claims asserted by the debentureholders that: (1) they expected that BCE Inc.’s management would maintain the investment grade trading value of their debentures and; (2) at a minimum, that management would consider their economic interests in maintaining the debentures’ trade value.\footnote{195}

The Supreme Court’s finding is problematic, however, because it states that where directors account for the interests of stakeholders in assessing the best interests of the corporation, courts should give appropriate deference to directors’ business judgment under the business judgment rule.\footnote{196}

In opposition to conventional wisdom, the business judgment rule does not properly apply to fiduciary duties, but only to duties of care. Notwithstanding the problems associated with the conflation of directors’ fiduciary duties and their duties of care in Delaware jurisprudence,\footnote{197} Justice Brandeis’s opinion in \textit{United Copper Securities Co. v. Amalgamated Copper Co.} is perfectly clear in stating that the business judgment rule applies only to the duties of care.\footnote{198}

As he asserted in that case, “Courts interfere seldom to control such discretion \textit{intra vires} the corporation, except where directors are guilty of misconduct equivalent to a breach of trust, or where they stand in a dual relation which prevents an un-prejudiced exercise of judgment.”\footnote{199} Thus, as stated in \textit{Lewis v. S.L. & E.},

\begin{itemize}
\item \textit{Id.} at 584.
\item \textit{Id.} at 602. For a discussion of this aspect of the judgment, see \textit{infra} Part II.B.3.b.
\item \textit{See} \textit{BCE Inc.}, [2008] 3 S.C.R. at 585.
\item \textit{See}, \textit{e.g.}, \textit{Emerald Partners}, 787 A.2d at 90; \textit{McMullin}, 765 A.2d at 917; \textit{Brinca}, 722 A.2d at 10; \textit{Cinerama}, 663 A.2d at 1164; \textit{Cede & Co.}, 634 A.2d at 361.
\item \textit{See} 244 U.S. 261, 263–64 (1917).

In the absence of fiduciary misconduct, courts refuse to inquire into the merits of a given business decision and to impose fiduciary liability regardless of the outcome of that decision under the doctrinal rubric of the business judgment rule. . . . When misconduct is characterized as a breach of the duty of care, the business judgment rule’s presumption is overcome and liability is imposed on the fiduciary without further inquiry beyond the amount of damages. . . . When the fiduciary’s misconduct is characterized as a breach of
\end{itemize}
Inc., “[T]he business judgment rule presupposes that the directors have no conflict of interest,” and that “[w]hen a shareholder attacks a transaction in which the directors have an interest other than as directors of the corporation, the directors may not escape review of the merits of the transaction.”200

As a result, courts need not defer to the actions of directors in applying their fiduciary duties but may appropriately review their decisions for consistency with fiduciary standards without offending the business judgment rule. Therefore, the purpose of the business judgment rule is not to insulate directors from liability for the exercise of their powers over the corporation, but to provide adequate deference to decisions that, as indicated in Aronson v. Lewis, are made “on an informed basis, in good faith and in the honest belief that the action was in the best interests of the company.”201

Some notable points that are relevant to the nature of directors’ fiduciary duties are also observable in the part of the BCE Inc. judgment focusing on oppression. Initially, the court indicated that both the corporation and its shareholders are “entitled to maximize profit and share value . . . but not by treating individual stakeholders unfairly.”202 The difficulty with this proposition is that both BCE Inc. and Peoples establish that stakeholders cannot claim a breach of fiduciary duty against management, since its fiduciary duties are owed only to the corporation. The court in BCE Inc., however, links the notion of unfair treatment to the oppression remedy, holding that fair treatment is “the central theme running through the oppression jurisprudence.”203 Accordingly, the duty to treat stakeholders fairly, as guaranteed by the oppression remedy, may serve as a limiting factor on directors’ ability to fulfill their fiduciary duties. This situation may explain why directors, in fulfilling their fiduciary duties to the corporation, may well wish to consider the impact of their actions on other stakeholders, as indicated in both Peoples and BCE Inc.

the duty of loyalty, courts do not typically impose liability on the fiduciary automatically but rather evaluate the transaction to determine whether it is fair to the corporation.

Id.

200 Lewis v. S.L. & E., Inc., 629 F.2d 764, 769 (2d Cir. 1980). Furthermore, as the court stated in Peoples, fiduciary duties and duties of care are “designed to secure different ends.” Peoples, [2004] 3 S.C.R. at 476–77.


203 Id.
The *BCE Inc.* judgment stresses that management must ensure that it comports itself “in accordance with [its] fiduciary duty to act in the best interests of the corporation, viewed as a good corporate citizen”\(^{204}\) where it is faced with the conflicting interests of the corporation and its stakeholders. This signifies that a court, in reviewing the actions of corporate management, must inquire whether “in all the circumstances, the directors acted in the best interests of the corporation, having regard to all relevant considerations, including, but not confined to, the need to treat affected stakeholders in a fair manner, commensurate with the corporation’s duties as a good corporate citizen.”\(^{205}\)

The court’s requirement in *BCE Inc.* that a corporation must act as a “good corporate citizen” requires that its management consider the interests of all of its stakeholders, not only its shareholders. This finding is consistent with the contention made herein that the shareholder primacy model is not reflective of Canadian law’s understanding of corporate governance. Any ambiguity on this point ought to be put to rest by the court’s subsequent assertion in *BCE Inc.* that “[t]here is no principle that one set of interests—for example the interests of shareholders—should prevail over another set of interests.”\(^{206}\) The key for corporate management in Canada, then, is to balance the interests of the various constituent groups for which it is obliged to account. This is clearly inconsistent with Hansmann and Kraakman’s “end of history” thesis.

3. Rejection of the Shareholder Primacy Model in Canadian Corporate Law Statutes

In addition to the Canadian Supreme Court’s recent corporate jurisprudence in *Peoples* and *BCE Inc.*, there are other substantive reasons to suggest that the shareholder primacy model does not hold sway in Canada. Two such reasons are firmly rooted in Canadian corporate law statutes: the existence of a more generally available derivative action than that existing in the United States, as well as the presence of a wide-ranging statutory oppression remedy.

\(^{204}\) *Id.* at 607–08.

\(^{205}\) *Id.* at 598.

\(^{206}\) *Id.*
a. *The Derivative Action*

Derivative actions allow designated individuals[^207] to act in a representative capacity on behalf of a corporation for wrongs committed against it when management itself does not initiate such actions.[^208] Any award made pursuant to a derivative action accrues to the corporation, not to the individual bringing the derivative suit.[^209] Pursuant to section 240 of the CBCA, the range of potential relief available to a corporation under a derivative action is limited only by a court’s imagination, as the section allows the court the discretion to “make any order it thinks fit.”[^210]

The Canadian derivative action is essentially similar to derivative actions that exist under U.S. corporate law statutes, but with one notable difference. Pursuant to U.S. corporate law, only shareholders may generally bring derivative actions.[^211] In Canada, any person who qualifies as a “complainant” under section 238 of the CBCA may be granted leave to bring a derivative action.[^212] This important difference is relevant in assessing whether corporate governance in Canada follows a shareholder primacy model. CBCA section 239(2) defines complainants as any of the following persons:

(a) a registered holder or beneficial owner, and a former registered holder or beneficial owner, of a security of a corporation or any of its affiliates;

(b) a director or an officer or a former director or officer of a corporation or any of its affiliates;

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[^207]: See CBCA § 238. Persons who are deemed to be appropriate “complainant[s]” and therefore have carriage of a derivative action are defined under the statutes that authorize such actions or under the common law, where appropriate. *Id.*

[^208]: See *id.* § 239. The derivative action exists only because of the problems inherent in the notion of corporate legal personality. Corporate decisions are made on a corporation’s behalf by its management, which is bound by fiduciary duties to act in the best interests of the corporation; enforcing these fiduciary duties is difficult, however, if the only actors who can represent the corporation are the very managers who may have violated those duties. This explains why other individuals are allowed to represent the corporation’s interests via the derivative action where management fails to assume such responsibility. *Id.*

[^209]: See *id.* (noting that complainant brings action “in the name and on behalf of a corporation”). Given that the derivative action is a representative action on behalf of the corporation that seeks recompense for harm done to the corporation, any proceeds awarded from the litigation logically flow to the corporation, not the complainant. *See id.* § 240.

[^210]: *Id.* § 240.

[^211]: Note, however, the exception for creditors who bring such claims where corporations are insolvent, which is discussed in greater detail below.

[^212]: CBCA § 238.
The key element in the definition of complainant is subsection (d), which, to date, has been interpreted to include creditors, but which is open-ended regarding potential complainants. In the United States, the assertion that only shareholders are generally able to bring derivative actions is subject to the financial condition of the corporation. Although U.S. case law extended the ability to bring derivative actions to creditors in circumstances where a corporation was “on the eve of” or “in the vicinity of” insolvency, in *Credit Lyonnais*, it has now limited that action, in *North American Catholic Educational Programming Foundation Inc. v. Gheewalla*, to situations of actual insolvency. Thus, in practice, those who have been able to bring derivative actions in Canada and the United States are the same individuals. A creditor in Canada, however, need not wait until a corporation is insolvent to be granted standing as a complainant. Where persons seeking leave to bring a derivative action are not shareholders, Canadian courts will assess the connection between the claimant, its interests, and the corporation’s own interests in deciding whether to grant the leave requested. Consequently, the derivative action is of potentially greater applicability in Canada than it is in the United States, as any interested

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213 See id. § 2(1). “‘Director’ means the Director appointed under section 260,” who is essentially the registrar for the Act. See id. § 260.
214 Id. § 239(2).
215 See, e.g., *Dylex*, 63 O.R.3d at 667–68.
216 See, e.g., *BCE Inc.*, [2008] 3 S.C.R. at 586 (noting that potential complainants include security holders, creditors, directors, and officers). As indicated by the CBCA, however, the range of possible complainants is much broader than this. See CBCA § 239.
218 See *Gheewalla*, 930 A.2d at 101–02. There is an important difference, however, between allowing creditors to bring derivative actions on behalf of corporations and allowing creditors to bring direct breach of fiduciary duty claims against corporate management. See, e.g., *Prod. Res. Group*, 863 A.2d at 793–95.
219 See, e.g., *Re Daon Dev. Corp.*, [1984] 10 D.L.R.4th 216, 223 (Can.). In this case, an application by a debentureholder to be certified as a complainant in order to bring a derivative action was denied on the basis that the debentureholder was not a “proper person” under the then-applicable British Columbia statute since the applicant’s “only interest in the management of the company is the general and indirect one of wishing to see the company prosper.” See id. The British Columbia statute in question did not include a provision characterizing “any other person” as a complainant, though. See *First Edmonton Place* v. 315888 Alba Ltd., [1988] 60 Alta. L.R.2d 122, 154 (Can.). In *First Edmonton Place*, however, it was held that a creditor need not hold a direct interest in the corporation to be a “proper person” to bring a derivative action on behalf of the corporation. See id. at 154–57.
person who may demonstrate a suitable connection to the corporation’s interests may be authorized to bring a derivative suit.\(^\text{220}\)

Blair and Stout have suggested that the existence of the shareholder derivative action appears to support the proposition that U.S. corporate law follows the shareholder primacy model.\(^\text{221}\) Nevertheless, they contend that the practical effects of the derivative action actually support the broader interests of the firm, rather than only those of shareholders.\(^\text{222}\) Most obviously, they note that the “requirement that damages be paid directly to the firm and not to the suing shareholders seems difficult to explain under the norm of shareholder primacy.”\(^\text{223}\) Allowing a greater range of persons to bring derivative actions certainly speaks more to communitarian models than to the shareholder primacy model.\(^\text{224}\)

The potential for a broader range of complainants that is provided for under Canadian division of powers corporate statutes, (like the CBCA), creates an important distinction between the Canadian derivative action and its U.S. counterparts. This distinction provides another basis for suggesting that the shareholder primacy model does not hold sway in Canada. Further supporting the opposition to shareholder primacy, the CBCA clearly indicates that evidence of shareholder approval is not determinative in a court’s consideration as to whether a motion to seek leave to commence a derivative action should be allowed.\(^\text{225}\)

\(^{220} \)See Stephanie Ben-Ishai, *A Team Production Theory of Canadian Corporate Law*, 44 ALTA. L. REV. 299, 307 (2007). While the statute allows derivative actions to be brought by any complainant, in practice, most derivative actions are brought by shareholders. See id.

\(^{221} \)See Blair & Stout, *supra* note 13, at 287–88, 293.

\(^{222} \)See id. at 293. These include: (1) the procedural hurdles and substantive limitations on the use of the derivative action; (2) the fact that relief goes to the corporation, rather than the party bringing the derivative action, and; (3) that in certain circumstances, such as in the case of an insolvent corporation or one in the vicinity of insolvency, non-shareholder stakeholders may be granted standing to bring derivative actions. See id. The procedural hurdles associated with the derivative action include, *inter alia*, a requirement for shareholders to first demand that directors take legal action on the corporation’s behalf before they may undertake a derivative action. See id. This requirement exists because corporate management, which possesses the duty to act in the corporation’s best interests, is best-positioned to bring a claim on behalf of the corporation. The exception to this rule arises in situations where a conflict of interest can be shown connecting management’s own actions, or inaction, to the harm the corporation allegedly suffered. See id.

\(^{223} \)Id. at 295.

\(^{224} \)Although Blair and Stout contend that the practical effects of the derivative action support a director primacy norm for U.S. corporate law, these effects do indicate a lack of support for the shareholder primacy model. See Blair & Stout, *supra* note 13, at 290–309.

\(^{225} \)See CBCA § 242(1).
The limited use to date of the derivative action in Canada does not provide conclusive proof that it cannot serve as a significant avenue for either shareholders or other complainants under Canadian law. The question of whether the derivative action is currently being effectively utilized presumably has more to do with the nature of the applications being made and the generally restrictive manner in which the courts have interpreted them, than the ineffectiveness of the action itself. Derivative action clauses in corporate law statutes, after all, are only permissive: they simply grant the ability to complainants to seek leave to bring an action, but they do not guarantee the ability to bring the action itself. That determination rests solely with the courts.

As a result of Peoples and BCE Inc., it is now generally understood that Canadian corporate law follows a model other than shareholder primacy. For this reason, the decisions should influence the manner in which judges assess motions for leave to bring derivative action claims in Canada. Further, the decisions are likely to broaden the instances and range of non-shareholder complainants granted leave to bring those actions in that country.

b. The Oppression Remedy

A person who qualifies as a complainant in order to launch a derivative action under Canadian corporate statutes is also eligible to bring an action for an oppression remedy. Creditors have been found to qualify as complainants under Canadian division of powers corporations statutes, such as the CBCA, and are thus able to seek an oppression remedy where corporate directors and officers act in a manner that is “oppressive or unfairly prejudicial to or that unfairly disregards [their] interests . . . .” In R. v. Sands Motor Hotel Ltd., a creditor was considered to be a “proper person” entitled to bring an application for relief under the oppression remedy. [1985] 36 Sask. R. 45, 48 (Can.); see also Sidaplex-Plastic Suppliers Inc. v. Elta Group Inc., [1999] 40 O.R.3d 563, 563 (Can.); Levy-Russell Ltd. v. Shieldings Inc., [1998] 41 O.R.3d 54, 55 (Can.). In First Edmonton Place, the Alberta Court of Queen’s Bench held that the oppression remedy “would be available if the act or conduct of the directors or management of the corporation which is complained of amounted to using the corporation as a vehicle for committing fraud upon a creditor.” First Edmonton Place, 60 Alta. L.R.2d at 145–46. The court stated:

[The test of unfair prejudice or unfair disregard should encompass the following considerations: the protection of the underlying expectation of a creditor in its arrangement with the corporation, the extent to which the acts complained of were unforeseeable or the creditor could reasonably have protected itself from such acts, and the detriment to the interests of the creditor.]

Id. at 146. The court did indicate, however, that these considerations were illustrative rather than exhaustive. See id.; see also Leonard I. Rotman et al., Canadian Corporate...
however, an oppression remedy is a personal rather than representative suit.\textsuperscript{227} As any awards made pursuant to an oppression remedy accrue to the complainant personally, one might wonder why complainants would not prefer to bring oppression claims as opposed to derivative action claims. The rationale is that important distinctions between these two forms of action exist which demonstrate that they are not interchangeable, and that the choice of action is not entirely the complainant’s to make. Moreover, the ensuing discussion of the oppression remedy in Canada reinforces the conclusion that Canada has rejected the “end of history” thesis. The oppression remedy in Canadian law is a wide-ranging statutory cause of action that gives broad discretion to courts to grant a range of remedial aid to complainants whose legal and equitable interests are deemed to have been “oppressed.” In this sense, it differs from the derivative action, pursuant to which any relief that is granted is awarded to the corporation. Also, unlike the derivative action, a complainant does not require leave of the court to bring an oppression claim. A complainant may file an oppression claim via simple application, which a court may summarily consider, whereas a derivative action may only be commenced by action.\textsuperscript{228}

In the United States, oppression actions may exist either by statutory authority or under the common law. Like the Canadian oppression remedy, they provide minority shareholders with a cause of action that protects them against majority control. Not all states have a statutory oppression remedy in their corporations statutes, however. For example, Delaware does not have an oppression remedy in its leading corporations statute.\textsuperscript{229} Even where statutory oppression actions do exist, they are not as broad as the Canadian variety. Some states have limited op-

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\textsuperscript{227} See Goldex Mines Ltd. v. Revill, [1974] 7 O.R.2d 216, 221 (Can.) (holding that a complainant may join representative and personal actions as long as the procedural requirements for each are fulfilled and the bases for the respective claims are sufficiently distinguished).

\textsuperscript{228} Although an oppression remedy may be pursued by application via the use of affidavit evidence, in practice, the issues in an oppression claim are usually sufficiently complex that a judge will require that the matter be tried by action in order to have the benefits of a full trial. See, e.g., Deluce Holdings Inc. v. Air Canada, [1992] 12 O.R.3d 131, 132 (Can.).

\textsuperscript{229} The lack of an oppression remedy in Delaware could, however, simply affirm the notion of the “race to the bottom,” as many commentators have suggested, given the lack of this broad-based form of stakeholder protection. See Louis K. Liggett Co. v. Lee, 288 U.S. 517, 558–59 (1933); William L. Cary, Federalism and Corporate Law: Reflections upon Delaware, 83 Yale L.J. 663, 664–66 (1974) (discussing the origins of the “race to the bottom” idea in corporate law).
pression provisions that allow for court dissolution of the corporation, while other states’ oppression claims provide for a far wider range of relief. Furthermore, common law oppression actions, which have been sanctioned in leading cases such as *Donahue v. Rodd Electrotype Co.*, are not always available from state to state. Notably, Delaware has failed to sanction the *Donahue*-type common law oppression action. Where oppression actions do exist under U.S. statute or common law, they are generally restricted to close corporations, which involve a rather different stakeholder dynamic than widely-held corporations. This restriction on the availability of oppression actions differs from the situation in Canada, where oppression can exist within either widely-held or close corporations.

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230 See Model Bus. Corp. Act § 14.30(2)(ii) (2005) (providing a similar limited form of oppression where “the directors or those in control of the corporation have acted, are acting, or will act in a manner that is illegal, oppressive, or fraudulent”). Upon proof of such circumstances by a shareholder, a court may dissolve the corporation. See id.

231 See Minn. Stat. Ann. § 302A.751 (West 2004) (authorizing “any equitable relief” and specifically authorizing a buyout of a shareholder’s interest); N.J. Stat. Ann. § 14A:12-7(1) (West 2003) (providing a nonexclusive list of possible relief that includes the order of a buyout and the appointment of a provisional director or custodian); Douglas K. Moll, *Shareholder Oppression and “Fair Value”: Of Discounts, Dates, and Dastardly Deeds in the Close Corporation*, 54 Duke L.J. 293, 308 n.54 (2004). Moll further indicates that domestic courts have asserted that they are not restricted to statutory remedies for oppressive conduct, but may invoke various equitable remedies. Id. at 308 n.55 (citing Brenner v. Berkowitz, 634 A.2d 1019, 1033 (N.J. 1993) (“Importantly, courts are not limited to the statutory remedies [for oppression], but have a wide array of equitable remedies available to them.”)); see also Baker v. Commercial Body Builders, Inc., 507 P.2d 387, 395–96 (Or. 1973) (listing ten “alternative remedies” for oppressive conduct). To the contrary position, however, Moll cites Giannotti v. Hamway, 387 S.E.2d 725, 733 (Va. 1990), which describes the dissolution remedy for oppression as “exclusive” and held that the trial court could not “fashion other . . . equitable remedies.” Other commentators have also indicated the growth of domestic corporate statutory provisions for oppression as extending beyond the remedy of dissolution. See, e.g., Robert B. Thompson, *The Shareholder’s Cause of Action for Oppression*, 48 Bus. Law. 699, 708–09 (1993) (“[I]t makes more sense to view oppression not as a ground for dissolution, but as a remedy for shareholder dissension.”).


233 See Nixon v. Blackwell, 626 A.2d 1366, 1379 (Del. 1993). It might, however, be plausibly argued that Delaware’s comparatively well-developed law of directors’ duties achieves substantially the same result as the oppression remedy, insofar as the majority’s acts of oppression generally require board action to implement. See Reinier R. Kraakman et al., *The Anatomy of Corporate Law: A Comparative and Functional Approach* 126 (2004).

234 That being said, the Canadian Supreme Court has expressly stated that “[t]he size, nature and structure of the corporation are relevant factors in assessing reasonable expectations.” *BCE Inc.*, [2008] 3 S.C.R. at 595–96. The court in *BCE Inc.* also said that “[c]ourts may accord more latitude to the directors of a small, closely held corporation to deviate from strict formalities than to the directors of a large public company,” and correspond-
Beck has described the oppression remedy in Canada as “beyond question, the broadest, most comprehensive and most open-ended shareholder remedy in the common law world . . . unprecedented in its scope.” As with the derivative action, the range of remedies that may be imposed where oppression is found is uncircumscribed: in addition to certain enumerated remedies under section 241(3) of the CBCA, a court possesses the discretion to “make any interim or final order it thinks fit.”

In most circumstances, an act of a corporation or its directors causes oppression. Nonetheless, the actions of shareholders or others may also cause oppression. Section 241 of the CBCA is illustrative of the form taken by the statutory oppression remedy in Canadian corporate law statutes, stating:

(1) Application to court re oppression—A complainant may apply to a court for an order under this section.
(2) Grounds—If, on an application under subsection (1), the court is satisfied that in respect of a corporation or any of its affiliates
(a) any act or omission of the corporation or any of its affiliates effects a result,
(b) the business or affairs of the corporation or any of its affiliates are or have been carried on or conducted in a manner, or
(c) the powers of the directors of the corporation or any of its affiliates are or have been exercised in a manner that is oppressive or unfairly prejudicial to or that unfairly disregards the interests of any security holder, creditor, director or officer, the court may make an order to rectify the matters complained of.

The CBCA describes who may be oppressed and provides indicia of oppression but does not define what it means to be “oppressed.” RA-

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235 Deluce Holdings, 12 O.R.3d at 133 (citing Stanley M. Beck, Minority Shareholder Rights in the 1980s, in Corporate Law in the 80s 311, 312 (Law Soc’y of Upper Can. ed., 1982)).
236 CBCA § 242(3); see Deborah A. DeMott, Foreword, 56 Law & Contemp. Probs. 1, 2 (1993) (describing oppression as “a protean, amoeba-like concept that resists initial definition and indeed operates, at least in the Canadian context, to discourage and even defeat ex ante specifications of entitlements”).
237 See CBCA § 242(1).
238 Id. § 241.
ther, this determination is left to the courts, which have developed a variety of criteria to assist them in this task, including the “reasonable” and “legitimate” expectations of the allegedly oppressed party. In *BCE Inc.*, the Canadian Supreme Court held that the determination of what is “reasonable” is an objective and contextual one rooted in the question: did the complainant reasonably hold the particular expectation claimed? Thus, the subjective expectations of any particular stakeholder are not conclusive. In addition, it said that not every unmet stakeholder expectation, even if reasonable, will give rise to an oppression claim under section 241, unless the conduct complained of is oppressive or unfairly prejudicial, or unfairly disregards the interests at stake.

In *BCE Inc.*, the Canadian Supreme Court suggested the following approach to interpreting the grounds of an oppression claim:

One should look first to the principles underlying the oppression remedy, and in particular the concept of reasonable expectations. If a breach of a reasonable expectation is established, one must go on to consider whether the conduct complained of amounts to “oppression”, “unfair prejudice” or “unfair disregard” as set out in s. 241(2) of the CBCA.

In *Arthur v. Signum Communications Ltd.*, Justice Austin set out a number of factors that indicate the presence of oppressive conduct:

(i) lack of a valid corporate purpose for the transaction;
(ii) failure on the part of the corporation and its controlling shareholders to take reasonable steps to simulate an arm’s length transaction;
(iii) lack of good faith on the part of the directors of the corporation;

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242 *Id.* at 591.

243 *Id.* at 600. The court further indicated that the terms “oppression,” “unfair prejudice,” and “unfair disregard” are not watertight compartments, but often overlap and intermingle. *Id.* at 601.

244 *Id.* at 590.
(iv) discrimination between shareholders with the effect of benefiting the majority shareholder to the exclusion or to the detriment of the minority shareholder;
(v) lack of adequate and appropriate disclosure of material information to the minority shareholders; and
(vi) a plan or design to eliminate the minority shareholder.245

In *BCE Inc.*, the Supreme Court added its own factors, drawn from existing jurisprudence, including “general commercial practice; the nature of the corporation; the relationship between the parties; past practice; steps the claimant could have taken to protect itself; representations and agreements; and the fair resolution of conflicting interests between corporate stakeholders.”246 The Supreme Court indicated in *BCE Inc.* that the oppression remedy, although statutorily created, is equitable in nature and seeks to “ensure fairness—what is ’just and equitable.’”247 Therefore, the oppression remedy provides courts with “broad, equitable jurisdiction to enforce not just what is legal but what is fair.”248 In making this assessment, the Supreme Court reveals in *BCE Inc.* that courts “should look at business realities, not merely narrow legalities.”249

The Canadian Supreme Court concluded that the debentureholders’ expectation of maintaining the investment grade trade value of their debentures was not reasonable. It found that the corporation had been put in play as a result of management exercising its duty to act in the corporation’s best interests. Further, all of the bids for BCE Inc. were leveraged and would have resulted in an increase in Bell Canada’s debt and a corresponding reduction in the trade value of the debentures. The court thus held that no evidence suggested that BCE Inc.’s management could have done anything to avoid the risk to the debentureholders, and, more importantly, the only evidence on point indicated that the risk posed to the debentureholders resulting from the LBO was inevitable.250 Accordingly, the court deferred to the business judgment of management to accept the purchaser’s offer.251

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247 *Id.* at 590.
248 *Id.*
250 *BCE Inc.*, [2008] 3 S.C.R. at 605–06. Indeed, in setting out the terms of the auction process, BCE Inc. had advised potential participants that, in evaluating their bids, it would
Although the court found that management had considered the interests of the debentureholders, there was no corresponding duty on management to act in those interests when management also had to consider competing stakeholder claims and the interests of the corporation itself. What the court did find was that management had considered the debentureholders’ interests and had assured them that the terms of the debentures would be met, but ultimately determined that those interests had to be subordinated to other concerns. As a result, the Supreme Court determined that there was no need for it to consider whether the conduct cited in the complaint oppressed, unfairly prejudiced, or unfairly disregarded the debentureholders’ interests.

In practice, Canadian courts have imported fiduciary duty considerations into their analyses of oppression claims. Thus, courts assessing whether oppression exists often examine whether management’s actions are consistent with the corporation’s best interests, rather than focusing solely on the reasonable and legitimate expectations of com-

“consider the impact that their proposed financial arrangements would have on BCE and on Bell Canada’s debentureholders and, in particular, whether their bids respected the debentureholders’ contractual rights under their trust indentures.” Id. at 576.

251 Id. at 607–08. The court stated:

The best interests of the corporation arguably favoured acceptance of the offer at the time. BCE had been put in play, and the momentum of the market made a buyout inevitable. . . . Provided that, as here, the directors’ decision is found to have been within the range of reasonable choices that they could have made in weighing conflicting interests, the court will not go on to determine whether their decision was the perfect one.

Id. The Business Judgment Rule does not properly apply to ward off allegations of management’s breach of fiduciary duty, however. See United Copper, 244 U.S. at 263–64.


253 Id. at 608. The court also held that the trial judge had not erred in approving the arrangement under section 193 of the CBCA, though that issue is not particularly relevant to the matters considered herein. Id. at 611.

254 See, e.g., Ballard Ltd., [1991] 3 B.L.R.2d at 113. The court held that:

while it would be appropriate for a director to consider the individual desires of one or more various shareholders . . . it would be inappropriate for that director (or directors) to only consider the interests of certain shareholders and to either ignore the others or worse still act in a way detrimental to their interests. The safe way to avoid this problem is to have directors act in the best interests of the corporation [and have the shareholders derive their benefit from a “better” corporation].

Id.
plaintiffs.\textsuperscript{255} Indeed, there are similarities between breach of fiduciary duty claims and oppression claims. Neither requires the presence of bad faith,\textsuperscript{256} notwithstanding that oppressive conduct is necessarily antagonistic to the interests of the complainant and may, in fact, be exploitative. Additionally, both oppression and fiduciary duty claims depend on context, are fact-specific, and are activated upon certain forms of inequitable conduct or unfairness.

Unlike breach of fiduciary duty claims, which concern duties owed to the corporation, the analysis of oppression claims concerns the reasonable and legitimate expectations of complainants. As the oppression remedy is personal to the complainant, it is only concerned with the complainant’s interests to the extent that those are consistent with the complainant’s reasonable and legitimate expectations. Meanwhile, management owes fiduciary duties to the corporation. Therefore, whether the actions of management in allegedly oppressing a complainant are consistent with the corporation’s best interests—which may or may not be consonant with the corporation’s best interests generally speaking—ought not be material to the disposition of the oppression claim.

The continued use of fiduciary duty analysis in oppression cases may be affected by the \textit{Peoples} judgment. In \textit{Peoples}, management’s fiduciary duty was distinguished from the oppression remedy through the court’s statement that the Peoples directors did not owe creditors a fiduciary duty, but that creditors ought to have instead argued that they were oppressed by the directors’ actions. That being said, the earlier warning to keep fiduciary duty analysis out of considerations of oppression claims in \textit{Brant Investments Ltd. v. KeepRite Inc.} seems to have had little impact on subsequent analyses of oppression claims. The \textit{Brant Investments} court had stated:

\textsuperscript{255} See \textit{Peoples}, [2004] 3 S.C.R. at 481 (referencing \textit{Ballard Ltd.} and approving the notion proposed in \textit{Ballard Ltd.}, that acting in the best interests of the corporation is an appropriate benchmark for management in resolving conflicts between majority and minority shareholders).

It must be recalled that in dealing with s. 234 [the oppression remedy section in the Ontario Business Corporations Act (“OBCA”)], the impugned acts, the results of the impugned acts, the protected groups, and the powers of the court to grant remedies are all extremely broad. To import the concept of breach of fiduciary duty into that statutory provision would not only complicate its interpretation and application, but could be inimical to the statutory fiduciary duty imposed upon directors in s. 117 [the provision for directors’ and officers’ fiduciary duties under the OBCA, which is now section 122(1)].

Adding to the confusion is that the judgment in BCE Inc. also indicates that fiduciary analysis *does* have a role to play in the assessment of oppression claims.

In assessing whether BCE Inc.’s management oppressed, unfairly prejudiced, or unfairly disregarded the debentureholders’ interests in agreeing to the LBO and reducing the trading value of their debentures below investment grade, the Supreme Court held that it had to consider whether management engaged in a fair resolution of the conflicting interests of the corporation and of its stakeholders. This required determining whether management discharged its fiduciary duty to act in the best interests of the corporation which, in turn, comprehended “a duty to treat individual stakeholders affected by corporate actions fairly and equitably.” Thus, if management did not equitably and fairly consider all competing interests of individual stakeholders in agreeing to the LBO as required by oppression jurisprudence, it would have also failed to discharge its fiduciary duty.

The Canadian Supreme Court in BCE Inc. effectively held that the process of assessing whether management engaged in the fair resolution of conflicting stakeholder interests—a necessary part of the inquiry into whether the expectations of a complainant are reasonable under the oppression remedy—is inextricably linked with management’s fiduciary duty to act in the corporation’s best interests. This inference is reflected in the court’s statement that, in oppression cases, it must inquire as to whether “in all the circumstances, the directors acted in the best interests of the corporation, having regard to all relevant considerations, including, but not confined to, the need to treat af-

257 See Brant Invs., [1991] 3 O.R.3d at 301.
259 Id.
fected stakeholders in a fair manner, commensurate with the corporation’s duties as a good corporate citizen.”

Before the court examines whether the complainant has been oppressed, however, it must first establish that the complainant’s expectations were reasonable or legitimate.

In assessing the threshold issue of whether the debentureholders reasonably held the expectation that the directors of BCE Inc. would have maintained the trading value of their debentures as investment grade, the Supreme Court indicated that it could take into account whether the debentureholders could have protected themselves against the harm they claim to have suffered. The court also stated that it would examine whether the directors attempted to resolve the conflicting interests of the various stakeholders and those of the corporation “in accordance with their fiduciary duty to act in the best interests of the corporation, viewed as a good corporate citizen.” As suggested above, this statement suggests that the corporation’s duties as a “good corporate citizen” require its management to consider the interests of all of its stakeholders, not only its shareholders.

This implication is not at all consistent with the adoption of a shareholder primacy model of corporate governance.

c. A Comparison of Statutory Remedies

Although a complainant in Canada is eligible to bring either a derivative action (with leave of the court) or an oppression claim, and may, in fact, join the two, in most circumstances the action giving rise to a derivative action claim will not give rise to an oppression remedy, and vice versa. Thus, complainants do not have the ability to choose whether to pursue a derivative action or an oppression remedy absent special or unique circumstances in which harm can be caused to both the corporation and to its shareholders from the same conduct.

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260 Id.
261 Id. at 597.
262 Id. at 597–98.
263 Id. at 598 (stating “[t]here is no principle that one set of interests—for example the interests of shareholders—should prevail over another set of interests”).
264 See Charlebois v. Bienvenue, [1967] 2 O.R. 635, 644 (Can.) (finding that the holding of an annual meeting and election of directors after directors had sent out a misleading information circular was a breach of the directors’ fiduciary duty to the corporation). In discussing this judgment, the Ontario Court of Appeal concluded that this action would also be a breach of duty to the shareholders as well as a breach of duty to the corporation. See Goldex Mines Ltd., [1974] 7 O.R.2d at 218–19.
In the absence of such rare circumstances, the determination of which of these causes of action is appropriate hinges on a court’s assessment of the party suffering the primary harm from the act alleged to have occurred, as cited in a complaint. Accordingly, if an action causes harm to a corporation and has incidental effects on its shareholders, a derivative action is the only appropriate claim. For example, where an impugned action causes a corporation to become insolvent, thereby resulting in a loss of shareholder equity, the shareholders’ loss is deemed to be merely incidental to the primary harm to the corporation. Consequently, a derivative action, not an oppression remedy, is the appropriate claim.

As with the conclusions drawn from the analyses of notable U.S. cases such as *Dodge*, *Shlensky*, *Unocal*, *Revlon*, and *Paramount*, the Canadian Supreme Court’s judgments in *Peoples* and *BCE Inc.* clearly demonstrate that Hansmann and Kraakman’s assertion of the triumph of the shareholder primacy model does not hold sway in Canada. Moreover, these judgments are consistent with the structure of Canadian division of powers corporations statutes, which illustrate—particularly through the breadth of the derivative action and the existence of the oppression remedy—that the shareholder primacy model does not accurately describe the operation of corporate governance in Canada.

**Conclusion**

On the basis of the arguments posed herein, it may fairly be stated that Hansmann and Kraakman’s bold proclamation of the end of history for corporate law is, at best, premature, and, at worst, incorrect.

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265 See *Hercules Mgmt. Ltd.*, [1997] 2 S.C.R. at 175. Shareholders acting in the capacity of supervising management’s conduct relied on negligently prepared auditor reports. Shareholders made decisions in reliance on those reports, which resulted in the corporation going into receivership. As a result, the shareholders lost their equity in the corporation. They sought an oppression remedy against the auditors in order to recover their lost equity. The Canadian Supreme Court held that the audit reports were prepared to allow the shareholders to supervise management’s conduct and to make decisions concerning the administration of the corporation. Consequently, the court determined that the shareholders were not relying on the audit reports to protect their own individual interests, but, in the “managerial role” they undertook, they relied on the reports to act for the general benefit of the corporation. The court concluded that the primary harm caused by the negligently prepared reports was to the corporation, which went into receivership, with the shareholders suffering an incidental harm—the loss of their equity in the corporation. See *id.* at 212–13; see also *Tooley v. Donaldson, Lufkin & Jenrette Inc.*, 845 A.2d 1031, 1039 (Del. 2004) (“The stockholder must demonstrate that the duty breached was owed to the stockholder and that he or she can prevail without showing an injury to the corporation.”).
This Article has provided various bases to suggest that the confidence with which they made their pronouncement has little substantive foundation in either U.S. or Canadian corporate jurisprudence.

Prominent U.S. corporate judgments as discussed in Part II.A fit far less comfortably with Hansmann and Kraakman’s suggestion of the end of history for corporate law than may have previously been surmised. These corporate judgments include *Dodge v. Ford*, *Shlensky v. Wrigley*, and *Unocal v. Mesa Petroleum Corp.*, which are generally regarded as the beacons for shareholder primacy advocates, and *Revlon Inc. v. MacAndrews & Forbes Holdings, Inc.*, which advocates the need to maximize shareholder benefits upon the inevitable breakup of a company subject to a takeover bid. Hansmann and Kraakman’s assertion of the triumph of the shareholder-oriented model of the corporation would, therefore, appear to be premised more upon conjecture and the power of suggestion, rather than upon a solid foundation in legal reality.

The Canadian Supreme Court’s recent judgments in *Peoples* and *BCE Inc.* reveal a rather different understanding of management’s duties in corporate governance than the view espoused by Hansmann and Kraakman. So, too, does the structure of Canadian corporate law statutes, as evidenced by the physical and conceptual separation of management’s fiduciary duties from its duty of care, the broader range of individuals granted standing to bring derivative actions on behalf of corporations in Canada than in the United States, and the existence of the statutory oppression remedy that provides significant relief for a broad range of aggrieved corporate stakeholders.

This is not to suggest that the shareholder primacy model is an entirely unattractive one. It appears to be a simple solution, buttressed by the “science” of law and economics. It is certainly easier to discern the success of management in fulfilling this model by looking to the price of corporate shares than it is to satisfy a broader constituency-based approach, which requires the satisfaction of multiple stakeholder interests. It might also be argued that the disparate interests of stakeholders under progressive models of corporate governance facilitate a “duty to many equals yet a duty to none” syndrome.

Fulfilling a stakeholder-centered model of corporate governance is necessarily more difficult than satisfying the shareholder primacy model. Appearances are often deceiving, however. The fact that the shareholder primacy model is easier to fulfill says nothing about whether it is a more appropriate basis for assessing the role of corporate management in corporate governance. The shareholder primacy model also places an inordinate amount of emphasis on share price, which might also encourage
share price manipulation or shady accounting practices to achieve that goal, as most notably seen in the Enron scandal.

Although the apparent simplicity and definitiveness of the shareholder primacy model is attractive, it drastically oversimplifies matters. As Plato once suggested in his dialogue Statesman, “A perfectly simple principle can never be applied to a state of things which is the reverse of simple.” Corporate law is complex, and attempts to oversimplify it are either bound to fail or, at a minimum, to mislead. Nonetheless, the idea that corporate governance ought to be understood solely by reference to theories of shareholder primacy is often treated by its proponents as if it was so obvious that everyone must accept it.

Indeed, Hansmann and Kraakman begin their article “The End of History for Corporate Law” by asserting that “there is no longer any serious competitor to the view that corporate law should principally strive to increase long-term shareholder value.” They conclude in much the same way, stating that “the triumph of the shareholder-oriented model of the corporation over its principal competitors is now assured.” This posturing has come largely in the place of substantive argument. In fact, it is almost as if they are asking readers to see shapes in the clouds simply by the force of suggestion. This is reminiscent of a dialogue in Shakespeare’s Hamlet between Hamlet and Polonius:

Hamlet: Do you see yonder cloud that’s almost in the shape of a camel?
Polonius: By th’ mass, and ’tis like a camel indeed.
Hamlet: Methinks, it is a weasel.
Polonius: It is back’d like a weasel.
Hamlet: Or like a whale?
Polonius: Very like a whale.

There is no need for those who study corporate law to play Polonius to the shareholder primacy Hamlets who seek to fill their heads with inappropriate characterizations of the status of contemporary corporate governance. The latter’s insinuations and conclusions are as amorphous as the clouds upon which they are based. This does not mean that we ought not listen to what shareholder primacy advocates have to say, only that we ought not uncritically accept it as gospel.

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266 Plato, Statesman, in The Dialogues of Plato 322 (Benjamin Jowett ed., 1937).
267 Hansmann & Kraakman, supra note 1, at 439.
268 Id. at 468.
269 See Hansmann, How Close Is the End of History?, supra note 45, at 745.
270 William Shakespeare, Hamlet act 3, sc. 2.
Winkler has indicated, the conclusion that corporate law has reached the end of history rests “on an artificially narrow understanding of corporate governance.” Nevertheless, the basis for the same assertion made herein differs from the rationale that he offers for it.

Winkler argues that the existence of broader stakeholder protections that sit outside of “traditional” corporate law serve as a basis for contesting Hansmann and Kraakman’s claim of the end of history for corporate law. As Winkler explains it:

Despite the common conception of corporate governance as pertaining to shareholder-management relations, the actual decisionmaking of corporate officers is heavily constrained by legal rules from outside of corporate law. . . . One must take into account environmental law, labor law, civil rights law, workplace safety law, and pension law, lest one be left with a distorted and incomplete view of how the law actually shapes those corporate decision matrices.272

This Article does not suggest that Winkler is incorrect in his assertions about the implications of the broader area of business law on corporate behavior and governance. Rather, it contends that the same conclusion can be reached within the narrower field of corporate law itself.

A noted commentator has provided the following appraisal of corporate management’s duties:

I venture to assert that when the history of the financial era which has just drawn to a close comes to be written, most of its mistakes, and its major faults will be ascribed to the failure to observe the fiduciary principle, the precept as old as holy writ, that “a man cannot serve two masters.” . . . No thinking man can believe that an economy built upon a business foundation can permanently endure without some loyalty to that principle.273

These words were written in 1934 by former U.S. Supreme Court Chief Justice Harlan Stone. Nevertheless, they remain as relevant today as they were then. Directors cannot properly serve the best interests of corporations and shareholders when the interests of these groups are frequently not aligned. Chief Justice Stone’s emphasis on the contin-


272 Id. at 128.

ued importance of foundational principles in corporate law may also be seen to parallel the sentiments of President Barack Obama in his inaugural speech characterizing the challenges that lie ahead for the United States as a result of the current economic climate:

That we are in the midst of crisis is now well understood. . . . Our economy is badly weakened, a consequence of greed and irresponsibility on the part of some, but also our collective failure to make hard choices and prepare the nation for a new age. . . . Nor is the question before us whether the market is a force for good or ill. Its power to generate wealth and expand freedom is unmatched. But this crisis has reminded us that without a watchful eye, the market can spin out of control—the nation cannot prosper long when it favors only the prosperous. . . . Our challenges may be new. The instruments with which we meet them may be new. But those values upon which our success depends—honesty and hard work, courage and fair play, tolerance and curiosity, loyalty and patriotism—these things are old. These things are true. They have been the quiet force of progress throughout our history. What is demanded then is a return to these truths.274

The reality of contemporary corporate law is that, some seventy years after the Berle-Dodd debate over corporate purpose and more than fifty years after Berle conceded defeat to Dodd’s vision, corporate law scholars continue to argue over the most appropriate model of corporate governance.275 This Article adds to a debate that is not likely to end soon. Such a situation is certainly not consistent with the “end of history” for corporate law.

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274 President Barack Obama, Inaugural Address (Jan. 20, 2009), available at http://www.whitehouse.gov/blog/inaugural-address/.

275 See Stout, supra note 133, at 1200 (arguing that the true issue emanating from the Berle-Dodd debate is which choice is worse, “to require directors to maximize shareholder wealth, even . . . where shareholder wealth maximization is inefficient? Or to allow directors to look at the interests of nonshareholder ‘stakeholders,’ recognizing that they may use their enhanced discretion to serve themselves?”).
PIRACY LAWS AND THE EFFECTIVE PROSECUTION OF PIRATES

Diana Chang*

Abstract: This Note analyzes the current international legal framework for the punishment and prosecution of maritime piracy. Piracy is an international problem that disrupts global maritime trade and endangers the safety and security of crewmen and ship owners. Although it is a well-recognized principle that each state has universal jurisdiction to prosecute pirates, the conflicting international definitions of piracy and the preponderance of attacks near states that lack resources to effectively prosecute pirates create a gap in enforcement within the international legal framework. This Note proposes that cooperating states should establish regional international piracy tribunals that can apply an appropriate, uniform definition of piracy while providing the judicial resources to enforce international piracy laws.

Introduction

Maritime piracy is a continuing international problem that disrupts shipping lanes, the world economy, and the safety and security of crewmen and ship owners.¹ In the first nine months of 2009, there were 294 reported pirate attacks from all over the world.² These attacks included thirty-four successful hijackings and 559 hostages.³ The majority of these reported attacks occur in Southeast Asia, off the Horn of Africa, and along the West Coast of Africa, with a few attacks scattered along the coast of South America.⁴

Within international law there is a well-recognized principle that each state has universal jurisdiction to prosecute pirates.⁵ Nevertheless,

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³ Id.
the current legal framework creates a problem of “catch and release” because pirates are often released shortly after their capture due to lax domestic laws that do not adequately punish the offenders, or due to a state’s unwillingness to prosecute the offenders for various political reasons.\(^6\)

Part I of this Note outlines the current international and regional legal framework for the prosecution of pirates. It discusses the applicable international treaties and organizations that relate to maritime security and how these treaties and organizations affect states on a regional and domestic level. Part II identifies problems with the existing international legal framework, specifically, the lack of uniformity in the prosecution and punishment of pirates. Part III suggests that the variety of domestic laws creates a confusing patchwork of penalties and procedures that could be resolved with the creation of regional piracy tribunals.

I. Background

A. International Legal Framework Governing the Safety of Maritime Navigation

Piracy is an international crime that falls under every state’s jurisdiction under customary international law.\(^7\) Universal jurisdiction endows every state with the right to prosecute and punish piracy regardless of where the attack occurs.\(^8\) Because of universal jurisdiction, each state has the responsibility to prosecute pirates under its own domestic laws irrespective of a pirate’s original nationality, the registry of the ship, or the destination of the cargo.\(^9\)

The United Nations Convention on the Law of the Sea (UNCLOS) codified the customary international law on piracy in Articles 100 to 107.\(^10\) Given that UNCLOS is a codification of customary international law, it is binding on every state including non-parties to the convention.\(^11\) Articles 100 to 107 of UNCLOS govern the provisions relating to

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\(^7\) Bederman, supra note 5, at 76.


\(^9\) Martin N. Murphy, Small Boats, Weak States, Dirty Money: The Challenge of Piracy 12 (2009); see Bederman, supra note 5, at 189.


\(^11\) Azubuike, supra note 8, at 49.
the definition, jurisdiction, and obligations of member states seeking to pursue, capture, and prosecute maritime pirates.\textsuperscript{12} Under UNCLOS, there are four essential elements to the definition of piracy: 1) an illegal act involving violence, detention, or depredation 2) committed for private ends 3) on the high seas 4) involving at least two ships.\textsuperscript{13} UNCLOS also reaffirms the idea of universal jurisdiction because it gives every state jurisdiction to seize and prosecute pirates according to that state’s domestic laws.\textsuperscript{14}

By contrast, the Suppression of Unlawful Acts Against the Safety of Maritime Navigation (SUA) expands the types of activity that may be prosecuted while limiting the jurisdictional requirements necessary to prosecute.\textsuperscript{15} This treaty defines an offense as 1) intentionally seizing or damaging a ship or 2) attempting to seize or damage a ship.\textsuperscript{16} The SUA definition eliminates the motive requirements that UNCLOS contains in its “for private ends” element.\textsuperscript{17} The convention also expands the UNCLOS definition of piracy because it applies to any ship navigating to, through, or from the territorial seas.\textsuperscript{18} Under SUA, a state has jurisdiction over an offense only if it is committed against a ship flying that state’s flag, in that state’s territory, or committed against a national of that state.\textsuperscript{19}

SUA also imposes an obligation on member states to extradite or prosecute the suspected offender.\textsuperscript{20} If the capturing state cannot establish jurisdiction, SUA requires that it extradite the offender to a state that has successfully established jurisdiction.\textsuperscript{21} Thus far, there are 134 countries that have subscribed to SUA, but the mandatory extradite or prosecute requirement deters many Southeast Asian states from ratifying it.\textsuperscript{22}

\textsuperscript{12} UNCLOS, \textit{supra} note 10, arts. 100–107.

\textsuperscript{13} \textit{Id.} art. 101; Rosemary Collins & Daud Hassan, \textit{Applications and Shortcomings of the Law of the Sea in Combating Piracy: A South East Asian Perspective}, 40 J. MAR. L. & COM. 89, 94 (2009).

\textsuperscript{14} See UNCLOS, \textit{supra} note 10, art. 105.


\textsuperscript{16} SUA, \textit{supra} note 15, art. 3.

\textsuperscript{17} Collins & Hassan, \textit{supra} note 13, at 107.

\textsuperscript{18} SUA, \textit{supra} note 15, art. 4.

\textsuperscript{19} \textit{Id.} art. 6.

\textsuperscript{20} Id. art. 10; Collins & Hassan, \textit{supra} note 13, at 108.

\textsuperscript{21} SUA, \textit{supra} note 15, art. 10.

In addition to multilateral treaties, there are several international organizations such as the International Chamber of Commerce’s International Maritime Bureau (IMB) and the International Maritime Organization (IMO) that seek to ensure the safe navigation of ships. The IMB is a non-profit organization whose stated goal is to fight maritime crime, such as piracy. The IMB established its Piracy Reporting Centre in Kuala Lumpur, Malaysia to monitor and provide advice on the growing piracy problem worldwide. The Piracy Reporting Centre is funded through voluntary contributions. The Centre’s stated purpose is to provide a centralized information center on pirate attacks and to educate and warn shippers and traders about high-risk areas. The IMB also performs other functions such as investigation services and litigation support. Additionally, it has the capability to track hijacked and phantom ships.

For statistical purposes, the IMB adopts a broad definition of piracy that includes actual and attempted attacks both when the ship is at anchor or at sea. Thus, the IMB defines “piracy and armed robbery” as “an act of boarding or attempting to board any ship with the apparent intent to commit theft or any other crime and with the apparent intent or capability to use force in the furtherance of that act.” The IMB’s expansive definition affects the number of attacks that the IMB will track. Since this definition differs from the UNCLOS and SUA

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25 IMB Piracy Reporting Centre, supra note 25.
26 Id.
27 Id.
29 IMB Investigation Services, supra note 28; IMB Case Work, supra note 28.
30 IMB Report, supra note 24, at 4.
31 Id.
definitions of piracy, not every incident reported to IMB would be considered formal piracy under international law.\footnote{Azubuike, \textit{supra} note 8, at 45.}

In contrast to the IMB’s stated purpose, the IMO’s purpose is to develop a regulatory framework to maintain safe, secure, and efficient shipping over the high seas.\footnote{Introduction to IMO, \textit{supra} note 23.} To improve security on the high seas and at port facilities, the IMO develops initiatives to combat two types of threats: piracy, as defined in UNCLOS, and armed robbery at sea.\footnote{Zou Keyuan, \textit{supra} note 32, \S\ 8; Int’l Marititme Org., Piracy and Armed Robbery Against Ships, http://www.imo.org/Facilitation/mainframe.asp?topic_id=362#top (last visited Apr. 20, 2010) [hereinafter Piracy and Armed Robbery Against Ships].} Piracy can only occur on the high seas, while armed robbery at sea can only occur in territorial waters that are within twelve miles of a nation’s coastline.\footnote{Azabuike, \textit{supra} note 8, at 50; Zou Keyuan, \textit{supra} note 32, \S\ 8.}

Recognizing the importance of domestic laws in the successful prosecution of pirates, the IMO passed Resolution A. 1025 (26), which encourages states to ratify enabling legislation that would codify their universal jurisdiction over piracy and establish procedures to facilitate the prosecution of pirates.\footnote{Int’l. Maritime Org. [IMO], \textit{Code of Practice for the Investigation of the Crimes of Piracy and Armed Robbery Against Ships}, IMO Assemb. Res. A. 1025 (26) (Dec. 2, 2009)).} Resolution A. 1025 (26) also recommends guidelines for piracy investigation strategies.\footnote{See generally id. (describing the suggested piracy investigation guidelines for member countries).} The resolution suggests that flag states of the victimized ship should take the lead in investigations for piracy incidents; conversely, the state in whose territorial waters the incident occurs should bear the responsibility to investigate armed robbery at sea.\footnote{Id.}

The IMO not only creates a technical framework to deal with piracy and armed robbery at sea, but it also aims to foster regional agreements to counter piracy.\footnote{Piracy and Armed Robbery Against Ships, \textit{supra} note 35.} It holds regional seminars and workshops in piracy-infested areas to identify measures that may diminish pirate attacks in that specific region.\footnote{INT’L MAR. ORG., IMO Leads New Anti-Piracy Initiative, Mar. 13, 2001, http://www.imo.org/ (follow “Newsroom” hyperlink; then follow “IMO Press Briefings” hyperlink; then follow “Archive - 2001 Press Briefings” hyperlink) [hereinafter IMO Leads Anti-Piracy Initiative]; Piracy and Armed Robbery Against Ships, \textit{supra} note 35.} In the past decade, the IMO has held re-
gional seminars in Southeast Asia, Brazil, and with the states in the Gulf of Aden.\footnote{42}

\section*{B. Regional Institutions and Domestic Developments in the Enforcement of International Laws}

In recent years, there has been a trend towards more regional approaches to solve the piracy problem.\footnote{43} In 2004, sixteen regional Southeast Asian states signed the Regional Cooperation Agreement on Combating Piracy and Armed Robbery Against Ships in Asia (ReCAAP), which was the first multilateral agreement to address piracy in Southeast Asia.\footnote{44} ReCAAP established an Information Sharing Centre in Singapore.\footnote{45} In 2009, twenty-eight nations and six international organizations formed the Contact Group on Piracy off the Coast of Somalia to address piracy problems emanating from the Horn of Africa.\footnote{46} The common stated objectives for both regional groups include promoting information exchange, supporting capacity-building efforts, and facilitating the regional operations of member states.\footnote{47}

Other regional organizations aimed at maintaining maritime security include the Maritime Organization of West and Central Africa (MOWCA), which has its own sub-regional coast guard network.\footnote{48} More recently, in an IMO-sponsored meeting for East African states, nine East African states signed the Djibouti Code, which creates a network of information centers to report pirate attacks.\footnote{49} Although this agreement is


\footnote{44} ReCAAP Info. Sharing Centre, About ReCAAP ISC, http://www.recaap.org/about/about1_2.html (last visited Apr. 20, 2010) [hereinafter About ReCAAP ISC].

\footnote{45} Id.


\footnote{47} Id.; About ReCAAP ISC, supra note 44, at 3.

\footnote{48} James Kraska & Brian Wilson, Combating Pirates of the Gulf of Aden: The Djibouti Code and the Somali Coast Guard, 52 Ocean & Coastal Mgmt. 516, 519 (2009).

\footnote{49} Id. at 519, 520.
not legally binding, signatories agreed to arrest and prosecute pirates and to help repatriate hostages.\textsuperscript{50}

Despite the codification of universal jurisdiction and the push for greater regional cooperation, customary international law still requires domestic legislation to prosecute the crime.\textsuperscript{51} Because states have discretion in their construction of domestic legislation on piracy, the incorporation of the full jurisdictional provisions from SUA and UNCLOS varies from state to state.\textsuperscript{52} For instance, China has no specific anti-piracy legislation but rather prosecutes piracy under its general Criminal Code.\textsuperscript{53} China’s general Criminal Code incorporates any crime that is defined in a Chinese-ratified international treaty.\textsuperscript{54} In contrast, Australia has incorporated all of UNCLOS’s piracy provisions into Part IV of its Crimes Act of 1914.\textsuperscript{55} Similarly, the United States has enacted the majority of the provisions from the SUA in 18 U.S.C. § 2280.\textsuperscript{56}

UNCLOS and SUA themselves are silent regarding the prosecution of captured pirates, leaving such decisions to the discretion of each individual state’s legal systems.\textsuperscript{57} Consequently, it is difficult for some states to prosecute pirates because of procedural impediments that are not “forward-thinking.”\textsuperscript{58} Other states lack resources to spend on a full trial and possible imprisonment of the accused.\textsuperscript{59}

Even in states that possess the necessary resources and procedures for pirate prosecution, political reasons may prevent a pirate’s prosecution.\textsuperscript{60} For example, the United Kingdom will not prosecute pirates of certain nationalities because its asylum laws might allow the offender to

\begin{itemize}
\item \textsuperscript{50} Id. at 520.
\item \textsuperscript{52} Murphy, supra note 9, at 12.
\item \textsuperscript{53} Collins & Hassan, supra note 13, at 102.
\item \textsuperscript{54} Id.
\item \textsuperscript{55} Id.
\item \textsuperscript{56} Violence Against Maritime Navigation, 18 U.S.C. § 2280 (1996); Dahlvang, supra note 51, at 23.
\item \textsuperscript{57} See SUA, supra note 15, art. 10; UNCLOS, supra note 10, art. 105.
\item \textsuperscript{58} Baumgartner Testimony—Piracy Hearing, supra note 43, at 27.
\item \textsuperscript{59} Kraska & Wilson, supra note 1, at 3.
\item \textsuperscript{60} International Efforts to Combat Maritime Piracy: Hearing Before the Subcomm. on International Organizations, Human Rights and Oversight of the Comm. on Foreign Affairs H.R., 111th Cong. 27 (2009) (testimony of Ambassador Stephen Mull, Senior Advisor, Under Secretary for Political Affairs, U.S. Department of State) [hereinafter Mull Testimony—Piracy Hearing].
\end{itemize}
remain in the country indefinitely after trial.\textsuperscript{61} In addition, the British Foreign Office in London issued a legal opinion stating that Somalian pirates who would be subject to harsh treatment in Somalia cannot be deported because such deportation would violate the British Human Rights Act.\textsuperscript{62} Similarly, the Portuguese will only arrest pirates when Portuguese nationals or ships are involved.\textsuperscript{63}

To resolve this enforcement problem, the United States and the United Kingdom signed a Memorandum of Understanding with Kenya in 2009 to send pirates captured by their navies to Kenyan courts for prosecution.\textsuperscript{64} Given the massive Kenyan caseload and Kenya’s inexperienced legal system, there are doubts as to whether this agreement will lead to more effective prosecutions of pirates.\textsuperscript{65}

Even after offenders are successfully prosecuted, states differ in the type of punishments meted out.\textsuperscript{66} For example, China has no word for “piracy,” and thus it prosecutes pirates for armed robbery and murder instead.\textsuperscript{67} Its punishments range from as few as ten years in prison to death.\textsuperscript{68} Likewise, the Brazilian pirates who robbed and murdered a famous New Zealand yachtsman were sentenced to thirty-seven years for armed robbery and murder, instead of piracy.\textsuperscript{69} When adjudicating on the charge of piracy, Indian courts sentenced fourteen Indonesian pirates to seven years of hard labor,\textsuperscript{70} and Argentina may sentence a pirate to three to fifteen years in prison even if no one is killed during the attack.\textsuperscript{71} By contrast, Indonesian courts have been known to give pirates as little as two to four years in prison.\textsuperscript{72}


\textsuperscript{63} Wrong Signals; Piracy. Pirates and Legal Knots, \textit{Economist}, May 9, 2009, at 1.

\textsuperscript{64} Baumgartner Testimony—Piracy Hearing, supra note 43, at 17.

\textsuperscript{65} See Mwaurap, supra note 61. But see Kraska & Wilson, supra note 1, at 3.

\textsuperscript{66} Mull Testimony—Piracy Hearing, supra note 60, at 32; see Dahlvang, supra note 51, at 24–25.

\textsuperscript{67} Zou Keyuan, supra note 32, ¶ 55.

\textsuperscript{68} Id.


\textsuperscript{70} Dahlvang, supra note 51, at 25.


\textsuperscript{72} Id. at 40.
The variations of legal frameworks within the international community and among states creates a variety of definitions and penalties for piracy.\(^{73}\) This lack of uniformity in piracy laws interferes with the effective prosecution of pirates.\(^{74}\)

II. Discussion

The current international legal framework on piracy is flawed because it does not provide a universally applicable definition of piracy, and because it does not create uniform guidelines for the prosecution and punishment of pirates.\(^{75}\) There is a discrepancy between the offense of piracy under international law and how the offense is actually prosecuted and punished under each state’s domestic laws.\(^{76}\)

The UNCLOS definition of piracy has four elements: 1) an illegal act involving violence, detention, or depredation 2) committed for private ends 3) on the high seas 4) involving at least two ships.\(^{77}\) Scholars criticize the first element because it categorically excludes all attempted hijackings or clandestine attacks, where attackers board at night and steal cargo without the knowledge of the crew.\(^{78}\) Thus, while this definition adequately describes Somali pirate attacks in which pirates are generally armed with AK-47s and rocket-propelled grenades,\(^{79}\) it does not adequately describe pirate attacks in Southeast Asia and Brazil that may include clandestine robberies of ships at anchor.\(^{80}\)

Moreover, the “private ends” element in the UNCLOS definition is heavily criticized because it incorporates a motive requirement that excludes political terrorism and not-for-profit attacks.\(^{81}\) For example, an armed attack meant to bring international attention to a group’s struggle for independence is not executed for “private ends” because it is not performed to profit the attackers.\(^{82}\) In similar fashion, hijacking

\(^{73}\) See generally Dahlvang, supra note 51; Zou Keyuan, supra note 32.

\(^{74}\) Baumgartner Testimony—Piracy Hearing, supra note 43, at 27.

\(^{75}\) Collins & Hassan, supra note 13, at 97–98, 108–09.

\(^{76}\) Id. at 112.

\(^{77}\) See UNCLOS, supra note 10, art. 101.

\(^{78}\) Collins & Hassan, supra note 13, at 96–97.


\(^{82}\) Collins & Hassan, supra note 13, at 99.
done for a political motive is also not piracy under the UNCLOS definition.\textsuperscript{83} Accordingly, political motivation becomes a legitimate defense to piracy under this definition.\textsuperscript{84}

Furthermore, the “two-ship” requirement excludes mutiny as an act of piracy because the internal seizure of a ship does not involve two separate ships.\textsuperscript{85} Scholars have often debated whether to add political terrorism and mutiny to the UNCLOS definition of piracy.\textsuperscript{86} Political terrorism and mutiny, however, have different root causes and different solutions than piracy does.\textsuperscript{87} Terrorists typically seek to draw attention to a cause regardless of whether the offenders profit from the attack, while pirates are solely motivated by profit and seek to avoid attention.\textsuperscript{88} For this reason, expanding the UNCLOS definition of piracy is not constructive in building an effective international legal framework for the prosecution and punishment of modern day piracy because piracy and terrorism require different solutions.\textsuperscript{89}

Finally, the “high seas” element of the UNCLOS definition of piracy may apply best to Somali piracy, but it is a severe limitation on Southeast Asian piracy.\textsuperscript{90} In the Gulf of Aden, the coordinated naval presence of an international fleet has driven pirates to attack up to 700 miles from the coastline, an area that is well past the twelve-mile territorial seas.\textsuperscript{91} Conversely, most attacks in Southeast Asia occur in narrow straits that fall within a nation’s territorial seas.\textsuperscript{92} Therefore, in Southeast Asia, even if caught, the attackers cannot be prosecuted for “piracy” because their acts would not fall within the UNCLOS definition of piracy.\textsuperscript{93}

While the SUA attempts to fill the legal gaps within the UNCLOS provisions, it is in no way a complete solution to the piracy problem.\textsuperscript{94} On the one hand, SUA creates a more comprehensive legal framework because it eliminates the private ends requirement, broadens the geo-
graphical limits of the crime, and imposes a strict prosecute or extra-
dite requirement on its members. On the other hand, SUA limits the
idea of universal jurisdiction by restricting jurisdiction to states that
have some connection to the offense. Moreover, SUA provisions are
only binding on states that are parties to the convention.

Additional confusion ensues among international and regional
organizations when determining which definition of piracy to en-
force. The IMB ignores both the UNCLOS and SUA definitions, and
instead defines piracy as boarding a vessel with the intent to commit a
crime. By contrast, the IMO recognizes two international maritime
crimes: piracy, as defined by UNCLOS, and armed robbery at sea. The
divide is further exacerbated at the regional cooperative level. ReCAAP follows the IMO bipartite definition of piracy while the U.S.-
led naval forces off the coast of Somalia promote the SUA definition.

If the diversity of definitions for piracy were not problematic
enough, it is compounded by the fact that no international legal frame-
work exists that establishes clear guidelines for the prosecution and pun-
ishment of pirates. UNCLOS does not establish a practical framework
to prosecute and punish pirates because it allows the individual seiz-
ing state to “decide upon the penalties.” UNCLOS only defines the
circumstances under which universal jurisdiction applies but does not
set a universal penalty or empower a single tribunal to hear the charge
of piracy. Similarly, SUA does not mention trial procedures or estab-
lish penalties for its defined offenses. The lack of uniformity on an
international level results in various punishments for piracy that range

95 Id.; Zou Keyuan, supra note 32, ¶ 21.
96 SUA, supra note 15, art. 6 (listing situations in which a state party can establish its ju-
risdiction); see Collins & Hassan, supra note 13, at 108.
97 Azubuike, supra note 8, at 56.
98 Compare Piracy and Armed Robbery Against Ships, supra note 35, with IMB REPORT,
supra note 24, at 4.
99 Dahlvang, supra note 51, at 21; Zou Keyuan, supra note 32, ¶ 10.
100 Piracy and Armed Robbery Against Ships, supra note 35.
101 Compare About ReCAAP ISC, supra note 44, with Baumgartner Testimony—Piracy Hear-
ing, supra note 43, at 17.
102 Zou Keyuan, supra note 32, ¶ 9.
103 See Baumgartner Testimony—Piracy Hearing, supra note 43, at 17.
104 See Zou Keyuan, supra note 32, ¶¶ 53–55.
105 Kavanagh, supra note 81, at 145.
106 UNCLOS, supra note 10, art 105.
107 Id.
108 Collins & Hassan, supra note 13, at 108.
from three years to life in prison. Additionally, a pirate will likely have no familiarity with the domestic criminal procedures of the prosecuting state.

This variety in prosecution and punishment can also lead to tense international relations when certain states are unwilling to expend their own resources to capture and prosecute pirates. UNCLOS leaves the prosecution of captured pirates to the discretion of each state, some of which are unwilling to prosecute pirates at all. Consequently, the enforcement of international piracy laws is only as effective as the domestic legal institutions that are willing and able to prosecute the crime. Thus, powerful countries with developed legal systems, which incorporate the international definitions of piracy, are more likely to punish pirates than less developed countries. This phenomenon has the unintended side-effect of imposing a Western view of retribution and punishment on pirates from developing countries. Furthermore, the uncertainty as to whether a pirate will be successfully prosecuted may decrease a state’s willingness to cooperate in the pursuit and capture of pirates altogether.

Universal jurisdiction is ineffective in successfully punishing piracy because it creates a patchwork of domestic legal frameworks for the prosecution and punishment of piracy which is inadequate to effectively address the modern piracy concern.

III. Analysis

To address the issue of effective piracy prosecution, scholars have proposed three categories of solutions: 1) change the existing international definition to a uniform definition of piracy followed by uniform domestic legislation; 2) supplement existing international treaties with multilateral and bilateral treaties; and 3) allow international courts to

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109 Baumgartner Testimony—Piracy Hearing, supra note 43, at 32; Mull Testimony—Piracy Hearing, supra note 60, at 32; Goodwin, supra note 71, at 1005.
111 Collins & Hassan, supra note 13, at 103, 109; Goodwin, supra note 71, at 1003.
112 See Kavanagh, supra note 81, at 145.
114 Id. at 556.
115 Id.
116 Collins & Hassan, supra note 13, at 109.
117 See Collins & Hassan, supra note 13, at 109; Kavanagh, supra note 81, at 145.
enforce international piracy laws.\textsuperscript{118} Of these three solutions, the establishment of regional international courts is the only option that can be accomplished without infringing on the territorial sovereignty of states and without creating a superfluous number of treaties.\textsuperscript{119}

Regional piracy tribunals could enforce an applicable regional definition of piracy and create a uniform criminal procedure and punishment.\textsuperscript{120} They could apply a uniform definition of piracy applicable to each region.\textsuperscript{121} Therefore, instead of states applying their own definition of piracy, regional piracy tribunals would apply a common definition of piracy to each region.\textsuperscript{122} Regional piracy tribunals could provide “uniformity in treatment”\textsuperscript{123} that would remove the problems created by the variety of punishments and procedures that currently exist and could result in the more effective prosecution of piracy.\textsuperscript{124}

Regional piracy tribunals can be created from the regional cooperative arrangements that currently exist and could mimic the treaty-based foundation of the International Criminal Court.\textsuperscript{125} For example, ReCAAP in Southeast Asia could establish its own regional piracy tribunal within one member state, MOWCA could sponsor its own regional tribunal for West Africa, while the signatory states of the Djibouti Code could create one for East Africa.\textsuperscript{126} Furthermore, each regional piracy tribunal could derive its jurisdiction from a modified territorial jurisdiction principle, through which member states would establish a geographic scope that falls within the tribunal’s power.\textsuperscript{127} Such a geo-

\textsuperscript{118} See Murphy, \textit{infra} note 9, at 19–20 (suggesting uniform definition and legislation); Collins & Hassan, \textit{infra} note 13, at 90 (suggesting the creation of regional piracy tribunals); Kraska & Wilson, \textit{infra} note 79, at 53 (suggesting supplementing international law with multilateral and bilateral agreements).


\textsuperscript{120} See Azubuike, \textit{infra} note 8, at 54 (noting that states may define and punish piracy according to their own laws).

\textsuperscript{121} See Collins & Hassan, \textit{infra} note 13, at 92; Kraska & Wilson, \textit{infra} note 79, at 44; Zou Keyuan, \textit{infra} note 32, ¶¶ 16–19 (discussing the deficiencies of the UNCLOS definition of piracy); see also IMB Piracy Incident Report 2009, \textit{infra} note 80.

\textsuperscript{122} See Murphy, \textit{infra} note 9, at 19.

\textsuperscript{123} Collins & Hassan, \textit{infra} note 13, at 109.

\textsuperscript{124} See \textit{id.} at 103.

\textsuperscript{125} See Bassiouni, \textit{infra} note 113, at 499.

\textsuperscript{126} See Kraska & Wilson, \textit{infra} note 48, at 519; About ReCAAP ISC, \textit{infra} note 44.

\textsuperscript{127} See Bottini, \textit{infra} note 110, at 511 (describing territorial jurisdiction).
graphic scope could include both territorial seas and the high seas, and it would clarify jurisdiction and eliminate the problems associated with establishing post hoc jurisdiction after a pirate attack occurs.

Because the regional piracy tribunals would be treaty-based, they would complement domestic criminal justice systems rather than replace them. The regional piracy tribunal would offer an alternative forum for both member states and non-member states that are unable or unwilling to prosecute pirates. Like the International Criminal Court, regional piracy tribunals would not infringe on a state’s national sovereignty or domestic legal system.

In contrast, changing the existing international definition of piracy would not be as effective in the prosecution of pirates because the type of pirate attacks in each region vary due to their diverse geography. There is no single international definition of piracy that can successfully incorporate the many different regional variations in attacks that exist. In addition, since international definitions of piracy still require domestic enabling legislation to prosecute piracy, creating a uniform definition will not ensure that individual states take the necessary measures to pass legislation that applies the new definition.

Moreover, regional piracy tribunals can prevent the disputes over jurisdiction that individual states must negotiate under the current le-

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128 See UNCLOS, supra note 10, art. 101 (stating that an essential element of piracy includes the high seas); Murphy, supra note 9, at 8 (explaining that armed robbery at sea can only take place in territorial seas).

129 Dr. Azubuike stated:

A classic illustration of the universality principle in relation to piracy is offered by the Alondra Rainbow incident and prosecutions. The Alondra Rainbow was a Japanese owned tanker with a Filipino crew under the command of two Japanese officers. The tanker was sailing from Indonesia to Japan when pirates hijacked the ship. The Indian Navy later captured the pirates and towed the vessel to India. The pirates were tried and convicted by an Indian court.

See Azubuike, supra note 8, at 55.

130 See Bassiouuni, supra note 113, at 499–500 (noting that the International Criminal Court does not supplant or substitute national criminal justice systems).

131 See Azubuike, supra note 8, at 58.

132 See Bassiouuni, supra note 113, at 500.

133 See Collins & Hassan, supra note 13, at 92. For an example of the different types of attacks in different regions, see IMB Live Piracy Map, supra note 4.

134 See Collins & Hassan, supra note 13, at 106–108 (discussing the deficiencies of SUA’s definition of piracy); Zou Keyuan, supra note 32, ¶¶ 16–19 (discussing the deficiencies of UNCLOS’s definition of piracy).

135 See Baumgartner Testimony—Piracy Hearing, supra note 43, at 27.
gal regime.\(^{136}\) By creating a single court that has jurisdiction over all incidents of piracy, irrespective of the states and nationalities involved, pirates can be prosecuted faster without the political wrangling that usually follows a pirate attack.\(^{137}\) Regional piracy tribunals can also operate despite the existence of states that are unable or unwilling to prosecute pirates in their own courts.\(^{138}\) These tribunals provide an alternative forum for states that lack the resources to prosecute pirates themselves.\(^{139}\)

On the contrary, the creation of more multilateral and bilateral treaties to supplement UNCLOS and SUA would not be as effective for the prosecution of pirates because most treaties only create binding obligations their member states.\(^{140}\) Thus, creating networks of mutual assistance through multilateral and bilateral treaties is only effective when every affected country is a party to that treaty.\(^{141}\) Although bilateral and multilateral treaties may help solve jurisdictional and prosecutorial issues,\(^{142}\) they are only effective when the seizing state has a treaty with all states possessing any interest in the specific attack.\(^{143}\) For example, if the seizing state does not have an extradition treaty with the particular states involved, the captured pirates may go unpunished.\(^{144}\)

Given the current international trend towards regional coordination in the fight against piracy, there already exists a basic foundation for coordination on which to create regional piracy tribunals.\(^{145}\) Regional coordination such as ReCAAP can set a uniform definition of piracy for all member states.\(^{146}\) Additionally, the IMB already has the capability to investigate international maritime crimes and to provide litigation support for countries seeking to prosecute international mari-

\(^{136}\) See Dahlvang, \textit{supra} note 51, at 23; Kavanagh, \textit{supra} note 81, at 156 (discussing jurisdiction in territorial waters).

\(^{137}\) See Kraska & Wilson, \textit{supra} note 79, at 51 (discussing the difficulties of determining who will assume jurisdiction immediately after capturing a pirate).

\(^{138}\) See Azubuike, \textit{supra} note 8, at 55, 58; Kraska & Wilson, \textit{supra} note 1, at 3.

\(^{139}\) See Azubuike, \textit{supra} note 8, at 55, 58.

\(^{140}\) \textit{Ian Brownlie, Principles of Public International Law} 627 (7th ed. 2008).

\(^{141}\) See Collins & Hassan, \textit{supra} note 13, at 108 (discussing an example in which offenders go unpunished because no extradition treaty exists); Dahlvang, \textit{supra} note 51, at 23 (discussing the problem with jurisdiction when extradition treaties exist).

\(^{142}\) See Kavanagh, \textit{supra} note 81, at 157; Kraska & Wilson, \textit{supra} note 79, at 53.

\(^{143}\) See Collins & Hassan, \textit{supra} note 13, at 108.

\(^{144}\) \textit{Id}.


\(^{146}\) See Zou Keyuan, \textit{supra} note 32, ¶ 9.
time offenders.\textsuperscript{147} Thus, international organizations such as the United Nations or the IMO could easily combine the existing regional networks of cooperation with the IMB’s investigative capabilities as a foundation for the creation of regional piracy tribunals.\textsuperscript{148}

**Conclusion**

Piracy is an international crime that is subject to universal jurisdiction, which gives every state the right to prosecute and punish pirates. Because of differences in geography and types of attacks, the international definitions of piracy as defined in UNCLOS and SUA are both under and over-inclusive. In addition, because each state has discretion regarding whether and how they choose to prosecute and punish pirates, there is no firm international legal framework by which to prosecute pirates. The best solution to this patchwork of criminal prosecutions is to place universal jurisdiction in the hands of regional piracy tribunals. Each tribunal could enforce a definition of piracy that is more applicable to each specific region, provide uniform procedures and penalties, and offer an alternative forum for prosecution to states that lack the resources to prosecute themselves.

\textsuperscript{147} IMB Investigation Services, \textit{supra} note 28.

\textsuperscript{148} For discussions concerning strengthening regional cooperation, see generally \textit{Hearing on International Efforts to Combat Maritime Piracy}, \textit{supra} note 6, at 17 (statement of Admiral William Baumgartner, J. Advocate Gen. and Chief Counsel, U.S. Coast Guard). For the ICC-IMB’s investigative capabilities, see IMB Investigation Services, \textit{supra} note 28.
FROM “PERSONAL AUTONOMY” TO “DEATH-ON-DEMAND”: WILL PURDY V. DPP LEGALIZE ASSISTED SUICIDE IN THE UNITED KINGDOM?

CAROL C. CLEARY*

Abstract: Debates over end-of-life issues and the “right to die” are becoming increasingly prevalent in many modern societies. In July 2009 the House of Lords addressed the question of whether the legal framework governing assisted suicide in the United Kingdom constitutes an unjustifiable infringement on privacy rights. The court decided that question in the affirmative, and this Note discusses the implications of Purdy v. Director of Public Prosecutions for the legality of assisted suicide in the United Kingdom. This Note uses evidence of legal developments in other jurisdictions that have grounded the right to assisted suicide in personal autonomy to argue that the Purdy court’s reasoning and the Director of Public Prosecution’s response to the decision paves the way for a gradual breakdown in restrictions on the practice.

Introduction

A recent movement to legalize assisted suicide and euthanasia has swept across some of the globe’s wealthier industrialized nations.1 While a handful of jurisdictions in Europe and the United States have legalized assisted suicide with varying degrees of restriction, laws that allow the practice remain the exception rather than the rule in most of the developed world.2 The United Kingdom is one region in which efforts to legalize assisted suicide have historically proven unsuccessful; under current U.K. law, suicide itself is not a crime, but aiding or abetting someone else’s suicide is a criminal offense, the prosecution of

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2 See generally Raphael Cohen-Almagor, Euthanasia and Physician-Assisted Suicide in the Democratic World: A Legal Overview, 16 N.Y. Int’l L. Rev. 1 (2003) (discussing the legal approaches to assisted suicide and euthanasia around the world, and noting that the Netherlands and Belgium are the only countries in the liberal world that accept both practices).
which is left to the discretion of the Director of Public Prosecutions (DPP). The legality of the ban on assisted suicide and the scope of prosecutorial discretion have recently come under scrutiny, especially as British citizens have begun to take advantage of the more liberal suicide laws in neighboring European countries like Switzerland. Switzerland is unique among jurisdictions that have legalized assisted suicide because Swiss law does not require that the person giving assistance be a physician, and there are no restrictions on foreigners who travel to the country merely to take advantage of its liberal assisted suicide provision. As a consequence of these legal idiosyncrasies, Switzerland has become a hotbed for what some have termed “death tourism,” and since 1998 over 100 British citizens are known to have traveled to the country to take their lives with the help of “right-to-die” centers.

To date, no one in the United Kingdom has been prosecuted under the Suicide Act for assisting in a suicide that takes place abroad. The fact that the ban remains in place, however, has led some to seek clarification from the British government regarding how the DPP chooses whether or not to prosecute perpetrators of the Act. In July 2009, the House of Lords ruled in Purdy v. Director of Public Prosecutions that the DPP must clarify which factors he would consider before deciding whether a prosecution under the Suicide Act would be in the public’s interest. The decision noted that, while it was not the place of the court to decriminalize assisted suicide, judges had a role to play in clarifying the law for cases in which “compassionate assistance” was required, i.e. where assistance was necessary to aid the terminally ill in ending their lives. The DPP issued draft guidelines in late September 2009 and after a period of public comment issued final guidelines in

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3 Suicide Act, 1961, 9 & 10 Eliz. 2, c. 60, §§ 1–2 (Eng.).
5 Srinivas, supra note 4, at 106–07.
6 See id. at 105, 107.
8 Id.
10 See Purdy, 3 W.L.R. at 414.
11 See id. at 413, 423.
late February 2010. The policy includes sixteen factors that weigh in favor of prosecution, and six factors that weigh against prosecution.

Upon issuing the draft guidelines, the DPP stated that his policy guidelines are not intended to undermine the force of the Suicide Act, and that no person is immune from prosecution. Almost immediately, however, the list generated controversy; some accused the DPP of usurping the role of Parliament and granting de facto immunity to certain classes of persons, while others hailed the guidelines as a step towards “greater patient choice.” The DPP’s initial policy placed an emphasis on the physical status of the individual committing suicide; under that policy, evidence of terminal illness or physical disabilities weighed against prosecution. After a period of public comment, the DPP revised his guidelines to place greater emphasis on the motives of the assister rather than the health of the victim. The DPP reiterated that the policy was not intended to change the prohibition on assisted suicide, but the very existence of such a policy remains a source of debate among those with differing views about the practice of assisted suicide. Regardless of the probable effect of the DPP’s guidelines, the factors themselves reveal the complexities and nuances attendant to the assisted suicide debate, one that has become increasingly relevant to societies around the world.

Part I of this Note provides a detailed overview of the “right-to-die” movement and the most recent jurisprudence on the issue of assisted suicide in the United Kingdom. Part II of the Note discusses this juris-

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14 See id.


16 See id.


19 See id.


prudence, as well as the DPP’s guidelines, in more detail. Finally, Part III presents the argument that the Purdy court’s desire to carve out a de facto exception to the Suicide Act for individuals with terminal illnesses and/or disabilities is at odds with its holding that the decision to commit suicide is a matter of personal autonomy. This Note further argues that by premising the right to kill oneself on notions of privacy and personal autonomy, the Purdy decision is likely to set the United Kingdom down a path towards relaxation of the assisted suicide ban and eventual legalization of the practice. Recent developments prove that the DPP cannot issue guidelines that draw a line between individuals with terminal illnesses or incurable disabilities and others who make rational decisions to end their own lives without articulating some kind of rationale that places relative worth on individual lives vis-à-vis the state.

I. BACKGROUND

A. The “Right to Die”

The concept of a “right to die” has its theoretical basis in the idea that an individual should be able to decide the time and manner of his or her own death, either by herself or with the aid of another if she so chooses.\(^{22}\) The right to die encompasses the right of an individual to commit suicide with or without assistance, as well as the right to request that another person commit acts that cause the death of the requesting party, or “voluntary euthanasia.”\(^{23}\) Voluntary euthanasia can be either “passive,” when a doctor or other actor refrains from performing acts that prolong an individual’s life, or “active,” when a doctor or some other actor acts to cause the death of another, e.g. by injecting a lethal medication.\(^{24}\) The distinction between assisted suicide and euthanasia thus rests on who actually carries out the act that ends the individual’s life.\(^{25}\)

Euthanasia remains a crime in most countries of the world.\(^{26}\) Assisted suicide is currently legal in the Netherlands, Belgium, and Switzerland,\(^{27}\) and in the U.S. states of Oregon, and Washington.\(^{28}\) Of these

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\(^{22}\) Manzione, *supra* note 1, at 445.

\(^{23}\) See Srinivas, *supra* note 4, at 94.


\(^{25}\) See Srinivas, *supra* note 4, at 94.

\(^{26}\) Cohen-Almagor, *supra* note 2, at 5.

jurisdictions, the Netherlands is considered to have the most liberal “right-to-die” laws, which permit euthanasia as well as assisted suicide.\textsuperscript{29} Though euthanasia is illegal in Switzerland, that nation also has a unique legal position on assisted suicide, a practice it has permitted since 1918.\textsuperscript{30} Swiss law allows lay persons as well as doctors to assist in the suicide of others, so long as the person assisting does not act with selfish intent; the law also does not require that persons seeking assistance be terminally ill.\textsuperscript{31}

A number of “right to die” organizations have sprung up in Switzerland to facilitate assisted suicide.\textsuperscript{32} One such organization, called “Dignitas,” does not discriminate against non-residents who travel to Switzerland to use its services.\textsuperscript{33} As a result, individuals from other nations where assisted suicide is illegal have begun to travel to Switzerland to end their lives, a phenomenon known as “death tourism.”\textsuperscript{34} In the past several years, over 100 British citizens have taken advantage of Dignitas’ services, igniting the right to die debate in the United Kingdom.\textsuperscript{35} Individuals seeking assistance in suicide, and those who seek to help them, are calling for a reform of the nation’s assisted suicide law,\textsuperscript{36} while supporters of the ban argue that the law is necessary to protect vulnerable individuals who might be pressured into taking their own lives if assisted suicide were legalized.\textsuperscript{37}

B. \textit{The Suicide Act, Prosecutorial Discretion \& the Right to Privacy—Controversy in the United Kingdom}

Suicide and attempted suicide ceased to be crimes in the United Kingdom when the Suicide Act was passed in 1961.\textsuperscript{38} The statute also created a new offense in section 2(1), which stipulates that any person who “aids, abets, counsels or procures the suicide of another, or an at-

\textsuperscript{29} See Cohen-Almagor, \textit{supra} note 2, at 5–6.
\textsuperscript{30} See Srinivas, \textit{supra} note 4, at 105–06.
\textsuperscript{31} See id.
\textsuperscript{32} See id. at 106.
\textsuperscript{33} See id.
\textsuperscript{34} See id. at 92–93.
\textsuperscript{35} See id.
\textsuperscript{36} See Srinivas, \textit{supra} note 4, at 92.
\textsuperscript{38} Suicide Act, 1961, 9 & 10 Eliz. 2, c. 60, § 1 (Eng.).
tempt by another to commit suicide” is liable on conviction to serve up to fourteen years in prison.\textsuperscript{39} Thus, under the Suicide Act, it is considered a crime to assist another person in a non-crime.\textsuperscript{40} Pursuant to section 2(4), however, no prosecutions may be brought for an offense under section 2 except by or with the consent of the DPP.\textsuperscript{41}

As the head of the Crown Prosecution Service, the DPP prosecutes criminal cases that the police of England and Wales have investigated.\textsuperscript{42} The basic reason for including a provision in a statute limiting the initiation of prosecutions is to prevent inappropriate prosecutions for actions that may fall under the scope of the statute.\textsuperscript{43} In general, the DPP will only bring a prosecution under a criminal statute when he deems it to be in the public interest.\textsuperscript{44} The DPP and his agents, in the form of Crown prosecutors, determine whether a prosecution is in the public interest by reference to a set of factors published in the Code for Crown Prosecutors (the Code).\textsuperscript{45} The Code, which the DPP issues and makes available to the public, applies to all criminal offenses and does not distinguish among different crimes.\textsuperscript{46}

The DPP’s role in the prosecution of crimes is at the heart of recent challenges to the legality of the Suicide Act; however, these cases are also unique because the litigants have argued that the ban on assisted suicide

\textsuperscript{39} Id. § 2(1).
\textsuperscript{40} See id. §§ 1–2.
\textsuperscript{41} Id. § 2(4).
\textsuperscript{43} See Purdy v. Dir. Pub. Prosecutions [2009] UKHL 45, [2009] 3 W.L.R. 403, 419 (U.K.). Other reasons to include a provision for limiting prosecutions are:

[T]o secure consistency of practice, to prevent abuse of the kind that might otherwise result in vexatious private prosecution, to enable account to be taken of mitigating factors and to provide some central control of the use of the criminal law where it has to intrude into areas which are particularly sensitive or controversial.

See id. at 419–20.
\textsuperscript{44} See id. at 420.
\textsuperscript{45} See id.
\textsuperscript{46} See id. The Code sets out two tests which prosecutors typically use to determine whether or not to proceed with a prosecution—the “Threshold Test” which is used at a very early stage in the investigation, and the “Full Code Test,” which entails consideration of the evidence followed by consideration of whether a prosecution is needed in the public interest. See id.
constitutes an intrusion into their right to privacy.\textsuperscript{47} For example, in \textit{Pretty v. United Kingdom}, plaintiff Diane Pretty sued the United Kingdom in the European Court of Human Rights (ECHR) after the DPP refused to grant her husband advance immunity for his anticipated assistance in her suicide.\textsuperscript{48} Pretty, who suffered from a motor neuron disease, claimed that the blanket ban on assisted suicide prevented her from exercising her lawful right to end her life because her deteriorating physical condition rendered her incapable of performing the act without assistance.\textsuperscript{49} Pretty sought a guarantee from the DPP that he would not prosecute her husband if he were to assist her in committing suicide.\textsuperscript{50} The court concluded, for the first time ever, that the right to privacy guaranteed by Article 8(1) of the European Convention of Human Rights (Convention) encompasses the right to make the decision to end one’s own life.\textsuperscript{51} The court held, however, that the DPP did not act inappropriately by refusing to grant advance immunity for Pretty’s husband.\textsuperscript{52} The court reasoned that it could be construed as a threat to the rule of law if the government were to exempt individuals or classes of individuals from the operation of the law, and that the gravity of assisting in someone else’s suicide was serious enough that the DPP’s refusal to acquiesce in Pretty’s request was not unreasonable.\textsuperscript{53}

In \textit{Purdy v. DPP}, plaintiff Debbie Purdy sought judicial review of the DPP’s actions after he refused to publish detailed guidelines regarding the factors he would consider before deciding whether or not to prosecute an individual under the Suicide Act.\textsuperscript{54} Owing to her primary progressive multiple sclerosis, Purdy foresaw a time when she would regard her continuing existence as unbearable, and she would wish to commit suicide.\textsuperscript{55} She anticipated, however, that by the time she reached that stage of her disease she would be unable to act without assistance and would need to travel to a country where assisted suicide was lawful.\textsuperscript{56} Purdy argued it was an injustice that the law was so unclear that she could not be sure whether her husband would be prosecuted for assist-

\textsuperscript{49} See id. at 6.
\textsuperscript{50} See id.
\textsuperscript{51} See id. at 36–37.
\textsuperscript{52} See id. at 39.
\textsuperscript{53} See id.
\textsuperscript{54} See Purdy, 3 W.L.R. at 414.
\textsuperscript{55} See id. at 409.
\textsuperscript{56} Id.
ing her in traveling to another country to commit suicide.\footnote{See id. at 413–14.} As a consequence, Purdy argued, she would have to commit suicide sooner than she would like while she was still well enough to do so by herself, rather than subject her husband to possible prosecution.\footnote{See id. at 414.}

First, the Purdy court followed Pretty in ruling that Article 8(1) encompasses the right to “self-determination,” which itself includes the right to make the decision to kill oneself.\footnote{See id. at 416–17, 431.} The court then held that the public interest factors set out in the current version of the Code were not applicable to the complex issues presented by assisted suicide cases.\footnote{See Purdy, 3 W.L.R. at 423.} Finally, the court ordered the DPP to issue an offense-specific policy identifying the facts and the circumstances that would be considered when deciding whether to prosecute individuals under the Suicide Act.\footnote{Id.} Pursuant to this ruling, the DPP issued interim guidelines on September 23, 2009.\footnote{See Gibb, supra note 15.} These guidelines were left open for public comment until December 16, 2009, and the DPP issued his final policy on February 25, 2010.\footnote{CPS Press Release 2/25/10, supra note 13; Press Release, Crown Prosecution Serv., DPP Publishes Interim Policy on Prosecuting Assisted Suicide (Sept. 23, 2009), http://www.cps.gov.uk/news/press_releases/144_09/.}

II. Discussion

The Purdy court’s recognition that Article 8(1) guarantees the right to self-determination was foundational to the court’s ultimate holding requiring the DPP to issue an offense-specific policy directing prosecutorial discretion in cases of assisted suicide.\footnote{See Purdy v. Dir. Pub. Prosecutions [2009] UKHL 45, [2009] 3 W.L.R. 403, 416–17, 431 (U.K.).} Article 8(1) of the Convention stipulates that all individuals have the right to respect for their private and family life.\footnote{See European Convention for the Protection of Human Rights and Fundamental Freedoms art. 8(1), Nov. 4, 1950, 213 U.N.T.S. 221, 230 [hereinafter ECHR].} Under Article 8(2), public authorities may not interfere with this right unless the interference is in accordance with the law, has an aim which is legitimate, and is necessary in a democratic society for that legitimate aim.\footnote{See Pretty v. United Kingdom, App. No. 2346/02, 35 Eur. H.R. Rep. 1, 37 (2002); see also ECHR, supra note 65, art. 8(2) (listing “national security, public safety or the economic well-being of the country, [for] the prevention of disorder or crime, [for] the protection
To meet the requirement of being “in accordance with the law,” any intrusion must be clearly authorized by law and precise enough for an individual to understand the law’s scope and foresee its consequences so that he or she may regulate his or her conduct accordingly. Purdy claimed that the Suicide Act did not meet this requirement because she did not understand how to conform her actions to avoid subjecting her husband to prosecution. This uncertainty resulted from the fact that the Suicide Act’s ban on assisted suicide did not allow for any exceptions, yet simultaneously provided for broad prosecutorial discretion in its enforcement. Thus, Purdy’s husband’s fate was wholly dependent upon the DPP’s interpretation of factors in the Code inapplicable to unique situations like hers. Purdy argued, and the court accepted, that because the Suicide Act as formulated, taken together with the Code, did not meet the requisite level of accessibility and foreseeability required by Article 8(2) of the Convention, it constituted an unjustifiable interference with her right to privacy in violation of the Convention.

In determining that Purdy’s right to privacy includes the right to make the decision to kill herself, the House of Lords emphasized that Article 8(1) relates to the manner in which a person lives his or her life, and that how a person chooses to spend the closing moments of his or her life is part of the act of living and therefore should be respected. The Purdy court relied on reasoning in Pretty v. U.K., in which the ECHR noted that when the law prevents an individual from exercising choices that affect her quality of life, as when she decides to avoid “what she considers will be an undignified and distressing end to her life,” this constitutes an interference with her right to privacy.
After concluding that Purdy’s Article 8(1) rights were implicated by the Suicide Act, the Law Lords examined the factors in the Code that the DPP customarily uses to determine whether a prosecution is in the public interest.\(^{74}\) Lord Hope noted that while the Code normally provides sufficient guidance to Crown Prosecutors,\(^{75}\) it fails to do so in cases involving the assisted suicide “of a person who is terminally ill or severely and incurably disabled,” and who, “having the capacity to take such a decision, does so freely and with a full understanding of the consequences.”\(^{76}\) Lord Hope also noted the clear disconnect between the text of the Suicide Act and the manner of its application in “compassionate” cases like Purdy’s.\(^{77}\) Furthermore, although the relatively small number of these “controversial” cases would undoubtedly grow, Lord Hope concluded that the DPP could likely define the class that would require “special treatment” narrowly.\(^{78}\) Similarly, Baroness Hale wrote that there could be individual cases in which “the deterrent effect of a prosecution would be a disproportionate interference with the autonomy of the person who wishes to end her life.”\(^{79}\) Accordingly, Hale concluded, any law that interferes with this decision must be formulated to protect an individual’s right to make a “genuinely autonomous choice.”\(^{80}\) In sum, an offense-specific policy for prosecutorial discretion under the Suicide Act was deemed necessary because there would otherwise be an inappropriate infringement on the right of autonomous individuals to make the decision to end their lives.\(^{81}\)

The final guidelines that the DPP issued on February 25, 2010 are an attempt to satisfy the Law Lords’ directive, and upon their release, the current DPP, Keir Starmer, noted that “only Parliament can change the law,” that he is unable to assure a person in advance of committing a crime that he will not bring a prosecution, and that no one should take his policy as any kind of assurance against charges.\(^{82}\) The policy applies when the acts that constitute assistance are committed in England and Wales, regardless of where the suicide or attempted suicide

\(^{74}\) See Purdy, 3 W.L.R. at 420–23.

\(^{75}\) See id. at 422.

\(^{76}\) See id. at 423.

\(^{77}\) See id.

\(^{78}\) See id.

\(^{79}\) See id. at 425.

\(^{80}\) See Purdy, 3 W.L.R. at 426.

\(^{81}\) See id. at 423, 426.

actually occurs.\textsuperscript{83} Thus, the policy is clearly intended to cover instances of death tourism as well as suicides in England and Wales.\textsuperscript{84}

The DPP’s policy lists sixteen factors that weigh in favor of prosecution and six that weigh against prosecution.\textsuperscript{85} The factors that weigh in favor of prosecution include that: the victim did not have the capacity to reach an informed decision to commit suicide; the victim had not reached a “voluntary, clear, settled and informed decision to commit suicide;” the victim had not clearly communicated his or her decision to commit suicide; the victim did not seek the assistance of the suspect on his or her own initiative; the suspect “was not wholly motivated by compassion,” was motivated by the prospect of financial gain, or was paid by the victim for his or her assistance; the suspect pressured the victim to commit suicide; and the victim was physically able to undertake the act that constituted the assistance him or herself, among others.\textsuperscript{86}

The six factors that weigh against a prosecution are that: the victim had reached a clear, settled, voluntary, and informed decision to commit suicide; the suspect was entirely motivated by compassion; the actions of the suspect were “of only minor encouragement or assistance;” the suspect had sought to dissuade the victim from committing suicide; the suspect’s actions constituted “reluctant encouragement or assistance” in the face of the victim’s determined wish to commit suicide; and the suspect reported the suicide to the police and fully cooperated in any investigation into the circumstances of the victim’s death.\textsuperscript{87}

III. Analysis

A. An Exception to the Ban

The DPP’s final guidelines clearly emphasize the victim’s autonomy in the prosecutorial analysis, and the policy disfavors prosecution in cases in which an individual has made a rational, autonomous, inde-
pendent decision to end his or her own life. These guidelines are consistent with the Purdy court’s stated intention to respect the autonomy of individuals in Purdy’s situation.

The Purdy court’s apparent desire, however, to carve out an exception to the Suicide Act for an individual suffering from a terminal illness or disability who wishes to make the decision to end his or her own life is inconsistent with the premise of the court’s directive to the DPP, a premise that is based on the principle of self-determination. If Purdy v. DPP stands in part for the proposition that the right to privacy protects an individual’s ability to make autonomous choices regarding the quality of his or her life, including even the choice to end that life, then any prosecutorial guidelines which by their content purport to respect this autonomy must exclude any qualifying factors regarding an individual’s physical condition; thus, there is a tension between protecting personal autonomy and stipulating when a person is suffering enough to end his or her own life.

At least one of the Law Lords recognized this tension; for example, Baroness Hale noted in her opinion that if the court “is serious about protecting autonomy” then it must “accept that autonomous individuals have different views about what makes their lives worth living.” Hale proceeded to note that though “[i]t is not for society to tell peo-

88 See Policy for Prosecutors, supra note 82. For example, so long as a victim manifested a resolute, clear intention or “determined wish” to commit suicide, and the decision was made independently and without pressure from outside sources, then a majority of the factors disfavoring prosecution would be satisfied, and six of the factors favoring prosecution would be negated. See id.


90 See id. at 422–23. The court’s desire to carve out an exception for individuals with terminal illnesses can be inferred ipso facto from the Purdy court’s directive to the DPP, which is premised on the holding that the original Code was inapplicable to cases of competent individuals who suffered from terminal illnesses, and who, as such, deserved special consideration under the law. See id.

91 See id. at 426; see also Neil M. Gorsuch, The Future of Assisted Suicide and Euthanasia 99 (2006). As Gorsuch points out, an assisted suicide regime wherein the individual is required not only to make a rational, autonomous choice, but also to meet some sort of benchmark requirement of terminal illness or suffering is inconsistent in its application because, while it “would advance the autonomy interests of some persons,” it would not respect the autonomy interests of others. Gorsuch, supra, at 96. This requirement would suppress many of what Gorsuch calls “rational, autonomous . . . decisions to die.” Id. Thus, in order to comport fully with principles of autonomy, a state arguably must “abstain from coercively interfering with any rational adult’s private decision to die, whatever the motive or reason for the individual’s considered decision.” See id. at 98.

92 See Purdy, 3 W.L.R. at 416–17.

93 See Gorsuch, supra note 91, at 96, 98–99.

94 See Purdy, 3 W.L.R. at 426.
ple what to value about their own lives,” at times it “may be justifiable for society to insist that we value their lives even if they do not.”\(^95\) The court has not provided any rationale for distinguishing between lives society must “insist” upon valuing versus those which society has less interest in protecting.\(^96\) Consequently, as it stands, the court’s “self-determination” rationale for implicating privacy rights in the decision to commit suicide leaves a gaping hole wherein any autonomous individual should, under the court’s logic, be able to pass judgment on the subjective quality of his or her own life and act accordingly.\(^97\)

The reaction to the DPP’s first attempt at formulating a policy for assisted suicide cases illustrates the line-drawing problem presented by the *Purdy* decision.\(^98\) The September guidelines, which took account of the physical situation of the victim and clearly disfavored prosecution in cases in which the individual was terminally ill or disabled and was helped to die by a family member or close friend,\(^99\) were criticized on the grounds that the policy amounted to a statement that certain kinds of life were entitled to less protection from the state.\(^100\) Therefore, by emphasizing autonomy and self-determination as the bases for the right to make a decision to end one’s own life, the *Purdy* court has in-

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95 See id. at 426–27.
96 See id. at 427. Baroness Hale raised the question of how it should be determined when “the law is justified in interfering with a genuinely autonomous choice” but did not provide any answers, instead expressing her hope that the DPP’s policy would include qualifying factors pertaining to the “reasons why the person . . . wished to be helped to end his or her life.” See id.
97 See id. at 426–27; see also Gorsuch, supra note 91, at 98–99; Daniel Callahan, *Reason, Self-determination, and Physician-Assisted Suicide*, in *The Case Against Assisted Suicide* 52, 61–62 (Kathleen Foley & Herbert Hendin eds., 2002). During the Parliamentary debates in July 2009, when a proposal to create an exception to the Suicide Act for terminally ill individuals who traveled abroad to take their lives was defeated, some lawmakers expressed concern that “any proposal to alter the current position involves a judgment that a certain kind of life, or a certain span of life, has become unworthy of support.” See David Aaronovitch, *It’s My Life and I Demand to End It When I Want*, *Times* (London), Sept. 22, 2009, http://www.timesonline.co.uk/tol/comment/columnists/david_aaronovitch/article6843426.ece.
99 See Interim Policy for Prosecutors, supra note 17. For example, in a case where an adult with a terminal illness indicated on her own initiative her clear wish to commit suicide and requested the aid of a spouse or loved one in doing so, under the interim policy at least five of the seven most important factors weighing against prosecution would be satisfied, and four of the factors weighing in favor of prosecution would be negated; thus, a prosecution would very likely not follow. See id.
100 See Editorial, supra note 98.
vited a situation in which it is very difficult for the state to articulate limits on this right without appearing disingenuous.\textsuperscript{101}

\section*{B. The Slippery Slope}

The tension between individual autonomy and the state’s role in the “quality of life” analysis is the conventional starting point of “slippery slope” arguments that have historically been invoked to justify laws prohibiting all forms of assisted suicide and/or euthanasia.\textsuperscript{102} Although such arguments are often over-stated, evidence from other jurisdictions that justify the practice of assisted suicide by appeals to personal autonomy or “quality of life” assessments reveals a legal trend wherein the category of individuals deemed acceptable candidates for the procedure is gradually being widened.\textsuperscript{103}

Recent developments in the Netherlands illustrate this gradual widening; in 1994, the Dutch Supreme Court squarely held in the \textit{Chabot} case that assistance in the suicide of an individual whose suffering is not physical and who is not terminally ill can be justified on necessity grounds because “the wish to die of a person whose suffering is psychic can be based on an autonomous judgment.”\textsuperscript{104} Seven years later, the

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\textsuperscript{101} See Purdy, 3 W.L.R. at 426; Policy for Prosecutors, supra note 82; Editorial, supra note 98.

\textsuperscript{102} See Griffiths et al., supra note 24, at 177; Craig Paterson, \textit{Assisted Suicide and Euthanasia: A Natural Law Ethics Approach} 173 (2008). For example, proponents of these arguments hold that euthanasia must be outlawed in all circumstances because when taken to its logical conclusion, a legal regime which allows the practice of euthanasia on the basis of personal autonomy has no argument against legalization in situations where a patient is not suffering, which the regime deems as unacceptable. See Griffiths et al., supra note 24, at 177. Griffiths takes issue with the logical slippery slope argument because the argument “presupposes that the forms of termination of life allegedly implied by legalization of euthanasia are obviously unacceptable.” See id.

\textsuperscript{103} See, e.g., Gorsuch, supra note 91, at 105–06; Griffiths et al., supra note 24, at 152–53; Paterson, supra note 102, at 176–78. For example, euthanasia and assisted suicide first became subjects of public debate in the Netherlands in the early 1970s, when a Dutch court indicated in the \textit{Postma} decision that dispensing of pain relief that hastens a patient’s death can be acceptable when a patient is incurably ill, finds his suffering mentally or physically unbearable, has expressed the wish to die, and the person who accedes to the request is a doctor. See Griffiths et al., supra note 24, at 51–53. By 1986, a series of court decisions had established that “when a patient who is suffering unbearably and hopelessly makes a voluntary and well-considered request” to be euthanized or to be assisted in his or her own suicide, a doctor who responds to the request and conforms to “requirements of careful practice” would not be guilty of a crime. Id. at 73. Eventually, assisted suicide and euthanasia were legalized in 2001 without any express requirement that a patient be “incurably ill.” See Gorsuch, supra note 91, at 106.

\textsuperscript{104} See Griffiths et al., supra note 24, at 80–82. In the wake of \textit{Chabot}, John Griffiths, a professor of sociology of law at the University of Groningen in the Netherlands specu-
Dutch Parliament actually legalized both practices; under the legislation doctors are primarily restricted by the requirements that the patient’s request be “voluntary and well-considered,” and that his or her suffering be “lasting and unbearable.”

Terminal illness is not a requirement for euthanasia or assisted suicide, and neither is a physical ailment of any kind; the “suffering” referenced in the bill is completely subjective, and to meet this requirement, a doctor who assists in the death of the patient “need only show that he or she believed that the patient endured some sort of unspecified suffering.”

Switzerland provides another striking example of the impact that autonomy-based arguments have in breaking down legal restrictions to assisted suicide: in 2006, the Swiss Federal Supreme Court ruled that assisted suicide should be available to individuals with mental illness and psychiatric disorders, so long as they were capable of making a “rational” and “well-considered” decision. In that case, the plaintiff, a manic depressive, based his argument on his Article 8(1) right to self-determination. In its decision, the court reasoned that serious mental disorders “could make life seem as unbearable to some patients as serious somatic ailments do to others” and that those individuals should have just as much of a right to end their lives.

Thus, in light of recent developments in other jurisdictions that accord deference to autonomy-based arguments, there is a high poten-
tial that in the post-Purdy age, the United Kingdom will begin its slide down the slope towards more permissive assisted suicide laws.\footnote{See Gorsuch, supra note 91, at 97–98; Paterson, supra note 102, at 176–77. See also Wesley J. Smith, Death on Demand: The Assisted Suicide Movement Sheds Its Fig Leaf, Weekly Standard, July 5, 2007, http://www.weeklystandard.com/Content/Public/Articles/000/000/013/831mhugn.asp. Smith uses the term “death-on-demand” in a 2007 piece in which he argues that the right-to-die movement is really about extending the right to assisted suicide to all rational persons, regardless of whether they are terminally ill. See id. Smith also uses evidence from several jurisdictions to demonstrate that “nearly every jurisdiction that has legalized assisted suicide for the seriously ill—as well as those that have refused to meaningfully enforce anti-assisted suicide laws—has either formally expanded the legal right to die to those suffering existentially, or shrugged in the face of illegal assisted suicides of the depressed.” See id.}

Conclusion

The Purdy court’s reasoning that grounds the decision to commit suicide under the umbrella of privacy rights is a significant step toward the gradual liberalization of assisted suicide laws in the United Kingdom, especially because restrictions on assisted suicide have proven difficult to uphold in other jurisdictions once autonomy-based arguments are invoked to challenge them. Purdy v. DPP has not by itself blown open the door for the legalization of assistance in suicide on-demand because the Suicide Act remains valid law in the United Kingdom and the DPP’s guidelines technically do not grant anyone immunity from prosecution. Nevertheless, a legal regime that accepts the principle that self-determination grants one the right to avoid what he or she considers to be an undignified end to his or her life by its own logic invites challenges to any sort of restrictions that would appear to limit the right to assisted suicide to those who suffer from a small subset of serious physical ailments. If personal autonomy persists as the sole rationale for recognizing the right to make decisions regarding the manner of one’s own death, it is only a matter of time before “death-on-demand” is available to all U.K. citizens, irrespective of their level of suffering.
CHINA’S ANTI-MONOPOLY LAW:
PROTECTIONISM OR A GREAT
LEAP FORWARD?

Britton Davis*

Abstract: Thirty years since China’s markets opened to the world, the People’s Republic has seen impressive growth, in large part due to an openness to foreign investment. In 2009, China was one of few nations to experience GDP growth. With a market based on competition for the first time in decades, China has begun to promulgate antitrust legislation to curb anticompetitive behavior. The creation of an Anti-Monopoly Law in 2008 has prompted concern from outside China that the law will be used to promote a protectionist agenda, shielding Chinese domestic industry from foreign competition or investment. This Note examines the root cause of such concerns using a recent decision by Chinese antitrust authorities to prevent a merger between a domestic Chinese fruit juice company and Coca-Cola. This Note recommends an implementation of merger guidelines by the Chinese government in order to provide more transparency in its antitrust regime.

Consumers associate happiness with our brand. In fact, Coca-Cola means “Delicious Happiness” in Mandarin.

—2008 Coca-Cola Annual Report1

INTRODUCTION

The Anti-Monopoly Law (AML) of the People’s Republic of China was promulgated by the Standing Committee of the National People’s Congress on August 30, 2007 and went into effect on August 1, 2008. The AML was enacted for the express purpose of “preventing and restraining monopolistic conducts, protecting fair competition in the market, enhancing economic efficiency, safeguarding the interests of consumers and social public interest, [and] promoting the healthy de-

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To date, unresolved questions persist regarding which of these lofty goals will be most served by the AML and what approach China intends to take regarding antitrust issues. Whether China will use the AML as a tool to promote a protectionist agenda, potentially harming global competition, is of significant concern. Considering that China is one of the few nations in 2009 to experience economic growth and is a fertile market for global corporate expansion, a shift by China to a more protectionist stand regarding foreign investment in domestic Chinese industries is undesirable for global economic stability. Such concerns are reinforced by stated goals of the AML focusing on safeguarding consumer and social public interests, as well as the opaque decision-making to date by Chinese antitrust enforcement agencies.

While many legal scholars contend that China is likely to approach its antitrust regime in a manner similar to the United States or the European Union, China is faced with the considerable challenge of being a new player in the global marketplace, breaking out of its centrally-planned, state-run system, while balancing concerns over unemployment, weathering the global financial crisis and stimulating domestic Chinese industries. The precarious global financial situation and a focus by Chinese policymakers on stimulus and stabilization will undoubtedly influence Chinese antitrust practice. The knowledge that China is one of the few successful markets in a global recession and an attractive marketplace for global corporations will likewise have a sig-

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4 See id. at 5.
6 See Anti-Monopoly Law, supra note 2, art. 1; Bush, supra note 3, at 4–5.
8 See Bush, Oracle Bones, supra note 3, at 1.
nificant impact on how the Chinese balance the interests of stability for domestic enterprises and continued growth from foreign investment.9 Part I of this Note provides a brief glimpse into the merger review process under the AML through the lens of the blocked Coca-Cola/Huiyuan Fruit Juice Company merger (Coca-Cola merger), along with an explanation of the state of the fruit juice industry in China. This section also details some of the concerns stemming from China’s decision to block the Coca-Cola merger. Part II lays out the legal framework for the creation and implementation of the AML, focusing on the merger review process under the new regime, as well as an explanation of the merger review process in the United States for the purpose of comparison. Part III analyzes the role protectionism, concerns regarding public interests, and the advancement of a socialist economy play in merger review under the AML. This section analyzes the potential underlying rationale for the decision to block the Coca-Cola merger and how China can improve on its merger review process through the adoption of clear merger guidelines for enforcement agencies. In addition, the need for improvement in transparency with merger analysis and decisions will be addressed. Part IV concludes with an explanation of why the adoption of merger review guidelines and greater transparency for China will diminish concerns about economic protectionism and will provide guidance to foreign firms who may be considering a merger or acquisition with a domestic Chinese enterprise in the future.

I. Background

On September 3, 2008, nearly one month after the AML went into effect in China, Coca-Cola announced plans to acquire the Huiyuan Fruit Juice Company (Huiyuan), a deal reportedly worth $2.3 billion.10 This announcement came one week prior to the collapse of Lehman Brothers Holdings, Inc., the first dramatic event signaling a global economic crisis.11 Huiyuan is China’s largest juice maker and controls 42% of the pure fruit juice market in China.12 Immediately following the announcement of the proposed merger, the Chinese public expressed con-

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9 See generally Blodgett, supra note 7, at 201–03 (discussing how “the drive for both foreign direct investment and foreign trade . . . occup[ies] a unique position[] of importance”).
10 Bush, supra note 3, at 8.
cern over a foreign brand potentially acquiring a highly successful private domestic enterprise such as Huiyuan. According to an online poll, more than 80% of over 76,000 Chinese polled were against the proposed merger. Though Coca-Cola is one of the most popular brands in China, holding about 50% of the carbonated beverage market inside the nation, Huiyuan holds a particularly special place in the hearts of the Chinese people who view it as a success story, as a domestic brand successfully competing with international rivals.

It is not surprising that Coca-Cola would pursue a larger presence in China, where growth has helped Coca-Cola counter the economic slowdown it has experienced in the United States, with 15% growth in the third quarter of 2009 and 19% overall volume growth in China in 2008, which Coca-Cola credits to aggressive advertising during the Summer Olympics in Beijing. Coca-Cola introduced Minute Maid Pulpy to China in 2008 and grew case volume for the Minute Maid brand by 40% in one year. It is also not surprising that Coca-Cola would look at Huiyuan as a potential acquisition, as it would enable Coca-Cola to take a major leap in the growing fruit juice market in China. While Coca-Cola already held an estimated 12% of the market share in the total fruit juice market in China, due to the success of its Minute Maid low juice concentrate brand, it had yet to break into the pure juice market, where the Huiyuan acquisition would have immediately yielded it a near 40% share of the market. Fruit juices are highly popular in China among younger consumers, who are typically willing to pay more for what they perceive to be healthy products.

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14 Id.
16 Widespread Worry, supra note 13.
18 See COCA-COLA COMPANY 2008 ANNUAL REVIEW, supra note 1, at 8, 28.
19 Id. at 24.
21 See id.
sively colas.\textsuperscript{23} Perhaps surprisingly, Sprite, a Coca-Cola brand, has become more popular in China than Coke itself, as it is perceived by consumers to be healthier than dark colas.\textsuperscript{24}

In fact, research shows that China, when compared to the rest of the world, has a much lower per capita fruit juice consumption—one-tenth the overall average level and one-fortieth that of developed nations.\textsuperscript{25} Furthermore, foreign companies such as Coca-Cola have yet to tap into the third- and fourth-tier cities inside China, where much of the predicted growth in the fruit juice market is likely to come.\textsuperscript{26} Acquisition of a domestic brand, such as Huiyuan, which has already begun to penetrate these less-developed markets, having an estimated 800 million potential consumers, makes perfect sense for Coca-Cola to increase its share of the Chinese fruit juice market.\textsuperscript{27}

Unfortunately for Coca-Cola, on March 18, 2009, the Chinese government put up a roadblock to the company’s hopes of entering the pure fruit juice market through its acquisition of Huiyuan, using the AML to block the transaction.\textsuperscript{28} The Ministry of Commerce (MOFCOM) posited a theory of competitive harm based on the theory of leveraging, finding that Coca-Cola’s dominance in the carbonated beverage market would allow Coca-Cola to carry over that dominance into the fruit juice market, thereby eliminating or restricting competition and harming consumers.\textsuperscript{29} Additionally, MOFCOM feared that Coca-Cola would have greater market power in the fruit juice beverage market after acquisition because it would then control both its Minute Maid low fruit juice brand and the pure fruit juice brand Huiyuan.\textsuperscript{30} MOFCOM also expressed concerns that the acquisition would squeeze out small- and medium-sized domestic enterprises, stifling innovation in the fruit juice industry.\textsuperscript{31} The Chinese government’s desire to protect small- and medium-sized domestic enterprises stems from the fact that many domestic industries are segmented, with production evenly distributed geographically across China, a holdover from decades of a

\textsuperscript{23} Id.
\textsuperscript{24} Id.
\textsuperscript{26} Rein, supra note 22.
\textsuperscript{27} Id.
\textsuperscript{28} Bush, supra note 3, at 8.
\textsuperscript{29} Id.
\textsuperscript{30} Id.
\textsuperscript{31} Id.
centrally-planned economy that favored local self-sufficiency.32 By contrast, Huiyuan is one of the only domestic fruit juice enterprises to successfully compete against international rivals, leading many scholars to believe MOFCOM’s decision to block the Coca-Cola merger was rooted in economic nationalism or protectionism.33

China’s shift from a demand market economy, controlled and planned by the State, to an open market with limited competition began in 1978 under the leadership of Deng Xiaoping.34 Prior to Deng Xiaoping’s reforms, competition, much less a formal competition policy, was non-existent, with state-owned enterprises (SOEs) dominating almost all aspects of China’s economy.35 These SOEs coordinated production according to directives from the government, with no input on pricing or output and no concern regarding profits.36 Prior to 1978, China lacked not just any legal structure regarding competition, but lacked a culture focused on competition at all.37

From 1978 until 1992, China allowed limited market competition; accordingly, the laws surrounding competition were limited in number and in scope.38 It was not until 1992, at the Fourteenth Meeting of the Chinese Communist Party, that a call for the establishment of a socialist market economy and a need for strong antitrust legislation emerged.39 Through the 1990s, China enacted legislation aimed at protecting competition and consumers, such as the Law Against Unfair Competition, the Consumer Rights and Interests Protection Law, the Price Law and the Decision on Rectifying and Regulating Market Economic Order, among several others.40 It would be sixteen years after China moved to an open market system that it would begin heavily legislating in the antitrust arena.

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33 See Bush, supra note 3, at 9.
36 See id. at 387.
37 Id. at 390.
39 Id.
40 Id. at 74–75.
II. Discussion

A. From a Closed Market to the Anti-Monopoly Law in Thirty Short Years

Although serious antitrust reform began in 1994, when the former State Economic and Trade Commission began drafting anti-monopoly legislation, the AML would not be finalized for thirteen years—the longest drafting period of any legislation in modern Chinese history.\footnote{See id. at 76.} Throughout the drafting process China continued to promulgate rules and regulations concerning competition in various forms, such as the Interim Provisions on Preventing the Acts of Price Monopoly in 2003.\footnote{See generally Interim Provisions on Preventing the Acts of Price Monopoly (promulgated by the State Dev. and Reform Comm., July 18, 2003, effective Nov. 1, 2003), translated at http://www.asianlii.org/cn/legis/cen/laws/ipoptaopm625.} This legislation was followed by the Provision on Mergers and Acquisitions of Domestic Enterprises by Foreign Investors (Provisions) in 2006.\footnote{See generally Provision on Mergers and Acquisitions of Domestic Enterprises by Foreign Investors (promulgated by MOFCOM, State-Owned Assets Supervision and Admin. Comm’n of the State Council, the State Admin. of Tax’n, the State Admin. for Indus. and Com., Secs. Reg. Comm’n of China, State Admin. of Foreign Exch., Aug. 8, 2008, effective Sept. 8, 2008), translated at http://www.asianlii.org/cn/legis/cen/laws/potmocsasaacotsctsotsaffiacscrocutaofeomaaodebfi20063704.}

The Provisions laid out guidelines for foreign investments in domestic Chinese enterprises, whether these investments involved the acquisition of a significant share of stock or wholesale acquisition of a Chinese enterprise.\footnote{See id.} After the implementation of the AML in 2008, MOFCOM updated these Provisions, adding an article stating that foreign investment would follow the declaration requirements mandated by the AML, unifying previous guidelines still technically in effect with the AML.\footnote{See Provisions on Mergers and Acquisitions of Domestic Enterprises by Foreign Investors (promulgated by MOFCOM, July 22, 2009, effective July 22, 2009), art. 51, translated at http://www.fdi.gov.cn/pub/FDI_EN/Laws/law_en_info.jsp?docid=108906.}

MOFCOM, the administrative body tasked with drafting the AML, consulted with foreign competition officials including the U.S. Department of Justice, the Federal Trade Commission, the American Bar Association, the World Bank, and the United Nations Conference on Trade and Development, among others.\footnote{Thomas Howell et al., China’s New Anti-Monopoly Law: A Perspective from the United States, 18 Pac. Rim L. & Pol’y J. 53, 56 (2009).} The drafting of the AML was conducted with greater transparency than many previous Chinese legislative efforts; engagement by Chinese officials with the international community was seen as a victory for global competition, as the final
draft eliminated many of the provisions included in previous versions of the law and that concerned foreign observers. What remains to be seen is how the Chinese government will interpret the AML and which of the lofty goals expressed in Article I will most influence the decisions made with regard to antitrust concerns, particularly merger and acquisitions review under Chapter IV.

B. AML in Action: Decisions to Date

Because only eighteen months have elapsed since the implementation of the AML, and the global financial crisis has slowed mergers and acquisitions, the body of AML-related decisions remains small; consequently, there is still much uncertainty regarding what goals the Chinese government is pursuing. The Antimonopoly Bureau of MOFCOM has the responsibility of managing the review of mergers, or “concentrations,” under the AML. Having been the administrative body to conduct such reviews under the Provision that preceded the AML, the Antimonopoly Bureau has been revised to create a unified approach to merger review alongside the AML. MOFCOM is also responsible for issuing guidelines and special notification thresholds that guide when a potential concentration requires review under the AML for alleged anticompetitive effects. While these substantive guidelines have certainly enhanced the reliability of the new merger review scheme, there are still many uncertainties regarding how merger review is conducted by MOFCOM; moreover, provisions in the AML provide significant flexibility to MOFCOM in its decision-making, while providing virtually no notice to would-be merging parties of how a transaction might be analyzed by MOFCOM.

A remarkable feature of the merger review under the AML has been the lack of transparency in analyses conducted by MOFCOM, which to date has published only five decisions and unconditionally cleared approximately forty deals with no public record of the analysis conducted in those decisions at all. Of the five decisions that have

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47 See Bush, supra note 7, at 1–2.
48 See Anti-Monopoly Law, supra note 2, arts. 1, 20–31; Bush, supra note 3, at 1.
49 See Bush, supra note 3, at 1.
50 Id.
51 Id. at 2.
52 See id. at 3.
53 See id. at 4–5; Matthew Murphy, China’s Anti-Monopoly Bureau Approves the Pfizer-Wyeth Transaction, GERSON LEHRMAN GROUP NEWS, Sept. 29, 2009, http://www.glgroup.com/News/Chinas-Anti-Monopoly-Bureau-Approves-the-Pfizer-Wyeth-Transaction-43739.html; MOC Sets Con-
been published, all but one was conditionally approved and all but that
same decision involved a merger or acquisition of two non-Chinese
corporations.\footnote{Bush, supra note 3, at 5–10; Murphy, supra note 53; GM-Delphi, supra note 53.} The Coca-Cola merger has been the only decision to
date in which MOFCOM has blocked an acquisition.\footnote{See Bush, supra note 3, at 5–10.}

In similar fashion to the prior publicly announced decisions,
MOFCOM’s decision to block the Coca-Cola merger was announced in
a “brief” notice on March 18, 2009.\footnote{See id. at 8.} MOFCOM surprised some by ra-
tionalizing the decision to block the acquisition under the theory that
Coca-Cola would leverage its brand dominance in the carbonated soft
drink market to the fruit juice market, which would provide it the ability
to eliminate or restrict competition, as discussed above.\footnote{Id. at 9.} In addition,
MOFCOM announced that it had afforded Coca-Cola an opportunity to
propose solutions to reduce the negative impact to competition and
that Coca-Cola had failed to do so.\footnote{Id. at 10.} The MOFCOM notice included a mere
five sentences of analysis regarding the concerns the acquisition would
have created.\footnote{See id. § 18a(a)(2).}

C. Horizontal Merger Review Under the United States Antitrust Regime

Merger review in the United States is, like the AML of China, a sta-
tutory byproduct.\footnote{See 15 U.S.C. § 18 (2006); Anti-Monopoly Law, supra note 2, arts. 20–31.} In 1976, the United States passed the Hart-Scott-
Rodino Act, which provides for pre-merger notification to U.S. en-
forcement agencies, in particular, the Federal Trade Commission (FTC)
and the Assistant Attorney General in charge of the Antitrust Division
of the Department of Justice (DOJ).\footnote{See 15 U.S.C. § 18.} The various filing or notification
requirements are similar in structure to those followed under the AML
in that they also require filing or notification of a proposed acquisition
or merger based either on the value of the transaction itself or the sales
figures of either of the parties involved.\footnote{See id. § 18a(a)(2).} Once notification has been
provided to the appropriate enforcement agencies, those agencies will
investigate the potential anticompetitive effects the merger or acquisition
will likely have and will, within thirty days, request more informa-

\textit{GM-Delphi Deal}, Xinhua News Agency (P.R.C.), Sept. 29, 2009 [hereinafter GM-
tion or allow the transaction to move forward by simply allowing the thirty days to pass.\textsuperscript{63}

The DOJ and FTC (Agency or Agencies) divide merger work by specializing in different industrial sectors.\textsuperscript{64} If, after the Agency has requested additional information and has weighed the anticompetitive potential of a merger or acquisition, the decision is made to block a merger, the Agency must go to court to seek a preliminary injunction blocking the merger.\textsuperscript{65} A private litigant in the United States also has the ability to request an injunction to block a merger, though that litigant will face the burden of discovery, and competitors in a particular industry will almost always lack standing to challenge the merger.\textsuperscript{66} In either case, a court will ultimately decide whether to block a merger if the merging parties challenge the Agency’s decision, and historically, the courts have given considerable deference to the Agency.\textsuperscript{67} Because of such deference, the Agency guidelines substantively determine whether a merger or acquisition will occur in the United States.\textsuperscript{68}

DOJ Merger Guidelines set forth five steps that the Agency will take in assessing whether to approve or block a merger: assess (1) whether the merger would significantly increase concentration and result in a concentrated market, properly defined and measured; (2) whether the merger, in light of concentration in the market and other factors that characterize the market in question, raises concern about potential adverse competitive effects; (3) whether entry would be timely, likely and sufficient either to deter or to counteract the competitive effects of concern; (4) whether there are any efficiency gains that cannot otherwise be achieved other than through a merger; and (5) whether, but for the merger, either party would be likely to fail and exit the market.\textsuperscript{69}

As market definition is a key component in merger review analysis, the Agencies tasked with merger review have developed guidelines that contain specific methodology for defining a relevant market and the use of concentration indices to determine when a proposed merger will

\textsuperscript{63} See id. § 18a(b)(B).
\textsuperscript{64} Einer Elhauge, \textit{United States Antitrust Law and Economics} 572–73 (Robert C. Clark et al. eds., 2008).
\textsuperscript{65} Id. at 573.
\textsuperscript{66} Id.
\textsuperscript{67} See id. at 574.
\textsuperscript{68} See id.
raise antitrust concerns.70 To define a relevant market, the Agency will focus on potential consumer responses.71 A market is defined as a product or group of products and a geographical area in which a hypothetical profit-maximizing producer or seller of the given product would impose at least a “small but significant and nontransitory increase in price” (SSNIP test).72 The relevant market for merger review purposes is the group of products and a geographic area that is no bigger than necessary to satisfy the SSNIP test.73 The SSNIP test gauges the likely reaction of buyers of a product to a price increase, generally 5% for Agency purposes.74 If buyers would shift to an alternative product in a market after a price increase and a hypothetical monopolist in that product market could not profitably sustain that price increase, the Agency will broaden the market to include the next-best substitute.75 This process continues until a market is defined that is broad enough that buyer substitution would not prevent a hypothetical monopolist from sustaining a 5% increase.76

Once the relevant market has been defined, an assessment of the number of firms in that market and their respective market shares are established to determine market concentration.77 The Agency employs the Herfindahl-Hirschman Index (HHI) to determine market concentration, calculated by determining the sum of the squares of the individual market shares of all participants in a particular market, both pre- and post-merger.78 Based on how much that number will change post-merger, the Agency determines if the market will become significantly more concentrated by the merger with an assumption that the more concentrated a market, the more likely a firm could exercise market power and therefore have a negative impact on competition.79 The Agency will also consider whether the merging firms produce differen-

71 See generally Richard A. Posner, Antitrust Law 147–58 (2d ed. 2001) (discussing how elasticity of demand from consumers is directly related to how a market is defined for antitrust purposes).
72 Merger Guidelines, supra note 69, at 4.
73 Id.
74 Elhauge, supra note 64, at 207–08.
75 Id. at 208.
76 Id.
77 Elhauge, supra note 64, at 578–79; see Merger Guidelines, supra note 69, at 15–16.
78 Elhauge, supra note 64, at 579; see Merger Guidelines, supra note 69, at 15–16.
79 Elhauge, supra note 64, at 580; see Merger Guidelines, supra note 69, at 15–16.
tiated products or whether the competitors are close substitutes for one another in the eyes of consumers. If the Agency concludes that merging firms have a combined market share of at least 35%, that the products are regarded by purchasers to be close substitutes for one another, and that no alternative competitors are able to step in and compete, the Agency is more likely to block a merger for potential adverse effects to competition.

III. Analysis

United States jurisprudence concerning antitrust law has held, time and again, that the Sherman Act and subsequent antitrust legislation reflects a judgment by Congress that faith in competition lies at the center of national economic policy in the United States. Much like the AML, the statutory language of the Sherman and Clayton Acts is opaque, using phrasing such as “substantially to lessen competition” or “monopolize”; as a result, courts and antitrust enforcement agencies have been left to interpret those phrases and to determine when to intervene if competition is threatened. Legislative deference to competition has operated on the assumption that all elements of a bargain in a free market—whether quality, service, safety, or durability—are favorably affected by competition, and thus, restraints on competition should be prohibited. Restraints on competition are anathema to the Congressional intent and economic principles underlying American antitrust law. The promotion of social goals through U.S. antitrust law has been absent in merger review analysis, as Agencies and courts have generally given deferred to Congressional concern with protecting “competition, not competitors.”

Due to vague language in relevant antitrust statutes and what appeared to be an inability of courts to consistently apply economic principles involved in determining what activities might lessen competition, the DOJ began to establish guidelines in 1968 with the hope of insuring “that the business community, the legal profession, and other interested persons [were] informed of the Department’s policy” in enforc-

80 Elhauge, supra note 64, 580–81.
81 Id. at 582.
83 See Posner, supra note 71, at 118–36.
85 See id.
When standards of conduct applied to a market system are ambiguous or unclear, the danger of political or business-related interference in competition becomes a real possibility. Thus, while the AML purports to protect consumer welfare by protecting competition, China’s adoption of guidelines that focus squarely on competition issues and leave other social goals to other areas of the law will better protect competition and benefit consumers in China, as well as provide market participants an adequate understanding of how to compete successfully, and legally, in China.

A. Protectionist Components Underlying the Coca-Cola Decision

Understanding why the decision to block Coca-Cola’s acquisition of Huiyuan may have been influenced by underlying protectionist considerations involves understanding what other policy goals beyond protecting competition influence competition authorities. Stability and a “harmonious society” are seen as primary goals for the Chinese government, which is attempting to unify a formerly segmented economy and rectify a severe socioeconomic divide between its urban and rural populations. That such concerns would find themselves reflected in government attitudes towards competition is not surprising and that such concerns might influence MOFCOM’s enforcement of competition rules is equally unsurprising.

Compound these policy concerns with the pervasive problem of local or regional administrative monopolies over segmented industries throughout China, and MOFCOM’s difficulty with focusing solely on competition becomes apparent. Simply put, Chinese officials have an acute awareness of how China trails international counterparts in being able to compete globally in certain industries and while foreign acquisitions bring technical expertise and other efficiencies Chinese industry lacks, Chinese leaders also want to protect key industries against foreign

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87 Monograph No. 7, supra note 70, at 68; see also Kenneth M. Parzych, Public Policy and the Regulatory Environment 110 (1993) (confirming that DOJ created merger guidelines “to minimize . . . uncertainty and to assist businesses in arriving at some sense of self-determination”).


89 See Pate, supra note 34, at 201.

90 See id. at 200.

91 See id. at 200, 202.

92 See id. at 200.

93 See id. at 202–03.
competition. As the growth potential in the fruit juice industry is immense, it makes some sense that China might regard the fruit juice industry as a key industry in need of protection from domination by global competitors such as Coca-Cola.

Huiyuan itself is not a product of the segmented fruit juice industry inside China, where local enterprises supply fruit juice beverages to various geographic regions under the vestiges of the pre-1978 economy. By the end of 2008, the Chinese fruit juice industry was teeming with more than 300 medium and small fruit juice enterprises. The loss of Huiyuan to Coca-Cola would have removed one of the only large, domestically-controlled fruit juice enterprises from the market, leaving China with hundreds of small and medium enterprises to compete against Coca-Cola and other international competitors. The reality that Huiyuan would become controlled by Coca-Cola and that China would lose a highly successful brand that had been able to compete against global beverage giants provides reasonable concern that China was protecting an important domestic brand rather than truly focusing on the effects the Coca-Cola merger might have had on competition in the fruit juice industry. In its decision to block the merger, MOFCOM did not voice any such concerns, but in fact, soundly rejected the idea that Huiyuan’s status as a national brand was a factor in its analysis at all. Beyond that proclamation, information regarding the analysis conducted and the findings used to make its decision are notably sparse.

94 See id. at 204–05, 207.
95 Res. and Mkts., supra note 25.
97 Id.
98 See id.
99 See generally Chinese Res. & Intelligence, supra note 96; Widespread Worry, supra note 13.
100 See Bush, supra note 3, at 10; China Explains Rejection of Coke’s Bid for Juice Maker, N.Y. Times, Mar. 26, 2009, http://www.nytimes.com/2009/03/26/business/worldbusiness/26coke.html (quoting a ministry spokesman, Yao Jian, stating “[w]hether Huiyuan is a national brand is not a factor that needs to be considered in an antimonopoly investigation and has nothing to do with the . . . rejection of this acquisition”).
101 See Bush, supra note 3, at 9–10.
B. Competitive Components Underlying the Coca-Cola Decision

Could MOFCOM’s decision to block Coca-Cola’s acquisition of Huiyuan have been based solely on anticompetitive concerns, as the Chinese government has argued? The absence of guidelines on how horizontal mergers are reviewed by MOFCOM leave it up to conjecture as to how China determined the relevant market or the impact the merger might have on the concentration of that market, two factors critical to understanding whether a proposed merger is likely to have anticompetitive effects.\(^\text{102}\)

Statements released after the decision indicate that China proposed a theory that Coca-Cola would use its dominance in the carbonated drink market to promote sales of Huiyuan, which would hamper competition and drive up prices in the fruit juice market.\(^\text{103}\) This “leveraging” theory has found very little support in other global markets, such as the United States.\(^\text{104}\) China expressed fear that Coca-Cola would bundle its carbonated beverages with its fruit juice brands (including Huiyuan, post-merger), though ministry officials did not point to any direct evidence to show that Coca-Cola had engaged in such conduct, either with its Minute Maid brand or another product in China.\(^\text{105}\) When faced with concerns regarding bundling in the United States, Agencies will determine the market power of the various parties and the concentration that exists in the relevant market to understand the potential anticompetitive effects bundling might have on the market, weighing those effects against potential efficiencies that might result to determine whether to bring action against a party.\(^\text{106}\) Bundling, even when it occurs, is not deemed per se illegal.\(^\text{107}\)

MOFCOM argued that post-merger, Coca-Cola would have stronger market power in the fruit juice beverage market, as it would then control Huiyuan and its own Minute Maid brand, and “given its current dominance over the carbonated beverage market and the carryover effect, the concentration will considerably raise barriers for potential competitors to enter the fruit juice beverage market.”\(^\text{108}\) The ac-

\(^{102}\) See Posner, supra note 71, at 147–58; Bush, supra note 3, at 9–10.

\(^{103}\) China Explains Rejection of Coke’s Bid for Juice Maker, supra note 100; see Bush, supra note 3, at 8.

\(^{104}\) Bush, supra note 3, at 9.

\(^{105}\) See id. at 8–9.

\(^{106}\) See Elhauge, supra note 64, at 408–16.

\(^{107}\) See id.

\(^{108}\) Bush, supra note 3, at 8 (quoting Zhonghua Renmin Gongheguo Shangwubu Gonggao [Notice [2009] No. 22 of MOFCOM of the P.R.C.] (issued by MOFCOM, Mar. 18, 2009,
quisition, MOFCOM believes, would squeeze out small and medium-sized domestic fruit juice enterprises, negatively affecting competition and the “sustained and sound development of the Chinese fruit juice industry.” ¹⁰⁹ Though Coca-Cola attempted to ameliorate these concerns through unpublicized proposals seeking to address specific issues disclosed by the Chinese government, MOFCOM ultimately rejected the proposed merger, and to date, no further information has been given as to the analysis conducted behind the scenes.¹¹⁰

While MOFCOM’s stated reasoning for blocking the merger falls near the boundaries of international antitrust practices, absent any knowledge of how the relevant market and pre- and post-merger concentration of that market was determined, it is difficult to know what the actual impact would have been on the fruit juice industry and on consumers in China had the merger been approved.¹¹¹ Considering the growth potential in the fruit juice industry in China, it should not have been surprising that players in the market would consider acquisitions to expand their market share.¹¹² Rarely would such mergers be prevented in circumstances where the relevant market is undersupplied, as it would be unlikely that any one player could tacitly collude to drive up prices with other market participants absent a highly concentrated market.¹¹³ Could Coca-Cola have been able to maintain supracompetitive pricing for its juice brands in light of the fact the fruit juice market in China has hundreds of participants who could potentially expand production and output in order to compete with Coca-Cola and capture unmet demand for fruit juice?¹¹⁴ With hundreds of potential competitors domestically alone, MOFCOM must have been making an assumption that the barriers to entry or expansion of these firms are high (not even considering potential entry by other international competitors), though it is uncertain whether there was any actual analysis done


¹⁰⁹ Id. (quoting Coke/Huiyuan Notice).

¹¹⁰ See id. at 8–9.

¹¹¹ See Posner, supra note 71, at 147–58; Bush, supra note 3, at 9.

¹¹² See Rein, supra note 22.

¹¹³ See generally Res. and Mkts., supra note 25; Posner, supra note 71, at 124 (discussing that the significance of concentration is that it facilitates collusion among firms in the market).

¹¹⁴ See Posner, supra note 71, at 127 (arguing that the ease and rapidity of entry into a particular market means firms are unable to fix prices without inducing rapid and widespread entry by new firms, forcing market price down to competitive levels). See generally Res. and Mkts, supra note 25.
to support this assumption.\textsuperscript{115} Certainly none was provided in the decision.\textsuperscript{116} If barriers to entry or expansion are low, Coca-Cola would have been unable to charge supracompetitive prices.\textsuperscript{117}

Absent guidelines as to how China might have determined the relevant market, how concentrated the market was pre- and post-merger or the barriers to entry or expansion in the market, Coca-Cola had no expectation of how its acquisition of Huiyuan would be analyzed by MOFCOM or what factors would determine the fate of the transaction.\textsuperscript{118} This lesson came with likely high transaction costs and ultimately, no return on investment for Coca-Cola.\textsuperscript{119}

**Conclusion**

It is not surprising that the first decision by China under the AML to block a proposed merger would draw some attention, and likely some criticism. The fact that the first instance of China flexing its anti-trust enforcement muscles came at the expense of such a globally recognized brand as Coca-Cola was certain to attract the international business community’s attention. For decades China has been seen as the land of opportunity and growth for foreign investors and only time will determine whether this decision signals a change in that policy. China would have us believe that this decision rested solely on China’s commitment to protecting competition. To protect itself from accusations of economic nationalism or protectionism in the future, China should embrace the U.S. approach to merger review, issuing clear guidelines for enforcement agencies to follow and increasing transparency in its decision-making so that future enterprises can better plan and continue to see China as a fertile ground for growth and expansion. Until then, global enterprises will hesitate investing the time and financial resources into Chinese expansion out of fear that they will be met with resistance sparked by non-competition-related concerns.

\textsuperscript{115} See Posner, *supra* note 71, at 127; Bush, *supra* note 3, at 8–9 (showing that MOFCOM’s announcement blocking the Coca-Cola merger was absent detailed analyses on the economic impact of the proposed merger).

\textsuperscript{116} See Bush, *supra* note 3, at 8–9.

\textsuperscript{117} See Posner, *supra* note 71, at 127.


\textsuperscript{119} See generally Monograph No. 7, *supra* note 70, at 68; Parzych, *supra* note 87, at 110 (highlighting the importance of the existence of merger guidelines for planning purposes in order for market participants to control costs and conduct business in an efficient manner).
TAMING THE PERFECT POISON:
A COMPARATIVE ANALYSIS OF THE
EMEA’S EPAR SYSTEM AND THE FDA’S
IMPROVED WARNING PROTOCOL

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Abstract: In Europe and the United States, regulatory agencies responsible for monitoring drug safety have struggled to address the health concerns raised by the burgeoning market for minimally invasive cosmetic procedures utilizing botulinum toxins, the active ingredients in Botox. A 2005 study published in the *Journal of the American Academy of Dermatology* drew attention to these shortcomings after an analysis of adverse event reports submitted to the Food and Drug Administration (FDA) linked twenty-eight patient deaths to Botox-induced respiratory arrest and myocardial infarction. After an independent review of adverse effects reports submitted to the European Medicines Agency (EMEA) revealed similar findings in Europe, the FDA and EMEA implemented bolstered product warnings aimed at increasing patient awareness of the drug’s health risks. This Note compares the FDA and EMEA’s heightened warning protocols and argues that the agencies’ recent efforts are unlikely to reduce the number of serious adverse events linked to botulinum toxins.

Introduction

The demand for minimally invasive cosmetic procedures utilizing botulinum toxins—the active ingredients in Botox—has exploded during the past decade in North America and Europe. Nevertheless, at home and abroad, regulatory agencies charged with ensuring drug safety have struggled to address the health concerns associated with this

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nascent area of medicine.² In 2005, a study published in the *Journal of the American Academy of Dermatology* (Coté Study) drew attention to these shortcomings after an analysis of adverse event reports submitted to the Food and Drug Administration (FDA) linked twenty-eight deaths to Botox-induced respiratory arrest and myocardial infarction.³ On the heels of this study, government watchdog groups petitioned the Agency to take stronger measures to protect patients.⁴ In 2009, the FDA responded by implementing a bolstered warning protocol mimicking the advisory system used by the European Medicines Agency (EMEA), the FDA’s European counterpart.⁵

It is unclear whether the FDA’s recent efforts are sufficient to deal with the crisis currently facing the cosmetic medicine industry.⁶ Botulinum toxins are the deadliest naturally occurring substances in the world.⁷ Improperly injected, botulinum toxins can cause severe life-threatening complications.⁸ Nonetheless, regulations governing who may perform such injections are quite lax.⁹ In the United States, Botox

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⁵ See id.; Bridget M. Kuehn, *FDA Requires Black Box Warnings on Labeling for Botulinum Toxin Products*, 301 JAMA 2316, 2316 (2009).


may be injected by non-physician practitioners in the absence of direct doctor supervision. In Great Britain, the Medicines and Healthcare Products Regulatory Agency even permits patients to perform self-administered injections.

This Note compares and evaluates the adequacy of safety regulations imposed by the FDA and EMEA on manufacturers of botulinum toxin products. In particular, this Note addresses the sufficiency of the FDA’s improved warning protocol as a method of reducing the incidence of serious adverse events related to botulinum toxin type A (Botox). Part I traces the history of botulinum toxin use and its emergence as a drug for cosmetic indications. Part II discusses the Coté Study’s independent review of adverse event reports submitted to the FDA in connection with botulinum toxin type A. This section also canvasses the EMEA’s European Public Assessment Report (EPAR) advisory system and the EMEA’s response to seventeen reported deaths in European Union (EU) member states linked to botulinum toxin products. Furthermore, Part II examines the FDA’s new warning protocol vis-à-vis botulinum toxin products as a response to criticism that the FDA lagged behind its European counterpart. Part III compares the FDA’s strengthened warning protocol to the advisory system employed by the EMEA and evaluates whether the improved protocol can reduce the number of serious adverse events in the United States. Finally, Part III proposes an alternative approach toward reducing the number of serious adverse events that relies on state-based regulatory action by medical licensing boards.

I. Background

Nineteenth-century physician Justinus Kerner first examined the effects of botulinum toxin after he identified more than two hundred cases of botulism attributed to the ingestion of inadequately pre-


10 See Med. Bd. of Cal., supra note 9, at 1, 9; MBRHA Memo, supra note 9.

11 See MHRA Botox, supra note 9.

12 Botulism, “a paralytic disease caused by [the] potent neurotoxin . . . Clostridium botulinum,” is separated into three distinct cases: (1) food-borne botulism, caused by the ingestion of food contaminated with C. botulinum; (2) wound botulism, which develops in wounds infected with the toxin; and (3) intestinal botulism, caused by “ingestion of spores and production of [the] toxin in the intestines” of infected individuals. Elias Abrutyn, Botulism, in HARRISON’S PRINCIPLES OF INTERNAL MEDICINE 841, 842 (16th ed. 2005). All incidences of the disease “begin[] with cranial nerve involvement,” with paralytic symptoms gradually spreading to the extremities. Id.
served blood sausages.\textsuperscript{13} In an 1817 monograph, Kerner suggested the toxin had potential therapeutic use in blocking abnormal motor movements and eliminating hypersecretion after observing its paralytic effect on the eye muscles and secretory glands.\textsuperscript{14} In the same monograph, however, Kerner expressed doubt over the tenability of such applications, hypothesizing that the toxin’s extreme lethality would make it difficult to manage in a clinical setting.\textsuperscript{15}

In 1989, the FDA approved botulinum toxin type A (BTX-A) for the treatment of adult strabismus (crossed eyes) and blepharospasm (eyelid tics) after a decade’s worth of data demonstrated BTX-A’s positive effect in eliminating eyelid and hemifacial spasms.\textsuperscript{16} Shortly thereafter, ophthalmologists noticed that blepharospasm patients injected with BTX-A around the eyes and upper face at intervals of three or four months demonstrated significant improvements in the appearance of glabellar rhytides (frown lines).\textsuperscript{17} In response, several clinical studies tested the efficacy and safety of this off-label cosmetic usage of BTX-A.\textsuperscript{18} In 2002, the FDA approved BTX-A “for the temporary improvement in the appearance of moderate to severe glabellar lines” (brow furrow) in adult patients.\textsuperscript{19}

\textit{Clostridium Botulinum}, the bacterium responsible for the foodborne botulism observed by Kerner, has “eight serotypes (A, B, C\textalpha, C\beta, D, E,
that produce seven . . . distinct neurotoxins.”20 Each serotype
shares the ability to block acetylcholine from being released in striated
muscles, which causes chemical denervation, temporary muscle paralysis
at the site of injection, and “smooth[es] hyperkinetic lines [facial
wrinkles].”21 Although botulinum toxin type B has been approved by
the FDA for therapeutic (non-cosmetic) indications,22 BTX-A is the on-
ly serotype currently approved for cosmetic use in the United States.23
Until April 2009, Botox was the only commercially available formula-
tion of BTX-A.24

Achieving the correct dosage of Botox is essential to safe and effective
use, and depends on the proficiency of the medical practitioner
who is performing the injection.25 Botox is a sterile, freeze-dried form
of BTX-A.26 It is distributed in a concentrated crystalline form, and
must be reconstituted with saline prior to use.27 The dilution ratio of
BTX-A to saline varies and depends on a range of factors that must be
assessed by the injector prior to use.28 Moreover, “incorrect dosages are

20 Arnold W. Klein, Complications, Adverse Reactions, and Insights with the Use of Botulinum
Toxin, 29 DERMATOLOGIC SURGERY 549, 549 (2003) [hereinafter Klein, Complications, Ad-
verse Reactions, and Insights]; see Erbguth & Naumann, supra note 13, at 1850.

21 See J. Alastair Carruthers & Jean Carruthers, Botulinum Toxin A in the Mid and Lower
Face and Neck, 22 DERMATOLOGIC CLINICS 151, 152 (2004) [hereinafter Carruthers & Car-
ruthers, Botulinum Toxin A in Face and Neck]; Arnold W. Klein, Contraindications and Compli-
cations with the Use of Botulinum Toxin, 22 CLINICS IN DERMATOLOGY 66, 66, 68 (2002) [here-
inafter Klein, Contraindications].

22 See Timothy C. Flynn, Myobloc, 22 DERMATOLOGIC CLINICS 207, 207 (2004); Press Re-
lease, Elan Pharm., FDA Approves Elan’s Myobloc Botulinum Toxin Type B Injectable
newsArticle&ID=137749&highlight=. See generally Craig Zalvan et al., Noncosmetic Uses of

23 See Arnold W. Klein, Complications with the Use of Botulinum Toxin, 22 DERMATOLOGIC
CLINICS 197, 198 (2004) [hereinafter Klein, Complications with the Use of Botulinum Toxin].

24 See J. Alastair Carruthers & Jean Carruthers, Use of Botulinum Toxin A for Facial En-
hancement, in TISSUE AUGMENTATION IN CLINICAL PRACTICE: PROCEDURES AND TECHNIQUES
A for Facial Enhancement]; Press Release, Ipsen & Medicis Pharm., FDA approves DysportTM
for Therapeutic and Aesthetic Uses (Apr. 30, 2009), available at http://www.ipsen.com/arti-
cles/investorrelations/regulatedinformation/20090430_dysport_usa_10.pdf.

25 See Coté et al., supra note 3, at 410–11 (finding that numerous AEs related to BTX-A
were caused by improper dilution modifications); Alan M. Mantell, Dilution, Storage, and
Electromyographic Guidance in the Use of Botulinum Toxins, 22 DERMATOLOGIC CLINICS 135,

26 See Carruthers & Carruthers, Botulinum Toxin A for Facial Enhancement, supra note 24,
at 119.

27 See Carruthers & Carruthers, Botulinum Toxin A in Face and Neck, supra note 21, at
151.

28 See id. (concluding that adjustments should be made prior to performing injections
in singers, musicians, and other patients who use their perioral muscles with intensity);
very likely to result in severe adverse effects.” Researchers have concluded that improper dilution of BTX-A is a significant cause of unintended spread of the toxin away from the site of injection, and may “[produce] symptoms of botulism.”

In 2002, an estimated 1.1 to 1.6 million patients received Botox injections in the United States. By 2003, Botox injections were the second most commonly performed cosmetic procedure in North America. Contemporaneously, several prominent medical journal articles allayed lingering concerns over the drug’s toxicity and detrimental health effects. Physicians urged that when “[p]roperly used, the incidence of complications [associated with the use of Botox] is low and their severity mild.” Additionally, they insisted that “most complications [were] related to poor injection techniques” and that there were no reported “long-term adverse effects or health hazards related to the use of Botox for any cosmetic indication.”

Klein, Complications, Adverse Reactions, and Insights, supra note 20, at 553; Mantell, supra note 25, at 135. Factors influencing the dilution ratio include the anatomy of the injection site, patient’s prior conditions, and the patient’s occupation. See Carruthers & Carruthers, Botulinum Toxin A in Face and Neck, supra note 21, at 156; Klein, Complications, Adverse Reactions, and Insights, supra note 20, at 553; Mantell, supra note 25, at 135.

See Mantell, supra note 25, at 135.

Coté et al., supra note 3, at 411; Bridget M. Kuehn, Studies, Reports Say Botulinum Toxins May Have Effects Beyond Injection Site, 299 JAMA 2261, 2262 (2008) [hereinafter Kuehn, Reports]. Botulism is characterized by “cranial nerve dysfunction (resulting in double vision (diplopia), inability to control or coordinate the muscles used in speaking (dysarthria), and/or difficulty swallowing (dysphagia)), followed by progressive descending muscle weakness or paralysis that can lead to respiratory failure and death.” Letter from Janet Woodcock, Dir., Ctr. for Drug Evaluation and Research, FDA, to Sidney Wolfe et al., Dir., Pub. Citizen (Apr. 30, 2009), available at http://www.fda.gov/downloads/Drugs/DrugSafety/PostmarketDrugSafetyInformationforPatientsandProviders/DrugSafetyInformationforHealthcareProfessionals/UCM143989.pdf (citing Abrutyn, supra note 12, at 842-45).

See Coté et al., supra note 3, at 408 (citing the findings of the Am. Soc’y of Aesthetic Plastic Surgeons).


See Klein, Complications with the Use of Botulinum Toxin, supra note 23, at 197.

See Alastair Carruthers & Jean Carruthers, Botulinum Toxin Type A for the Treatment of Glabellar Rhytides, 22 DERMATOLOGIC CLINICS 137, 141 (2004).

See Klein, Contraindications, supra note 21, at 68 (citing Peter Hambleton & A. Peter Moore, Botulinum Neurotoxins: Origin, Structure, Molecular Actions, and Antibody, in Handbook of Botulinum Treatment 17, 27 (A. Peter Moore ed., 1995)).
II. Discussion

A. Independent Review of Adverse Event Reports Submitted to the FDA

In 2005, data emerged that cast grave doubt on the safety of Botox. A study published in the *Journal of the American Academy of Dermatology* (Coté Study) reviewed 1437 adverse events (AEs) reported to the FDA in connection with both therapeutic and cosmetic uses of BTX-A. Researchers of this study set out to independently tally the number of serious AEs linked to BTX-A. They classified AEs according to the statutory definition outlined by Title 21 of the U.S. Code of Federal Regulations. According to this provision, an AE is defined as “[a]ny adverse experience occurring at any dose that results in [inter alia] . . . [d]eath, a life-threatening adverse experience, inpatient hospitalization or prolongation of existing hospitalization.”

The Coté Study found that 217 of the 406 AEs related to therapeutic use of BTX-A satisfied the statutory definition of “serious.” Of these, BTX-A was causally linked to twenty-eight deaths and seventeen seizures. Researchers also identified thirty-six serious AEs related to cosmetic use of BTX-A, including five instances of focal facial paralysis and dysphagia (difficulty swallowing).

In explaining why the number of serious AEs was significantly greater for therapeutic use as opposed to cosmetic use, researchers hi-
highlighted the differences between the clinical characteristics of therapeutic and cosmetic cases.\textsuperscript{46} Notably, for therapeutic cases, “doses were higher . . . and patients tended to have serious underlying diseases.”\textsuperscript{47} By contrast, patients receiving cosmetic BTX-A injections “typically had no underlying disease reported, and [they] were injected with much smaller doses.”\textsuperscript{48}

More significantly, the Coté Study emphasized that many AEs tied to cosmetic injections were caused by a “lack of adherence to [basic] precepts” of BTX-A use: “[c]areful attention to drug dose, dilution, handling, storage, and site of injection.”\textsuperscript{49} In more than a dozen cosmetic cases, patients were injected with five times the maximum labeled dosage of BTX-A.\textsuperscript{50} Researchers also found that many cosmetic injections deviated from the labeled dilution procedure.\textsuperscript{51} In fact, “[d]rug dilution modifications were reported frequently with such diluent substitutions as bupivacaine, lidocaine, water, and previously reconstituted [BTX-A], rather than the recommended saline diluent.”\textsuperscript{52} In a similar vein, common handling errors included “injecting reconstituted product after the recommended 4-hour expiration, freezing or refrigerating reconstituted product for future use, [and] injecting multiple patients with [BTX-A] from a vial labeled for single-patient use.”\textsuperscript{53}

B. EMEA Warnings Regarding Adverse Reactions to BTX-A and BTX-B

The EMEA has implemented its own adverse reactions reporting system since 2004.\textsuperscript{54} Medicines meeting the EMEA’s standards of quality, safety, and efficacy are granted Marketing Authorization after undergoing review by the Committee for Medicinal Products for Human Use (CHMP).\textsuperscript{55} Once Marketing Authorization has been granted, the CHMP publishes a European Public Assessment Report (EPAR), which details “the reasons for its opinion in favour of granting authorisation.”\textsuperscript{56} In addition, EPARs contain a Summary of Product Characteris-

\textsuperscript{46} See Coté et al., \textit{supra} note 3, at 409.
\textsuperscript{47} \textit{Id.}
\textsuperscript{48} \textit{Id.}
\textsuperscript{49} \textit{Id.} at 410.
\textsuperscript{50} See \textit{id.} at 410–11.
\textsuperscript{51} \textit{Id.} at 411.
\textsuperscript{52} See Coté et al., \textit{supra} note 3, at 411.
\textsuperscript{53} \textit{Id.}
\textsuperscript{54} See 2004 O.J. (L 136) 12; Pub. Citizen Health Res. Group, \textit{supra} note 4 (recognizing the EMEA’s system as the counterpart to the FDA’s MedWatch reporting system).
\textsuperscript{55} See 2004 O.J. (L 136) ¶¶ 13, 23.
\textsuperscript{56} \textit{Id.} ¶ 3.
tics (SPC). On botulinum toxin products, the SPC includes a “special warnings and precautions for use” section that succinctly addresses all the major issues related to migration of [the] injected drug.” All EPARs are written “in a manner that is understandable to the public” and are published on the EMEA’s website.

In March of 2005, the CHMP updated its SPC for Neurobloc (BTX-B) after an interim analysis found that thirty percent of the total number of adverse reactions reported to the EMEA between January 2001 and December 2003 satisfied the EMEA’s definition of “serious.” Mirroring the conclusion reached by the Coté Study with respect to BTX-A-related AEs reported to the FDA, the CHMP found that most adverse reactions associated with BTX-B were caused by spread of the toxin beyond the injection site.

Eight months later, the CHMP issued a second, more robust, advisory. European health officials announced that they had discovered evidence linking BTX-B to the deaths of seventeen patients in Europe. Furthermore, the CHMP clarified that the reported negative side effects were “not specific of [BTX-B] but of the whole class [of botulinum toxins].” In connection with this finding, the updated EPAR warned patients of an “overall concern on the class of botulinum toxins regarding dysphagia and fatal outcomes.” The EMEA further responded by requiring BTX-B manufacturers to package an updated set of warning leaflets along with every drug vial, explaining how patients should be

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60 EMEA, Procedural Steps, supra note 59, at 7, 8.
61 See 2001 O.J. (L 83) ¶ 12. European Community Regulations define “serious adverse reaction” as “a reaction which results in death, is life-threatening, requires inpatient hospitalisation or prolongation of existing hospitalisation, results in persistent or significant disability or incapacity, or is a congenital anomaly/birth defect.” Id.
62 Compare Coté et al., supra note 3, at 410 (concluding that the majority of AEs reported to the FDA in connection with BTX-A were caused by distant spread of the toxin), with EMEA, Procedural Steps, supra note 59, at 4 (concluding that most adverse effects reported to the EMEA in connection with BTX-B were caused by distant spread of the toxin).
63 See EMEA, Procedural Steps, supra note 59, at 5.
64 Id.
65 See id.
66 See id. at 4–5.
given BTX-B, and warning against the possibility of serious adverse effects caused by the spread of the toxin from the site of injection. 67

C. The FDA’s Response to Calls for Stronger Patient Warnings

Heeding the EMEA’s call for an aggressive stance toward botulinum toxin products, regulatory agencies in the United Kingdom and Germany “amplified the EU[’s] warning[s] [by requiring manufacturers to issue] ‘Dear Doctor Letters’” that “alert[ed] physicians in its 27 member states about the need to monitor for signs of botulinum toxin adverse events.” 68 Despite the Coté Study’s somber findings, however, “no similar official warnings [were issued] by the FDA [in the United States].” 69 Responding to government inaction in the United States, in January 2008, Public Citizen Health Research Group (Public Citizen) sent a letter to FDA Commissioner Andrew von Eschenbach petitioning the Agency to take stronger measures to warn patients of the dangers associated with BTX-A and BTX-B. 70 Using the EMEA’s EPAR advisory system as a model for reform, the petition set forth three basic recommendations for protocol change. 71

First, the petition called for clearer, more stream-lined, physician-directed warnings. 72 Unlike the warnings issued by the EMEA, in the United States, information for physicians was “scattered throughout the labels,” or obliquely listed under an “Adverse Reactions” section. 73 In response, Public Citizen requested a concise description of “all major issues related to migration of the injected drug.” 74 The petition also requested that the FDA clarify that “the phenomenon of distant spread is not restricted to patients [undergoing therapeutic BTX-A treatment]” but equally applies to cosmetic use of BTX-A. 75

Second, Public Citizen called for a clear and consistent set of patient-directed warnings. 76 In the United States, only a fraction of drugs possess patient-friendly labels that provide complete and accessible in-

68 See id.
69 See id.
72 See id.
73 See id.
74 See id.
75 See id.
76 See id.
formation regarding adverse effects.\textsuperscript{77} For BTX-A products in particular, “the ‘Information for Patients’ section [was] very brief, and [did] not approach the five-page EU patient information in [terms of] comprehensiveness.”\textsuperscript{78} For example, on the label then-existing for Botox, the only information provided “was that ‘[p]atients or caregivers should be advised to seek immediate medical attention if swallowing speech or respiratory disorders arise.’”\textsuperscript{79} The labeling also failed to consistently advise patients of the health risks posed by distant spread of the toxin.\textsuperscript{80}

Third, the petition urged the FDA to require “detailed written information in the form of FDA-approved Medication Guides” to be dispensed by the physician at the time the drug is injected into the patient.\textsuperscript{81} In this respect, Public Citizen addressed the concern that “[e]ven if [the] . . . labeling [was] more complete, there [was] no evidence that physicians [would] actually discuss [the] information with their patients.”\textsuperscript{82}

In April of 2009, the FDA responded to Public Citizen’s petition by granting all three of its requests for protocol reform.\textsuperscript{83} The Agency notified all Biologics License Application (BLA) holders for botulinum toxin products that “the risk of spread of botulinum toxin effects from the site of injection should be included in the labeling of the products (including a boxed warning).”\textsuperscript{84} Additionally, the FDA sent notification letters to BLA holders advising that a “Risk Evaluation and Mitigation Strategy (REMS) . . . is necessary to ensure that the benefits of these products outweigh the risks.”\textsuperscript{85} Lastly, it required that every REMS must include “a Medication Guide and Communication Plan, including a Dear Health Care Provider letter, and a timetable for submission of assessments.”\textsuperscript{86}

III. Analysis

The FDA’s improved warning protocol vis-à-vis BTX-A represents a considered response to Public Citizen’s criticism that the Agency lagged

\textsuperscript{78} See id.
\textsuperscript{79} Id.
\textsuperscript{80} Id.
\textsuperscript{81} Id.
\textsuperscript{82} Id.
\textsuperscript{83} See generally Woodcock, supra note 30 (providing the FDA’s response to Public Citizen’s petition).
\textsuperscript{84} Id. at 1.
\textsuperscript{85} Id.
\textsuperscript{86} Id.
behind its European counterpart. Like the Summary of Product Characteristics accompanying every EPAR, the FDA’s new BTX-A labeling requirements include a strengthened “Warnings and Precautions” section that provides a stream-lined advisory regarding the spread of botulinum toxin effects beyond the site of injection. The FDA-required physician-distributed Medication Guides mimic the “Package Leaflet: Information for the User” pamphlets accompanying botulinum toxin products distributed in the EU. Both publications are “additional method[s] of communicating the signs and symptoms of the spread of botulinum toxin effects” and “can help ensure that the patient or caregiver is aware of and can self-monitor for serious risks.” Finally, the FDA-mandated “Dear Health Care Professional” letters—considered a minimum component of the FDA’s REMS communication program—are functionally similar to the “Dear Doctor Letters” required by regulatory agencies in the United Kingdom and Germany.

The FDA’s bolstered warning protocol may raise public awareness of the health risks posed by botulinum toxins. Nevertheless, it is unclear whether this protocol will reduce the number of serious AEs linked to BTX-A. Despite reports by mainstream media of BTX-A related deaths, the number of Botox injections performed in the United States rose by eight percent in 2008. This statistic offers compelling

87 See Pub. Citizen Health Res. Group, supra note 4. See generally Woodcock, supra note 30 (outlining the FDA’s improved warning protocol vis-à-vis botulinum toxins).
89 See EMEA, BTX-B SPC, supra note 88; Woodcock, supra note 30.
90 Woodcock, supra note 30, at 17; see EMEA, BTX-B SPC, supra note 88, at 26–28.
92 See Pub. Citizen Health Res. Group, supra note 4 (concluding that “failure to immediately [implement the strengthened warning protocol] is likely to result in more preventable serious adverse reactions and deaths from [botulinum toxin] products”).
94 Id.; see, e.g., Gardiner Harris, Group Seeks New Warning About Botox, N.Y. TIMES, Jan. 25, 2008, at A19.
evidence that the U.S. Botox market may be unwilling to part with the drug’s wrinkle-reducing effects.\footnote{95}{See ASPS, supra note 93, at 5.}

For a stalwart population of U.S. patients receiving Botox injections, a heightened warning protocol alone may not provide a practical strategy for minimizing the incidence of complications.\footnote{96}{See id.} Although the new warning protocol obligates BTX-A manufacturers to provide patients with a clearer list of complications caused by the distant spread of the toxin, the FDA has not required manufacturers to educate patients or caregivers about why distant spread occurs or ways to prevent it.\footnote{97}{Woodcock, supra note 30, at 14–15; see Pub. Citizen Health Res. Group, supra note 4.} FDA Director Janet Woodcock conceded this point in her response to Public Citizen’s petition: “[a]lthough we do not currently have recommendations for how to prevent these events, it is essential that the potential for distant spread of toxin effects be considered in assessing the risks and benefits of using botulinum toxin products.”\footnote{98}{Woodcock, supra note 30, at 14–15.}

In order to reduce the number of serious AEs linked to BTX-A, it may be necessary for officials to identify the cause of distant spread, and require manufacturers to educate caregivers and patients about ways to prevent it.\footnote{99}{See Coté et al., supra note 3, at 410.} The Coté Study made substantial contributions to the first step of this proposal.\footnote{100}{See id. at 410–11.} In that study, researchers concluded that distant spread of botulinum toxins frequently occurred when practitioners ignored fundamental precepts of BTX-A usage: proper handling, storage, dilution, and injection of BTX-A.\footnote{101}{See id.} If this conclusion is correct, minimum training requirements and additional guidelines with respect to BTX-A injection practices may be necessary in order to reduce the number of AEs related to BTX-A.\footnote{102}{Id. at 408 (concluding that “[t]he FDA does not have authority to control decisions made by qualified health care practitioners . . . or to otherwise regulate medical or surgical practice”).}

The power to regulate medical practices, however, falls squarely outside of the FDA’s authority.\footnote{103}{Id. at 410–11.} In the United States, the FDA’s drug approval power is governed by the Food, Drug, and Cosmetic Act.\footnote{104}{21 U.S.C. § 355 (2006); Rebecca Dresser & Joel Frader, Off-Label Prescribing: A Call for Heightened Professional and Government Oversight, 37 J. L. Med. & Ethics 476, 477 (2009) (citing R.A. Merrill, The Architecture of Government Regulation of Medical Products, 82 Va. L. Rev. 1755 (1996)).}
Once the FDA approves a drug for a particular use, it issues a “specific label [that] includes information about approved indications for product use, as well as the approved dosage, method of administration and patient population.”\(^{105}\) Nevertheless, “[o]nce a drug . . . has been approved or cleared . . . health-care professionals may lawfully use or prescribe that product for uses or treatment regimens that are not included in the product’s approved labeling.”\(^{106}\) The FDA’s refusal to monitor and restrict such “off-label” uses has been interpreted by the U.S. Supreme Court as “a necessary corollary of the FDA’s mission to regulate [medicine] without directly interfering with the practice of medicine.”\(^{107}\)

In contrast, states retain broad latitude to define and regulate the practice of medicine.\(^{108}\) Many states have medical boards that are responsible for overseeing medical practices, and are authorized to promulgate rules, license practitioners and conduct disciplinary proceedings.\(^{109}\) Despite this fact, states have similarly struggled to arrive at an adequate solution to the problem of improper BTX-A medical practices.\(^{110}\)

Physicians representing national boards of plastic surgeons and dermatologists have disagreed over what training physicians should be required to undergo in order to perform minimally invasive cosmetic

\(^{105}\) Dresser & Frader, supra note 104, at 477.

\(^{106}\) Food and Drug Admin., Good Reprint Practices for the Distribution of Medical Journal Articles and Medical or Scientific Reference Publications on Unapproved New Uses of Approved Drugs and Approved or Cleared Medical Devices 3 (Jan. 2009), available at http://www.fda.gov/OHRMS/DOCKETS/98fr/FDA-2008-D-0053-gdl.pdf; see also 21 U.S.C. § 396 (2006) (providing that the FDCA shall not be interpreted “as limiting or interfering with the authority of a health care practitioner to prescribe or administer any legally marketed device to a patient for any condition or disease within a legitimate health care practitioner-patient relationship”).


\(^{108}\) See 243 Mass. Code Regs. 2.01 (2009) (defining the practice of medicine as the “maintenance of human health by the prevention, alleviation, or cure of disease [through] . . . diagnosis, treatment, use of instruments or other devices, or the prescription or administration of drugs for the relief of diseases or adverse physical or mental conditions”). Other states, however, have opted not to provide a statutory definition of medical practice. See, e.g., Johnson v. Missouri, 58 S.W.3d 496, 499 (Mo. 2001) (holding that “the phrase ‘the practice of medicine,’ is not legislatively defined [in Missouri], but has been construed by the courts to include the diagnosis and treatment of the sick”).


Procedures such as Botox injections.\textsuperscript{111} State medical boards, however, have grappled with an even more basic issue: whether licensed non-physician practitioners, such as nurses and physicians assistants, should be allowed to perform Botox injections.\textsuperscript{112} Among those states that do permit licensed non-physician practitioners to perform Botox injections, there is wide disagreement about the level of oversight that must be invested by supervising physicians.\textsuperscript{113} In other states, there remains a lingering debate about whether unlicensed non-physician practitioners, such as medical assistants, should be allowed to administer Botox.\textsuperscript{114}

**Conclusion**

Justinus Kerner first warned that harnessing the benefits of botulinum toxins would require future practitioners to overcome the inherent difficulties of handling the toxins in a clinical setting. Kerner’s prognostic commentary from over a century ago offers surprising insight into a dilemma that currently grips the cosmetic medicine industry.

The FDA’s strengthened labeling requirements and Risk Evaluation and Mitigation Strategy, which mirrors the European Medicines Agen-

\textsuperscript{111} See generally Matthew C. Camp, Mapping the Future of Plastic Surgery: Demographic and Geographic Analysis of Providers of Cosmetic Services in the Greater Los Angeles Area, Presentation Before the 88th Annual Meeting of the Am. Ass’n of Plastic Surgeons 1, 14 (March 23, 2009) (unpublished monograph, on file with the Am. Ass’n of Plastic Surgeons) (concluding that consumers have sought minimally invasive cosmetic procedures from practitioners with a more limited skill set than surgeons, in part because such procedures are not legally required to be performed by plastic surgeons).

\textsuperscript{112} See, e.g., Med. Bd. of Cal., supra note 9, at 1 (providing that “[p]hysicians . . . may inject Botox, or they may direct registered nurses, licensed vocational nurses, or physician assistants to perform the injection under their supervision”).

\textsuperscript{113} See MBRHA Memo, supra note 9. The Missouri Board of Registration for the Healing Arts recommends “direct supervision,” entailing that the supervising physician is located in the same facility as the practitioner administering BTX-A. Id. The Board only requires “indirect supervision,” meaning that the physician is located within twenty miles or thirty minutes of the treatment facility. Id. In contrast, the Medical Board of California only requires supervising physicians to be “immediately available by electronic communications.” See Memoranda from the Med. Bd. of Cal., Supervision of Physicians Assistants (May 18, 2008), available at http://www.pac.ca.gov/forms_pubs/sup_of_pa.pdf.

\textsuperscript{114} See Harasim, supra note 110, at B1. In September 2009, the Nevada Medical Board promulgated a rule that would have prevented medical assistants from performing shots of any kind, including Botox injections. Id. As an effect of that rule, medical assistants were temporarily prohibited from administering influenza vaccinations, including vaccinations for the H1N1 virus. See Edward Vogel, Nevada Medical Board Director Ling Resigns, LAS VEGAS Rev.-J., Oct. 10, 2009, at B1. After a district judge granted a temporary injunction blocking that rule, the Board overturned its earlier decision, prompting the Director of the Medical Board to resign. See Michael Blasky, Judge Blocks Rules for Medical Assistants, LAS VEGAS Rev.-J., Sept. 30, 2009, at A1.
cy’s European Public Assessment Report system, represents a positive step toward raising public awareness of the health risks related to botulinum toxins. Nonetheless, for a U.S. cosmetic medicine market that appears unwilling to part with the aesthetic benefits offered by products such as Botox, it is doubtful that this improved protocol, *tout court*, will reduce the number of serious adverse events linked to BTX-A.

Following Kerner’s advice, a reduction in the number of adverse events requires that practitioners surmount the dangers attendant to clinical BTX-A use. As the Coté Study suggests, this means practitioners must follow well-established precepts of BTX-A use, including proper handling, storage, dilution, and injection. Although regulatory action to that effect falls outside of the FDA’s authority, it remains available to the states and their respective medical boards.
“WHERE IS MY VOTE?”: DEMOCRATIZING IRANIAN ELECTION LAW THROUGH INTERNATIONAL LEGAL RECOURSE

TANYA OTSUKA

Abstract: In 2009, massive demonstrations ensued in response to the allegedly fraudulent reelection of Iranian president Mahmoud Ahmadinejad. The Iranian government met these protests with violence, imprisonment, and death. Yet, given the Iranian government’s structure and election law, the ability to resolve election disputes through domestic legal means is virtually non-existent. Many provisions of Iranian election law are democratically flawed, even though Iran is a party to numerous international agreements requiring free and fair elections. This Note examines the availability of international legal recourse for the provisions of Iran’s election law that fail to live up to these standards. The Note suggests that the international community apply multi-lateral political pressure to encourage Iranian election reform.

Introduction

As thousands of Iranians took to the streets, the world watched as a nation experienced its largest protest since the 1979 Islamic Revolution.1 Iran’s 2009 presidential election, a contest primarily between two leading candidates, incumbent Mahmoud Ahmadinejad and reformist candidate Mir Hossein Mousavi, illustrated the dichotomy between traditional, conservative Iranians and an invigorated wave of progressive, reform-oriented voters.2 After Iran’s Interior Ministry announced Ahmadinejad the winner, Iranians discontent with the election outcome participated in numerous demonstrations disputing an allegedly fraudulent election that did not represent the true voice of the people.3 For the protesters,

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3 See id.
the phrase, “Where is my vote?,” became the battle cry of the movement.4

Following his reelection, Ahmadinejad and the Iranian government initiated violent efforts to quell protests.5 This led to hundreds of injuries and arrests, prison rape and torture, and even deaths.6 Ahmadinejad demanded that opposition leaders be tried for their actions, exemplifying the government’s harsh line against peaceful protest.7

The Iranian government’s actions against peaceful protesters clearly violate the International Covenant on Civil and Political Rights (ICCPR) to which Iran is a party.8 The extent to which Iran’s election laws violate the ICCPR, however, is less than clear. President Ahmadinejad celebrated his reelection as “glorious and fully democratic.”9 Yet given Iran’s uniquely structured government, claiming to be both a theocracy and a democracy, its election laws and the role of the Guardian Council also reflect this often contradictory theme.10

Part I of this Note provides a synopsis of some of the unique features of the Islamic Republic’s government relating to elections. Part II discusses the extent to which Iran’s presidential election law conforms to the ICCPR. Part III analyzes the availability of international legal recourse for provisions that do not comply with the ICCPR, specifically through United Nations (U.N.) institutional and multilateral mechanisms. Although problems of enforceability abound, there should ultimately be some organized international effort to influence domestic transformation of undemocratic elections without infringing on state sovereignty.

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4 See Nazila Fathi, A Recount Offer Fails to Silence Protests in Iran, N.Y. TIMES, June 17, 2009, at A1.
5 See Erdbrink, supra note 2.
7 Id.
I. BACKGROUND

A. Unique Features of the Iranian Government

In understanding the democratic underpinnings of Iranian election law, it is necessary to briefly discuss some of the unique mechanisms of Iranian government. As a theocratic democracy, or self-proclaimed “Islamic Republic,” the democratic aspects of Iranian government are intertwined with, and often trumped by, Islamic law. First, sovereignty is sanctioned by God and delegated to the Supreme Leader, an Islamic cleric who has absolute power in determining whether legislation and political actions conform to Islam. In 1989, the Assembly of Experts, a body of clerics elected by the people and charged with monitoring the Supreme Leader, appointed Iran’s current Supreme Leader, Ayatollah Ali Khamenei. The Supreme Leader is the highest-ranking political and religious official in the government. With much more power and influence than the president or Parliament, he authorizes domestic and foreign policy, serves as head of the military, has broad appointment power, and has the sole power to declare war.

Second, the Iranian Constitution mandates another powerful institution that assures laws are compatible with Islam. The Guardian Council, composed of six clerics and six lawyers appointed by the Supreme Leader and the judiciary, has the power to interpret the constitution, veto parliamentary resolutions, and supervise presidential and parliamentary elections. For example, the Guardian Council must approve all prospective presidential candidates before they are allowed to run for office, and election results are not official until the Guardian Council certifies them.

12 Bouroumand & Bouroumand, supra note 10, at 132–33.
13 Id.
15 See id.
16 See id.
19 Bouroumand & Bouroumand, supra note 10, at 133.
Third, the president’s role in the Iranian government is executive in nature, but his powers extend only to those not reserved for the Supreme Leader.\textsuperscript{20} He also shares executive power with the Council of Ministers, a cabinet selected by the president and confirmed by Parliament.\textsuperscript{21} While the president’s actual political power vis-à-vis other institutional bodies is limited, he does serve as the liaison between each branch of government.\textsuperscript{22} The president manages Iran’s economic policy and plays some role in foreign policy and national security, though his actions and political decisions are ultimately subject to the Supreme Leader’s approval.\textsuperscript{23}

\textbf{B. Electing the President}

The Guardian Council plays an extremely important role in the election process.\textsuperscript{24} The constitution requires the Guardian Council to supervise national elections and to approve all prospective candidates for president.\textsuperscript{25} According to the constitution, presidential candidates must not only be of Iranian origin and nationality, but must also meet certain religious and moral standards.\textsuperscript{26} In many elections, this greatly curtails the number of people who may actually run as official candidates for the office.\textsuperscript{27} For example, hundreds of potential candidates may register, but the Guardian Council may choose to select far fewer for the final slate.\textsuperscript{28}

In order to vote, Iranians must present their national identifications, or \textit{shenasnameh}, at any polling location in the country.\textsuperscript{29} Since there is no national electoral registry, electoral officers stamp voters’ national identifications with an ink seal, certifying that the voters have not already voted in the current election.\textsuperscript{30} Ballots have a detachable slip that is removed before a voter enters the voting booth.\textsuperscript{31} The voter

\textsuperscript{20} Schirazi, \textit{supra} note 18, at 16.
\textsuperscript{21} See Hoch, \textit{supra} note 14.
\textsuperscript{22} Schirazi, \textit{supra} note 18, at 16.
\textsuperscript{24} Bouroumand & Bouroumand, \textit{supra} note 10, at 133.
\textsuperscript{25} Qanuni Assassi Jumhuri’i Isla’mai Iran arts. 99, 118; Bouroumand & Bouroumand, \textit{supra} note 10, at 133.
\textsuperscript{26} Qanuni Assassi Jumhuri’i Isla’mai Iran art. 115.
\textsuperscript{28} See id.
\textsuperscript{29} See id.
\textsuperscript{30} See id.
\textsuperscript{31} See id.
manually writes the name of his desired candidate and deposits the remaining portion of the ballot into the ballot box. 32 Once the Interior Ministry, charged with overseeing election procedures, 33 counts the ballots and announces the results, the Guardian Council certifies the election. 34 Finally, the Supreme Leader officially declares the winning candidate by issuing a presidential decree. 35 This is an important provision to note, especially in the 2009 election. 36 Once the Supreme Leader declares the winner, protesting the results is an affront not only to the election itself, but also to the authority of the Supreme Leader. 37

These voting procedures provide the most opportunity for fraud. 38 The speed with which officials counted the ballots in the 2009 election is a strong indicator of foul play, but there is no hard evidence of actual fraud. 39 At each polling station, electoral officers count and record votes on a form approved by candidate representatives, the Interior Ministry, and the Guardian Council, though the information on the forms is kept secret. 40 The Interior Ministry then compiles these forms and reports the final results. 41 In the 2009 election, however, government officials counted half of the over forty million hand-written paper ballots within three hours of the polls closing, an extremely unrealistic feat. 42

Election fraud is not a problem specific to Iran; even highly democratized countries like the United States suffer from charges of election fraud. 43 Nevertheless, what is especially problematic about the 2009 Iranian presidential election is the relation between the inability to contest fraudulent results and the anti-democratic nature of the election struc-

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32 See id.
33 Erdbrink, supra note 2.
34 Bouroumand & Bouroumand, supra note 10, at 133.
37 See id.
39 Id.
40 Id.
41 Id.
42 Id.
ture. Multilateral institutions such as the United Nations have attempted to establish standards for democratic elections through the adoption of Article 21 of the Universal Declaration of Human Rights (UDHR). Similarly, Article 25 of the ICCPR broadly calls for the will of a nation’s people to be expressed through universal and equal suffrage. While it may be difficult to enforce these definitions, they provide a framework for analyzing the democratic weight of Iranian election law. As a U.N. member nation and signatory to the ICCPR, Iran is obligated to abide by the provisions governing free and fair democratic elections.

II. Discussion

A. Criteria for Free and Fair Elections

Article 25 of the ICCPR establishes the right to free and fair elections, stating that:

Every citizen shall have the right and the opportunity . . . to take part in the conduct of public affairs, directly or through freely chosen representatives; to vote and to be elected at genuine periodic elections which shall be by universal and equal suffrage and shall be held by secret ballot, guaranteeing the free expression of the will of the electors; to have access, on general terms of equality, to public service in his country.

These principles are specifically reaffirmed and endorsed by the Inter-Parliamentary Union’s (IPU) Declaration on Criteria for Free and Fair Elections (Election Criteria), to which Iran is also a signatory. Though the IPU mainly focuses on maintaining relationships between parliamentary governments, it provides an in-depth framework by which member nations should abide in any election.

44 See Shirin Ebadi, Keynote Address: Islam, Human Rights, and Iran, 23 Emory Int’l L. Rev. 13, 19 (2009); Kar, supra note 11, at 161.
47 See U.N. Charter art. 2.
48 See ICCPR, supra note 46, art. 25.
This framework expands on the general election rights under the UDHR, explicitly stating the requirements for an election to be free and fair.\textsuperscript{51} One important provision entitles voters the right to equally weighted votes, which is particularly relevant in cases of election fraud.\textsuperscript{52} The Election Criteria also include the right to an equal opportunity to run for political office.\textsuperscript{53} Moreover, individuals or political parties whose candidacy rights are restricted “shall be entitled to appeal to a jurisdiction competent to review such decisions and to correct errors promptly and effectively.”\textsuperscript{54}

The IPU also sets forth the rights and responsibilities of states in running free and fair elections.\textsuperscript{55} It advises states to establish election frameworks in accordance with their national constitutions, but also “in accordance with their obligations under international law.”\textsuperscript{56} National governments should enact measures reflecting impartial and transparent election systems, such as monitoring ballot counting and preventing fraud.\textsuperscript{57} Particularly significant in the context of Iranian elections, the IPU urges states to “ensure that violations of human rights and complaints relating to the electoral process are determined promptly within the timeframe of the electoral process and effectively by an independent and impartial authority, such as an electoral commission or the courts.”\textsuperscript{58}

B. Conformity to International Law and Democratic Norms

The fact that Iran has an established election system is important, especially given the theocratic elements of its government.\textsuperscript{59} Yet it is unclear that all of its election provisions meet even the broadly defined standards set forth in the ICCPR.\textsuperscript{60} Some of these provisions, such as requirements that candidates are of Iranian nationality and are elected by absolute majority, are uncontroversial and generally comply with normative democratic principles.\textsuperscript{61} The Guardian Council’s role in the

\textsuperscript{52} See id.
\textsuperscript{53} See id.
\textsuperscript{54} Id.
\textsuperscript{55} Id.
\textsuperscript{56} Id.
\textsuperscript{57} See Inter-Parliamentary Union, supra note 51.
\textsuperscript{58} See id.
\textsuperscript{59} See Schirazi, supra note 18, at 14.
\textsuperscript{60} See Election Process, supra note 49.
\textsuperscript{61} See GOODWIN-GILL, supra note 50, at 54.
administration of elections, however, is one of the most troubling aspects of Iranian election law.\footnote{See Election Process, supra note 49.}

Although the Guardian Council supervises elections in an administrative context, its role in approving all prospective candidates conflicts with democratic norms.\footnote{See id.} First, the Guardian Council excludes candidates because of certain political ideologies, especially if they drastically conflict with the ideology of the Guardian Council or election officials.\footnote{See id.} Because the Islamic Republic bans independent political parties, the Interior Ministry disqualifies candidates on this basis even before they reach the Guardian Council.\footnote{Bouroumand & Bouroumand, supra note 10, at 134.} For example, the Interior Ministry automatically disqualifies candidates who have participated in or sympathized with nationalist, democrat, or socialist parties.\footnote{Id.}

Second, candidates must meet a religious and moral standard, which the Guardian Council decides and subjectively administers.\footnote{See id.} Even after the Ministry of Information investigates a candidate’s political “legitimacy,” the Guardian Council evaluates his beliefs and behavior.\footnote{See id.} For instance, it determines whether women in his family wear a chador, whether the candidate attends religious services, whether he participates in events supporting the regime, and whether he has criticized the government or the Supreme Leader.\footnote{Id.}

During this process, the Guardian Council is not required to justify its decisions and is accountable only to the Supreme Leader.\footnote{Id.} Candidates and other citizens must appeal to the Guardian Council itself if they are dissatisfied with the final list of candidates or the results of the election.\footnote{Bouroumand & Bouroumand, supra note 10, at 134.} This lack of accountability makes it highly unlikely that an appeal will be successful, given the lack of oversight by other governmental bodies, such as the judiciary or Parliament.\footnote{See Shoamanesh, supra note 8.} In 2009 for example, Mousavi, the favored but losing candidate, disputed the results of the election and called for its annulment.\footnote{Id.} The government refused to
invalidate the election, and after a speedy partial recount the Guardian Council reaffirmed its initial decision.74

Thus, the legal provisions governing the Guardian Council’s role violate the principle that citizens have an “equal opportunity to become a candidate for election” established in the IPU’s Election Criteria.75 Although Iranian citizenship requirements can be applied objectively, the religious and moral fitness requirement leaves enormous discretion to the unelected Guardian Council in essentially cherry-picking candidates to its own liking.76 As an ideological barrier to political participation, this criterion violates not only Article 25 of the ICCPR, but also Article 19, which guarantees freedom of expression.77 This outcome has anti-democratic consequences for the people of Iran as well as for the candidates themselves.78 Because the group of candidates for which citizens may vote is pre-selected by the Guardian Council, Iranians are deprived of the full ability to freely choose their representatives.79 Practically, of course, a State may narrow down its list of candidates to make the final choice more feasible, or restrict candidates by age or residence.80 The fact that the candidate selection process is run by an unelected body, however, detracts from the election as a full expression of the will of the people.81

Rather than compare a nation’s election laws to a broad international normative standard, some international election specialists contend that “evaluations should be made within the historical and political context of the country in question.”82 The Iranian people played a critical role in the creation of the Islamic Republic through the 1979 Revolution, after a long history of thwarted attempts at democracy because of external interference and dictatorial rule.83 In this vein, therefore, the current government and its laws must at least to some extent be taken seriously.84

75 See Inter-Parliamentary Union, supra note 51.
76 See Goodwin-Gill, supra note 50, at 55.
77 See id.
78 See Ebadi, supra note 44, at 19.
79 See ICCPR, supra note 46, art. 25.
80 See Goodwin-Gill, supra note 50, at 54–55.
81 See ICCPR, supra note 46, art. 25; Bouroumand & Bouroumand, supra note 10, at 134.
82 Álvarez et al., supra note 45, at 2.
83 See Schirazi, supra note 18, at 291–92.
84 Álvarez et al., supra note 45, at 2.
In similar fashion to the 1979 uprising, the Iranian people demanded action from their government after the 2009 presidential election. The allegations of an undemocratic presidential election initially came from the Iranian people, rather than from an external source. More importantly, because of the Guardian Council’s dominant role in elections, Iranians disconcerted with the results, fraudulent or not, have no de facto legal recourse. The Guardian Council, rather than the courts, reviews all election challenges. Appealing to the very government body that approves presidential candidates and refuses to disclose official ballot reports is effectively meaningless. While there are valid concerns about the role of international law in disputed domestic elections, there must be some international support for the citizens of a government that belongs to numerous international treaties but fails to abide by them.

III. Analysis

A more democratic, appealable election structure should ultimately be the product of internal reform. There are, however, opportunities for the international community to significantly impact Iranian domestic legal change without drastically interfering with sovereign authority. Disputes with Iran over nuclear proliferation and security concerns make the international community more cautious in dealing with Iran. Acting in a way that reaffirms a commitment to fair elections without delving too deeply into Iran’s internal affairs is particularly important.

85 See Erdbrink, supra note 2.
86 See id.
87 See Bouroumand & Bouroumand, supra note 10, at 134.
88 See id.
89 See id.
90 See Shoamanesh, supra note 8.
94 See Goodwin-Gill, supra note 50, at 27.
A. International Political Pressure: An Analogy to Human Rights Advocacy

In light of the Iranian government’s recalcitrance vis-à-vis its international legal obligations, the international community should exert political pressure on Iran to reform its election laws. Although political pressure may not immediately convince the government to amend its election laws or administer elections more carefully, it may at minimum force the government to engage in dialogue on the subject of its election laws. In reality, the government does alter its behavior in response to external pressure, even as it announces its absolute resistance to international demands. This tactic is used to help release political prisoners and often has positive results. As Iranian human rights lawyer and Nobel Laureate Shirin Ebadi articulates:

On the surface, the Iranian government shows that it will not take action based on the concerns raised by the international community. But the truth is different. For 15 years . . . experience has shown me that when the world voices its concern over the arrest of a political prisoner, it puts a lot of pressure on the government. It has to react in some way.

Haleh Esfandiari’s release from Iran’s Evin Prison demonstrates that broad international support can be a successful means of influencing the Iranian government. In 2006, Iranian authorities arrested Esfandiari, Director of the Woodrow Wilson International Center for Scholars’ Middle East Program, for alleged crimes against Iranian national security. Esfandiari’s release came after multilateral international appeals to Iranian government officials. For example, Wilson Center President and former U.S. Congressman Lee H. Hamilton successfully appealed to Supreme Leader Khamenei after failed attempts

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95 See Shoamanesh, supra note 8.
96 See Ebadi, supra note 78, at 22.
97 Id.
98 See Maziar Bahari, Four Months Inside an Iranian Prison, Newsweek, Nov. 30, 2009, at 41 (explaining that international pressure to free Bahari from prison influenced his eventual release); Ebadi, supra note 78, at 22; cf. Robin Wright, Iran Frees U.S. Scholar from Prison, Wash. Post., Aug. 22, 2007, at A10 (stating that American social scientist Kian Tajbakhsh and others are still detained for alleged roles in postelection protests).
99 See Ebadi, supra note 78, at 22.
100 See HALEH ESFANDIARI, MY PRISON, MY HOME: ONE WOMAN’S STORY OF CAPTIVITY IN IRAN 205–07 (2009) (explaining that international efforts hastened her release from prison); Wright, supra note 98.
101 Wright, supra note 98.
102 Id.
to contact other Iranian leaders. Additionally, former U.N. Secretary General Kofi Annan, European Union foreign policy leader Javier Solana, and diplomats from more than 20 governments appealed to Iranian officials and the foreign ministry. By Esfandiari’s own account, she knew her release was imminent when her jailer informed her that then-Senators Barack Obama and Hillary Clinton issued statements about her detainment.

International criticism of the Iranian government’s civil rights record will also influence the level of its domestic support. The current regime is noticeably concerned with its image, exemplified by its attempt to deflect attention from the election. For this reason, the international community must be persistent in pressuring the Iranian government to abide by ICCPR election standards. Shortly after the 2009 election, for example, President Ahmadinejad repeated his infamous anti-Semitic statements. An outraged international community castigated him for his insensitive and blatantly incorrect comments. Nonetheless, Ahmadinejad succeeded in avoiding the hard questions about the election and subsequent rights violations in Iran at the U.N. General Assembly. International criticism against Iran for its disregard of the ICCPR and other treaties is especially important at a time when citizens are defiant of the government’s rule. This timely pressure would demonstrate to Iranians the international community’s support for and commitment to fair and democratic elections, not just its reactions to Ahmadinejad’s “provocative rhetoric.”

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103 Id.
104 Id.
105 Id.
106 Esfandiari, supra note 100, at 152–54.
108 See id.
109 See Shoamanesh, supra note 8.
110 Parsi, supra note 106.
111 See Mark Landler & Nazila Fathi, President of Iran Defends His Legitimacy, N.Y. TIMES, Sept. 24, 2009, at A14.
112 See Parsi, supra note 106.
113 Id.
B. Internal Influence Through External Means

1. General Assembly Resolution and Multilateral Support

Political pressure should be applied primarily in the form of a U.N. General Assembly resolution because there is a legal basis for implementing provisions of the U.N. Charter and the ICCPR.114 The United Nations can justify its position with legally binding documents that secure the formal political rights of citizens, rather than merely engaging in arbitrary criticism.115 Similarly, the United Nations has a specific division that assists in organizing and observing elections and is equipped to advise the General Assembly.116 The Electoral Assistance Division is a structured election unit with well-established rules and guidelines for election laws.117 From 1989 to 2005, the Electoral Assistance Division provided electoral assistance in ninety-six countries with expertise in various areas, such as election administration and electoral laws.118

A General Assembly resolution reaffirming the election rights set forth in the ICCPR and requesting that Iran provide a meaningful election appeals process is also preferable to a Security Council resolution.119 The General Assembly’s duties and powers are more closely aligned with the maintenance of civil and political rights, whereas the Security Council’s role is more focused on maintaining peace and security.120 More importantly, it is unlikely that China or Russia will agree to a resolution.121 China, for example, objects to U.N. election monitoring in a sovereign state as a violation of Article 2(7) of the U.N. Charter.122 Iran may also reduce a Security Council resolution to a threat from the United States alone, defeating the purpose of organized international action.123 A General Assembly resolution, however, allows political pressure to come from a more multilateral front, composed of representa-

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114 See U.N. Charter arts. 11, 13; ICCPR, supra note 46, art. 25.
116 Pierre Cornillon, Foreword to GOODWIN-GILL, supra note 50, at vii.
118 See U.N. Electoral Assistance Div., supra note 117.
120 See U.N. Charter arts. 12, 13, 26.
121 See Is the Dream Already Over?: The Crisis in Iran, ECONOMIST, June 27, 2009, at 54–55 [hereinafter Dream].
122 See GOODWIN-GILL, supra note 50, at 18.
123 See Shoamanesh, supra note 8.
tives from all 192 member states.\textsuperscript{124} It is also more likely to pass, given the prior passage of General Assembly resolutions reaffirming the value of free and fair elections and proscribing electoral assistance.\textsuperscript{125}

Individual nations should also engage in continuous political pressure alongside a General Assembly resolution, especially as the international focus drifts away from the elections to Iran’s nuclear program.\textsuperscript{126} As the human rights examples illustrate, political pressure is most effective when invoked continuously.\textsuperscript{127} Pressure from countries with substantial diplomatic or economic ties with Iran, such as France, Germany, Italy, and Brazil, may also be particularly effective.\textsuperscript{128} Shirin Ebadi has suggested that the European Union disengage in political dialogue with Iran “until the violence stops and fresh elections are held.”\textsuperscript{129} Yet, in light of global concerns over the development of Iran’s nuclear capabilities, many nations will view cutting off communication with Iran as an impractical strategy.\textsuperscript{130} A more moderate approach would be to include discussion about the election in negotiations with Iran regarding its nuclear program.\textsuperscript{131} Foreign diplomats should pressure Iran to answer its citizens’ calls for democratic elections while still maintaining a firm hand on the nuclear energy issue.\textsuperscript{132}

To be clear, this Note does not argue that the United Nations or other countries should demand a drastic government restructuring in order to make Iranian election laws more democratic. Elections are arguably “matters which are essentially within the domestic jurisdiction” of the State, in which the U.N. Charter prohibits international interference.\textsuperscript{133} The United Nations has recognized that the international community is not to evaluate a nation’s compliance with international

\begin{itemize}
\item \textsuperscript{126} See Basu et al., supra note 93.
\item \textsuperscript{127} See Ebadi, supra note 78, at 22; Parsi, supra note 106; Wright, supra note 98.
\item \textsuperscript{128} See Shoamanesh, supra note 8.
\item \textsuperscript{129} See Dream, supra note 121, at 54–55.
\item \textsuperscript{130} See Basu et al., supra note 93.
\item \textsuperscript{131} See generally id.; Hamid Dabashi, Commentary: Huge Risks in Iran Sanctions, CNN, Aug. 5, 2009, http://www.cnn.com/2009/WORLD/meast/08/05/dabashi.sanctions.iran/index.html (noting that the international community has refocused its attention to Iran’s nuclear program and away from the legitimacy of its regime, even though Iranians who view the election as invalid nevertheless support Iran’s pursuit of a peaceful nuclear program); Dream, supra note 121, at 54–55.
\item \textsuperscript{132} See Dabashi, supra note 131; Wright, supra note 98.
\item \textsuperscript{133} See U.N. Charter art. 2(7).
\end{itemize}
norms based on its choice to adopt a certain type of election system or political structure. But Iran has ceded some of its sovereignty by voluntarily becoming a member of the United Nations and party to the ICCPR. When election procedures clearly limit the will of the people in violation of the ICCPR, the United Nations is justified to respond within its legal bounds.

2. The Failure of Economic Sanctions

Economic sanctions are another means to achieve an international policy objective. While widely used and currently in place against Iran, imposing sanctions with regard to Iranian election laws would be unproductive. Economic sanctions have a sizably negative effect on Iranian citizens but little to no impact on the Iranian government’s policies. U.N. Security Council sanctions, for instance, largely affect the most economically and politically vulnerable members of society. As a result, sanctions become counterproductive, because the government uses the adverse impact on its citizens to bolster its own position against the international community. Furthermore, it would be impractical to issue sanctions based on a failure to comply with ICCPR and democratic standards for elections. Although there is legal precedent for the imposition of sanctions to encourage free and fair elections, such as the Security Council’s application of sanctions against Haiti in 1993, there are at least two problems associated with placing additional sanctions on Iran. First, as discussed above, it is unlikely China will agree to sanctions for what it per-

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135 See Shoamanesh, supra note 8.
138 Susman, supra note 9.
139 See Shoamanesh, supra note 8.
140 See id.
143 See Farrall, supra note 137, at 458–59; Goodwin-Gill, supra note 50, at 18.
144 Farrall, supra note 137, at 133–36, 326 (arguing that in addition to the general objective of sanctions as a means to maintain and restore international peace and security under Chapter VII of the U.N. Charter, sanctions are “fine-tuned” to include implicitly related objectives such as protecting human rights).
ceives as a domestic issue. Second, given Iran’s resistance to U.N. sanctions in the closely-scrutinized area of nuclear energy, it is doubtful that sanctions regarding domestic elections will have a stronger effect. Despite the 1737 sanction regime issued in 2006, Iran continued to build its nuclear program. Today, its nuclear capability remains a pressing and unresolved international issue.

C. Looking to the Future: Election Assistance and Support for Domestic Initiatives

At the request of a member state, the United Nations can organize, supervise, or verify elections, as accomplished in Namibia, Nicaragua, and Haiti. U.N. involvement of this magnitude is rare and requires a specific General Assembly mandate. Nevertheless, the United Nations may also support international observation and election assistance through analysis, advice, or training, which are more accepted levels of involvement. The current Iranian government will likely oppose U.N. election assistance, but in many ways it may be in Iran’s interest.

Considering the Iranian government’s diminished domestic support, it would be beneficial to the current regime to restore confidence in its citizens. As discussed, the government is furtively concerned that it lacks widespread domestic approval. In response to the protests, the government used force to squelch a potential uprising through the use of imprisonment, death sentences, and accusations of foreign-backed protests. The current regime has set the stage for defiance by its people, and even by a few leading clerics. Concerns loom that continuing in this direction will lead to negative consequences for the government. Inviting international bodies to evaluate the elections will

145 See Goodwin-Gill, supra note 50, at 18.
146 See Farrall, supra note 137, at 458–59.
147 Id. at 458.
148 See Basu et al., supra note 93.
149 Id.
150 Goodwin-Gill, supra note 50, at 17–18.
151 Id. at 18.
152 See id. at 18–19.
153 See Dream, supra note 121, at 54–55.
155 See Dream, supra note 121, at 54–55; Parsi, supra note 106.
156 Prosecute Opposition Leaders–Iranian President, supra note 6.
157 See The Iranian Question; The G8 Leaders Have Been Too Slow to Respond to the Crackdown by Tehran, TIMES (London), July 9, 2009, at 2.
158 See id.
legitimize the regime and the election system itself and potentially appease the opposition movement.\textsuperscript{159} If the government wants to remain in power, it cannot exclude its citizens from popular sovereignty to such a grave extent that they have no other option but to revolt.\textsuperscript{160}

Until there is a U.N. mechanism for individual citizens or other states to submit complaints or request election investigations, these requests must come from the Iranian government itself, an option it will likely reject.\textsuperscript{161} Another possibility, however, is for the international community to support any domestic initiatives established to modify Iranian election laws.\textsuperscript{162} Following the election, for example, many reformists called for initiatives to “make the Iranian political system transparent and respectful of the law.”\textsuperscript{163} If in the future Iranian citizens establish a grassroots campaign to amend election laws, the United Nations and international community should provide assistance.\textsuperscript{164}

**Conclusion**

Diplomacy with Iran is complex. This Note does not favor political pressure to reform election laws at the expense of other concerns. The international community can and should, however, pressure the Iranian government to address flaws in its election law, as it does in confronting Iran’s human rights violations and nuclear program. These issues are closely intertwined with the anti-democratic provisions of Iranian election law. A different election outcome could have resulted in a more open foreign policy to the benefit of both Iran and the international community.

Given the extreme power of Iran’s unelected leaders, especially the Supreme Leader, electing a president is one of the few opportunities for Iranians to participate in the political process. Regardless of whether the Iranian people are correct about a rigged election, their calls to create a more transparent election process should not be ignored.Demanding the ability to appeal election decisions to other branches, rather than to the Guardian Council, is duly justified under international and Iranian law.

By the same token, the Guardian Council’s influence over Parliament in passing new laws is strong, just as it is in other aspects of gov-

\textsuperscript{159} See Bouroumand & Bouroumand, supra note 10, at 142.
\textsuperscript{160} See id. at 136; Esfandiari, supra note 154; Kar, supra note 11, at 161.
\textsuperscript{161} See Goodwin-Gill, supra note 50, at 16–18; Shoamanesh, supra note 8.
\textsuperscript{162} See Shoamanesh, supra note 8.
\textsuperscript{163} See id.
\textsuperscript{164} See id.
ernment. Iranians who favor an election law structure reflecting democracy and transparency will meet steadfast resistance from the Guardian Council and current regime. Despite this likelihood, inaction is not the proper solution. Many Iranians have demonstrated their dissatisfaction with the status quo. In light of the hostile domestic political environment, Iranians will be better equipped to transform elections with the knowledge that they have international support behind them.
CARROT OR STICK?: THE BALANCE OF VALUES IN QUALIFIED INTERMEDIARY REFORM

STEVEN NATHANIEL ZANE*

Abstract: The qualified intermediary program allows foreign financial institutions to assume certain tax responsibilities ordinarily borne by U.S. withholding agents. The purpose of the program is to collect more foreign taxpayer information by creating a more direct link between the I.R.S. and recipients of foreign income payments. By accepting more responsibility, qualified intermediaries are provided numerous benefits that make business less costly. Nevertheless, the program has recently come under attack due to perceived abuse by wealthy U.S. citizens who use the system to evade income taxes. In response, the Obama Administration proposes numerous changes to the program, intended to strengthen it. But these changes fail to appreciate the balance of values at stake in reforming the qualified intermediary system. This Note argues that until more benign changes are made, the unique jurisdictional dilemma created by the U.S. international income tax system should not be solved by shifting from a “carrot” to a “stick” approach for foreign intermediaries.

Introduction

A country faces a host of important choices when it decides to collect revenue through taxation.1 The most obvious is the subject to be taxed: usually property, income, or consumption.2 The United States relies most heavily on income taxation, the largest single source of federal revenue.3 Additionally, unlike most other countries, the United States taxes income primarily based on citizenship rather than resi-

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2 See id.

Income paid to nonresident aliens from within the United States (U.S. source income) is also subject to taxation by the United States, and special “source rules” determine whether an item of income is U.S. source income. If the rules dictate that income is U.S. source, the payment will be taxed by the United States even if the recipient is neither a U.S. citizen nor a resident.

To enforce its income tax regime against nonresident aliens with U.S. source income, the United States requires tax to be withheld from the income payment (or “withholding tax”) along with information reporting on the foreign beneficial owner of the income. These requirements create a large amount of responsibility for those U.S. entities making income payments abroad, known as “withholding agents.” In 2000, the United States created a program to reduce the burden for withholding agents: the qualified intermediary (QI) program.

The QI program allows foreign financial institutions to enter into an agreement with the I.R.S. to assume some or all responsibilities of U.S. withholding agents. The program’s purpose is to strengthen enforcement of the U.S. withholding regime, but it has recently come under attack due to perceived abuse by wealthy U.S. taxpayers who have, somewhat ironically, used the system to hide income and thereby evade income tax. Recent proposals for strengthening the QI program in light of these perceived abuses have sparked intense debate among commentators in the tax community.

This Note addresses the Obama Administration’s recent proposals to strengthen the QI program, with an eye to the program’s original purpose. Part I explains the QI program within the context of the U.S. income tax system and presents the current problems facing the program. Part II focuses on the proposals for strengthening the program in light of its perceived failures and discusses the various responses to these

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4 U.N. Cтр. on Transnational Corps., International Income Taxation and Developing Countries 7, 9 (1988). In doing so, the United States asserts its tax jurisdiction on a world-wide basis. Id.
5 See id. at 3.
7 See U.N. Cтр. on Transnational Corps., supra note 4, at 3.
10 See Susan S. Morse, Qualified Intermediary or Bust?, 124 Tax Notes 471, 471 (2009).
11 See Morse & Shay, QI Status Act I, supra note 3, at 334.
12 See Dep’t of the Treasury, General Explanations of the Administration’s Fiscal Year 2010 Revenue Proposals 41 (2009).
proposals in the international tax community. Part III analyzes the competing values at stake in the debate discussed in Part II. As a result of this analysis, Part III suggests a more benign approach to QI reform that considers the economic uncertainty regarding the effects of the Administration’s proposals and questions whether the United States should be able to shift costs to foreign institutions when such costs are a direct result of the United States’ unique jurisdictional decisions.

I. Background

From the United States’ perspective, it is irrelevant that an income payment is made outside the United States as long as the payment recipient is a U.S. citizen. If income is paid to a nonresident alien rather than U.S. citizen, the United States will tax the payment in one of two ways depending on whether it is business income or investment income. If the income payment is “connected with United States business,” then it will be subject to a graduated tax rate as if the taxpayer were a U.S. citizen. If the income payment is not connected with U.S. business, it is generally taxed at a flat rate of 30%. In general, then, U.S. source income paid to foreign investors is taxed at a flat 30% rate. This rate may be reduced or eliminated pursuant to a tax treaty or an exemption under another section of the Internal Revenue Code. Further, if the beneficial owner of the income payment—the owner of the income for tax purposes—is in fact a U.S. citizen or resident rather than a nonresident alien, the 30% withholding tax does not apply.

15 See I.R.C. § 871(a)–(b) (2009).
16 See id. § 871(b). I.R.C. § 6012 requires foreign persons engaged in U.S. business to file a U.S. tax return. Id. § 6012.
17 See id. § 871(a) (2009). For the list of exceptions, see I.R.C. § 1441(c) (2009). The primary income payments subject to the 30% tax are “fixed or determinable annual or periodical gains, profits, and income” (FDAP income), including interest payments, dividend payments, and rent payments. See id. § 871(a)(1)(A).
18 See id. § 871(a)(1)(A).
19 See, e.g., id. § 871(h) (30% tax rate does not apply to portfolio interest earned by nonresident aliens); id. § 871(j) (30% tax rate does not apply to certain gambling winnings by nonresident alien persons); id. § 1441(c) (listing twelve exceptions to the general 30% withholding rate); Treas. Reg. § 1.1441–6(a) (as amended in 2003) (withholding tax rate may be reduced in accordance with an income tax treaty between the United States and the foreign country in which the nonresident alien resides).
21 See id. § 1.1441–1(b)(1). Income payments made to U.S. citizens abroad are subject to backup withholding, and a separate reporting system (form 1099 rather than form
U.S. source income payments to foreign persons thus present a unique jurisdictional dilemma.\textsuperscript{22} Although the United States claims tax jurisdiction over all U.S. source income paid abroad, collecting this tax requires more than mere assertion of jurisdiction.\textsuperscript{23} The United States’ solution is twofold: (1) to require a 30\% withholding tax on foreign income payments;\textsuperscript{24} and (2) to require information reporting on the beneficial owner.\textsuperscript{25} Both these requirements create liability for withholding agents, the U.S. entities making income payments abroad.\textsuperscript{26} The withholding agent is responsible for gathering information on the beneficial owner of the income payment and withholding accordingly.\textsuperscript{27} The withholding agent is liable for any tax it is required to withhold.\textsuperscript{28} Failure to obtain reliable documentation is no excuse.\textsuperscript{29}

A central information gathering function of the withholding agent is to determine whether the beneficial owner is a U.S. person or a foreign person.\textsuperscript{30} For foreign persons, the withholding agent must further determine whether the income payment is exempt from withholding or whether a reduced withholding rate applies.\textsuperscript{31} In the event a withholding agent cannot obtain reliable documentation providing beneficial owner information, a set of complicated legal presumptions ob-

\textsuperscript{22} Cf. Morse & Shay, \textit{QI Status Act I}, supra note 3, at 332 (stating that “[l]imitations on jurisdiction to enforce are the Achilles heel of any system for taxing international income”).


\textsuperscript{24} See I.R.C. § 1441(a) (2009).

\textsuperscript{25} See Treas. Reg. § 1.1441–1(b)(1) to (2) (as amended in 2003).

\textsuperscript{26} See id. The withholding agent’s function is literal: it acts as an \textit{agent} of the I.R.S. by withholding tax from income payments it makes abroad. \textit{See id.} § 1.1441–1(c)(7).

\textsuperscript{27} See id. § 1.1441–1(b)(1).

\textsuperscript{28} See I.R.C. § 1461.

\textsuperscript{29} See Treas. Reg. § 1.1441–1(b)(7) (as amended in 2003). Further, any willful failure to collect tax or willful attempt to evade tax by a withholding agent will result in penalties additional to the liability for the withholding tax. \textit{See I.R.C.} § 6672 (2009).

\textsuperscript{30} Treas. Reg. § 1.1441–1(d) to (e) (as amended in 2003). This function is central because a separate withholding system applies to presumed or known U.S. persons who fail to identify themselves as such. \textit{See Neuenhaus, supra note 21, at 913}.

\textsuperscript{31} See Morse & Shay, \textit{QI Status Act I}, supra note 3, at 333. For example, if the beneficial owner of a foreign income payment is in fact a U.S. citizen, the withholding agent must obtain reliable documentation to that effect and reduce or eliminate its withholding accordingly. \textit{See Treas. Reg.} § 1.1441–6(b)(1), (d). Similarly, if a nonresident alien is subject to a reduced tax rate due to a tax treaty or other exception, the withholding agent must obtain reliable documentation to that effect. \textit{See id.} § 1.1441–6(b).
tain.\textsuperscript{32} Clearly, this information gathering function creates a somewhat large burden for U.S. withholding agents.\textsuperscript{33} Yet the information reporting is essential to ensure that U.S. source income payments abroad do not evade U.S. tax jurisdiction.\textsuperscript{34}

In most cases income payments abroad will not be made directly to the beneficial owner of the income but rather to a foreign financial institution.\textsuperscript{35} This foreign intermediary accepts the payment on behalf of its account holder, whether the beneficial owner or some other intermediary.\textsuperscript{36} The foreign intermediary must provide a withholding certificate to the withholding agent through which the intermediary identifies itself as a foreign person and intermediary with respect to the income payment rather than the beneficial owner.\textsuperscript{37} A foreign intermediary is doubtless in a better position to collect beneficial owner information than is the U.S. withholding agent.\textsuperscript{38} Hence, the I.R.S. created the QI system in 2000 to encourage foreign intermediaries to assume withholding and information reporting responsibilities for U.S. withholding agents.\textsuperscript{39}

A QI is a foreign intermediary that has entered into an agreement with the I.R.S. to assume certain responsibilities normally imposed on withholding agents and to submit to external audits to ensure compli-

\textsuperscript{32} See Treas. Reg. § 1.1441–1(b)(3)(v). As a general matter, these presumptions direct the withholding agent to treat an income payment to an unknown beneficial owner as if made to a U.S. person and to withhold 31% of the payment, called backup withholding. See \textit{id.} § 1.1441–1(b)(3)(i), (iii); David Luntz, \textit{What Is Really Wrong with the QI Program and How It Should and Should Not Be Fixed}, 25 \textit{TAX MGMT’R REAL EST.} J. 43, 43 (2009).


\textsuperscript{34} See Morse & Shay, \textit{QI Status Act I}, supra note 3, at 332; \textit{see also} Greenaway, supra note 23, at 759–60 (reasoning that “jurisdiction without information is useless” and that “[t]he best tax enforcement tool is the information return”).

\textsuperscript{35} See generally Morse & Shay, \textit{QI Status Act I}, supra note 3, at 333 (describing how intermediaries act on behalf of beneficial owners in receiving income payments).

\textsuperscript{36} Treas. Reg. § 1.1441–1(c)(13).

\textsuperscript{37} \textit{Id.} § 1.1441–1(e)(3)(i). If the intermediary attaches a beneficial owner certificate to the withholding certificate, the withholding agent can treat income payments to the intermediary as being made to a foreign person. \textit{Id.} § 1.1441–1(e)(1)(ii)(A)(1); \textit{see Luntz, supra note 32, at 43. If a foreign intermediary does not furnish the withholding agent with any beneficial owner information, backup withholding may apply. See Morse, supra note 10, at 472.

\textsuperscript{38} See U.S. Gov’t Accountability Office, \textit{QI Program Provides Some Assurance That Taxes on Foreign Investors Are Withheld and Reported, but Can Be Improved} 12 (2007); Morse & Shay, \textit{QI Status Act II}, supra note 33, at 269.

\textsuperscript{39} See Morse, \textit{supra} note 10, at 471.
ance with this agreement. In exchange for its agreement to become a foreign agent of the I.R.S., the intermediary is provided special treatment. This treatment includes, most importantly, the ability to submit beneficial owner information in an aggregate rather than individual owner-by-owner basis. Information reporting in so-called “rate pools” provides intermediaries with two major benefits. First, “rate pools” are far more cost-efficient than reporting beneficial owner information on an individualized basis, eliminating some of the burden of information reporting. Second, providing information in the aggregate better preserves client confidentiality compared to information reporting on an individualized basis. These benefits are intended to provide a “market-oriented” incentive to foreign intermediaries to become QIs. From the perspective of the I.R.S., the more foreign intermediaries become QIs, the more beneficial owner information will actually be collected because the foreign intermediary is in the best position to collect such information. By transforming the role of non-U.S. financial institutions in the administration and enforcement of the U.S. withholding regime, the QI program is intended to improve U.S. enforcement of its withholding tax on income payments abroad.

A nonqualified intermediary (NQI) is simply a foreign intermediary that does not enter into a withholding agreement with the I.R.S. The NQI must still submit an intermediary withholding certificate to the withholding agent, but the responsibility for withholding and information reporting remains solely with the withholding agent. Unless the foreign intermediary has actual knowledge that a person for whom it collects income is a U.S. non-exempt recipient, the NQI is not re-

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40 See Treas. Reg. § 1.1441–1(e)(5)(i) to (iii) (as amended in 2003). The external audit is performed by the intermediary’s “approved auditor,” not by the I.R.S directly. See id. § 1.1441–1(e)(5)(iii)(B).
41 See id. § 1.1441–1(e)(5)(ii)(B).
42 See id. § 1.1441–1(e)(5)(iii)(B), (v)(C)(1).
43 See Morse & Shay, QI Status Act I, supra note 3, at 334.
45 Morse & Shay, QI Status Act II, supra note 33, at 267–68; Morse & Shay, QI Status Act I, supra note 3, at 334.
46 Morse & Shay, QI Status Act I, supra note 3, at 331.
47 See generally Morse & Shay, QI Status Act III, supra note 44; Morse & Shay, QI Status Act I, supra note 3, at 334.
48 See Morse & Shay, QI Status Act II, supra note 33, at 260–61.
50 See Morse & Shay, QI Status Act I, supra note 3, at 334.
quired to disclose any information regarding such persons. But because the NQI has not agreed to assume withholding and reporting responsibilities, it may not submit beneficial owner information in the aggregate. On one hand, this prohibition provides a disincentive to foreign intermediaries to remain nonqualified, both in terms of higher administration costs and reduced ability to preserve confidentiality for clients who desire to claim withholding tax reductions or exemptions. On the other hand, the NQI does not assume the same responsibilities as a QI and does not agree to external audits. As a result, the liability of an NQI is substantially lower than that of a QI. Ultimately, the decision to become a QI is a complex calculus that is highly context-specific.

Recently, the QI program has come under critical scrutiny. Although the QI system successfully enhanced assurance that tax benefits are properly provided to nonresident aliens, the majority of U.S. source income payments do not travel through the QI system. More visibly, the system has been subject to abuse. The recent United Bank of Switzerland scandal is a prominent example. The Swiss bank allegedly advised U.S. clients to establish non-U.S. companies as account holders in QIs, and thus appear as foreign beneficial owners, possibly owed reduced withholding rates. Consequently, many wealthy U.S. citizens successfully exploited the QI system to evade paying their full amount of income tax. The current administration has proposed several changes to the QI program in response to such perceived abuses of the system. These proposals are designed both to strengthen the with-

52 See Morse & Shay, QI Status Act I, supra note 3, at 334.
53 See id. at 339.
54 See id. at 339–40.
55 See id. at 340.
56 See id. at 341.
57 See Luntz, supra note 32, at 43.
58 U.S. Gov’t ACCOUNTABILITY OFFICE, supra note 38, at 3, 14. Some commentators claim that the QI program has been highly successful. See Edward Tanenbaum, In Defense of the Qualified Intermediary Program, 37 TAX MGMT’T INT’L J. 220, 221 (2009) (“That the QI program has been a success cannot be denied. Thousands upon thousands of financial institutions have signed onto the program. More withholding tax revenue has poured into the U.S. treasury than ever before.”).
59 See Luntz, supra note 32, at 43.
61 See id. at 488–89.
63 See DEP’T OF THE TREASURY, supra note 12, at 41–45.
holding and reporting rules under the QI regime and to provide fur-
ther incentives for NQIs to enter into QI agreements with the I.R.S.\textsuperscript{64}

II. Discussion

In response to perceived abuse by wealthy U.S. citizens using the
QI program to evade U.S. taxes, the Obama Administration has made
several proposals intended to “ensure that U.S. persons are properly
paying tax in connection with foreign income and accounts and that
proper withholding tax applies with respect to foreign persons.”\textsuperscript{65} The
Administration’s approach to strengthening the QI program is two-
fold.\textsuperscript{66} First, increase reporting requirements for QIs to prevent U.S.
taxpayers from manipulating the system to evade taxes.\textsuperscript{67} Second, cre-
ate incentives for NQIs to become QIs.\textsuperscript{68} With more foreign intermedi-
aries acting as QIs, coupled with increased reporting responsibilities,
the Administration suggests that tax evasion through offshore accounts
will be significantly reduced, thereby increasing withholding revenue.\textsuperscript{69}
For present purposes, two of the proposals are especially pertinent.\textsuperscript{70}
First, the Administration proposes that QIs be required to identify all
account holders that are U.S. persons, by filing Form 1099’s with
respect to all payments to U.S. account holders.\textsuperscript{71} In addition, the U.S.
Treasury would be authorized to issue regulations to implement this
proposal, including the possible requirement that financial institutions
may only be QIs if all commonly-controlled financial institutions are
also QIs.\textsuperscript{72} Second, the Administration proposes to mandate that U.S.
withholding agents withhold tax from all income payments made to
NQIs, thereby requiring the underlying beneficial owners to seek a re-
fund if the blanket withholding tax results in over-withholding.\textsuperscript{73} The
Administration reasons that this proposal will discourage tax evasion by

\textsuperscript{64} Id. at 41.

\textsuperscript{65} Id. The Obama Administration’s proposals are not the first of their kind. See, e.g.,
I.R.S. Announcement 2008–98, 2008–44 I.R.B. 1087. Rather, they can be viewed as the
culmination of a variety of similar proposals, such as those made by the Government Ac-
countability Office in December 2007. See U.S. Gov’t Accountability Office, supra note
38, at 34–35.

\textsuperscript{66} See Dep’t of the Treasury, supra note 12, at 41.

\textsuperscript{67} Id.

\textsuperscript{68} Id.

\textsuperscript{69} See id.

\textsuperscript{70} See id. at 41–43.

\textsuperscript{71} Id. at 42.

\textsuperscript{72} Dep’t of the Treasury, supra note 12, at 42.

\textsuperscript{73} Id. at 43. Technically, this is limited to FDAP income, such as interest or dividend
payments. See id.
incorrect information reporting conducted through NQIs and encourage the use of QIs “by requiring withholding of tax on payments made through nonqualified intermediaries.”

Although most commentators agree that addressing tax evasion in today’s economic climate is especially important, the reactions to the Administration’s proposals are varied. Indeed, more radical proposals would eliminate the program altogether. Some commentators argue that the QI program was a mistake from the start, a “purely administrative program designed for the comfort of foreign banks.” From this perspective, the program naively trusts foreign banks to act as the I.R.S.’s sole means of information gathering and withholding, and thereby facilitates tax evasion, as demonstrated by the United Bank of Switzerland. Moreover, such commentators argue, the program does not even offer any tangible benefit to the United States because it has not significantly increased revenue through withholding. Other commentators have implied that the program’s scope, and recent proposals to expand this scope, represents the latest form of U.S. imperialism. As one commentator colorfully puts it, “Obama wants banks everywhere to behave as if they were on Main Street, Ohio.” From this perspective, a program that requires foreign banks to become agents of the U.S. government—such as the QI program—is far more problematic than tax evasion. Nevertheless, notwithstanding these more radical positions,

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74 Id.
77 Sheppard, Ineffectual Information Sharing, supra note 76, at 1144.
79 Sheppard, Ineffectual Information Sharing, supra note 76, at 1144. Elsewhere Sheppard argues that tax treaties and other information agreements are much more effective than the QI program because the withholding tax is used more often by the United States as a bargaining chip in treaty negotiations rather than as an actual enforcement mechanism. Sheppard, UBS’s Sweet Deal, supra note 62, at 852. Thus, the immediate purpose of the U.S. withholding regime has never been to collect revenue. See id.
80 See Maddox, supra note 76.
81 Id.
82 See id.
most commentators seem to agree that the QI program serves an important function and that it can, and should, be fixed.\textsuperscript{83}

The QI system is designed to improve the U.S. withholding regime, with the goal in mind to attract foreign capital.\textsuperscript{84} Because eliminating tax evasion through foreign financial accounts is virtually impossible, any controls aimed at deterring tax evasion should not be viewed independently of their effects on foreign capital influx.\textsuperscript{85} Thus, any analysis of the proposals must consider the effects on the willingness of foreign financial institutions to become QIs.\textsuperscript{86} The immediate response of foreign intermediaries to increased reporting requirements was concern over additional costs.\textsuperscript{87} Financial institutions must ask themselves whether QI status is worth the additional costs associated with identifying and reporting all foreign source income made to their U.S. account holders.\textsuperscript{88} It is entirely possible that many will decide that QI status is not worth this price.\textsuperscript{89}

Therefore, some argue, the increased reporting requirements ignore adverse efforts borne by the majority of QIs who abide by the program.\textsuperscript{90} Indeed, the requirement’s success in preventing tax evasion could be “Pyrrhic” if the resulting program fails to attract foreign financial institutions who no longer consider the “carrot” of QI status sufficiently appealing to enter the agreement with the I.R.S.\textsuperscript{91} Given that confidentiality is the single greatest attraction of the QI system, some suggest it is naive to presume that the adverse effects of the Administra-

\textsuperscript{83} See Shay testimony, supra note 75, at *7; see also Banking Secrecy Practices, Wealthy Taxpayers: Hearing Before the H. Subcomm. on Select Revenue Measures of the H. Comm. on Ways & Means, 111th Cong. (2009) (testimony of Doug Shulman, Comm’r, Internal Revenue Service), 2009 WL 828059, at *3 [hereinafter Shulman testimony] (stating that “the QI system is critical to facilitating sound tax administration in a global economy”); Banking Secrecy Practices, Wealthy Taxpayers: Hearing Before the H. Subcomm. on Select Revenue Measures of the H. Comm. on Ways & Means, 111th Cong. (2009) (testimony of Peter H. Blessing, Lawyer, Shearman & Sterling LLP), 2009 WL 828057, at *15 [hereinafter Blessing testimony] (stating that the QI program is “well-conceived and plays a key role in the U.S. withholding tax regime”). Shay argues that in a world without the QI program it would be much more likely for withholding agents to simply treat foreign banks as beneficial owners and fail to withhold appropriately, notwithstanding their liability for doing so. See Shay testimony, supra note 75, at *7.

\textsuperscript{84} See Shay testimony, supra note 75, at *12.

\textsuperscript{85} See Blessing testimony, supra note 83, at *2.

\textsuperscript{86} See id. at *15.

\textsuperscript{87} See Alyce Nelson, European QI Community Fears Cost of U.S. Proposals, 52 Tax Notes Int’l 264, 265 (2008).

\textsuperscript{88} Parillo, supra note 13, at 680.

\textsuperscript{89} See id.

\textsuperscript{90} See Luntz, supra note 32, at 45.

\textsuperscript{91} See id. at 49.
tion’s proposal will be minimal. Furthermore, the documentation requirements are already incredibly complex, and adding to this confusion will make compliance more difficult for honest QIs. The information reporting requirement therefore seems to punish compliant QIs—who must now breach their confidentiality agreements—for the activities of a few noncompliant QIs such as the United Bank of Switzerland. From this perspective, the increased information reporting requirement looks excessive: an uncritical overreaction to a politically “hot topic.”

Others argue that, on the contrary, the increased reporting requirement would not likely discourage foreign financial institutions from becoming QIs. Proponents of increased information reporting do seem to have one ace in the hole: the QI system, as it stands, is easy to abuse, and requiring QIs to report all U.S. account holders rather than submitting information in the aggregate is one way to decrease tax evasion through the program. In addition, doing so places the obligation for reporting “more securely in the internal processes and computing systems of the gatekeeper closest to the client,” contributing to the

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92 See id. at 44; see also U.S. Gov’t Accountability Office, supra note 38, at 11 (finding that “[o]ne of the principal incentives for foreign financial institutions to become QIs is their ability to retain the anonymity of their client list”). Confidentiality is a critical component of the QI program because disclosure may be prevented by regulations within the QIs’ jurisdiction, and QIs do not want to share client information with competing financial institutions. Luntz, supra note 32, at 44.

93 See Ruth Ann Schneider, Qualified Intermediaries: Caught in the Complexity of New U.S. Withholding Requirements, Taxes, Dec. 2000, at 18. Indeed, QIs may make honest mistakes based on their unfamiliarity with the incredibly complex U.S. tax regime. Luntz, supra note 32, at 52. The Administration and its supporters seem to presume that any QI that fails to comply with its obligations does so intentionally, and further that any complying QI would have no problem with increased information reporting. See id. at 48, 52. But both these assumptions seem false. See id.

94 See id. at 48; see also Nelson, supra note 87, at 265 (noting the “potential risk that clients who have always complied with documentation requirements would bear the cost burden of a few U.S. tax evaders, many of whom may not even be clients of the same financial institution”).

95 See Luntz, supra note 32, at 45, 50. Luntz admits that some may view tax evasion as possessing social significance that would justify the costs to the QI program. Id. at 50. In this view, tax evasion “warp[s] the social fabric” and inefficient solutions such as increased information reporting are therefore worthwhile. Id. Ultimately, Luntz concedes, it is a question of social values. Id.

96 See Shay testimony, supra note 75, at *9. But Shay is aware that “an important question is how much burden and risk of liability can be imposed on QIs without causing material participants to leave the QI system.” Id. at *8.

efficiency and clarity of the information reporting process.\textsuperscript{98} As a result, many commentators have recommended increased reporting.\textsuperscript{99}

The reaction to the Administration’s proposal to require blanket withholding on nonqualified intermediaries has received less attention from those in support of the proposals, perhaps because it seems less controversial.\textsuperscript{100} The Administration’s rationale appears simple enough: NQIs do not enter into a special agreement with the U.S. government; thus, there is no reason to refrain from full withholding to prevent tax evasion.\textsuperscript{101} Moreover, default withholding rules already apply to NQIs who fail to forward detailed beneficial owner documentation to withholding agents.\textsuperscript{102} The Administration’s proposal would simply apply these default rules universally, which amounts to no longer trusting NQIs to collect beneficial owner information because they do not agree to any form of U.S. oversight—such as an external audit.\textsuperscript{103}

But some commentators have responded negatively to increasing the burden of being an NQI.\textsuperscript{104} Although this kind of intermediary does not agree to be an agent of the I.R.S., it is not thereby relieved of all withholding responsibilities.\textsuperscript{105} And without the ability to aggregate accounts, the NQI system is already more “cumbersome and expensive” than the QI system.\textsuperscript{106} Adding to these higher costs is no trivial matter.\textsuperscript{107} And what is even more concerning, not all NQIs choose to forego QI status: many simply cannot become QIs because the I.R.S. does not approve of their home country’s “know-your-customer” rules for identifying beneficial owners.\textsuperscript{108} Some commentators have expressed special concern over extending authority to the Treasury to grant QI status conditional upon whether all commonly-controlled financial in-

\textsuperscript{98} See Morse, \textit{ supra} note 10, at 472.
\textsuperscript{99} See, \textit{e.g.}, id.
\textsuperscript{100} Compare the discussion of increased 1099 reporting requirements for QIs with the lack of any discussion for strengthening withholding obligations of NQIs in Shay testimony, \textit{ supra} note 75, at *9–11, 23–26.
\textsuperscript{101} \textit{See Dep’t of the Treasury, supra} note 12, at 43.
\textsuperscript{102} Morse, \textit{ supra} note 10, at 472.
\textsuperscript{103} \textit{See id.}
\textsuperscript{104} See Parillo, \textit{ supra} note 13, at 680.
\textsuperscript{105} \textit{See} Marnin J. Michaels et al., \textit{Being an NQI in a ‘QI World,’22 Tax Notes Int’l} 2139, 2145 (2001).
\textsuperscript{106} Morse & Shay, \textit{QI Status Act I, supra} note 3, at 339.
\textsuperscript{107} \textit{See id.}
\textsuperscript{108} Michaels et al., \textit{supra} note 105, at 2140. These rules are central to the QI program. \textit{See} Morse & Shay, \textit{QI Status Act II, supra} note 33, at 262.
stitutions are also QIs.\textsuperscript{109} To these commentators, such a measure would force NQIs into QI status when they have no legitimate business reason to do so.\textsuperscript{110} Rather than encouraging foreign intermediaries to become QIs through a “carrot” approach, the proposal simply discourages foreign intermediaries from remaining NQIs through the “stick” of making business more difficult.\textsuperscript{111}

Thus, a wide range of positions has been adopted by commentators in response to the Administration’s proposals for the QI program. Irrespective of the merit of these proposals, their very promulgation and subsequent debate highlights the important role the program was designed to play in the U.S. withholding tax regime.\textsuperscript{112}

III. Analysis

Ultimately, the Administration’s proposals fail to adequately consider the important balance of values in QI reform.\textsuperscript{113} Until more benign and higher order changes, such as increased U.S. oversight of external audits, are made, the United States should neither increase reporting requirements on QIs nor require blanket withholding on NQIs.\textsuperscript{114} Clearly, tax evasion is a serious problem, both economically and legally.\textsuperscript{115} But the simplest solution to tax evasion—eliminating the QI program and requiring complete withholding and information reporting on all foreign income payments by withholding agents—ignores the balance of values at stake and would represent throwing the baby out with the bathwater.\textsuperscript{116} As commentators have indicated, the privacy of

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\bibitem{109} Parillo, \textit{supra} note 13, at 680.
\bibitem{110} \textit{Id.} (“Essentially, you’re taking affiliates that did not become QIs because they had no reason to be a QI—either because they’re not handling U.S. source payments, they’re only doing local banking or foreign-source stuff, and may have only a trickle of U.S. expats that they’re dealing with—and making them become a QI.”).
\bibitem{111} \textit{Id.} at 487–88.
\bibitem{112} \textit{See generally} Morse & Shay, \textit{QI Status Act III, supra} note 44.
\bibitem{113} \textit{Cf.} Luntz, \textit{supra} note 32, at 45 (implying that earlier similar proposals failed to consider the important balance of values at stake).
\bibitem{114} \textit{See generally id.} at 51 (explaining the attractiveness of requiring increased oversight by the I.R.S.).
\bibitem{115} \textit{See} Shay testimony, \textit{supra} note 75, at *3 (“Taking steps to address the so-called tax gap, the difference between taxes due and taxes actually collected, is an important element of putting our fiscal house in order.”); Shulman testimony, \textit{supra} note 83, at *1 (“It is of paramount importance to our system of voluntary compliance with the tax law that citizens of this country have confidence that the system is fair. We cannot allow an environment to develop where wealthy individuals can go offshore and avoid paying taxes with impunity.”).
\bibitem{116} \textit{Cf.} Luntz, \textit{supra} note 32, at 47 (arguing that “given the uncertainty as to the actual losses to the Treasury . . . any proposed changes to the Program should not be dispropor-
nonresident aliens is an important consideration.\textsuperscript{117} Even more important, at least from the United States’ perspective, is attracting foreign capital investment.\textsuperscript{118} Every step made to reduce tax evasion potentially discourages foreign investment and potentially decreases financial privacy for foreign investors.\textsuperscript{119} Additionally, the QI program is not, and was never intended to be, the primary system for enforcing tax compliance outside the United States.\textsuperscript{120} In assessing QI reform, then, it is necessary to keep these various considerations in mind and to appreciate the overarching U.S. economic interest when focusing on the relatively minor problems caused by offshore tax evasion.\textsuperscript{121}

A. The Balance of Values and the Administration’s Proposals

The uncertainty regarding the effects of the Administration’s proposals, in conjunction with the United States’ unique jurisdictional decisions, demonstrate that the proposals do not adequately reflect the balance of values in QI reform.\textsuperscript{122} The noneconomic concern with privacy may not seem as noteworthy as the economic concern with attracting foreign capital.\textsuperscript{123} Indeed, the effects of increased reporting requirements on client confidentiality, along with any negative implications of eliminating confidentiality, are highly uncertain.\textsuperscript{124} Yet if we assume, at a minimum, that financial privacy is a value, it is unwise to disregard this uncertainty.\textsuperscript{125} Although the value of financial privacy may not trump the value of tax compliance, neither should it be ignored.\textsuperscript{126}
Regardless of the final judgment regarding the value of financial privacy, the prospect of discouraging foreign capital investment in the United States should not be taken lightly.\textsuperscript{127} A chief purpose of the QI program is, after all, to increase tax compliance while simultaneously making investment in the United States more attractive to nonresident aliens.\textsuperscript{128} Especially given the United States’ current economic situation, attracting foreign investment is a top priority.\textsuperscript{129} If the proposals are likely to discourage foreign investment, this is a major defect.\textsuperscript{130} Moreover, any new international tax policy adopted by the United States is bound to have unintended economic consequences.\textsuperscript{131} Due to the complex interrelatedness of the global market and all its interactions, it would be irresponsible to pretend that even the short-term effects of the current proposals can be successfully predicted.\textsuperscript{132} This does not, by any means, necessitate inaction; however, it does serve as a reminder that when the United States runs an “experiment” with tax policy, small steps are more prudent than large transformations.\textsuperscript{133} Furthermore, were it not for the United States’ unique jurisdictional choices, QIs would not be put in the uncomfortable position of enforce the tax obligation of the depositor to his home country.” See id. at 632. For an alternative perspective on the balance of financial privacy and tax compliance, and its implications for the QI program, see David R. Burton, \textit{Financial Privacy and Individual Liberty} 22–23 (Austrian Scholars Conf., Working Paper, 2003), \textit{available at} http://www.mises.org/asc/2003/asc9burton.pdf.

\textsuperscript{126} See Blum, \textit{supra} note 117, at 624–25 (“The more significant concern of a nonresident depositor is that the IRS will convey [its] information to the tax authority of [its] residence country. . . . The [resident’s] government might use this financial information about its resident to carry out illegitimate acts such as expropriation or persecution.”).

\textsuperscript{127} See Blessing testimony, \textit{supra} note 83, at \#2 (suggesting that attempts to decrease tax evasion cannot place “undue burden[s] on the benefits that come with free flows of capital across borders”).

\textsuperscript{128} See Morse & Shay, \textit{QI Status Act I}, \textit{supra} note 3, at 331 (noting that the QI program was designed to create a “market-oriented” incentive to comply with the U.S. tax system).

\textsuperscript{129} See Shay testimony, \textit{supra} note 75, at \#12 (reasoning that the United States’ ability to tax investment income abroad is constrained by “its interest in attracting foreign capital to the United States”).

\textsuperscript{130} See Blessing testimony, \textit{supra} note 83, at \#2; Shay testimony, \textit{supra} note 75, at \#12.

\textsuperscript{131} See Blessing testimony, \textit{supra} note 83, at \#2.


\textsuperscript{133} Cf. Morse & Shay, \textit{QI Status Act I}, \textit{supra} note 3, at 341 (describing the QI program as an “experiment in international tax enforcement” and noting the difficulty of predicting the effects of making changes to the program).
potentially facilitating tax evasion by U.S. citizens. In taxing its citizens and residents on a world-wide basis, the United States creates a unique situation: in addition to collecting tax on U.S. source income paid to foreign persons, the United States collects tax on the income of U.S. citizens and residents abroad. There are thus two separate regimes for tax withholding at play and two separate information reporting systems. Both systems are involved in the QI program because the original obligations of withholding agents implicate both types of income payment.

If the United States had no interest in determining U.S. citizenship status for foreign account holders (for purposes of 1099 reporting), withholding agents—and by implication QIs—would not be required to identify whether the beneficial owners of income payments were U.S. persons. From the perspective of cost-shifting, placing the burden of 1099 reporting on foreign intermediaries seems disproportionate. Although tax evasion is a serious problem, as long as the United States retains its jurisdictional choice to tax citizens on a worldwide basis, the burden of discovering U.S. account holders should not be placed disproportionately on the shoulders of QIs. This argument does not imply that the program should not be strengthened to enforce the U.S. withholding regime, but it does reinforce the value of taking small steps in QI reform.

B. Requiring Increased U.S. Oversight Is a Better First Step

In light of the inherent uncertainty regarding the economic and noneconomic effects of the host of proposed changes, as well as the United States’ unique jurisdictional decisions, the most reasonable first

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134 See Neuenhaus, supra note 21, at 918 (“[A]n intermediary’s obligation to report and withhold regarding U.S. payees can be imposed on both U.S.- and non-U.S.-source income.”).
135 See U.N. Ctr. on Transnational Corps., supra note 4, at 9; Neuenhaus, supra note 21, at 914.
136 Neuenhaus, supra note 21, at 914. The first involves reporting for nonresident aliens to whom U.S. source income is paid, called 1042-S reporting. Id. The second involves reporting for presumed U.S. citizens to whom any income is paid, called 1099 reporting. Id.
137 See Shay testimony, supra note 75, at *15–17.
138 See Treas. Reg. § 1.1441–1(b)(5).
139 See Luntz, supra note 32, at 47.
140 See id.
141 See id.
step in QI reform seems to be the one with the least impact.\textsuperscript{142} The two major proposals discussed above are connected by a sense of tightening restrictions and punishing noncompliance rather than rewarding compliance: a drastic shift from “carrot” to “stick.”\textsuperscript{143} As one commentator points out, a more benign change to the program would involve the United States more directly in the QI external audit requirement, by requiring external auditors to “associate” with U.S. auditors.\textsuperscript{144} Although this proposal may not possess the same promise of curbing U.S. tax evasion as a more “integrated” approach, it does represent a less intrusive requirement for foreign intermediaries and may help significantly reduce honest errors made in the reporting process.\textsuperscript{145} Moreover, this requirement imposes a change at a higher level in the program than individual financial institutions: the involvement of the U.S. government in administering the program.\textsuperscript{146} Because this requirement does not require much more of an obligation from QIs, individual institutions are less likely to perceive it as a burden than the current proposals.\textsuperscript{147} Therefore, the association requirement better respects the competing values of protecting financial privacy and attracting foreign investment.\textsuperscript{148}

This proposal is championed by many commentators, but it is usually suggested as part of an “integrated approach” involving many more changes—such as increased information reporting—to be made at once.\textsuperscript{149} But such an “integrated approach” is precisely the wrong approach given the uncertainty surrounding the effects of QI reform.\textsuperscript{150} Taking a small step at the level of U.S. oversight of the QI system rather than increasing regulations for foreign financial institutions represents an initial compromise that better balances the values of attracting foreign investment, respecting financial privacy, and curbing tax evasion.\textsuperscript{151}

\textsuperscript{142} Cf. id. at 45 (arguing that any attempt at QI reform should “maximize[] the benefits and minimize[] the costs of each affected party”).
\textsuperscript{143} See Parillo, supra note 13, at 680.
\textsuperscript{144} See Luntz, supra note 32, at 51.
\textsuperscript{145} See id. at 51–52.
\textsuperscript{146} See id.
\textsuperscript{147} See id. at 49, 51.
\textsuperscript{148} See id. at 45.
\textsuperscript{149} See Shulmam testimony, supra note 83, at *2, 4.
\textsuperscript{150} See Blessing testimony, supra note 83, at *2 (noting that “[t]ax measures adopted in response to legitimate concerns can have unanticipated and unhappy consequences from the standpoint of economic efficiency”).
\textsuperscript{151} See Luntz, supra note 32, at 47; Maddox, supra note 76.
Conclusion

The qualified intermediary program was created as a compromise among competing values. In exchange for facilitating U.S. withholding tax enforcement, foreign financial institutions would be provided privileges for reporting taxable U.S. income. In light of perceived abuse of this program by wealthy U.S. taxpayers, the Obama Administration proposes reform that will strengthen reporting requirements and further “encourage” nonqualified intermediaries to enter the QI regime. Yet these proposals come at a cost, in terms of increasing the burden of being a QI, and thus represent a drastic shift from “carrot to stick” in the QI program. Although there is disagreement about whether foreign financial institutions will in fact be discouraged from entering the program, the uncertainty surrounding the proposed changes provides ample reason for alarm, especially considering the importance of attracting foreign capital at present economic times. Moreover, the United States’ decision to tax U.S. citizens and residents on a world-wide basis—the only developed country to do so—is directly responsible for the enhanced responsibilities of U.S. withholding agents and, by implication, QIs. Given these considerations, a more responsible first step in QI reform would be increasing U.S. involvement in the external audit procedure already in place, rather than increasing reporting requirements for QIs and increasing the burden of remaining an NQI. As long as the United States desires to keep the QI program and its unique system of international tax jurisdiction, it is necessary to involve compromises the Administration’s proposals fail to make.