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Business Organizations as Natural Objects of Ownership

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BUSINESS ORGANIZATIONS AS NATURAL OBJECTS OF OWNERSHIP

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I. INTRODUCTION

Given the importance of "property rights" in American law and culture, academic and judicial disagreement over the content of the concept is a problem. Professor Eric Claeys makes considerable progress toward resolving this problem in his forthcoming book, *Natural Property Rights*. Using John Locke's labor theory of property, the treatise identifies intelligible limits to the kinds of objects that qualify as property and provides guidance on how legal rights should operate for a given category of objects. It also identifies several examples of American law that already follow a Lockean framework. The chapters Designing Property Rights and Dividing Property Rights pull examples from cases discussing rights in animals, land, and water. This Article is the first to use Claeys's natural property rights approach to explain the law of business organizations.[1] Business organizations are the quintessential object of Lockean property because they are created by their proprietors

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1. Eric Claeys, Natural Property Rights 147–48 (Sept. 17, 2021) (unpublished manuscript) (on file with the Texas A&M Journal of Property Law) (Professor Claeys uses unfair competition doctrine to concretize an early part of his conceptual project, but he does not offer examples that apply his natural property rights framework to business organizations.); *see also* Eric R. Claeys, *Natural Property Rights: An Introduction*, 9 TEX. A&M J. PROP. L. 415 (2023) [hereinafter "Claeys, *Introduction*"].

exercising control over several external resources. Put differently, exercising control to create a business is an ideal example of using labor to create a valuable object and the associated natural property rights. Moreover, the right to control a business is itself an object of ownership that can be transferred as a subcomponent of the broader rights in a business.[2] Finally, several features of the Lockean approach may help us to better understand and resolve some contentious corporate governance debates. For example, we might shed light on the debate over whether to prioritize shareholder profits or stakeholder interests by exploring Locke's response to the assumption that a community's raw materials belong to everyone in common.

Although property concepts play an important role in business organization case law, the scholarship in this space often prioritizes the view that firms are only "complex sets of contracts."[3] Scholars who adopt this view attempt to use contract doctrine to understand almost every element of business organization law. Many courts have even adopted the contractarian view of the firm. For example, in addition to the corporation's articles of incorporation and the state's corporate statute, the Delaware "Supreme Court has made clear that [corporate] bylaws constitute a binding part of the contract between a Delaware corporation and its stockholders."[4] Adopting a contractarian view of the firm makes sense, given that several basic business relationships can only exist through the mutual agreement of all the parties involved.[5] However, several scholars have recognized the importance of property concepts for explaining business organization law in general and corporate law in particular. Sanford J. Grossman and Oliver D. Hart have adopted a "property rights theory of the firm," in which the firm is viewed as the owner of the assets of the business.[6] Eugene F. Fama, Michael C. Jensen, and Margaret M. Blair have emphasized the importance of separating ownership from control for understanding publicly traded corporations.[7] In addition, several more recent articles have used property

2. *See* Henry Manne, *Mergers and the Market for Corporate Control*, 73 J. POL. ECON. 110, n. 21 (1965).

3. John Armour & Michael J. Whincop, *The Proprietary Foundations of Corporate Law*, 27 OXFORD J. LEGAL STUD. 429, 429 (2007).

4. Boilermakers Local 154 Ret. Fund v. Chevron Corp., 73 A.3d 934, 955 (Del. Ch. 2013).

5. See discussion *infra* Part III.

6. Sanford J. Grossman & Oliver D. Hart, *The Costs and Benefits of Ownership: A Theory of Vertical and Lateral Integration*, 94 J. POL. ECON. 691, 693 (1986) (defining a firm as "those assets that it owns or over which it has control.").

7. Eugene F. Fama & Michael C. Jensen, *Separation of Ownership and Control*, 26 J.L. & ECON. 301 (1983); Margaret M. Blair, *Locking in Capital: What Corporate Law Achieved*

doctrine to address controversial policy debates in business organization law and securities regulation.[8]

Almost none of the business organization law or securities regulation scholarship explicitly adopts a Lockean approach to property for grappling with doctrinal or policy questions.[9] Moreover, almost no one recognizes the firm as an object of ownership.[10] One exception is Adolph Berle, who is arguably most famous for rejecting the application of common law property doctrine to understanding conflicts in modern businesses, especially publicly traded corporations.[11] This Article hopes to advance this area of scholarship and legal doctrine in two ways. First, applying the approach outlined in *Natural Property Rights*, this Article explains why firms—regardless of ownership structure—should be viewed as things a person can own. Second, this Article will use the scope and limits of the property framework outlined by Claeys to explain several features of business organization law. These features include the formation process of agency relationships and general partnerships, the apparent and implied authority of agents, and why—despite their contribution of labor—it is appropriate for agents to have no ownership interests in the products or profits of their principals' business.[12] This Article concludes by showing how a natural rights approach to business organizations also explains protecting shareholders' rights to profits from the competing demands of various stakeholders.

for Business Organizers in the Nineteenth Century, 51 UCLA L. REV. 387 (2003).

8. Lua Kamal Yuille, *Corporations, Property, & Personhood*, 97 DENV. L. REV. 557 (2020); George A. Mocsary, *Freedom of Corporate Purpose*, 2016 BYU L. REV. 1319 (2016); Robert Anderson IV, *A Property Theory of Corporate Law*, 2020 COLUM. BUS. L. REV. 1 (2020); Danielle D'Onfro, *Limited Liability Property,* 39 CARDOZO L. REV. 1365 (2018); Heather Hughes, *Property and the True-Sale Doctrine*, 19 U. PA. J. BUS. L. 870 (2017); Kevin R Douglas, *Missing the Role of Property in the Regulation of Insider Trading*, 69 CATH. U. L. REV. 209 (2020).

9. One exception is Gary Lawson, *The Ethics of Insider Trading*, 11 HARV. J. L. & PUB. POL'Y 727 (1988).

10. Margaret M. Blair & Lynn A. Stout, *Team Production Theory of Corporate Law*, 85 VA. L. REV. 247, 260 (1999) ("Building on this idea, some economists define the firm as a bundle of assets under common ownership (and therefore, common control).").

11. *See* Adolf A. Berle Jr., *The Theory of Enterprise Entity*, 47 COLUM. L. REV. 343 (1947); see also his warnings about the separation of ownership and control in publicly traded companies, A. A. Berle, Jr. and Gardiner C. Means, *Corporations and the Public Investor*, 20 THE AM. ECON.REV. 54-71 (1930).

12. This Article uses "agent" and employee interchangeably and uses "principal" and employer interchangeably.

II. PROFESSOR CLAEYS ON NATURAL PROPERTY RIGHTS

Claeys begins his natural property rights framework with theories of natural law "that ground morality in people's capacities to flourish as rational beings."[13] He differentiates his approach to property from the schools of thought he describes as "law and economics" and "pragmatist." Claeys's primary critique of the law and economics defense of property is that the goal of economic efficiency fails to provide "a government [with] legitimate authority to order citizens to surrender their rights and to back the order with the implied threat of violence."[14] The pragmatist camp includes scholars who purport "to evaluate resource disputes by considering all possible costs and benefits of different policy proposals on a case-by-case basis."[15] Pragmatists often treat "property rights" as an open-ended bundle of rights, leaving officials to arbitrarily wield their authority over civilians' resources and resource disputes.[16] Claeys also singles out Robert Nozick's theory of property, which focuses on "autonomy"—Claeys critiques Nozick's and other deontological accounts of property rights for their failure to take into account "whether and how much [property rights] helps people survive or flourish."[17] By contrast, *Natural Property Rights* focuses on ways in which property rights facilitate the *use* of resources in order to promote individual welfare and social harmony.

The same issues are present in the scholarship applying property analysis to business organizations. One prominent securities regulation scholar, Henry Manne, adopted the bundle of sticks framework when responding to critics of his scholarship on insider trading. In his seminal book applying law and economics to the issue, Manne suggested that allowing insider trading might increase efficiency.[18] He proposed using insider trading to compensate entrepreneurs in companies and argued that the practice allowed prices to reflect confidential business information—making the price more accurate—without disclosure, which often undermines the value of the information to the company. At least one critic of Manne's recommendations argued that "insider trading must be outlawed because the information is the 'property' of the

13. Claeys, *supra* note 1, at 17.
14. *Id.* at 33; *see also* Claeys, *Introduction*, *supra* note 1, at 422–23.
15. Claeys, *supra* note 1, at 36.
16. *Id.* at 37.
17. Claeys, *supra* note 1, at 131; *see also* Claeys, *Introduction*, *supra* note 1, at 439–40.
18. HENRY G. MANNE, INSIDER TRADING AND THE STOCK MARKET (1966); Henry G. Manne, *Insider Trading and the Law Professors*, 23 VAND. L. REV. 547, 578–79 (1970).

shareholders."[19] In line with the strong form of the bundle of sticks framework, Manne responded that "the concept of property is no more nor less than the rights and obligations recognized by law."[20] Interestingly, Jennings and others that describe the prohibition on insider trading as necessary to protect property rights could be seen as adopting the view that exclusion is the most important stick in the bundle.[21] After asserting that inside information is the shareholders' property, Richard Jennings concluded that "a sound prophylactic rule requires" forbidding insider trading.[22] Recommending a prophylactic rule to protect shareholders' supposed property rights in inside information ignores the possibility that shareholders might decide it is *useful* to consent to insiders trading on their information.[23] By contrast, scholars adopting a Kantian framework have suggested that a property approach requires allowing information owners to consent to insider trading.[24]

The disagreement among business law scholars about the requirements of adopting a property approach demonstrates the need for the clarity offered by *Natural Property Rights*. The remainder of this Article will discuss two business organization topics through the framework developed in Claeys's forthcoming book. First, this Article demonstrates that several legal doctrines treat business enterprises as res, as defined

19. Manne, *supra* note 18, at 549 (quoting Richard Jennings, *Book review,* 55 CAL. L. REV. 1219, 1235 (1967)).

20*. Id.* at 550.

21. Preet Bharara, et al., *Report of the Bharara Task Force on Insider Trading*, (Jan. 2020), https://www.bhararataskforce.com/s/Report-of-the-Bharara-Task-Force-on-Insider-Trading.pdf [https://perma.cc/E5VR-5RAN].

22. Alternatives to prophylactic laws include default rules and burden shifting.

23. A growing body of scholars emphasize that property rights cannot be explained by exclusion alone. *See* Adam Mossoff, *What Is Property? Putting the Pieces Back Together*, 45 ARIZ L. REV. 371, 376 (2003) (arguing that rights to "acquisition, use, and disposal . . . are necessary for a *sufficient*" conception of property); *see also* Adam Mossoff, *Exclusion and Exclusive Use in Patent Law*, 22 HARV. J.L. & TECH. 321, 347–70 (2009) (describing "how the legal realists used patents in arguing for an exclusion concept of property in land, and [arguing that] this revolution in property theory in the early twentieth century led patent lawyers to later mistakenly accept the legal realists' characterization of property as securing only the right to exclude."); RICHARD A. EPSTEIN, TAKINGS: PRIVATE PROPERTY AND THE POWER OF EMINENT DOMAIN 59–62 (Harvard Uni. Press) (1985) (describing property as a "unified" concept which always includes the rights to possess, use and dispose); Eric R. Claeys, *Takings, Regulations, and Natural Property Rights*, 88 CORNELL L. REV. 1549, 1568 (2003) (Instead of exclusion alone, describing property rights as including "the trinity of disposition, use, and control."); Kevin R. Douglas, *How Fatal Ambiguity Undermines Effective Insider Trading Reform*, 48 MICH. ST. U. J. CORP. L. 353, (2023).

24*. See* John P. Anderson, *The Final Step to Insider Trading Reform: Answering the "It's Just Not Right!" Objection*, 12 J. L. ECON. & POL'Y 279, 300 (2016) ("These deontological considerations . . . deprive the opponent of legalizing issuer-licensed insider trading of any reason-based justification in terms of fraudulent deception, justice or fairness.").

by Claeys in Chapters 4 and 10 of his book. Second, this Article will explore how the *Natural Property Rights* interpretation of the doctrine of increase provides a factual, moral basis for resolving the dispute over how to divide business profit among principals, employees, stockholders, and stakeholders.

III. BUSINESS ORGANIZATIONS AS THINGS (RES)

The legal rights and obligations of parties in a dispute often turn on the kinds of interests at stake. For example, recognizing a trade secret as a property interest makes injunctions available to owners and broadens each owner's rights against third parties.[25] Recognizing trade secrets as contract interests may reduce available remedies to a damages payment, leaving a breaching counterparty or negligent third party free to practice and share the trade secret. Therefore, whether it is best to recognize a business enterprise as merely a nexus of contracts or as a separate object of ownership has important legal implications. Consider the criteria established in *Natural Property Rights*. In Chapter 4, Claeys identifies separable, non-human resources as the kinds of objects in which a person can have property rights. "Separable resources constitute a distinct field of goods that people might use or claim."[26] For example:

> A person's body just is a basic part of that person, and a person's capacities to make a living, associate with others, and migrate are all extensions of his freedom to engage in deliberate, intelligent, and morally valuable activity. By contrast, if a resource seems detached from the right-claimant, if it seems the sort of thing that could just as easily owned by Sally or Jane as by Dick, it is separable and a fitting candidate for property. This judgment explains why relatively "personality free" resources—land, animals, tools, minerals, or water—are all objects of property.[27]

It may be difficult to imagine how businesses are "separable," given that they are intangible. Moreover, like many scholars, one could view business principals as simply owning the individual assets used to run the business but not recognize principals as creating some unified object by employing those assets. *Natural Property Rights* offers an illuminating principle on the second concern. Claeys writes that when "several

25. *See* Metallurgical Indus., Inc. v. Fourtek, Inc., 790 F.2d 1195 (5th Cir. 1986) ("distinguishing remedies."); *see also* Eric R. Claeys, *Private Law Theory and Corrective Justice in Trade Secrecy*, 4 J. TORT L. 1 (2011).
26. Claeys, *supra* note 1, at 104.
27. *Id.* at 107.

resources tend to go together and to be used together, they should be clustered into one conventional res; when they tend to run separately and to be used separately, they should get separate res."[28]

If business enterprises were simply a nexus of agreements, we might expect that the termination or transfer of a business would always involve transferring or terminating several individual agreements. Instead, several legal doctrines distinguish transferring an entire business, on the one hand, and transferring individual business assets. The Uniform Partnership Act ("UPA") and the Model Business Corporation Act distinguish between a business's liquidation value and its "going concern" value. Under the UPA, partners leaving the partnership are entitled to cash equal to either the liquidation value or the "going concern" value of the partnership's assets, whichever is greater. Liquidation value is determined, in part, based on the sale of individual business assets. Going concern value, however, is based on methods normally used to price operating businesses.[29] When a business dissolves, there may be a dramatic difference between the price of a continuing business and the price of the business's individual assets.

Most U.S. corporation statutes recognize a similar distinction by describing the requirements of a merger in one section and describing the requirements of a sale of all or substantially all assets in a separate section.[30] The difference, however, is that the merger provisions in corporation and partnership statutes lay out the requirements of merging one or more legal persons into a single legal person. If we accept the legal fiction and view the corporation as a legal principal, merger statutes outline how corporate shareholders can merge several legal principals into one. Merging the fictitious principals also has the effect of making one legal person the owner of several businesses that were previously separately owned organizations.[31] The board of directors of the new

28. *Id.* at 274.

29. Weinberger v. UOP, Inc., 457 A.2d 701, 713 (Del. 1983) (DE case transferring to DCF) (In accepting the discounted cash flow method, the Delaware Supreme Court adopted an approach that includes "proof of value by any techniques or methods which are generally considered acceptable in the financial community and otherwise admissible in court, subject only to our interpretation of . . . .").

30. MODEL BUS. CORP. ACT §§ 11.02, 12.01 (Comm. of Corp. L. of the Section of Bus. L. 2016); UNIFORM PARTNERSHIP ACT §§ 302, 806, 906 (NAT'L CONF. OF COMM'RS ON UNIF. STATE L. 1997).

31. STEPHEN BAINBRIDGE, MERGERS AND ACQUISITIONS: A TRANSACTIONAL PERSPECTIVE, 17 (4th ed. 2021). ("This happens because a number of events take place by operation of law and without the need for further action after the merger becomes effective, including most notably: (1) the separate existence of all corporate parties comes to an end, with the exception of the surviving corporation; (2) title to all assets owned by each corporate party is automatically vested in the surviving corporation; (3) the surviving

legal person is now free to integrate the operations of the distinct businesses as they see fit. Merging legal persons allows all rights and obligations—including contract rights and fiduciary relationships—of the separate entities to transfer to the surviving entity using one legal process. On the other hand, a sale of all of a corporation's assets requires separately transferring title to each piece of property used in the business, assigning each agreement and license used in the business, and much more.

Finally, consider the continuity-of-enterprise doctrine. This doctrine holds a successor corporation liable for the acts of its predecessor corporation, if—among other requirements—the successor maintains the same "general business operations of the predecessor corporation."[32] The same general business might have "the same employees, doing the same jobs, for the same supervisors, under the same working conditions, and using the same production processes to produce the same products for the same customers."[33] The continuing enterprise doctrine is strange in that bona fide purchasers of property are seldom held responsible for the legal liabilities of a seller.[34] Still, this real-world Ship of Theseus problem recognizes that the discrete components required to create a business organization can be replaced without creating a completely new organization.

Each preceding doctrine recognizes bundles of several business resources as one conventional res, the business enterprise. These doctrines are distinct from those that recognize partners in general partnerships or shareholders in corporations as, respectively, holding their partnership interests or corporate stock as personal property. The UPA recognizes partners as owning and having a right to transfer their partnership interests.[35] Moreover, these interests include certain governance and economic rights over the partnership business.[36] However,

company succeeds to all liabilities of each corporate party; and (4) the consideration passes to non-dissenting shareholders.").

32. Foster v. Cone-Blanchard Mach. Co., 460 Mich. 696, 703 (1999).

33. *Substantial-Continuity Doctrine*, BLACK'S LAW DICTIONARY (11th ed. 2019).

34. *See Bona Fide Purchaser*, WESTLAW, https://1.next.westlaw.com/Document/I0fa00bceef0811e28578f7ccc38dcbee/View/FullText.html?originationContext=document&transitionType=DocumentItem&ppcid=4258676703a2499b9efc3dfe2595950d&contextData=(sc.DocLink)&firstPage=true&oWSessionId=2da09cdb93da448c9da2de06b93e4e9d&isplcus=true&fromAnonymous=true&bhcp=1 [https://perma.cc/WLQ7-FWLQ].

35. UNIFORM PARTNERSHIP ACT § 502 (NAT'L CONF. OF COMM'RS ON UNIF. STATE L. 1997).

36. *Id.* § 503, cmts. ("A partner's rights in a partnership are bifurcated into economic rights (the transferable interest) and governance rights (including management rights, consent rights, rights to information, rights to seek judicial intervention).").

only the partnership as a separate legal entity is recognized as owning specific partnership assets.[37] The going concern and continuity of enterprise doctrines are also distinct from models that treat business organizations as mere nexuses of contracts. Business organizations are what principals create by organizing business assets—including the property, contracts, and relationships that constitute the enterprise.

IV. NATURAL PROPERTY RIGHTS IN BUSINESS ORGANIZATIONS

Natural Property Rights offers sensible limits to the scope of ownership rights in various objects. In Chapter 5, Claeys identifies productive use and claim communication as required to establish property rights in an object. He also describes each owner's rights as properly limited by Locke's sufficiency and necessity provisos. Most would accept that these baseline expectations easily explain the laws protecting subsistence farmers and sole proprietors with no employees. However, these expectations also provide a solid foundation for legal doctrines establishing people's rights when many parties have overlapping interests in the same objects. As a result, Claeys's framework has the potential to provide sensible resolutions to disputes about who has the right to the profits generated by business enterprises. For example, consider that employees and their employers both usually contribute their labor to a business's production process. Therefore, how can we justify only recognizing the employer as having a right to the business's profits (to the fruits of both parties' labor)?[38] Similarly, given that most modern economic activity is incredibly interdependent, can we view any party's labor as single-handedly producing any resource? If not, does that mean that advocates of a stakeholder theory of corporate governance have the moral high ground under a Lockean property theory?

Before answering the more complicated questions, let us explore how well current business organization doctrines meet the requirements for establishing property rights outlined by Claeys and how well they respect the limits he identifies. *Natural Property Rights* states that to

> establish a natural property right in relation to a resource, a claimant must use it in a manner that contributes to someone's preservation or flourishing; that is a requirement of *productive use*. The user must also give others in his community reasonably clear notice that he is

37. UNIFORM PARTNERSHIP ACT § 203.

38. *See* RESTATEMENT (SECOND) AGENCY § 387 (AM. L. INST. 1957) (Unless otherwise agreed, an agent is subject to a duty to his principal to act solely for the benefit of the principal in all matters connected with his agency.); *see also* UNIFORM PARTNERSHIP ACT § 409(b) (NAT'L CONF. COMM'RS UNIF. STATE L., amended 2013).

> using it and does not want his uses to be interfered with; this is a requirement of *claim communication*.[39]

Many elements of how courts define the creation of agency relationships and partnerships evoke concerns about productive use and claim communication. Under the Uniform Partnership Act of 1997 ("UPA"), partnerships are formed by "the association of two or more persons to carry on as co-owners a business for profit."[40] The UPA also presumes that someone with the right to "a share of the profits of a business is . . . a partner in the business."[41] "Agency is the fiduciary relationship that results from the manifestation of consent by one person to another that the other shall act on his behalf and subject to his control, and consent by the other so to act."[42] Courts sometimes recognize the parties in agency relationships as creating non-financial benefits for a principal.[43] However, when courts discuss agents of a for-profit enterprise working on a principal's behalf, the assumption is that both agents and principals are working to generate financial profits for the principal.

Based on the formation processes described above, business organizations easily meet the requirement of productive use. Partnerships and agency relationships are formed to pursue profits, especially money. The claim communication elements are less obvious but seem to be fulfilled by the requirement that partnerships and agency relationships are formed by the parties to the relationship agreeing to conduct themselves in a specific way. "Subjective intent to create the legal relationship of 'partnership' is irrelevant."[44] Still, explicitly or implicitly agreeing to some ongoing activity requires communication. This claim communication inquiry is more apparent in doctrines that deal with obligations to third parties. For example, a principal is not usually liable for contracts created by her agent when the agent is operating outside of the scope of his actual authority.[45] However, under the doctrine of apparent authority, principals can be made liable for unauthorized acts if the principal's actions caused the third party to reasonably believe that the agent was authorized to bind the principal.[46] Similarly, the corporation by estoppel doctrine prevents a third party from seeking financial relief

39. Claeys, *supra* note 1, at 117.
40. UNIFORM PARTNERSHIP ACT § 202.
41. *Id.* § 202(c)(3).
42. A. Gay Jenson Farms Co. v. Cargill, Inc., 309 N.W.2d 285, 290 (Minn. 1981).
43. *Id.* at 291 ("Warren acted on Cargill's behalf in procuring grain for Cargill as the part of its normal operations which were totally financed by Cargill.").
44. UNIFORM PARTNERSHIP ACT § 202(a) cmt.
45. RESTATEMENT (SECOND) OF AGENCY § 140 (AM. L. INST. 1957).
46. *Id.* § 8 cmt. c.

from a purported shareholder of a non-existent corporation if that third party relied on the existence of the corporation when interacting with the defendants in a case.[47] More formally, many state and local governments require business owners to register their business names so that third parties can find who is ultimately responsible for the enterprise's contractual, tort, and other liabilities.[48] In addition, most corporate statutes require business corporation names to contain "Inc.," "Corp.," or some other indication of its corporate status. This requirement gives third parties notice that they are dealing with an entity that limits liability for its shareholders or members.

Several business organization doctrines also evoke a relaxed version of the limiting principles identified in *Natural Property Rights*. Claeys offers two provisos that allow a third-party's interests to override the ownership rights of parties who have met the claim communication and productive use requirements described above. "The necessity proviso entitles someone who does not hold property in a resource to commandeer it to address an unavoidable and urgent need. The sufficiency proviso protects people's access to some share of resources in a class when most of the resources in that class have already been appropriated."[49] It is difficult to imagine a life-or-death scenario that would require commandeering an entire business. However, the necessity proviso may be expressed in the doctrine of implied authority, which gives an agent the authority to take those steps that are *necessary* to complete an expressly authorized act.[50] Less of a stretch are those doctrines that limit a principal's rights to restrict the competition of a former agent or partner. One element of the duty of loyalty for agents and other fiduciaries is that they are barred from competing with their principals during the course of the fiduciary relationship. However, in the absence of a non-compete agreement between the principal and agent, agents are free to compete with their former principals after the relationship ends. In addition, those states that enforce non-compete agreements usually require that these agreements include reasonable limits. Courts generally consider non-competes unreasonable if the non-compete period is too long or if the agreements apply to a large geographical area. Finally, despite the duty

47. Duray Dev., LLC v. Perrin, 792 N.W.2d 749, 756 (Minn. 2010) ("The general rule is: 'Where a body assumes to be a corporation and acts under a particular name, a third party dealing with it under such assumed name is estopped to deny its corporate existence.'").

48. *Register Your Business*, U.S. SMALL BUS. ADMIN., https://www.sba.gov/business-guide/launch-your-business/register-your-business [https://perma.cc/BV7R-EZLQ].

49. Claeys, *supra* note 1, at 117–18.

50. RESTATEMENT (SECOND) OF AGENCY § 7.

not to compete with one's principal during the fiduciary relationship, several courts have concluded that agents may prepare to compete during the relationship.[51] Therefore, as long as they fulfill their other fiduciary obligations while still employed by their old firm, partners in a law firm may prepare to establish a competing law firm by leasing new office space or marketing their future services on brand-new letterhead.[52]

If we adopt a flexible view of business competition, the limits and exceptions to the fiduciary duty not to compete with one's principal seem like a form of Claeys's sufficiency proviso. Consider that Claeys explicitly excludes analysis of the kind of Lockean property that modern legal scholars would categorize as a liberty interest. Non-compete agreements can be understood as contracts over one's liberty, which would place them outside of the scope of *Natural Property Rights*. However, we can also understand non-compete agreements as covering something derivative of one's exercise of liberty. If business enterprises are res, then non-compete agreements cover the creation or maintenance of an organization in the same industry, trade, or profession. The limits on non-compete agreements and fiduciary duties, therefore, may be an attempt to ensure that each person in a community has sufficient opportunity to produce or join a profitable enterprise. Given how long it can take someone to master a new trade, profession, or industry, common law courts may be trying to ensure that everyone still has the capacity to provide for themselves (to flourish) after ending a business relationship. This commitment to ensuring that each member of the community is free to engage in the work required to survive may even be an expression of the necessity proviso if we relax the requirement of imminent danger. In that case, the limits on non-compete can be understood as protecting a person's ability to do what is always necessary to live—work.

The foregoing demonstrates that several forms of business organization fit the requirements of treating an object as someone's property, and many business law doctrines embody the provisos required to make sure that third parties are also able to flourish. Now let us consider how well the principles identified in *Natural Property Rights* allow us to deal with disputes over who has the best claim to the wealth created by businesses.

51. Meehan v. Shaughnessy, 404 Mass. 419, 435 (1989).
52. Town & Country House & Home Serv., Inc. v. Newbery, 3 N.Y.2d 554, 561–62 (1958).

V. THE RIGHTS OF STOCKHOLDER AND STAKEHOLDERS

A. *Profits as Increase to Res vs. Profits as Incentives to Bear Risk*

Let us return to our original questions. First, can we justify only recognizing principals as having a right to a business's profits when both principals and agents are contributing their labor to a business's production process? Second, given that most modern economic activity is incredibly interdependent, does the labor theory require recognizing communal ownership of the profits and other products of an economy? One popular method of explaining who keeps the profits generated by a business is to identify who bears the risk of an organization's activities.[53] Unlike secured and unsecured creditors of a business, the equity holders—owners—of a business are presumed to be fully responsible for all of the liabilities generated by the business. This includes tort, contract, and regulatory liabilities.[54] Before limited liability entities and bankruptcy courts were available, only secured and unsecured creditors could cap their losses at the amount of their investment. Frank Knight and other scholars used this fact to defend allowing entrepreneurs to keep the profits of their business: unlimited exposure to the risk of loss creates an unlimited right to profits. This risk-based justification of profits seems intuitive until we acknowledge that employees also face unlimited risk from doing their jobs. First, it is true that principals are responsible for the torts committed by their agents if committed in the scope of the agents' employment.[55] However, agents are also held personally responsible for the specific torts that they commit while employed, exposing them to unlimited liability in at least one narrow

53. FRANK H. KNIGHT, RISK, UNCERTAINTY AND PROFIT 48 (1921) (Profit "is clearly the result of risk, or what good usage calls such, but only of a unique kind of risk, which is not susceptible of measurement.").

54. UNIFORM PARTNERSHIP ACT § 306. (Partner's Liability) ("all partners are liable jointly and severally for all debts, obligations, and other liabilities of the partnership unless otherwise agreed by the claimant or provided by law."); Walkovszky v. Carlton, 18 N.Y.2d 414, 417, 223 N.E.2d 6, 8 (1966) ("In other words, whenever anyone uses control of the corporation to further his own rather than the corporation's business, he will be liable for the corporation's acts 'upon the principle of Respondeat superior applicable even where the agent is a natural person . . . Such liability, moreover, extends not only to the corporation's commercial dealings . . . but to its negligent acts as well.") (internal citations omitted.)

55. Ira S. Bushey & Sons, Inc. v. U.S., 398 F.2d 167, 171 (2d Cir. 1968) (describing respondeat superior as applied to business principles as resting on "a deeply rooted sentiment that a business enterprise cannot justly disclaim responsibility for accidents which may fairly be said to be characteristic of its activities.").

category.[56] Second, some jobs are so dangerous that the agent regularly faces the risk of death. The risk-based rationale for profits cannot explain why these open-ended risks do not result in a default or mandatory rule in favor of employees having some right to the profits that they help to generate through the business organization.

In Chapter 10 of *Natural Property Rights*, Claeys takes a detailed look at the boundary problems that develop when different individuals have an interest in using the same resource. His discussion of the concepts of increase and accession offers powerful insights for explaining the laws that currently determine who has a right to business profits. Consider an analogous conflict. If a bull owned by one person sires offspring with a cow owned by a second person, which party owns the offspring? Claeys identifies one easy-to-apply doctrine that presumes that the mother's owner is the owner of the calf. In pertinent:

> the doctrine of increase holds that "the offspring or increase of tame or domestic animals belongs to the owner of the dam or mother." In no way does the doctrine change the principle that the newborn calf constitutes a thing in law separate from the mother. But the doctrine does reverse the presumption that ownership of any one animal has little relation to ownership of any other. "[I]n the absence of an agreement to the contrary," cases hold, ownership of the offspring runs by operation of law with ownership of the mother.[57]

Any business with at least one agent (employee) raises similar questions. If many parties are involved in the production process, who has a right to the values generated by the business or by using the business's assets? As described above, agents are presumed to work for the sole benefit of their principals in the context of their agency relationship. This means that except for any agreed-upon compensation for the agent, all economic values created by their joint efforts usually belong to the principal. The example of the offspring belonging to the owner of the mother seems sensible because (at least in mammals) the mother's body does most of the work associated with procreation. The presumption that principals receive all of the value associated with the joint efforts of the principal and agent is just as sensible but for reasons that are more abstract. The principal retaining all of the value generated by their joint efforts is what the principal and agent have agreed to, and it is that agreement that creates the agency relationship. General partnerships are formed through a different kind of agreement. General partners agree to co-own a business. In addition to control over the business, the

56. RESTATEMENT (SECOND) OF AGENCY § 343 (AM. L. INST. 1957).
57. Claeys, *supra* note 1, at 275.

UPA defines ownership as involving "a right to share in the profits of the co-owned business."[58]

Like every other aspect of the rights and obligations between the parties in these relationships, both the UPA and common law agency principals recognize that rights to profits are created by, and can be modified by, the agreement between the parties. As a result, courts will even recognize a partner as having bargained away the right to retain control of a business created by that partner's labor.[59] Similarly, courts will also recognize an employee as having bargained for a right to profits or a portion of a business's owner's equity.[60] Ultimately, if a person has a right to the fruits of his or her own labor, then that person has the right to choose to when and how to share that labor with someone else—for free, for wages, or for profits.

Using the rule of increase to justify protecting a business owner's right to keep the profits of the business meets the *Natural Property Rights* criteria of being "good enough for government work."[61] Claeys designates laws as good enough for government work when they are flexible enough to apply to different subject matters yet clear enough to provide intelligible guidance to officials and civilians. If both cows and business organizations are objects of ownership (res), then the case law in one area should provide some guidance for resolving disputes in the other area. If a farmer owns a cow and the cow births a calf, the same farmer owns the calf. If an entrepreneur owns a business and the business generates profits, the same entrepreneur owns those profits. This approach seems more practical than the risk-bearing justification of profits discussed above. Ironically, justifying profits as increase to property maybe the source of Knight and other scholars adopting the rationale that profits are a reward for bearing risks. Praising the work of another economist, Knight states that the "entrepreneur is the owner of all real wealth, and ownership involves risk; the coordinator 'makes decisions,' but it is the entrepreneur who 'accepts the consequences of

58. UNIFORM PARTNERSHIP ACT § 202(a) cmt.

59. Day v. Sidley & Austin, 394 F. Supp. 986 (D.D.C. 1975), *aff'd sub nom.* Day v. Avery, 548 F.2d 1018 (D.C. Cir. 1976) (J. Edward Day was a senior partner Sidley & Austin, a Chicago law firm. Although Day "was instrumental in establishing a Washington office" for the partnership, he did not bargain for the right to control the D.C. office and therefore did not have a legal claim after the firms executive committee reduced his control over the D.C. office.)

60. Rash v. J.V. Intermediate, Ltd., 498 F.3d 1201, 1205 (10th Cir. 2007) ("The parties signed an employment agreement providing Rash a base salary of $125,000, a bonus of 20% of JVIC–Tulsa's net profits, and a termination bonus of 20% of the division's equity.").

61. Claeys, *supra* note 1, at 24.

decisions.'"[62] In other words, if entrepreneurs must take the bad with the good, it makes sense to conclude that they have a right to take the good with the bad. However, without acknowledging the property rights of principals, risk-based justifications of profits simply beg the question, "why do entrepreneurs and principals bear the risk"?

Further, the issue of who has a right to profits generated in an agency relationship is in part answered by recognizing business organizations as the quintessential objects of Lockean property. Let us take for granted that the sufficiency proviso in the context of business organization law protects each party's freedom to leave a business relationship and to form or join competing enterprises for their own benefit. In *Natural Property Rights*, the sufficiency proviso is partially justified by the "community of goods" assumption—the basic normative assumption that every person "has an inchoate interest in every resource" in that person's community. It is the community of goods assumption that motivates Locke to spend an entire chapter in his Second Treatise on Government explaining that private property is morally justified because it is required for individuals to make use of the raw materials of the world "to the best advantage of life, and convenience."[63] Business organizations are the quintessential objects of Lockean property because creating one does not require any specific raw materials as inputs. Moreover, some service businesses require no raw materials at all (i.e., babysitting or dog walking). These facts should make it even less of a concern that principals keep all of the profits generated with the aid of the agents in their organizations. Why? Because these profits are less dependent on the raw materials viewed as belonging to everyone under the community of goods assumption, which is Claeys's and John Locke's motivation for including the sufficiency proviso.

B. *Individual Ownership Following Joint Production*

The foregoing still leaves us with the need to explain why the interdependent nature of the modern economy does not require recognizing every member of the community as having a moral right to the products of our joint creative efforts. Put differently, if no single person can create a pencil, does every person and organization in the supply chain leading to the ultimate product have a moral right to either the pencil itself or

62. KNIGHT, *supra* note 53, at 45.
63. *See* JOHN LOCKE, TWO TREATISES OF GOVERNMENT para. 26 (Peter Laslett ed., Cambridge Univ. Press 1988) (1690).

to the profits generated once the pencil is sold?[64] These concerns were expressed by economists who described early capitalist economies as replacing serfdom and slavery with a new form of oppression.[65] Given that *Natural Property Rights* identifies making productive use of a resource as a requirement for creating an ownership interest, readers should be especially troubled by the profit rights of passive equity investors. For example, several courts have declared that "a business corporation is organized and carried on primarily for the profit of the stockholders."[66] In addition, cases that concluded that it is appropriate for corporations to make charitable contributions historically only did so after identifying how making the gift was beneficial to the corporation.[67] Yet, there are cases and statutes that support the contention that business corporations may owe something to the stakeholders in their communities and should not focus solely on their stockholders. For instance, over "30 states have adopted nonshareholder-constituency statutes that authorize directors to consider nonshareholder interests when making corporate decisions."[68] In addition to the financial impact on stockholders, these statutes allow directors to consider "the social, legal and economic effects of an offer upon employees, suppliers, customers and others having similar relationships with the corporation, and the communities in which the corporation conducts its business."[69] Even Delaware courts have determined that in some circumstances, directors may approve a transaction that will yield lower financial returns for

64. Leonard E. Read, *I, Pencil*, FOUND. FOR ECON. EDU. (Mar. 3, 2015), https://fee.org/resources/i-pencil/ [https://perma.cc/KK2R-N3UX].

65. Karl Marx, *Communist Manifesto*, https://www.marxists.org/archive/marx/works/1848/communist-manifesto/ch01.htm [https://perma.cc/4PVN-2JT2] ("In place of the old local and national seclusion and self-sufficiency, we have intercourse in every direction, universal inter-dependence of nations. And as in material, so also in intellectual production. The intellectual creations of individual nations become common property."); *id.* ("The bourgeoisie keeps more and more doing away with the scattered state of the population, of the means of production, and of property. It has agglomerated population, centralised the means of production, and has concentrated property in a few hands. The necessary consequence of this was political [and economic] centralisation.")

66. Dodge v. Ford Motor Co., 170 N.W. 668, 684 (1919).

67. A. P. Smith Mfg. Co. v. Barlow, 98 A.2d 581, 590 (N.J. 1953) (Approving a donation to a private school after finding that there was "no suggestion that it was made indiscriminately or to a pet charity of the corporate directors in furtherance of personal rather than corporate ends.").

68. Stephen M. Bainbridge and Iman Anabtawi, MERGERS AND ACQUISITIONS: A TRANSACTIONAL PERSPECTIVE 726 ch. 10 § 10.5, (2017) (B.A Note on the ALI Principles' Approach).

69. Stephen M. Bainbridge, *Interpreting Nonshareholder Constituency Statutes*, 19 PEPP. L. REV. 971, 984 (1992)

shareholders than a viable alternative if directors can point to the need to preserve a business enterprises' culture or some other competing interest.[70]

This Author is convinced that these concerns can be resolved using two methods: first, by considering the characteristics of the economic interactions at issue, and second, by exploring some assumptions made by John Locke that are not covered in this edition of *Natural Property Rights*. First, the facts about what is required for people to flourish and the facts about how people actually do interact in the economy undermine the expectation of the joint ownership of all of the resources produced in a community (or produced by the species). The idea that the division of labor and trade results in the common ownership of all products in the economy makes the mistake of reifying metaphors that analogize human societies to beehives or anthills. Unlike bees, however, human beings do not produce a bunch of goods and then pile them up in places where all members of the community have access to the goods. Outside of theft and taxation, human beings generally obtain goods from one another through consensual exchanges or by one person agreeing to make a gift to another person. Because of this, it seems sensible to treat the chosen consideration received in any exchange as satisfying any moral obligations that the counterparties have to one another or to any other person along the supply chain.

Second, this view that each consensual transaction terminates any additional obligation that counterparties owe one another is reinforced by Locke's recognition that human beings are fundamentally separate and equal.[71] This starting point in his *Second Treatise of Civil Government* is a rebuttal to the claim that any person has the divine right to rule over everyone in his community.[72] Having rejected divine right as a source of legitimacy for government officials, Locke pivots to the unanimous consent of the governed to form a civil society and the will of the majority to guide the use of government force.[73] Receiving unanimous consent from a large population to form and maintain a civil government is improbable but not impossible. Moreover, there is ample evidence that American law and culture have a longstanding commitment to both Locke's separate and equal principle and his consent of the governed principle. As imperfect as the American founding was, the Declaration

70. *See* Paramount Commc'ns, Inc. v. Time Inc., 571 A.2d 1140 (Del. 1989) (free press and culture . . . .).
71. LOCKE, *supra* note 63, at para. 96.
72. *Id.* at Para. 1.
73. *Id.* at Para. 96.

of Independence and early constitutional conventions make clear that it was an attempt to form several civil governments based on the consent of the governed.[74] Moreover, the most obvious form of America's imperfection—the institution of slavery—was attacked by prominent abolitionists who relied on Locke's starting assumptions that each person is fundamentally separate and equal. A beautiful example of this approach to the abolitionist movement was an argument made by Fredrick Douglass in a letter to his former owner. Advocates of chattel slavery understood Douglass's escape as the act of "stealing" himself from his former owner. In defending the righteousness of his escape, Douglass wrote the following:

> The morality of the act, I dispose as follows: I am myself; you are yourself; we are two distinct persons, equal persons. What you are, I am. You are a man, and so am I. God created both, and made us separate beings. I am not by nature bound to you, or you to me. Nature does not make your existence depend upon me, or mine to depend upon yours. I cannot walk upon your legs, or you upon mine. I cannot breathe for you, or you for me; I must breathe for myself, and you for yourself. We are distinct persons, and are each equally provided with faculties necessary to our individual existence. In leaving you, I took nothing but what belonged to me, and in no way lessened your means for obtaining an honest living. Your faculties remained yours, and mine became useful to their rightful owner. I therefore see no wrong in any part of the transaction.[75]

The artist and entrepreneur Shawn Corey Carter articulates a modern and more colloquial version of Douglass's argument in the song "Heart of the City." In response to those who might be motivated to attack him out of jealousy for his wealth and other success, Carter reminds his potential adversaries that "what you eat don't make me shit."[76] Similarly, a modern expression of the principle that consent is the foundation of legitimate authority can be found in the formation doctrines for agency relationships and general partnerships. Recall that under common law, these organizations only exist once the parties in these relationships agree on how a business will be controlled and how the benefits will be divided.[77] Furthermore, by default the UPA requires the consent of a majority of partners to change how the partnership handles ordinary

74. *See* THE DECLARATION OF INDEPENDENCE (U.S. 1776).
75. Letter from Frederick Douglass to Thomas Auld (Sept. 3, 1848), https://glc.yale.edu/letter-thomas-auld-september-3-1848 [https://perma.cc/46NZ-EZ39].
76. JAY-Z, *Heart of the City (Ain't No Love)*, *on* THE BLUEPRINT (2001), https://genius.com/Jay-z-heart-of-the-city-aint-no-love-lyrics [https://perma.cc/AG7D-8V2N].
77. *Supra* note 38.

issues and unanimous consent to make extraordinary changes to the management of the partnership.[78]

The prevalence and perpetuity of these Lockean principles in American law and culture reinforce the sensibility of treating members of the economy as fundamentally separate beings who are primarily producing goods for their own enjoyment. The only obligations to others recognized by law should be obligations created through binding agreements between specific members of the community. This means that when entrepreneurs form business enterprises to generate profits, they owe their employees bargained-for wages, and they owe customers and suppliers the bargained-for consideration. Everything else that entrepreneurs might do for the members of their communities can be recognized as making a gift under the *Natural Property Rights* framework. Moreover, given the Judeo-Christian origins of the expectation that the wealthy have moral obligations to provide for the less fortunate,[79] a full commitment to a Lockean approach likely requires leaving each person free to decide how to serve the members of his or her community.[80]

VI. CONCLUSION

Much more could be said about how business organization law exemplifies Professor Claeys's theory of natural property rights. However, the examples above demonstrate that a Lockean theory of property helps to explain many areas of business organization law.

78. UNIFORM PARTNERSHIP ACT § 401(k) (NAT'L CONF. OF COMM'RS ON UNIF. STATE L. 1997).
79. *See Matthew* 25:31–46; *see also 1 Timothy* 6.
80. JOHN LOCKE, LETTER CONCERNING TOLERATION 352 (1765).