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Is Economic Nationalism in Corporate Governance Always a Threat?

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IS ECONOMIC NATIONALISM IN CORPORATE GOVERNANCE ALWAYS A THREAT?

MARTIN GELTER*

Abstract

Corporate law and corporate governance debates during the past decades have generally been skeptical of elements of economic 'Nationalism' or 'protectionism.' Arguably, globalization and convergence in corporate governance have resulted in a reduction of protectionist policies. However, recently COVID-19 has resulted in nationalist and protectionist conduct in economic policy across jurisdictions. Contrary to the predominant view, this paper argues that corporate governance policies intended to serve the interest of a particular country may at times be justified. First, globalization and convergence in corporate governance are likely to have beneficial effects only when outside investors pursue financial rather than political goals. Protectionist policies may protect domestic firms from outside competition of this type, e.g., from being taken over by foreign firms controlled by or having heavy backing from its government. Second, some degree of protectionism may be necessary to sustain a country's institutional arrangements and economic prosperity. Significant outside financial investors or multinational groups may not interact with domestic constituencies in the same way as the existing ones, thus triggering disruption to the social compact. This may be necessary to preserve the balance of the political economy in a country that has allowed it to maintain productive in the past. In addition, preserving a particular economic arrangement is often necessary to protect political stability, which is a precondition to productive efficiency. Third, COVID-19 has highlighted the need for resilient structures in corporate governance, which may include integration into a domestic economic network. Protectionist policy may serve the purpose of protecting the viability of industry in times of political crisis, e.g., by protecting supply chains. Moreover, being integrated into a national network often helps firms to weather situations of crisis even if such

* Professor of Law, Fordham University School of Law; Research Member, European Corporate Governance Institute (ECGI). I am deeply grateful to Julia Puaschunder as well as to participants of the Ohio State Business Law Journal's 2021 symposium for very helpful comments on the paper and discussions on the topic. In addition, I thank Mariana Pargendler and Mathias Siems for insightful comments on a prior draft. Errors remain my own.

embeddedness is not aligned with efficiency goals as usually understood in corporate governance debates.

Keywords: COVID-19, corporate governance, convergence, path dependence, ownership structure, varieties of capitalism, nationalism, protectionism, stakeholder theory, shareholder primacy, SEOs, state ownership of firms, political economy of corporate governance, resilience, Golden Shares, foreign direct investment (FDI), embeddedness, multinationals, footlooseness

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1. INTRODUCTION

COVID-19 and the lockdowns that it triggered have resulted in economic turmoil unprecedented in decades. Both the economic reactions and the public health responses by many governments around the world can be

described as nationalistic or at least protectionist. COVID-19 has resulted in more nationalist and protectionist policies being implemented, which mainstream economic and corporate governance theory typically consider to be problem. This symposium article developed out of previous work with Julia Puaschunder.[1] It takes a few themes further and expands one theme – specifically issues relating to nationalism, state ownership, and economic protectionism, which we suggested will increase with COVID-19.[2] While economic 'nationalism' and 'protectionism' are mainly subjects of other areas of law, such as foreign direct investment or international trade law, literature in recent years has documented a close interaction with corporate law and governance. Scholarly perspectives and mainstream policymaking on economic 'nationalism' or 'protectionism' in corporate governance have typically tended to be skeptical. In the introduction to their book, Ringe and Bernitz argue that "remaining un-protectionist is necessary, yet not sufficient."[3] Mariana Pargendler's influential article emphasizes how economic nationalism influences the development of corporate law. Where globalization and pro-investor corporate laws have led to capital markets being populated by foreign investors, nationalist tendencies may result in a backlash to protect the interests of domestic managers, workers, and controlling shareholders.[4] This symposium article argues that there are reasons for protectionism that should not be considered pernicious. While most of the literature takes a negative perspective on protectionist policies in corporate governance, this paper suggests that it may not always be as bad as we usually think it is.

A caveat needs to be made about terminology because of the political connotations that the term 'nationalism' typically carries. This paper attempts to stay neutral and descriptive in its analysis and uses the term 'protectionism' for policies that seek to shield a country's economy from the outside. By contrast, it uses the term 'nationalism' for policies that seek to enhance the country's economic standing or project its (economic or political) power into the outside world. In other words, this article uses 'protectionism' for measures that could be described as passive or reactive, whereas the term 'nationalism' is used for active measures that seek to help firms outside the country.

One of the most important topics of comparative corporate governance during the 1990s and 2000s was convergence.[5] Scholars argued about whether and to what extent corporate governance laws and practices would

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[1] Martin Gelter & Julia M. Puaschunder, *COVID-19 and Comparative Corporate Governance*, 46 J. CORP. L. 557 (2021).
[2] *Id.*
[3] *See* ULF BERNITZ & WOLF-GEORG RINGE, COMPANY LAW AND ECONOMIC PROTECTIONISM: NEW CHALLENGES TO EUROPEAN INTEGRATION (1st ed. 2010) [hereinafter PROTECTIONISM].
[4] Mariana Pargendler, *The Grip of Nationalism in Corporate Law,* 95 IND. L.J. 533, 537, 584–85, 589 (2020).
[5] *See infra* notes 14–16 and accompanying text.

converge to a single model. Those arguing in favor of convergence generally predicted that a shareholder model would prevail in which firms would be compelled to pursue the interest of all equity investors (as opposed to controlling shareholders, employees, or the government). In this model, which was a consequence of the economic globalization of the time, all investors regardless of origin were to be treated equally as firms were seeking international investment.[6] This is not to say that nationalist or protectionist aspects disappeared from corporate governance during this period; convergence was a trend that never reached an end point.[7] However, if such a point were reached worldwide (or in a significant subset of jurisdictions), elements in the corporate governance system oriented toward a "national" interest or benefitting primarily domestic interest groups would fade away. This is in part because countries would find it in their own interest to espouse a globalized shareholder primacy model. Accordingly, scholars favoring convergence typically had a rather negative view of protectionism in corporate law and governance.

This trend changed directions during the years following the financial crisis, during which globalization slowed and convergence in corporate governance went on a different track. The COVID-19 pandemic has reinforced this trend since 2020. State ownership has made a comeback to some extent, as have mechanisms that protect domestic firms both from foreign competition in product markets and from foreign control in financial markets. The latter include, for example, state minority ownership, loyalty shares, or protections against hostile takeovers.[8]

In this light, it is time to reevaluate the debates scholars have had about "protectionist" or even "nationalist" elements in the corporate governance system. This symposium article suggests that such policies, which are intended to serve the interest of the implementing country, can be justifiable for several reasons. First, international openness in corporate governance, which is characteristic of the globalization and convergence debates, rests on certain assumptions. Protectionist policy may serve the purpose of protecting the viability of the industry in times of political crisis, e.g., by protecting supply chains.[9] The convergence model assumes that foreign investors pursue financial rather than political goals. Consequently, countries seeking to preserve their economic system in the long run may have reasons to create shields against – at least some types of – foreign ownership. "Openness" in corporate governance will thus not necessarily be in each country's best interest. Most of all, such policies may protect domestic firms from unfair

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[6] *See infra* notes 29–32 and accompanying text.
[7] *See* Pargendler, *supra* note 4, at 589 ("prognoses about the irrelevance of corporate nationality in
the 1990s turned out to be premature").
[8] *See infra* notes 42–60 and accompanying text.
[9] *See infra* notes 103–111 and accompanying text.

financial competition, e.g., from being taken over by foreign firms controlled by or having heavy backing from its government.[10]

Second, on a more abstract level, protectionist policies may serve the purpose of shielding a particular socio-economic model. Certain capitalist models may require some degree of protection to sustain themselves. Corporate governance systems are characterized by sets of institutional complements in the financial and labor markets that interoperate in specific ways depending on the country's institutional arrangements.[11] Foreign financial investors or multinationals will likely interact differently with local interest groups, thus upsetting established bargaining arrangements. Maintaining a particular arrangement will sometimes be necessary for economic reasons, specifically to preserve prosperity, or for political reasons, e.g., to protect the social contract underlying the economic arrangement.[12]

Third, a corporate governance system may be adjusted to a particular environment's propensity to develop recurring economic crises that endanger the existence of firms. This aspect has been highlighted by COVID-19, which has shown that corporate governance will often balance the goals of efficiency and resilience. A system that creates the most value in "normal" times may not always be best suited to survive a severe crisis. "Embeddedness" into a domestic economic network may be an instrument that helps firms to weather situations of crisis even if they are not necessarily efficient in non-crisis circumstances.[13] In jurisdictions where crises often recur, or in specific historical context, protectionist policies may thus be desirable.

This article proceeds as follows. Section 2 discusses the pre-COVID context, in particular the development of globalization and convergence in corporate governance during the past decades. Section 3 surveys nationalist and protectionist corporate law policies that we have already observed during the COVID-19 crisis, and possible others that governments might additionally pursue in the future. Section 4 surveys the advantages and risks of economic protectionism and nationalism, arguing that does not necessarily have to be detrimental to welfare or politically illegitimate. Section 5 summarizes and concludes.

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[10] *See infra* notes 115–122 and accompanying text.
[11] *See infra* notes 125–136 and accompanying text.
[12] *See infra* notes 138–145 and accompanying text.
[13] *See infra* notes 146–162 and accompanying text.

2. THE PRE-COVID CONTEXT: GLOBALIZATION OF CORPORATE GOVERNANCE

A. *The Convergence Debate*

A key economic development during the past decades was globalization. After the ostensible "end of history" in the political world with the fall of communism and the apparent victory of capitalist democracy in the early 1990s, the world entered a phase characterized by increasing economic integration. Analysts observed internationalized product markets, increasing cross-border investment and international supply chains. The world saw steadily rising cross-country economic integration through the WTO as well as regional agreements such as the EU's common market, NAFTA, and MERCOSUR.

In corporate governance, this key trend opposing protectionism is convergence, which can be seen as a larger aspect of the globalization debate. Scholars identified increasing convergence during this period, especially during the 1990s and 2000s. Most famously, Hansmann and Kraakman asserted an "End of History for Corporate Law" in 2001,[14] echoing Francis Fukuyama's assertion for the political world nine years prior.[15] Convergence scholars argued that corporate law was moving toward a shareholder primacy model in which the interests of other constituencies of the firm (such as workers) would be less important, and where other stakeholder, public, or state interests would eventually be pushed to the sidelines.[16]

While the dissemination of shareholder primacy is not logically tied to dispersed ownership as it existed in the US and the UK at the time,[17] there is at least a debate that it may be more suitable for a system with strong capital markets, and hence considerable diffusion of ownership in a significant subset of firms around the world.[18] Participants in the convergence debate observed a growing propensity among multinational corporations to access capital markets,[19] growing capital markets,[20] an unravelling of control

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[14] Henry Hansmann & Reinier Kraakman, *The End of History for Corporate Law*, 89 GEO. L.J. 439, 443 (2001).
[15] FRANCIS FUKUYAMA, THE END OF HISTORY AND THE LAST MAN (1992).
[16] *See* Hansmann & Kraakman, *supra* note 14, at 443–49.
[17] *Id.* at 443; *see also* Ruth V. Aguilera & Cynthia A. Williams, *"Law and Finance": Inaccurate, Incomplete, and Important*, 2009 BYU L. REV. 1413, 1418–20 (2009) (noting that dispersed ownership is not necessarily optimal).
[18] Hansmann & Kraakman, *supra* note 14, at 452.
[19] Jeffrey N. Gordon, *Convergence and Persistence in Corporate Law and Governance, in* THE OXFORD HANDBOOK OF CORPORATE LAW AND GOVERNANCE 28, 28 (Jeffrey N. Gordon & Wolf-Georg Ringe eds., 2018).
[20] John C. Coffee, Jr., *Convergence and its Critics: What are the Preconditions to the Separation of Ownership and Control?* in CORPORATE GOVERNANCE REGIMES 83, 88–90 (Joseph A. McCahery, Piet Moerland, Theo Raaijmakers & Luc Renneboog eds., 2003).

blocks[21] and a reduction of state ownership,[22] all of which paralleled the legal development. The direction of causality is not always clear. On the one hand, a system prioritizing the interests of *all* equity investors may be a precondition for capital market development and a separation of ownership and control;[23] on the other hand, causation may be reversed, meaning that a growing interest group of equity investors throughout society, such as owners of retirement plans, may have helped to make shareholder-oriented corporate law more politically palatable.[24]

In any event, corporate law would at least superficially adopt some "Anglo-Saxon" governance models both in wealthy European and East Asian countries, and in emerging markets.[25] There is widespread agreement that there was a pro-shareholder trend in the 1990s and 2000s,[26] which was in part driven by economic openness and globalization. With international product and financial markets integrating, firms were forced to compete more intensely. This in turn meant that better governed firms are more likely to survive, forcing others to adjust.[27] The issue of course remained debated,

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[21] MATHIAS M. SIEMS, CONVERGENCE IN SHAREHOLDER LAW 281–88 (2008).
[22] Gordon, *supra* note 19, at 29.
[23] On the 'law matters' thesis, which posits that concentrated ownership persists where corporate law insufficiently protects minority investors, *see* Rafael La Porta, Florencio Lopez-de-Silanes, Andrei Shleifer & Robert W. Vishny, *Legal Determinants of External Finance,* 52 J. FIN. 1131 (1997); Rafael La Porta, Florencio Lopez-de-Silanes, Andrei Shleifer & Robert W. Vishny, *Law and Finance,* 106 J. POL. ECON. 1113, 1145–51 (1998); *see also* John C. Coffee, Jr., *The Future as History: The Prospects for Global Convergence in Corporate Governance and Its Implications,* 93 NW. U.L. REV. 641, 647–48 (1999); Bernard S. Black, *The Legal and Institutional Preconditions for Strong Securities Markets,* 48 UCLA L. REV. 781, 834–35 (2001); Brian R. Cheffins, *Does Law Matter? The Separation of Ownership and Control in the United Kingdom,* 30 J. LEGAL STUD. 459, 461–65 (2001); Simon Deakin, Prabirjit Sarkar & Mathias Siems, *Is There a Relationship Between Shareholder Protection and Stock Market Development?* 3 J. L. FIN. & ACCT. 115 (2018).
[24] Hansmann & Kraakman, *supra* note 14, at 453; Ruth V. Aguilera & Rafel Crespi-Cladera, *Global corporate governance: On the relevance of firms' ownership structure,* 51 J. WORLD BUS. 50, 54–55 (2016); specifically on retirement plans *see* PETER A. GOUREVITCH & JAMES SHINN, POLITICAL POWER AND CORPORATE CONTROL 210–18 (2005); Martin Gelter, *The Pension System and the Rise of Shareholder Primacy,* 43 SETON HALL L. REV. 909 (2015).
[25] *See* SIEMS, *supra* note 21, at 226–27 (considering a tendency toward Americanization).
[26] *E.g.*, JEFFREY N. GORDON & MARK J. ROE, CONVERGENCE AND PERSISTENCE IN CORPORATE GOVERNANCE 42–45 (2004); ALAN DIGNAM & MICHAEL GALANIS, THE GLOBALIZATION OF CORPORATE GOVERNANCE 303–92 (2009); Mathias M. Siems, *Convergence in Corporate Governance: A Leximetric Approach*, 35 J. CORP. L. 729 (2010); Gordon, *supra* note 19, at 34–41.
[27] *See* Hansmann & Kraakman, *supra* note 14, at 450–51; Mark J. Roe, *The Shareholder Wealth Maximization Norm and Industrial Organization*, 149 U. PA. L.

especially in light of the argument that convergence would be hindered by path dependence.[28]

Crucially, the convergence debate left no space for a "national" interest. Convergence was arguably in part driven by economic openness and international competition in product markets.[29] Financial markets and firms' appetite for foreign capital were equally important. Outside investors in the convergence debate were often foreign institutional investors (typically from the US and the UK) that sought to diversify their portfolios internationally.[30] Firms' need to raise capital arguably created pressure to cater to the interest of these groups.[31] Institutional investors will only invest overseas if they are equally protected against managers and local controlling shareholders, or at least they will require an additional risk premium from the investee firms.[32] As having to pay such a premium will put these firms at a disadvantage, they will be interested in protecting foreign investors as well as they are protected in their home jurisdictions. Consequently, it would typically seem to be in a country's "national" interest to open itself to investment and espouse a shareholder-oriented model of corporate governance. However, as this symposium article argues below in section 4, this is not universally true.

B. *Benefits of corporate governance globalization*

Globalization and convergence obviously have many benefits. Both in the production of goods and services, the traditional Ricardian argument applies. In this view, the location of the production of goods (and services) is determined by comparative advantage, which makes everyone better off by allowing countries to specialize in producing goods and services for which they have the relatively lower opportunity cost.[33] With a larger number of locations in a trade network, more countries can benefit from trade, which

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REV. 2063 (2001); Massimiliano Vatiero, *On the (Political) Origin of 'Corporate Governance' Species*, 31 J. ECON. SURV. 393, 395 (2017).

[28] *E.g.*, Lucian Arye Bebchuk & Mark J. Roe, *A Theory of Path Dependence in Corporate Ownership and Governance*, 52 STAN. L. REV. 127 (1999); Amir N. Licht, *The Mother of All Path Dependencies Toward a Cross-Cultural Theory of Corporate Governance Systems*, 26 DEL. J. CORP. L. 147 (2001).

[29] Hansmann & Kraakman, *supra* note 14, at 450–51; Gordon, *supra* note 19, at, at 54

[30] Gordon, *supra* note 19, at 32.

[31] *See* René M. Stulz, *Globalization, Corporate Finance, and the Cost of Capital*, 12 J. APP. CORP. FIN. 8, 10 (1999) (discussing how openness to foreign investment reduces firms' cost of capital).

[32] Gordon, *supra* note 19, at 32.

[33] *E.g.*, Bruce D. Fisher, *NAFTA: Testing Ricardo's Theory of Comparative Advantage by Empirical Evidence Pre-and Post NAFTA*, 15 CHI.-KENT J. INT'L & COMP. L. 1, 5–6 (2015); Charles W. Murdock, *Why Ricardo's Theory of Comparative Advantage Regarding Foreign Trade Doesn't Work in Today's Global Economy*, 5 U. BOLOGNA L. REV. 59, 64–70 (2020) (both describing Ricardo's theory in the context of a critical account).

ideally will generate income, train human capital, and spread wealth and prosperity around the globe. This is not to say that global trade has eradicated poverty, but it has resulted in the development of a highly productive middle class in some major emerging economies that successfully joined the global network. Capitalism also has important socio-political effects. Competition assigns income (and ultimately wealth) based on market demand,[34] which creates incentives to accumulate financial and fortify human capital to get ahead in society. International competition erodes rents from within-country market concentration, thus bringing better products to consumers at lower prices.[35]

One can make similar arguments for convergence in corporate governance and shareholder wealth orientation as key aspects of globalized financial markets. Open markets allow capital to flow to its most profitable use because of competition between firms demanding capital and between investors supplying it.[36] On the demand side, firms implement financing decisions to obtain capital swiftly and flexibly when it is needed, and to return it to investors when it is not necessary.[37] This means that firms will disfavor legal and political restrictions on capital inflows, as well as formal ex ante corporate law constraints that slow down share issues, (international) mergers, repurchases of shares and dividends or M&A transactions. However, in all

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[34] MILTON FRIEDMAN, CAPITALISM AND FREEDOM 166–68 (40th Anniversary ed. 2002).

[35] *E.g.*, FREDRIK ERIXON, THE ECONOMIC BENEFITS OF GLOBALIZATION FOR BUSINESS CONSUMERS 13 (2018); *see also* Franklin Allen & Douglas Gale, *Corporate Governance and Competition*, in CORPORATE GOVERNANCE 23, 60–62 (Xavier Vives ed., 2000).

[36] Eugene F. Fama, *Efficient Capital Markets: A Review of Theory and Empirical Work*, 25 J. FIN. 383, 383 (1970) ("[T]he ideal is a market in which prices provide accurate signals for resource allocation . . ."); Raghuram G. Rajan & Luigi Zingales, *Which Capitalism? Lessons from the East Asian Crisis*, 11 J. APP. CORP. FIN. 40, 41 (1998); Kevin Haeberle, *Stock-Market Law and the Accuracy of Public Companies' Stock Prices*, 2015 COLUM. BUS. L. REV. 122, 137–39 (2015).

[37] If firms would otherwise underuse available capital, they can avoid downward pressure on the stock price by returning capital to shareholders, e.g., through dividends or share repurchases. *See* Michael Bradley & Michael Rosenzweig, *Defensive Stock Repurchases*, 99 HARV. L. REV. 1377, 1378 (1986) (discussing repurchases intended to raise stock price to inhibit hostile takeovers); Wm. Gerard Sanders & Mason A. Carpenter, *Strategic Satisficing? A Behavioral-Agency Theory Perspective on Stock Repurchase Program Announcements*, 46 ACAD. MGMT. J. 160, 161 (2003) ("Repurchase programs tend to result in persistently higher stock prices, and, eventually, increased earnings per share"); Ken C. Yook & Partha Gangopadhyay, *Free Cash Flow and the Wealth Effects of Stock Repurchase Announcements*, 49 Q.J. FIN. & ACCT. 23, 23 (2010) ("There is ample evidence that stock repurchases generate significant announcement-period abnormal returns."); Hostile takeover bids often force firms to return capital to shareholders. Michael C. Jensen, *Agency Costs of Free Cash Flow, Corporate Finance, and Takeovers*, 76 AM. ECON. REV. 323, 328 (1986).

these transactions, international outside investors will require some protection against opportunism by managers and controlling shareholders that prevent or penalize, among other things, tunneling transactions or dilution of their stock.[38]

Given the cost of formal ex ante protections, often ex-post protection in the form of effective corporate law (such as fiduciary duties) seems preferable. For such mechanisms to be effective, a country must provide an effective legal system and an impartial judiciary that is not hostile to foreign investors.[39] Decisions affecting corporations should not be made with the immediate interests of domestic companies in mind, as this can erode investor confidence and increase firms' cost of (international) capital in the long run. In this view, government interference in the economy is negative because it distracts from and undermines the pursuit of investor interests.[40] Arguably, some voters might lose their jobs in an international restructuring of a corporate group, but in the long run the country's economy will benefit.[41]

3. Types of Corporate Law Nationalism and Protectionism

Government interference can take many forms, which can be classified as nationalism or protectionism. This article uses 'protectionism' for the goal to shield a country's economy and firms from the outside (both in terms of ownership and influence). 'Nationalism', by contrast, refers to the goal of improving the country's economic position vis-à-vis the outside world, or to project its economic or political power. However, often the same instruments are used for both nationalist and protectionist purposes. The following two sections outline how governments sometimes control firms or at least maintain a minority stake (section 0), and how they shield firms with private owners from being taken over by foreign firms or investors (section 0).

A. *Government Control and Minority Ownership of Firms*

The most obvious form of government involvement in the economy is government ownership of a firm. Ownership may follow a bailout, but it could also result from politicians taking a long-term perspective for controlling the economy. Companies might be wholly owned, or they might be held

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[38] *E.g.*, Stulz, *supra* note 31, at 10–18 (discussing how shareholder protection can reduce the cost of capital).

[39] On the significance of effective courts in corporate law, *see, e.g.*, Luca Enriques, *Do Corporate Law Judges Matter? Some Evidence from Milan*, 3 EUR. BUS. ORG. L. REV. 765 (2002); Donald C. Clarke & Nicholas C. Howson, *Pathway to Minority Shareholder Protection: Derivative Actions in the People's Republic of China,* in THE DERIVATIVE ACTION IN ASIA: A COMPARATIVE AND FUNCTIONAL APPROACH 243 (Dan W. Puchniak, Harald Baum & Michael Ewing-Chow eds., 2012).

[40] *E.g.*, Hansmann & Kraakman, *supra* note 14, at 447.

[41] *See infra* section 0.

in a situation sometimes described as "mixed enterprise." This includes historical examples in Europe that arose after World War II, such as Renault in France.[42] Firms of these type often combine political and profit goals, one of which may be maintaining a certain level of employment, as was in the past often the case in Europe.[43] Prominent examples today include firms that are partly controlled by the Chinese government through SASAC[44] or by Singapore through Temasek.[45] In general, the public sector continues to hold significant percentages of the stock market around the world, including in Latin American, European and Asian countries.[46] Typically this ownership is concentrated in strategically important sectors such as basic materials, energy, financials, utilities and telecommunications.[47] Outside investors may not be particularly well protected from government opportunism in such cases, particularly because courts might be unlikely to support them if defendants are managers elected by the government as the controlling shareholder, or closely involved with it. However, the firm's political connections could be beneficial for investors in some cases because the firm may have strong public backing.[48]

An attenuated version of this is minority government ownership. Here, the profit motive may prevail, but the government could attempt to veto certain transactions. For example, it might retain a blocking minority that permits it to veto transactions for which a supermajority is required under the law.[49] European governments have historically often maintained so-called

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[42] Renault was nationalized in part because Louis Renault had been accused of collaborating with the Nazi occupation. *See* JOSEPH HAMEL & GASTON LAGARDE, 1 TRAITE DE DROIT COMMERCIAL, para. 894 (1954); JEAN-FRANÇOIS ECK, HISTOIRE DE L'ECONOMIE FRANÇAISE DEPUIS 1945, 13 (4th ed. 1994).

[43] *E.g.*, Andrei Shleifer, *State versus Private Ownership*, 12 J. ECON. PERSP. 133, 141–42 (1998) (discussing examples of political motives to maintain employment).

[44] Li-Wen Lin & Curtis J. Milhaupt, *We Are the (National) Champions: Understanding the Mechanisms of State Capitalism in China*, 65 STAN. L. REV. 697, 735–45 (2013).

[45] Christopher C. H. Chen, *Solving the Puzzle of Corporate Governance of State-Owned Enterprises: The Path of the Temasek Model in Singapore and Lessons for China*, 36 NW. J. INT'L L. & BUS. 303 (2016).

[46] ADRIANA DE LA CRUZ, ALEJANDRA MEDINA & YUNG TANG, OWNERS OF THE WORLD'S LISTED COMPANIES, OECD CAPITAL MARKET SERIES 27 (2019), http://www.oecd.org/corporate/Owners-of-the-Worlds-Listed-Companies.htm [https://perma.cc/V9TL-RFKH]; Gur Aminadav & Elias Papaioannou, *Corporate Control around the World*, 75 J. FIN. 1191, 1205 (2020).

[47] *Id.* at 31.

[48] *See, e.g.*, Yun-chien Chang & Yu-Hsin Lin, *Do State-Owned Enterprises Have Worse Corporate Governance? An Empirical Study of Corporate Practices in China*, EUR. BUS. ORG. L. REV. (forthcoming 2021).

[49] *See, e.g.*, Tamás Szabados, *Recent Golden Share Cases in the Jurisprudence of the Court of Justice of the European Union*, 16 GERMAN L.J. 1099, 1114 (2015)

"Golden Shares" in privatized utilities or firms in key industries.[50] In a series of key cases of the Court of Justice of the European Union (CJEU), the court addressed veto powers of the government enshrined either in law or in the company's articles.[51] The EU law question in these cases was whether these 'Golden Shares' constituted a violation of the principle of free movement of capital. In the view of the court, in almost all cases they did because they potentially discouraged cross-border investment.[52] Only in one of the early cases, *Commission v. Belgium*,[53] the court upheld a Golden Share because of its limited scope. The court stated that "the objective pursued by the legislation at issue, namely the safeguarding of energy supplies in the event of a crisis, falls undeniably within the ambit of a legitimate public interest." This was the case because the veto power concerned specified strategic assets.[54] As the principle of free movement of capital applies within the common market but not outside, EU law limits protectionist measures between the Member States, but not necessarily with respect to non-EU countries.

Corporate law and industrial policies can also be considered nationalist when they provide active support of domestic firms. This could mean supporting and subsidizing "national champion" companies or favoring domestic firms in public procurement. The WTO's Agreement on Subsidies and Countervailing Measures prohibits subsidies contingent on export performance or the use of domestic over imported goods.[55] In the EU, subsidies are more severely curtailed. EU state aid law restricts subsidies to narrow

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(discussing blocking minorities in the context of Volkswagen's articles of association); Valentin Jentsch, *Board Composition, Ownership Structure and Firm Value: Empirical Evidence from Switzerland*, 20 EUR. BUS. ORG. L. REV. 203, 217 (2019) (discussing the role of blocking minority ownership under Swiss law).

[50] *E.g.*, Mariana Pargendler, *State Ownership and Corporate Governance,* 80 FORDHAM L. REV. 2917, 2967 (2012).

[51] The question whether just using general supermajority powers of corporate law to effectively create a veto right was never fully resolved. *See* Wolf-Georg Ringe, *Company Law and Free Movement of Capital*, 69 CAMBRIDGE L.J. 378, 387–89 (2010) (discussing the question whether "general" company law could be considered a violation of free movement of capital as well).

[52] *E.g.*, Case C-483/99, Comm'n v. France, 2002 E.C.R. I-4785; Case C-503/99, Comm'n v. Belgium, 2002 E.C.R. I-4812; Case C-367/98, Comm'n v. Portugal, 2002 E.C.R. I-4756; among others, see also the subsequent "Volkswagen" case, Case C-112/05, Comm'n v. Germany, 2007 E.C.R. I-9020; *see, e.g.*, Pargendler, *supra* note 4, at 554; Martin Gelter, *EU Company Law Harmonization Between Convergence and Varieties of Capitalism*, *in* RESEARCH HANDBOOK ON THE HISTORY OF COMPANY AND CORPORATION LAW 323, 333 (Harwell Wells ed., 2018).

[53] Case C-503/99, Comm'n v. Belgium, 2002 E.C.R. I-4812. The Court also held for Germany in Volkswagen II, which concerned the implementation of the first Volkswagen judgment. Case C-95/12, Comm'n v. Germany, 2013 E.C.R.

[54] Ringe, *supra* note 51*,* at 384.

[55] Agreement on Subsidies and Countervailing Measures, art. 3, Jan. 1, 1995, Marrakesh Agreement Establishing the World Trade Organization, Annex 1A, 1869 U.N.T.S. 1.

circumstances,[56] such as natural disasters and other exceptional occurrences.[57] Reportedly, the EU's state aid regime was one of the most contentious issues in the Brexit negotiations because the UK desired freedom in subsidizing its industry.[58] In addition, EU public procurement law limits how Member States may organize public procurement. One aspect of this is that they may not give preference to domestic bidders over foreign ones.[59] For both policies, the goal is a level playing field for companies across countries. Thus, Member States should not enter a race to subsidize and bestow favors on champion firms rather than allowing firms to compete and the market to decide.[60]

For purposes of the debate on economic nationalism and protectionism, it is important to emphasize that these EU measures were introduced to create a common market within which the freedoms of movement of goods,

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[56] Consolidated Version of the Treaty on the Functioning of the Eur. Union, art. 107, Dec. 1, 2016, 2016 O.J. (C 202) 1 [hereinafter TFEU]. ("Save as otherwise provided in the Treaties, any aid granted by a Member State or through State resources in any form whatsoever which distorts or threatens to distort competition by favouring certain undertakings or the production of certain goods shall, in so far as it affects trade between Member States, be incompatible with the internal market.").

[57] TFEU art. 107(2)(b).

[58] Wolfgang Münchau, *The risk of a no-deal Brexit is rising, and that's no bad thing*, FIN. TIMES, (Aug. 23, 2020), https://www.ft.com/content/46087061-3fa7-4bd2-9f0d-d130fa58a409 [https://perma.cc/W7G3-8ZFT]; Max Colchester & Laurence Norman, *Boris Johnson Wants Scope to Boost Government Intervention, Rattling Brexit Talks,* WALL ST. J. (Sep. 8, 2020), https://www.wsj.com/articles/boris-johnsons-plan-to-pick-business-winners-stalls-brexit-talks-11599559858 [https://perma.cc/NU6M-FLDE]; David Dowling, *The Role of the Company in the Time of Covid-19*, 32 KING'S L.J. 37, 44–45 (2021). The final agreement requires the UK to establish a robust state-aid regime but will give it more flexibility relative to EU law. Trade and Cooperation Agreement Between the European Union and the European Atomic Energy Community, of The One Part, and The United Kingdom of Great Britain and Northern Ireland, of The Other Part, Part Two, Title XI, Ch. 3, Dec. 21, 2020, 2020 O.J. (L 444) 14. *See, e.g.*, George Peretz, *The subsidy control provisions of the UK-EU trade and cooperation agreement: a framework for a new UK domestic subsidy regime*, EU REL. L. BLOG (Dec. 28, 2020), https://eurelationslaw.com/blog/the-subsidy-control-provisions-of-the-uk-eu-trade-and-cooperation-agreement-a-framework-for-a-new-uk-domestic-subsidy-regime [https://perma.cc/6R2B-JVFS].

[59] Directive 2014/24/EU, of the European Parliament and of the Council of 26 Feb. 2014 on Public Procurement and Repealing Directive 2004/18/EC, 2014 O.J. (L 94) 65; Directive 2014/25/EU, of the European Parliament and of the Council of 26 Feb. 2014 on Procurement by Entities Operating in the Water, Energy, Transport and Postal Services Sectors and Repealing Directive 2004/17/EC, 2014 O.J. (L 94) 243; Directive 2014/23/EU, of the European Parliament and of the Council of 26 Feb. 2014 on the Award of Concession Contracts, 2014 O.J. (L 94) 1.

[60] *E.g.*, Ruth Mason, *Identifying Illegal Subsidies*, 69 AM. U. L. REV. 479, 488–89 (2019).

movement of capital, movement of persons, and the freedoms of establishment and to provide services apply. The opening of markets is often accompanied by harmonizing legislation that attempts to create equivalent protections across countries;[61] consequently, policy arguments in favor of protectionism on the country level will typically be much less persuasive within the EU.

B. *Shielding Domestic Firms from Foreign Competition and Control*

Protectionist policies can also take a passive form where governments attempt to shield local firms from foreign influence rather than actively enhancing their domestic firm's interests abroad. Such policies can be implemented both in product and financial markets. Governments may protect domestic firms from international competition by setting up import barriers such as tariffs. Laws and corporate governance institutions might be configured to favor large, domestic shareholders, such as the historical *noyaux durs* ('hard core') in France.[62] In such cases, an interconnected set of domestic owners including other corporations, financial institutions, families and foundations ensure that firms stay within domestic control. Corporate law instruments can be used to maintain ownership structures favoring domestic controlling shareholders (or coalitions of domestic shareholders). Policies that buttress such a system include permissiveness toward non-voting or super-voting stock as well as loyalty shares that increase the voting power of long-term owners.[63] If the overarching goal is to maintain a core shareholder

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[61] *E.g.,* Gelter, *supra* note 52, at 325–30; *see also* Andrew Johnston, *Varieties of Corporate Governance and Reflexive Takeover Regulation,* in PROTECTIONISM, *supra* note 3, at 161 ("EU law has always been concerned to strike a balance between market integration and the national interest in regulation.").

[62] *E.g.*, James A. Fanto, *The Role of Corporate Law in the Adaptation of French Enterprises*, 1998 COLUM. BUS. L. REV. 97, 107–08 (1998); Ben Clift, *French Corporate Governance in the New Global Economy: Mechanisms of Change and Hybridisation within Models of Capitalism*, 55 POL. STUD. 546, 550–52 (2007); Paul Davies, Edmund-Philipp Schuster & Emilie van de Walle de Ghelcke, *The Takeover Directive as a Protectionist Tool?* in PROTECTIONISM, *supra* note 3, at 106, 149.

[63] "Loyalty shares" provide that shareholders that exceed a certain duration of ownership have additional voting power. A 2014 French law that was enacted in reaction to a foreign takeover of a former national champion, made loyalty shares the default rule of publicly traded firms. Loi 2014-384 du 29 mars 2014 visant à reconquérir l'économie réelle [Law No. 2014-384 of Mar. 29, 2014 Aimed at Reclaiming the Real Economy], JOURNAL OFFICIEL DE LA REPUBLIQUE FRANÇAISE [J.O] [OFFICIAL GAZETTE OF FRANCE], Apr. 1, 2014, p. 5. *See* Marco Becht, Yuliya Kamisarenka & Anete Pajuste, *Loyalty Shares with Tenure Voting — Does the Default Rule Matter? Evidence from the Loi Florange Experiment* (Eur. Corp. Governance Inst., Working Paper No. 398, 2018), https://ssrn.com/abstract=3166494 [https://perma.cc/WNT8-NM2H]; Pargendler, *supra* note 4, at 543–44; for Italy, *see* Augusto Santoro, Ciro Di Palma, Paolo Guarneri & Alessandro Capogrosso,

structure, providing few protections against self-dealing transactions or dilutive mergers involving controlling shareholders will help to maintain concentrated ownership. Domestic shareholders will enjoy greater private benefits of control, thus generating fewer incentives for them to sell out. Thus, it will remain financially more attractive to retain a large stake instead of diversifying their holdings internationally.

Policies favoring controlling shareholders are sometimes backed up by tax law. For example, corporate taxes that exempt income streams from controlled corporations (such as intra-group dividends) make it easier for concentrated ownership structures to persist.[64] Estate and inheritance taxes also play an important role, especially regarding family firms. If a country does not levy a significant estate tax or provides exemptions for the transfer of business assets or investments upon a significant shareholder's death, family control is more likely to persist. By contrast, a confiscatory estate tax might eventually force a family to sell out when one generation passes the torch to the next.[65] This may sometimes result in a foreign entity or multinational corporation taking over.

Deviations from the One Share - One Vote Principle in Italy: Recent Developments – Multiple Voting Rights Shares and Loyalty Shares, 5 BOCCONI LEGAL PAPERS 141, 142–43 (2015); Alessio M. Pacces, *Exit, Voice and Loyalty from the Perspective of Hedge Funds Activism in Corporate Governance*, 9 ERASMUS L. REV. 199, 213 (2016); Chiara Mosca, *Should Shareholders Be Rewarded for Loyalty: European Experiments on the Wedge between Tenured Voting and Takeover Law*, 8 MICH. BUS. & ENTREPRENEURIAL L. REV. 245, 252–54 (2019).

[64] *See* Randall Morck, *How to Eliminate Pyramidal Business Groups: The Double Taxation of Intercorporate Dividends and Other Incisive Uses of Tax Policy*, 19 TAX POL'Y & ECON. 135, 153 (2005) (suggesting that intercorporate taxation of dividends resulted in the dissolution of corporate pyramids in the US); Brian R. Cheffins & Steven A. Bank, *Corporate Ownership and Control in the UK: The Tax Dimension,* 70 MOD. L. REV. 778, 787–92 (2007) (discussing how taxes historically set incentives for British blockholders to unwind their stock holdings); *e.g.*, Norbert Herzig, *Tax and the Separation of Ownership and Control – Comment on the paper by Steven Bank and Brian R. Cheffins*, in TAX AND CORP. GOVERNANCE 171, 173 (Wolfgang Schön ed., 2008) (discussing incentives set by exemption of the taxation of intra-corporate dividends and sales of ownership stakes for the retention and dissolution of large blocks of shares against the backdrop of German law).

[65] *See* Volker Grossmann & Holger Strulik, *Should continued family firms face lower taxes than other estates?*, 94 J. PUB. ECON. 87, 87–88 (2010) (surveying concerns among European policymakers about family firms being harmed by estate taxes); Henriette Houben & Ralf Maiterth, *Endangering of Businesses by the German Inheritance Tax? – An Empirical Analysis*, 4 BUR – BUS. RESEARCH 32, 32–33 (2011) (discussing possible effects of the German inheritance tax on family business); *see also* Hojong Shin, *Avoiding inheritance taxes in family firms*, 49 FIN. MGMT. 1051 (2020) (discussing a 1999 increase in Korean estate taxes that triggered significant avoidance activity through mergers).

Takeover law also plays a significant role. Following the UK example, many countries (as well as the EU[66]) have adopted a "mandatory bid rule", which requires an acquirer of control over a firm to buy out minority shareholders at the same or a similar price. While the UK initially developed this rule to allow minority stockholders to share in the private benefits of control,[67] its effect in concentrated ownership jurisdictions is largely a protectionist one. While the rule does not affect entrenched, existing controllers that maintain their position, a new acquirer that might try to build a larger stake could be caught and be required to submit a bid.[68] Sometimes the rule includes exemptions for privileged transfers within a family, among promoters or within an existing group.[69] This allows an intra-group restructuring while shutting out other, especially foreign owners.

Otherwise, the effect of takeover law depends in part on whether the country has adopted a "neutrality" or "passivity" rule that prohibits management and boards from defending against hostile takeovers.[70] Where it does not (as in Delaware[71] or Germany[72]), boards will typically be within their fiduciary obligation when engaging in actions that keep foreign owners out. Contemporary German takeover law was arguably strongly influenced by

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[66] Directive 2004/25/EC, of the European Parliament and of the Council of 21 Apr. 2004 on Takeover Bids, 2004 O.J. (L 142) 12.
[67] On the origins of the rule, *see, e.g.*, Martin Gelter & Alexandra M. Reif, *What is Dead May Never Die: The UK's Influence on EU Company Law*, 40 FORDHAM INT'L L.J. 1413, 1428 (2017).
[68] Marco Ventoruzzo, *Takeover Regulation as a Wolf in Sheep's Clothing: Taking U.K. Rules to Continental Europe*, 11 U. PA. J. BUS. L. 135, 140 (2008); Edmund-Philipp Schuster, *The Mandatory Bid Rule: Efficient, After All?*, 65 MOD. L. REV. 529, 534 (2013).
[69] For India, see, *e.g.*, Umakanth Varottil, *The Nature of the Market for Corporate Control in India* 23–27 (Nat'l Univ. Sing., Working Paper 2015/011, 2015).
[70] THE PANEL ON TAKEOVERS AND MERGERS, THE CITY CODE ON TAKEOVERS AND MERGERS, Rule 21.1(a) (8th ed. 2006), https://www.thetakeover-panel.org.uk/wp-content/uploads/2008/11/code.pdf?v=7Nov2019 [https://perma.cc/Y5VJ-NTYD] (prohibiting any frustrating action by the offeree company's board without shareholder consent once a bona fide bid has materialized).
[71] Under the *Unocal* case and its progeny, a takeover defense must be reasonable in relation to the threat posed. Unocal Corp. v. Mesa Petroleum Co., 493 A.2d 946 (Del. 1985); Air Prods. & Chems., Inc. v. Airgas, Inc., 16 A.3d 48 (Del. Ch. 2011).
[72] Wertpapiererwerbs- und Übernahmegesetz (WpÜG) [Securities Acquisition and Takeover Act], § 33(1) (2001) (Ger.) (permitting the supervisory board to approve defensive actions); *see* Guido Ferrarini & Geoffrey P. Miller, *A Simple Theory of Takeover Regulation in the United States and Europe*, 42 CORNELL J. INT'L L. 301, 321–23 (2009) (discussing the German implementation). An EU report of 2013 found that Belgium, Denmark, Germany, Hungary, Luxembourg, the Netherlands, and Poland did not implement the (optional) passivity rule. MARCCUS PARTNERS, EU COMM'N, THE TAKEOVER BIDS DIRECTIVE ASSESSMENT REPORT 64–66 (2013); *see also* Davies et al., *supra* note 62, at 135–38 (surveying transposition choices).

concerns that German firms would be asymmetrically vulnerable to being taken over by foreign firms, especially in light of Vodafone's takeover of Mannesmann in 2000.[73] The EU Takeover Directive's reciprocity option was designed to enable Member States to create a level playing field for firms subject to a takeover bid from a (foreign) firm not applying the neutrality rule.[74]

Within corporate law, employee representation on the board also sometimes serves as a protectionist instrument. Not only does it not extend to workers outside Germany,[75] but employee representatives are typically a constituency that does not favor a change in ownership that might lead to a reduction of jobs. Employee representatives and the unions that (*de facto* or *de jure*) nominate them are typically rooted in the socioeconomic structure of the country. They will often be able to maintain alliances with domestic shareholders, politics and the media to prevent foreign control.

Finally, the bluntest instrument against foreign ownership are foreign direct investment (FDI) laws, which several important jurisdictions have tightened in recent years, including both the US[76] and EU.[77] The expansion of Italy's 2012 Golden Power Law[78] in 2020 to include acquisitions relating

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[73] John W. Cioffi, *Restructuring "Germany Inc.": The Politics of Company and Takeover Law Reform in Germany and the European Union,* 24 L. & POL'Y 355, 378, 385–86 (2002).

[74] According to the "reciprocity" principle, Member States exempt companies from applying the neutrality or breakthrough rules to opt out of these regimes when they are subject to an offer by a firm not applying these rules. Directive 2004/25/EC, art. 12(2). *See* Matteo Gatti, *Optionality Arrangements and Reciprocity in the European Takeover Directive,* 5 EUR. BUS. ORG. L. REV. 553, 572–75 (2005); Davies et al., *supra* note 62, at 105–06.

[75] See in particular the CJEU's decision in Case C-566/115, Konrad Erzberger v. TUI AG, EU:C:2017:562 (finding that Germany's restriction of codetermination rights to employees within Germany is not in violation of EU law); *see, e.g.*, Martin Höpner, *Curbing Negative Integration: German supervisory board codetermination does not restrict the common market*, 25 MAASTRICHT J. EUR. & COMP. L. 246 (2018); Sara Lafuente Hernández & Zane Rasnača, *Can Workers' Rights Ever Catch up? The Erzberger Case and EU Cross-border reality,* 48 INDUS. L.J. 98, 100–01 (2018) (discussing the territoriality principle under German codetermination law).

[76] On the expansion of the Committee on Foreign Investment in the United States (CFIUS) review process, *see* Jeffrey N. Gordon & Curtis J. Milhaupt, *China as a 'National Strategic Buyer': Toward a Multilateral Regime for Cross-Border M&A*, 2019 COLUM. BUS. L. REV. 192, 232.

[77] Council Regulation 2019/452, of the European Parliament and of the Council of 19 Mar. 2019, Establishing a Framework for the Screening of Foreign Direct Investments into the Union, 2019 O.J. (L 791) 1. *See, e.g.*, Wolf Zwartkruis & Bas de Jong, *The EU Regulation on Screening of Foreign Direct Investment: A Game Changer?*, 31 EUR. BUS. L. REV. 447, 467–70 (2020).

[78] Decreto-Legge [Decree-Law], 15 marzo 2012, n. 21 (It.).

to financial industry and food security is another recent example.[79] This law even allows the curtailment of certain acquisitions from other EU countries following changes implemented during the COVID-19 crisis.[80]

4. IS ECONOMIC NATIONALISM ALWAYS A THREAT?

A. *Vices of State Interference in Corporate Governance*

From the normative perspective of shareholder primacy and the convergence model, government ownership and interference (more generally) does not seem desirable for several reasons. First, government ownership is thought to be inefficient because government does not normally have a profit motive.[81] This means that decisions made by such firms will be driven by other, mainly political considerations, which detract from an economic efficiency goal. This is also true when the government can influence or veto business decisions of major firms with a significant minority stake. In such cases, profit-oriented majority shareholders will sometimes have to negotiate plans with the government. If the government insists on the continuation of a loss-making firm to preserve voters' jobs, arguably resources will be misallocated and cannot be shifted to a more productive use, e.g., because goods are produced according to the preferences of politicians rather than market demand.[82]

Companies that deviate far from profit goals will find it hard to attract outside investment, thus encouraging the government to intervene further. This is true where, as is often the case, careers in politics and politically connected firms are intertwined, with functionaries moving between both tracks.[83] High-ranking individuals will likely engage in rent-seeking; because market-oriented profit motives are at best attenuated, competition will not be

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[79] Decreto-Legge [Decree-Law], 8 aprile 2020, n. 23 (It.). *See, e.g.*, Simon Clark & Ben Dummett, *Coronavirus Accelerates European Efforts to Block Foreign Takeovers*, WALL ST. J. (Apr. 10, 2020), https://www.wsj.com/articles/coronavirus-accelerates-european-efforts-to-block-foreign-takeovers-11586516403 [https://perma.cc/D35M-KZZA]; Francesca Torricelli & Pietro Missanelli, *Italian Law: Corporate Transparency and 'Golden Power' Provisions in Emergency Legislation for Coronavirus Disease 2019*, NAT'L L. REV. (Apr. 23, 2020), https://www.natlawreview.com/article/italian-law-corporate-transparency-and-golden-power-provisions-emergency-legislation [https://perma.cc/9GCY-C4QE].

[80] Decreto-Legge [Decree-Law], 8 aprile 2020, n. 23 (It.); Clark & Dummett, *supra* note 79.

[81] *E.g.*, Shleifer, *supra* note 43, at 138 (noting the weak incentives of government employees to reduce cost and to innovate).

[82] Andrei Shleifer & Robert W. Vishny, *Politicians and Firms*, 109 Q. J. ECON. 995, 996 (1994); D. Daniel Sokol, *Competition Policy and Comparative Corporate Governance of State-Owned Enterprises*, 2009 BYU L. REV. 1713, 1721 (2009).

[83] Lin & Milhaupt, *supra* note 44, at 737–43 (discussing how careers in the Chinese Communist Party and management of state-controlled firms are intertwined).

primarily for products and profits, but mainly for political gain. In democracies, politically connected managers will at least have to help their parties to curry favor with the electorate, to which a successfully run state-owned enterprise can contribute.[84] In one-party states, political motives diverge even more from the interest of (potential) voters. Thus, competition will likely only be for primarily individual advancement within the political hierarchy.

Second, government ownership or interference may distort the political economy of corporate governance, both on the level of legislation and adjudication. Legislation – which will typically apply to all firms, not only those under government influence – will likely favor controlling shareholders, including both the government itself and politically connected large shareholders.[85] These will have the ability to influence corporate law legislation because of their political clout. In addition, courts and regulators are unlikely to challenge the government as a controlling shareholder or politically connected managers.[86] Consequently, doctrines protecting investors against opportunism of corporate controllers may (depending on circumstances) remain underdeveloped.[87]

Third, government interference may serve the interests of highly organized local interest groups. Takeover law, which I have touched upon above,[88] sometimes serves the interests of domestic interest groups such as management and labor, while outside investors, including foreign ones, will oppose takeover defenses.[89] Where institutional investors are not an

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[84] But note that politicians may cater to specific interest groups rather than the median voter, thus further distorting social choice. Shleifer & Vishny, *supra* note 82, at 997; Mariana Pargendler, Aldo Musacchio & Sergio G. Lazzarini, *In Strange Company: The Puzzle of Private Investment in State-Controlled Firms*, 46 CORNELL INT'L L.J. 569, 576 (2013).

[85] Mariana Pargendler, *State Ownership and Corporate Governance*, 80 FORDHAM L. REV. 2917, 2919, 2973 (2012).

[86] *See* Marcel Kahan & Edward B. Rock, *When the Government is the Controlling Shareholder*, 89 TEX. L. REV. 1293, 1324 (2011) (discussing Delaware's likely reluctance to challenge the federal government); Michael Firth, Oliver M. Rui & Wenfeng Wu, *The Effects of Political Connections and State Ownership on Corporate Litigation in China*, 54 J. L. & ECON. 573 (2011) (finding that politically connected defendants have an advantage in corporate litigation in China); regarding securities regulators, *see* Pargendler et al., *supra* note 84, at 584.

[87] Pargendler, *supra* note 85, at 2948–51 (comparing the cases of Italy and Brazil and suggesting that the role of the state as a controlling shareholder in important companies had an impact on the development of the law).

[88] *Supra* notes 66–74 and accompanying text.

[89] *See* Klaus J. Hopt, *European Company and Financial Law: Observations on European Politics, Protectionism, and the Financial Crisis,* in PROTECTIONISM, *supra* note 3, at 13, 21 (discussing the influence of Volkswagen on Germany's position on the EU draft Takeover Directive).

important domestic interest group (as it is in the UK[90]), takeover law is likely to tilt in favor of insiders. A well-known example is France's 2014 law making loyalty shares the default in publicly traded firms.[91] It was passed because of a widely discussed takeover of a French firm by an Indian conglomerate.[92]

In addition to important local shareholders or employees, another interest group using corporate law for rent-seeking purposes could be legal professionals such as lawyers or civil law notaries.[93] An example might be the prevention of the use of foreign legal forms within a country. Historically, many Continental European countries prevented the creation of pseudo-foreign corporations. An entrepreneur would not be able to set up a business entity in country A in order to do business in country B, thus taking advantage of A's corporate law.[94] (By contrast, in the US it has been possible since the late 19th Century to set up a corporation in one state to do business in other state.)[95] The market for corporate law was tenuously opened up with a series of cases of the CJEU starting with *Centros* in 1999.[96] This case and its progeny effectively allowed incorporations in other Member States, even if the real seat or main business was elsewhere.[97] In spite of the *Inspire Art* case,[98] it is still debated to what extent Member States can apply national laws to

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[90] John Armour & David A. Skeel, Jr. *Who Writes the Rules for Hostile Takeovers, and Why? – The Peculiar Divergence of U.S. and U.K. Takeover Regulation,* 95 GEO. L.J. 1727, 1767–76 (2007) (identifying institutional investors as the key interest group behind the UK City Code).
[91] *Loi 2014-384 du 29 mars 2014 visant à reconquérir l'économie réelle*, JOURNAL OFFICIEL DE LA REPUBLIQUE FRANÇAISE (2014).
[92] Pargendler, *supra* note 4, at 543.
[93] For example, formal requirements when creating a business entity and procedures necessary for corporate transactions could be maintained to allow rent-seeking opportunities for civil law notaries to persist. *See, e.g.*, Marco Becht, Luca Enriques & Veronika Korom, *Centros and the Cost of Branching*, 9 J. CORP. L. STUD. 171, 176, 178, 181, 182, 184 (2009); Reiner Braun, Horst Eidenmüller, Andreas Engert & Lars Hornuf, *Does Charter Competition Foster Entrepreneurship? A Difference-in-Difference Approach to European Company Law Reforms*, 51 J. COMMON MKT. STUD. 399, 402, 404–05 (2013).
[94] To that end, Member States such as Germany used the "real seat theory" to determine which country's laws apply to a legal form. *E.g.*, Martin Gelter, *Centros, the Freedom of Establishment for Companies and the Court's Accidental Vision for Corporate Law*, in EU LAW STORIES 309, 309–11 (Fernanda Nicola & Bill Davies eds., 2017).
[95] *E.g.*, Christopher Grandy, *New Jersey Corporate Chartermongering*, *1875–1929,* 49 J. ECON. HIST. 677 (1989).
[96] Case C-212/97, Centros Ltd. v Erhvervs-og Selskabsstyrelsen, 1999 E.C.R. I-1459; Case C-208/00, Überseering BV v. Nordic Construction Co. Baumanagement GmbH, 2002 E.C.R. I-9919; Case C-167/01, Kamer van Koophandel en Fabrieken voor Amsterdam v. Inspire Art Ltd., 2003 E.C.R. I-10155 [hereinafter *Inspire Art*].
[97] *E.g.*, Becht et al., *supra* note 93, at 171–72.
[98] *Inspire Art*, *supra* note 96.

foreign firms in order to protect "public interests."[99] Arguably, the "real seat doctrine" protected mainly the law of the Member States using it from regulatory competition, and interest groups such as domestic lawyers or civil law notaries deriving business from it.[100] In general, when local interest groups engage in rent-seeking, they obtain profits exceeding those that would garner in a market-oriented environment. Incentives for work and innovation may be reduced as time and energy will rather be invested in political negotiations instead of the improvement of corporate processes and products.

Fourth, restrictions on cross-border trade may make products costly and inhibit global supply chains. A parallel argument applies to cross-border ownership and corporate investment. At times it might be difficult for companies to obtain much-needed capital.[101] As discussed in the context of the convergence debate in section 2, certain firms sought a more open corporate governance framework to tap international capital markets and attract outside investment. If the government prevents the inflow of foreign capital to protect certain firms, the same barriers may prevent other, more internationally oriented businesses from growing.[102]

B. *Economic Reasons for Government Ownership and Control*

The following sections will explore reasons for protectionism and economic nationalism. The first set of rules are overtly political and can be considered very briefly here due to their obviousness. This category includes national security concerns, including access to key resources and infrastructure (e.g., 5G, vaccines, medical supplies),[103] but also economic reasons.

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[99] For an overview, *see* CARSTEN GERNER-BEUERLE, FEDERICO MUCCIARELLI, EDMUND SCHUSTER & MATHIAS SIEMS, STUDY ON THE LAW APPLICABLE TO COMPANIES 206–15 (European Commission ed. 2016).

[100] Harald Halbhuber, *National Doctrinal Structures and European Company Law*, 38 COMMON MKT. L. REV. 1385, 1411–14 (2001).

[101] Gordon, *supra* note 19; Stulz, *supra* note 31 and accompanying text.

[102] A government may of course offer competing legal regimes that permit firms seeking to attract international investors to opt into a regime more suitable for this purpose. *See* Ronald J. Gilson, Henry Hansmann & Mariana Pargendler, *Regulatory Dualism as a Development Strategy: Corporate Reform in Brazil, the United States, and the European Union*, 63 STAN. L. REV. 475 (2011).

[103] *E.g.*, James A. Lewis, *New Objectives for CFIUs: Foreign Ownership, Critical Infrastructure, and Communications Interception*, 57 FED. COMM. L.J. 457, 457 (2005) (discussing national security issues in communication firms); Joseph Mamounas, *Controlling Foreign Ownership of U.S. Strategic Assets: The Challenge of Maintaining National Security in a Globalized and Oil Dependent World*, 13 L. & BUS. REV. AM. 381, 385–86 (2007) (discussing national security issues raised by foreign ownership in the defense industry); Christopher S. Kulander, *Intruder Alert! Running the Regulatory Gauntlet to Purchase, Own, and Operate American Energy and Mineral Assets by Foreign Entities*, 46 TEX. TECH L. REV. 995, 997, 1004–07 (2014) (discussing limitations on foreign ownership in the oil and gas industry).

There are at least three types of the latter kind, namely externalities created by key infrastructure, the maintenance of supply chains, and protectionism as a development strategy for infant industries.

First, a reason for government in ownership in key firms could be that they provide a positive externality for other firms. A classic case are public goods, such as the services provided by infrastructure. For example, an airport serving as a major hub may attract regional or international headquarters.[104] Similarly, a well-functioning rail or road network will bring products closer to customers and generally enhance the competitive location of nearby firms. Especially for a smaller country, it may be important to maintain a well-connected airport and infrastructure to enhance the competitive position of its economy. State ownership is not necessarily the only way of ensuring the maintenance of infrastructure. A theoretical alternative could be ownership by the benefiting businesses. However, in most cases this will not be feasible because of high transaction and coordination cost, especially in a fluid economy where firms will enter and exit the market, and where the degree of benefits reaped by each firm will change over time. Some firms will have incentives to free-ride and not help to subsidize infrastructure. Non-contributing firms would likely have incentives to overuse it. Consequently, there is a good case for government ownership.

Second, protectionist policies may serve the maintenance of important supply chains. Even before the COVID-19 crisis, there was a debate about an increasing dependence on China, e.g. in the pharmaceutical and automobile industries,[105] as well as the delivery of raw materials such as certain

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[104] Germà Bel & Xavier Fageda, *Getting there fast: globalization, intercontinental flights and location of headquarters*, 8 J. ECON. GEO. 471 (2008) (finding that the availability of international flight connection has a large effect on headquarter choices); *see also* Kenneth Button & Somik Lall, *The Economics of Being an Airport Hub City*, 5 RES. TRANSP. ECON. 75 (1999) (finding that an airport hub correlates with more high-tech employment); Richard Florida, Charlotta Mellander & Thomas Holgersson, *Up in the air: the role of airports for regional economic development*, 54 ANNALS REGIONAL SCI. 197 (2015) (finding that airports add to regional GDP within the US).

[105] Joe McDonald, *Companies prodded to rely less on China, but few respond*, AP NEWS (June 29, 2020), https://apnews.com/bc9f37e67745c046563234d1d2e3fe01[https://perma.cc/GK9Q-E73T]; Shinzo Abe, Prime Minister of Japan, Statement at Council on Investments for the Future (Mar. 5, 2020), https://japan.kantei.go.jp/98_abe/actions/202003/_00009.html [https://perma.cc/9YSA-EKNP]; Philip Blenkinsop, *EU Trade Chief Urges for More Diverse Supply Chains After Crisis*, US NEWS (Apr. 16, 2020, 10:15 AM), https://money.usnews.com/investing/news/articles/2020-04-16/eu-trade-chief-urges-for-more-diverse-supply-chains-after-crisis; Vasileios Theodosopoulos, *The Geopolitics of Supply: Towards a new EU approach to the security of supply of critical raw materials?*, POL'Y BRIEF (Inst. for Eur. Studies, Brussels) July 2020.

minerals.[106] This led some governments, such as the Trump administration in the U.S.,[107] to develop plans to 're-shore' spread-out value chains or key industries.[108] COVID has strengthened such movements, e.g. in Japan.[109] Moreover, countries may use national security concerns to control multinational firms, especially when the firm has connections to a foreign government or owners under such influence.[110] From an economic perspective, it may be important that foreign governments and competitors are not in the position to shut down a domestic firm supplying a key resource. The government will often be in a better position than firms themselves to prevent supply

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[106] Yujia He, *The trade-security nexus and U.S. policy making in critical minerals*, 59 RESOURCES POL'Y 238, 238 (2018); Exec. Order No. 13817, 83 Fed. Reg. 60835 (Dec. 20, 2017).

[107] Robert E. Lighthizer, *The Era of Offshoring U.S. Jobs Is Over*, N.Y. TIMES (May 11, 2020), https://www.nytimes.com/2020/05/11/opinion/coronavirus-jobs-offshoring.html [https://perma.cc/D7JR-QPQ2]; Andrea Shalal et al., *U.S. mulls paying companies, tax breaks to pull supply chains from China*, REUTERS (May 18, 2020), https://www.reuters.com/article/us-usa-china-supply-chains/u-s-mulls-paying-companies-tax-breaks-to-pull-supply-chains-from-china-idUSKBN22U0FH [https://perma.cc/TRR6-EWZZ]; Geoffrey Gertz, *How to Deglobalize*, FOREIGN POL'Y (July 24, 2020, 4:19 PM), https://foreignpolicy.com/2020/07/24/how-to-deglobalize [https://perma.cc/4YXE-K759].

[108] *The steam has gone out of globalisation*, THE ECONOMIST (Jan. 26, 2019), https://www.economist.com/leaders/2019/01/24/the-steam-has-gone-out-of-globalisation [https://perma.cc/9HY5-Z23D]; *Multinational companies are adjusting to shorter supply chains: The risks of not knowing who supplies your supplier*, THE ECONOMIST (July 11, 2019), https://www.economist.com/special-report/2019/07/11/multinational-companies-are-adjusting-to-shorter-supply-chains [https://perma.cc/W34F-VTG5].

[109] Simon Denyer, *Japan helps 87 companies to break from China after pandemic exposed overreliance*, WASH. POST (July 21, 2020), https://www.washingtonpost.com/world/asia_pacific/japan-helps-87-companies-to-exit-china-after-pandemic-exposed-overreliance/2020/07/21/4889abd2-cb2f-11ea-99b0-8426e26d203b_story.html [https://perma.cc/4DUT-FHZB]; Julian Ryall, *Leave China? No thanks, some Japanese firms say to Tokyo's cash incentives*, S. CHINA MORNING POST (May 13, 2020, 7:00 AM), https://www.scmp.com/week-asia/economics/article/3083988/leave-china-no-thanks-some-japanese-firms-say-tokyos-cash [https://perma.cc/3DL7-ZQYF].

[110] *Will TikTok Survive?*, THE ECONOMIST (Sept. 19, 2020), https://www.economist.com/leaders/2020/09/17/will-tiktok-survive [https://perma.cc/66RD-NPW9] (discussing the Trump administration's effort to establish US control of the social media platform TikTok and suggesting that more governments will demand domestic control of key firms in other industries such as mining); *but see* Georgia Wells, *TikTok Download Ban Is Blocked by Second Judge*, WALL ST. J. (Dec. 8, 2020), https://www.wsj.com/articles/tiktok-download-ban-is-blocked-by-second-judge-11607390564 [https://perma.cc/2YJ2-7ZZ2] (discussing the District of Columbia District Court's recent injunction against the Trump administration's restrictions on TikTok).

chains from being choked if a foreign competitor (possibly supported by its own government) seeks to obtain a monopoly position.

A third economic reason may be to prop up domestic firms as a development strategy before exposing them to international competition. Some countries have continued to use this strategy to grow their economy by first developing firms as "national champions" before opening them up for competition.[111] This may be done through direct government ownership or by supporting domestic controlling shareholders. While such companies develop products and grow, a country might shield them from foreign competition through tariffs or other restraints of trade before exposing them to the world market. In recent decades, international policy-making organizations such as the World Bank and the IMF have advised countries that openness to trade would be beneficial, and trade agreements within the framework of the WTO have resulted in much more global markets.[112] In parallel, ownership of firms has integrated across countries, meaning that many firms today are

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[111] *See generally* HA-JOON CHANG, KICKING AWAY THE LADDER: DEVELOPMENT STRATEGY IN HISTORICAL PERSPECTIVE (2002). *See also* Richard Baldwin, *Trade and Industrialization after Globalization's Second Unbundling, in* GLOBALIZATION IN AN AGE OF CRISIS: MULTILATERAL ECONOMIC COOPERATION IN THE TWENTY-FIRST CENTURY 165, 171–73 (Robert C. Feenstra & Alan M. Taylor eds., 2013); Richard Baldwin, *Global supply chains: Why they emerged, why they matter, and where they are going*, *in* GLOBAL VALUE CHAINS IN A CHANGING WORLD 13, 24 (Deborah K. Elms & Patrick Low eds., 2013) (both noting that before globalization of supply chains, countries would have to industrialize to become competitive, while afterwards that could benefit by joining a supply chain); Curtis J. Milhaupt & Mariana Pargendler, *Governance Challenges of Listed State-Owned Enterprises Around the World: National Experiences and a Framework for Reform*, 50 CORNELL INT'L L.J. 473, 518–29 (2017) (discussing Singapore's and China's experience with SOEs); Lars Sorgard, *The Economics of National Champions*, 3 EUR. COMPETITION J. 49, 49–50 (2007) (discussing the shift from national champion policies to open market policies in Europe); Paul Guest & Dylan Sutherland, *The impact of business group affiliation on performance: Evidence from China's 'national champions'*, 34 CAMBRIDGE J. ECON. 617 (2010) (exploring the business success of China's national champions). On the larger theory of state-led industrialization by "developmental states see for example Merideth Woo-Cumings, *Introduction,* in THE DEVELOPMENTAL STATE 1 (Merideth Woo-Cumings ed. 1999).

[112] *E.g.*, Zakia Afrin, *Foreign Direct Investments and Sustainable Development in the Least-Developed Countries*, 10 ANN. SURV. INT'L & COMP. L. 215, 217, 223, 224–25 (2004); Daniil E. Fedorchuk, *Acceding to the WTO: Advantages for Foreign Investors in the Ukrainian Market*, 15 N.Y. INT'L L. REV. 1, 2, 12, 39 (2002); Asha Kaushal, *Revisiting History: How the Past Matters for the Present Backlash Against the Foreign Investment Regime*, 50 HARV. INT'L L.J. 491, 505–07 (2009); Tracy A. Kaye, *Taxation and Development Incentives in the United States*, 62 AM. J. COMP. L. 617, 623–26 (2014) (all showing how international organizations have emphasized the advantages of foreign direct investment and put pressure on developing countries to permit it); *see also* WORLD BANK, LEGAL FRAMEWORK FOR THE TREATMENT OF FOREIGN INVESTMENT (1992).

no longer domestically owned.[113] Still, openness to international trade and investment may not always be the best development or growth strategy. Some important jurisdictions, including China or Singapore, continue to hold on to firms closely connected with or owned by a government entity.[114] An aggressive strategy of this type allows a country to project economic power in the international sphere through economically dominant firms propped up by the government with financial support and tax breaks. The question is, of course, to what extent this is possible in a globalized economy when such strategies may undercut profit-making in some cases and render companies potentially less profitable if they serve primarily political interests.

C. *Competition and Investment With Non-Financial Motives*

A key, but maybe unspoken assumption of the debate about financial integration and convergence in corporate governance is that market participants, especially investors, operate on a level playing field and pursue primarily financial and business interests.[115] But this is not always true. Some foreign firms may pursue the interest of their government, especially if it holds significant shares. This is often alleged, e.g., for Chinese firms, which tend to have significant government ownership and seem to purchase firms internationally to pursue political goals to expand political interests.[116] In recent years, it is increasingly debated to what extent some countries (including China) use investment in other countries to advance political influence overseas.[117] Governments that pursue political interests with the ownership of companies that engage in investment overseas may seek to extend their influence and hence prop up these companies. This has been debated in the context of Chinese firms as "National Strategic Buyers,"[118] but it may also be true for some sovereign wealth funds.[119] Arguably, Chinese buyers in

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[113] *See* DE LA CRUZ ET AL., *supra* note 46, at 27; Aminadav & Papaioannou, *supra* note 46.

[114] Chen, *supra* note 45 and accompanying text.

[115] Regarding sovereign wealth funds, *see* Lawrence Summers, *Funds That Shake Capitalist Logic*, FIN. TIMES (July 29, 2007), https://www.ft.com/content/bb8f50b8-3dcc-11dc-8f6a-0000779fd2ac [https://perma.cc/7SGT-RQRJ]; Gordon & Milhaupt, *supra* note 76, at 196.

[116] Gordon & Milhaupt, *supra* note 76, at 218–26.

[117] *See generally* Wesley N. Harris, *China Energy: A Crossroads Historiography*, 37 T. MARSHALL L. REV. 255, 259, 282 (2012); Kent Hughes Butts, *Geopolitics of Resource Scarcity*, 3 PENN ST. J.L. & INT'L AFF. 1, 6 (2015); Dimitrije Canic, Comment, *The Balkan Loophole: China's Potential Circumvention of EU Protectionism*, 27 U. MIAMI BUS. L. REV. 99, 101–17 (2018); Daniel Michaels, *Behind China's Decade of European Deals, State Investors Evade Notice*, WALL ST. J. (Sept 30, 2020), https://www.wsj.com/articles/behind-chinas-decade-of-european-deals-state-investors-evade-notice-11601458202 [https://perma.cc/2LRX-KWYQ].

[118] Gordon & Milhaupt, *supra* note 76, at 212–26.

[119] *See generally* Paul Rose, *The Political and Governance Risks of Sovereign Wealth Funds*, 4 ANNALS CORP. GOV. 244, 312–20 (2019).

international M&A transactions sometimes hope to gain access to a foreign technology through the back door.[120] Ownership of local firms by Chinese or Russian owners, or by a sovereign wealth fund from an OPEC country could raise concerns because this type of capital may not be in the best interest of the country where this money is invested.[121]

The problem here may be that such firms will not be subject to the same rules and market forces as financially oriented strategic investors. Foreign firms and sovereign wealth pursuing political goals of their government will likely receive considerable political support. This could result in better financial backing or an uncontested position in their home market that increases their resources.[122] They may also be able to call in political favors in their home country at the expense of competitors' fitness. Actors in the political sphere may, for example, be inclined to bail them out in situations of dire financial need. Companies with such political backing enjoy a competitive advantage over purely private firms. In a contest for control over a firm abroad, they would likely have an advantage compared to purely financially interested competing bidders. Defensive actions on the part of the country where such companies are attempting to gain a foothold may therefore be in the country's best interests. Gordon and Milhaupt have proposed a multilateral regime applying where firms with significant state involvement would have to commit to the pursuit of exclusively financial and commercial objectives to be eligible to engage in a cross-border merger.[123] While the introduction of such a system on the international level is unlikely, target countries could in principle integrate it into their national law.[124]

D. *Protecting the Socioeconomic System*

Another reason for protectionism is a concern for the country's socio-economic system as well as its economic stability. Different elements of a corporate governance system are often seen as part of a set of institutional complementarities. From this perspective, concentrated ownership is not necessarily a dysfunctional consequence of bad law or politics but serves a useful

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[120] Gordon & Milhaupt, *supra* note 76, at 197–99, 212–13, 218–22.

[121] On such concerns prior to COVID-19, *see, e.g.*, Klaus J. Hopt, *European Company and Financial Law: Observations of European Politics, Protectionism, and the Financial Crisis*, *in* PROTECTIONISM, *supra* note 3, at 13, 14; on sovereign wealth funds, *see* Heike Schweizer, *Sovereign Wealth Funds – Market Investors or 'Imperialist Capitalists'? The European Response to Direct Investments by Non-EU State-Controlled Entities*, *in* PROTECTIONISM, *supra* note 3, at 250, 255–57; Joongi Kim, *Fears of Foreign Ownership: The Old Face of Economic Nationalism,* 27 SAIS REV. 167, 169 (2007).

[122] *E.g.*, Sokol, *supra* note 82, at 1730; *see also* Gordon & Milhaupt, *supra* note 76, at 247 (suggesting that national strategic buyers have a competitive advantage).

[123] Gordon & Milhaupt, *supra* note 76, at 245.

[124] *Id.* at 246 ("Compliance with the eligibility regime could be woven into national cross-border merger review schemes through local law.").

function in combination with other aspects of corporate governance. Financial systems have sometimes been classified into 'arm's length' (or outsider) and a 'control-oriented' (or insider) system.[125] Arm's length systems rely on business relations negotiated in individual interactions, where public markets play the most important role for firms seeking capital. Investors thus rely mainly on the enforcement of their legal rights for protection.[126] By contrast, in control-oriented systems, the major providers of finance are typically banks or large shareholders. These will typically have enough leverage to intervene directly due to their large equity or debt stakes invested in the firm in question.[127] For lenders and borrowers it thus becomes important to foster long-term relationships with each other that are not common in arm's length systems.[128]

The 'varieties of capitalism' theory broadens this analysis by including labor and other aspects into the set of institutional complementarities and generally classifies countries into "liberal" and "coordinated" economic systems.[129] In systems operating under 'liberal' capitalism (which tend to be arm's length financial systems), workers tend develop generally transferable skills that come with a great deal of flexibility, but less collective representation by unions. By contrast, 'coordinated' capitalist systems typically have strong labor and employment law. Here, workers typically enjoy a relatively powerful bargaining position of workers that tends to go hand in hand with

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[125] *E.g.*, Erik Berglöf, *A Note on the Typology of Financial Systems*, *in* COMPARATIVE CORP. GOVERNANCE 151, 159–64 (Klaus J. Hopt & Eddy Wymeersch eds., 1997); DIGNAM & GALANIS, *supra* note 26, at 64; Christian Leuz, *Different approaches to corporate reporting regulation: How jurisdictions differ and why*, 40 ACCT. & BUS. RES. 229, 236–37 (2010); *see also* Reinhard H. Schmidt & Marcel Tyrell, *Financial systems, corporate finance and corporate governance*, 3 EUR. FIN. MGMT. 333, 334 (1997) (contrasting market-based and bank-based financial systems); Martin Gelter, *The Dark Side of Shareholder Influence: Managerial Autonomy and Stakeholder Orientation in Comparative Corporate Governance*, 50 HARV. INT'L L.J. 129, 176–81 (2009) (describing institutional complementarities between the strength of shareholder and labor power).

[126] Schmidt & Tyrell, *supra* note 125, at 343; Leuz, *supra* note 125, at 237.

[127] Berglöf, *supra* note 125, at 159–64; *see also* Raghuram G. Rajan & Luigi Zingales, *Which Capitalism? Lessons from the East Asian Crisis*, 11 J. APPLIED CORP. FIN. 40, 41 (1998) ("Relationship-based systems can survive in environments where laws are poorly drafted or contracts not enforced.").

[128] Rajan & Zingales, *supra* note 127, at 40; Leuz, *supra* note 125, at 237; DIGNAM & GALANIS, *supra* note 26, at 68 (discussing bank-based corporate governance systems); *see also* FRANKLIN ALLEN & DOUGLAS GALE, COMPARING FINANCIAL SYSTEMS 19–22 (2000) (analyzing advantages and disadvantages).

[129] *See generally* Peter A. Hall & David Soskice, *An Introduction to Varieties of Capitalism*, *in* VARIETIES OF CAPITALISM 8–9 (Peter A. Hall & David Soskice eds., 2001); Richard W. Carney, CONTESTED CAPITALISM 3 (2010) (both discussing the distinction between the two types of capitalism).

the concentrated ownership of control-oriented financial systems.[130] In these systems, we can observe a greater role of groups aggregating the interests of e.g. workers and representing them collectively vis-à-vis associations representing business interests and unions. These groups have long-term relations with each other and engage in collective bargaining agreements that cement the country's socioeconomic system.[131] One aspect of this is that in "coordinated" systems, labor relations are sometimes different because firms make greater use of internal labor markets, and they encourage firm-specific human capital development of employees to a greater extent. Long-term cooperative agreements are a prerequisite because of the risk of opportunism.[132] For example, in the context of takeovers, the board having the ability to defend against hostile takeovers is more consistent with long-term implicit contracts with workers.[133] In other words, shareholders and employees must be able to commit to each other on the collective level.[134] Countries that enjoy a modicum of success will likely have found a certain balance between capital and labor that is effective in the domestic context, both on the economic and political level.

Protectionism may sometimes serve the purpose of shielding a country's variety of capitalism from change, or to protect socioeconomic stability in the country. The first point relates to the argument of institutional complementarities just laid out. If foreign influence or intrusion undermines a complementary building block, the economic system overall may not work as well anymore, thus harming competitiveness in the country in the long run. This may concern "coordinated" systems more than arm's length ones. Institutional investors from a more finance-oriented system may not interact with institutions in the country in the same way as domestic owners. While a controlling family may, for example, accept long-term deals with domestic workers or suppliers because of its integration into the domestic economic

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[130] *E.g.*, MARK J. ROE, POLITICAL DETERMINANTS OF CORPORATE GOVERNANCE 52 (2003); Mariana Belloc & Ugo Pagano, *Co-evolution of politics and corporate governance*, 29 INT'L REV. L. & ECON. 106, 107 (2009).

[131] Hall & Soskice, *supra* note 129, at 16–17; *see* Carney, *supra* note 129.

[132] DIGNAM & GALANIS, *supra* note 26*,* at 75–76.

[133] Johnston, *supra* note 61, at 164–65.

[134] It is not entirely clear whether and under which circumstances a dispersed or a concentrated ownership structure is more conducive to commitment. For a theoretical model, *see* Giulio Ecchia, Martin Gelter & Piero Pasotti, *Corporate Governance, Corporate and Employment Law, and the Costs of Expropriation*, 8 REV. L. & ECON. 457 (2012); *see also* Gelter, *supra* note 125, at 176–81; Belloc & Pagano, *supra* note 130; Martin Gelter, *Corporate Governance: Old and New*, *in* UNDERSTANDING THE COMPANY 37, 48–50 (Barnali Choudhury & Martin Petrin eds., 2017); Mark J. Roe & Massimiliano Vatiero, *Corporate Governance and its Political Economy*, *in* THE OXFORD HANDBOOK OF CORP. L. AND GOVERNANCE 56, 67–70 (Jeffrey N. Gordon & Wolf-Georg Ringe eds., 2018); *see also* Ugo Pagano, *The Evolution of the American Corporation and Global Organizational Biodiversity*, 35 SEATTLE U.L. REV. 1271, 1279–90 (2012) (discussing historical origins).

and political network,[135] foreign financial investors may have different objectives. A hedge fund, but also a pension fund attempting to produce returns for savers back home, may not have the same conduct vis-à-vis firms in a 'coordinated' country as a local investor. They may have less patience for cozy labor relations, e.g., in some of Europe, that seem to have served these countries well.[136] While breaking up such a system may at times be advantageous, the question is in part at what time and what pace such a system should be broken up.

E. *Protecting Political Stability*

Another aspect is foreign investors' or firms' interaction with the national business environment, which in extreme cases could have an impact on socioeconomic stability.[137] One concern relates to what is sometimes described as the "footlooseness" thesis of multinational firms.[138] For example, when a multinational acquirer takes over a firm in a target country, it is not guaranteed that operations in the target country will continue as they did before. An international merger serves the purpose of benefiting from synergies, among other things. Multiple factors will influence whether a firm whose operations span several countries will maintain operations everywhere to the same degree, including the cost of labor and other production factors, political stability, and the skills of the workforce. However, all else being equal, connections between the firm's leadership and the location's political and social ecosystem will matter. A company that is mainly integrated into the socio-political and personal network of country A will be more likely to shut down operations (or parts of operations) in country B, where the approval of whose politicians and populations matters less to them.[139] When

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[135] *E.g.*, Mark Lehrer & Sokol Celo, *German family capitalism in the 21st century: Patient capital between bifurcation and symbiosis*, 14 SOCIO-ECON. REV. 729, 730 (2016) ("The multigenerational perspective of family owners gives them an inherent incentive to consider the long-term impact of decisions on key relational stakeholders like employees and customers.").

[136] *See, e.g.*, Howard Gospel, Andrew Pendleton, Sigurt Vitols & Peter Wilke, *New Investment Funds, Restructuring, and Labor Outcomes: A European Perspective*, 19 CORP. GOVERNANCE: INT'L REV. 276, 276–81 (2011) (surveying the debate about the labor market impact of hedge funds, private equity funds, and sovereign wealth funds).

[137] *See also* Pargendler, *supra* note 4, at 575 (noting that free trade may sometimes increase inequality and hence reduce overall welfare).

[138] José Mata & Ernesto Freitas, *Foreignness and exit over the life cycle of firms*, 43 J. INT'L BUS. STUD. 615, 618–21 (2012) (contrasting the "liability of foreignness" and "footlooseness" interpretation of why foreign firms are more likely to exit a market than domestic ones).

[139] *See* Holger Görg & Eric Strobl, *'Footloose' Multinationals?*, 71 MANCHESTER SCH. 1 (2003) (finding that domestically owned plants are more likely to survive than those owned by multinationals in Ireland); Mata & Freitas, *supra* note 138, at

looking for short- or medium-term cost-cutting opportunities during a crisis, it will be easier to push through shutting down a research and development department, or an entire production site in country B. Owners less connected to the local socio-economic environment may be less inclined to retain key parts of the business (such as a research and development location) in a country and will rather centralize it in their headquarter state. Moreover, in a temporary downturn, they may be more likely to shut down production than a domestic family would. Maintaining a local core shareholder base may help to shield the firm from unfettered influence of a foreign financially oriented owner or multinational group. In this vein, foreign ownership of domestic firms has sometimes created concerns about employment effects.[140] Because these firms are not part of the domestic political and economic ecosystem, unlike a traditional family or other controlling shareholder, other stakeholders or the government may be in a less good position to put pressure on them.

More generally, foreign owners may not interact with domestic interest groups in the same way as local ones. Coming from a different cultural and economic background, they are subject not only to different social norms, but also less likely to be integrated and represented in the domestic political system.[141] This can at times mean that they are less easy to influence for domestic politicians and maybe sometimes less prone to corruption. However, there is also a greater risk that their presence and conduct will be seen as illegitimate or problematic in the host country. As Mark Roe wrote in 2003,

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624, 626–28 (finding that foreign firms are more likely to exit as well as support for the "footlooseness" interpretation); Roger Bandick, *Multinationals and plant survival*, 146 REV. WORLD ECON. 609 (2010) (finding that foreign multinationals were more likely to close Swedish plants than other firms); Anna Maria Ferragina, Rosanna Pittiglio & Filippo Reganati, *Does Multinational Ownership Affect Firm Survival in Italy?*, 15 J. BUS. ECON. & MGMT. 335 (2015) (finding that foreign multinationals were more likely to close Italian plants than Italian local owners or Italian multinationals); Pierre Blanchard, Emmanuel Dhyne, Catherine Fuss & Claude Mathieu, *(Not So) Easy Come, (Still) Easy Go? Footloose Multinationals Revisited*, 39 WORLD ECON. 679, 681 (2016) (finding that foreign multinationals were more likely to shut down Belgium operations conditioned on a number of control variables, including sunk costs).

[140] *E.g.*, Terry R. Spencer & Christian B. Green, *Foreign Direct Investment in the U.S.: An Analysis of Its Potential Costs and Benefits and a Review of Legislative Tools Available to Shape Its Future Course*, 6 TRANSNAT'L L. 539, 553 (1993) (discussing concerns by unions about negative employment effects of foreign ownership); Stephen B. Moldof, *Determining What Rules Apply When the Union-Employer Relationship Extends Beyond the United States: "Extraterritoriality" – Useful Guidepost or Convenient Buzzard Used to Avoid Meaningful Analysis?*, Cv039 ALI-CLE 457 (2014) (discussing possible downward pressure on US airline employees under foreign ownership). *But see* Michael Ulan, *Should the U.S. Restrict Foreign Investment?*, 516 ANNALS AM. ACAD. POL'Y & SOC. SCI. 117, 122–23 (1991) (criticizing such arguments).

[141] *See* Pargendler, *supra* note 4, at 577.

"[b]efore a nation can produce, it must achieve social peace."[142] Roe described elements of the corporate governance system developing in Europe and Japan after World War II, which were deeply affected by the disruption that the war and the collapse of financial markets during the depression had wrought. This point can be generalized: most efficient law might not always be politically attractive, or it might not even be politically achievable. A corporate governance change that redistributes from workers to shareholders may be efficient when capital is the scarce bottleneck factor, but it might cause political turmoil or at least intermittent disruptions that detract from profit making. This means that decisions will sometimes have to be made not from an economic efficiency perspective, but from the perspective of political feasibility and stability of the system.

Often, a corporate governance system will be part of a social compact within the country that involves a specific distribution of income and resources. In addition, the 'public' or 'national' interest may be affected. In his famous 1917 book on corporations, the leading German industrialist Walter Rathenau, who later served as the Weimar Republic's foreign minister, argued that shareholders could not be allowed to vote to dissolve Deutsche Bank, even if they would benefit from this financially.[143] A particular firm could be important to the national economy or other political goals, which domestic shareholders are likely to respect. Foreign shareholders with financial goals might disagree and push harder for dissolution or other measures at odds with such overarching goals.

Another increased reason to protect the national socioeconomic system could be emergency situations such as the COVID-19 pandemic. When capital continued to flow while labor became immobile during the early pandemic, there was a strong argument to protect labor, e.g. by subsidizing employment or short-term work programs.[144] Workers are, of course, a voter group to which politicians may feel they owe a certain level of responsibility or allegiance, in the context of which corporate law protectionism may be justifiable. However, it is important to note that economic turmoil can of course lead to a political backlash of a protectionist nature.[145] If "foreign"

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[142] ROE, *supra* note 130, at 1.
[143] WALTHER RATHENAU, VOM AKTIENWESEN: EINE GESCHÄFTLICHE BETRACHTUNG 39 (1917).
[144] *E.g.*, Tom Fairless & Eric Sylvers, *Europe Locked Its Economy in Place. Unlocking It Could be Ugly*, WALL ST. J. (Feb. 17, 2021), https://www.wsj.com/articles/europe-froze-its-economy-in-place-the-thaw-could-be-ugly-11613586536 [https://perma.cc/2CBK-TTZB] (discussing subsidized worker furlough programs in Europe).
[145] On political backlash destroying efficient economic arrangements where they are not perceived as fair, *see* Mark J. Roe, *Backlash*, 98 COLUM. L. REV. 217 (1998); Mark J. Roe & Jordan I. Siegel, *Political instability: Effects on financial*

control of firms is increasingly seen as illegitimate, a political backlash will likely be more severe than under domestic ownership, given the less close domestic integration of foreign owners into local political systems. Preemptively taking measures to protect firms from foreign influence that could have such an effect may forestall an even stronger protectionist reaction with damaging consequences for the overall political system.

F. *COVID-19: The Need For Resilience And Corporate Embeddedness*

The final argument for protectionism comes from the experience with COVID-19 during the past two years. COVID-19 has highlighted the need for resilience in corporate governance.[146] Convergence in corporate governance and financial market integration is to some extent a pursuit of stable periods when firms are not experiencing a deep shock. In a stable environment, competitive pressures guide firms toward introducing "efficient" structures, such as international supply chains and low levels of "corporate fat," such as financial reserves or excess employment. By contrast, the efficiency goals extolled in the convergence debate fail in severe crisis. "Corporate fat" and "corporate embeddedness" may be beneficial in situations of severe crisis.[147]

For the point of this paper, the aspect of embeddedness is clearly most important. The argument is that a firm integrated into a larger political and economic network will be more likely to survive a crisis (including a pandemic). Embeddedness describes not only corporate ownership structures, but also long-term lending relationships, and customer-supplier relationships. In addition, relationships with employees are a considerable aspect. Again, this relates to the debate about different financial and socioeconomic systems of which corporate governance is a part. A well-known example is provided by Rajan and Zingales, who describe relationship-based financial systems as creating a system with 'intertemporal cross-subsidies.'[148] Different members of an interconnected group provide insurance for each other. Being in a continuous relationship with other network members, firms are more likely to participate in rescues and bailouts. They will also have the political clout that make aid from the government possible. While embeddedness is not a guarantee for survival, it surely increases the chances.[149]

Embeddedness has been largely ignored during the convergence debate because those developed Western and East Asian countries most

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development, roots in the severity of economic inequality, 39 J. COMP. ECON. 279 (2011) (providing evidence that political instability can damage financial development).

[146] Gelter & Puaschunder, *supra* note 1, at 578–95.

[147] *Id*. at 560.

[148] Rajan & Zingales, *supra* note127, at 42.

[149] Gelter & Puaschunder, *supra* note 1, at 587.

affected by convergence were economically relatively stable, thus allowing political considerations to fade into the background. Jurisdictions outside of the English-speaking world have – in corporate governance debates – been typically characterized as having concentrated ownership.[150] While the U.S. has developed a dispersed ownership system where management for a long time had a great latitude for independent action, this has typically not been true elsewhere, as board and managers needed to navigate the influence of controlling shareholders and shareholder coalitions, as well as the impact of important blockholders with a significant influence on the firm. This aligns with the discussion of differences between financial systems above.[151]

In a market-oriented system, dispersed ownership firms without deep meaningful connections are less likely to be bailed out in severe crisis, unless there is a public reason to do so (such as their systemic significance). A retail investor or even a mutual fund with only a small stake can disinvest in times of crisis and cut its losses. By contrast, embeddedness can help a firm to survive.[152] Shareholders – but also other stakeholders – that are deeply invested into a relationship with a firm will have additional incentives to maintain it by helping the firm to survive. Large shareholders typically will not be able to disinvest without taking a significant loss and generating additional downward pressure on the stock price.[153] Strategic benefits from the relationship mean that they will have additional losses not only from the value of the investment, but also from a lost relationship. Being a strategic investor creates an incentive to help the corporation survive. Most obviously, a similar situation will apply in cross-ownership structures such as a Japanese *keiretsu*.[154] Here, the group overall provides diversification in the form of a conglomerate of firms that are to some extent dependent on each other. These firms are not

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[150] *See, e.g.*, Marco Becht & Alisa Roëll, *Blockholdings in Europe: An International Comparison*, 43 EUR. ECON. REV. 1049, 1055 (1999); Rafael La Porta, Florencio Lopez-de-Silanes & Andrei Shleifer, *Corporate Ownership Around the World*, 54 J. FIN. 471, 472 (1999); Mara Faccio & Larry H.P. Lang, *The Ultimate Ownership of Western European Corporations*, 65 J. FIN. ECON. 365, 379–80 (2002); GOUREVITCH & SHINN, *supra* note 24, at 18; PEPPER D. CULPEPPER, QUIET POLITICS AND BUSINESS POWER 31–32 (2011).

[151] *See supra* section 0.

[152] *See* Tarun Khanna & Krishna Palepu, *Is Group Affiliation Profitable in Emerging Markets? An Analysis of Diversified Indian Business Groups*, 55 J. FIN. 867 (2000) (showing that group affiliation is advantageous in an environment with weak economic institutions).

[153] Gelter & Puaschunder, *supra* note 1, at 587.

[154] Randall K. Morck & Masao Nakamura, *A Frog in the Well Knows Nothing of the Ocean: A History of Corporate Ownership in Japan*, *in* A HISTORY OF CORPORATE GOVERNANCE AROUND THE WORLD: FAMILY BUSINESS GROUPS TO PROFESSIONAL MANAGERS 367, 432–37 (Randall K. Morck ed., 2005).

likely to allow each other to go under even in a severe crisis. The 'main bank' of the group will, if necessary, orchestrate the rescue of a struggling firm.[155]

The same is likely true for significant shareholders that are part of a controlling family, and for industrial shareholders. An important entrepreneurial family may hold considerable political clout and enjoy connections to politics,[156] but also have ties to lenders[157] in the country. Family members may frequently interact with unions and the workforce, as well as the business and social community where the firm is located.[158] Tentative evidence from the early days of the COVID-19 pandemic from Italy showed that family-controlled firms were more likely to survive.[159] The same is also likely true when the government is a key shareholder of a firm and tends to use it to pursue political goals. In this case, it will not likely let the firm falter, especially if many voters' jobs are at stake. A government connection is less likely to allow a firm to go out of business for obvious political reasons. It will generally endow firms with "patient" capital that will typically help them to better weather crises.[160] A connection to the government will mean that firms are inherently politically connected, thus creating direct

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[155] *See* Rajan & Zingales, *supra* note 127, at 42 (providing the example of Mazda's rescue orchestrated by a bank).

[156] Mario Daniele Amore and Alessandro Minichilli, *Local Political Uncertainty, Family Control, and Investment Behavior*, 53 J. FIN. & QUANTITATIVE ANALYSIS 1781, 1782 (2018); Mariana Pargendler, *Controlling Shareholders in the Twenty-First Century: Complicating Corporate Governance Beyond Agency Costs*, 45 J. CORP. L. 953, 966 (2020).

[157] Marianne Bertrand & Antoinette Schoar, *The Role of Family in Family Firms*, 20 J. ECON. PERSP. 73, 77–78 (2006); Leandro D'Aurizio, Tommaso Oliviero & Livio Romano, *Family firms, soft information and bank lending in a financial crisis*, 33 J. CORP. FIN. 279 (2015); Marco Cucculelli, Valentina Peruzzi & Alberto Zazzaro, *Relational capital in lending relationships: Evidence from European family firms*, 52 SMALL. BUS. ECON. 277 (2019).

[158] Bertrand & Schoar, *supra* note 157, at 75–76; Laurent Bach & Nicolas Serrano-Velarde, *CEO identity and labor contracts: Evidence from CEO transitions*, 33 J. CORP. FIN. 227 (2015); Carl Magnus Bjuggren, *Sensitivity to shocks and implicit employment protection in family firms*, 119 J. ECON. BEHAV. & ORG. 18 (2015) (finding that family firms offer implicit employment protection); William Mullins & Antoinette Schoar, *How do CEOs see their roles? Management philosophies and styles in family and non-family firms*, 119 J. FIN. ECON. 24 (2016).

[159] Mario Daniele Amore, Fabio Quarato & Valerio Pelucco, *Family Ownership During the Covid-19 Pandemic* (2021), https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3773430 [https://perma.cc/J43F-ST3Z].

[160] Sergio G. Lazzarini & Aldo Musacchio, *State ownership reinvented? Explaining performance differences between state-owned and private firms*, 26 CORP. GOVERNANCE: INT'L REV. 255, 258 (2018).

communication channels between executives and officials that potentially must decide about financial emergency support.[161]

The conclusion is that these various types of "embeddedness" should help firms survive shocks to the economy such as COVID-19. Thus, in an environment characterized by a high degree of uncertainty, we may expect connected firms to generally become more prevalent through an evolutionary process. Firms with more resilient structures are more likely to survive shocks such as the one created by COVID-19, but also internal and external political instability. Corporate structures that "convergence in corporate governance" toward a shareholder model may have eliminated – such as concentrated ownership structures, cross-ownership, as well as long-term lending and labor relationships – may be adaptations to environments with a higher degree of uncertainty.

If we consider the advantages of eliminating embeddedness (such as lower agency cost and private benefits of control) and resiliency of firms to stand in a relationship of a tradeoff, we may expect recurring crises to push more firms in favor of resilient structures. In the standard investor-oriented convergence theory, embedded structures would be considered inefficient, largely because they generate agency costs and such firms would be less likely to prevail in an open market. However, embeddedness likely has a "survivor" advantage that allows firms to persist under adverse conditions. These implicit rescue structures may have historically been more prevalent in some countries compared to others, which is why more firms of this type survive under conditions of political, economic, or social uncertainty.[162]

5. CONCLUSION

Overall, we can say that there are several reasons for the prioritization of "nationalist" or "protectionist" policies in corporate governance. Many of them appear legitimate and potentially beneficial. Politicians owe a fiduciary duty to their constituents, in the context of which corporate law protectionism may wish them to implement such policies. Arguably, this leaves open the question what (if any) the right geographic range of protectionism is – the nation state, the EU as a supranational organization, other

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[161] *See* Christine Zhenwei Qiang & Georgiana Pop, *State-owned enterprises and COVID-19: Policy principles*, WORLDBANK BLOGS (July 30, 2020), https://blogs.worldbank.org/psd/state-owned-enterprises-and-covid-19-policy-principles [https://perma.cc/5S46-HCUW] (finding that SOEs were often bailed out by the government during the COVID-19 crisis); Luca Enriques, *Pandemic-Resistant Corporate Law: How to Help Companies Cope with Existential Threats and Extreme Uncertainty During the Covid-19 Crisis*, 2020 EUR. COMPANY & FIN. L. REV. 257, 271 (discussing the political capital necessary to secure government protection in the context of a hostile acquisition).

[162] Gelter & Puaschunder, *supra* note 1, at 589.

groups of cooperating jurisdictions, or maybe in some cases subnational unit? Protectionist measures appear to be less (if at all) justified where the degree of international harmonization is considerable, such as in the EU.[163] In any event, one reason for protectionist measures that even the strongest supporters of globalization of corporate governance should accept is backlash. Preempting a heavy-handed intervention that might come after a situation or political turmoil will likely be beneficial if the protectionist policies initially prompted are less harmful than the ones that might follow. A moderate level of protectionism may be better than a radical solution that inflicts serious long-term damage.

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[163] *Supra* note 61 and accompanying text.