University of St. Thomas Law Journal

Volume 6
Issue 2 *Winter 2009*

Article 6

2009

Our National Challenge: A Blueprint for Restoring the Public Trust

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Bluebook Citation
Lyman Johnson & Neil W. Hamilton, Introduction, *Our National Challenge: A Blueprint for Restoring the Public Trust*, 6 U. St. Thomas L.J. 397 (2009).

INTRODUCTION

OUR NATIONAL CHALLENGE: A BLUEPRINT FOR RESTORING THE PUBLIC TRUST

LYMAN JOHNSON AND NEIL W. HAMILTON

EDITOR'S NOTE: These remarks were presented at the Medtronic Business and Law Roundtable, "Our National Challenge: A Blueprint for Restoring the Public Trust," at the University of St. Thomas School of Law on March 19, 2009.

NEIL HAMILTON: Welcome to this program on "Our National Challenge: A Blueprint for Restoring the Public Trust." I am Neil Hamilton. I direct the Holloran Center for Ethical Leadership in the Professions.

We are very, very thankful for the support of Medtronic for this Medtronic Business and Law Roundtable. Medtronic supports three to four of our programs every year. We have been very fortunate for their support. I also want to thank our co-sponsor for this program, the Center for Ethical Business Cultures at the Opus College of Business, and its president, Ron James. Thank you, Ron, for all of your help and all the service you do for our community, and also for all the help with the Holloran Center.

Our moderator and final speaker today is Lyman Johnson; Lyman holds a joint appointment with both the University of St. Thomas School of Law as well as Washington and Lee University Law School in Virginia. At St. Thomas, he holds the LeJeune Distinguished Chair in Law, and at Washington and Lee, he holds the Robert O. Bentley Chair.

Lyman has Minnesota roots. He went to Carleton College, and to the University of Minnesota Law School. He practiced with Stacker and Ravich, which merged into the Robins law firm. He is an expert in corporate law, business planning, corporate finance, and securities regulation. His scholarship is widely recognized around the country.

LYMAN JOHNSON: Thank you, Neil. Let me also extend a warm welcome to all of you and thank you for coming. We have a great program in store for you. Let me make some introductory remarks to set the stage.

The last several months have certainly been tumultuous. What started in 2007 as a financial market problem became, late in 2008, a market meltdown followed by a severe worldwide and ongoing recession. The staggering loss in value of publicly-traded equities exceeds $35 trillion.[1] That does not include the loss of value of equity in homes, private corporations, private partnerships, or private limited liability companies, which would make that figure substantially higher.

Who would have thought that such household names as General Motors, Citigroup, or Bank of America would become "penny stocks" like some high-risk start-up venture with a great idea but few assets. Yet that is the price range in which their stocks now trade. Millions have been laid off, and many, many more millions live in daily fear that they might be laid off. Downturns do not just hurt financially, they also cause discouragement, and when a company acts fraudulently or with misconduct—whether from a Bernard Madoff, an Allen Stanford, or far too many others—they can lead to anger, fear, and a pervasive loss of trust.

Let me offer one of many possible measures of just how dispirited Americans have become about vital financial institutions in our society. In January of this year, the University of Chicago Graduate Business School, in conjunction with the Northwestern University Graduate Business School, announced the first findings of a new financial trust index.[2] That is not something that trades on the Exchange; it is something else. The index involved a survey of one thousand American households, and let me share three findings from this. First, only twenty-two percent of Americans trust the nation's financial system.[3] Put another way, four out of five Americans do not trust the financial system. Second, twelve percent trust the stock market.[4] Put another way, seven out of eight Americans do not trust the stock market, the central engine of capital formation and a key component of social and private wealth. Third, interestingly, among respondents who favor greater federal intervention in the financial sector, seventy-five percent had actually lost confidence as a result of recent federal initiatives.[5] This is a group that favors federal intervention, yet their confidence has waned as a result of federal intervention.

Now Americans, of course, have seen many other recessions before and we have experienced the Great Depression before, and we have certainly seen many momentous frauds, scandals, and breaches of trust in the past. One cannot read the financial history of the United States without

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1. *See* FTSE Mondo Visione Exchanges Index Monthly Analysis – March 2009 (2009), http://www.mondovisione.com/pdf/FTSEMVExInRpt0309.pdf.

2. Chicago Booth/Kellogg School Financial Trust Index, http://www.financialtrustindex.org/ (last visited May 22, 2009).

3. Allen Friedman, *Financial implications of eroding trust: Study shows how trust has become powerful motivator for Americans' financial decisions*, U. Chi. Chron., Feb. 5, 2009, *available at* http://chronicle.uchicago.edu/090205/trust.shtml; *see* Chicago Booth/Kellogg School Financial Trust Index, Results – Wave I, http://www.financialtrustindex.org/resultswave1.htm (last visited May 22, 2009) [hereinafter Results – Wave I].

4. Friedman, *supra* note 3; *see* Results – Wave I, *supra* note 3.

5. Friedman, *supra* note 3; *see* Results – Wave I, *supra* note 3.

being taken aback by the vast number of swindles that have taken place. We have come through these, and we have prospered. Many today, I think, however, sense something different. Not simply that there has been a dramatic decline in trust, but a genuine concern as to whether and how trust can be fully restored.

That is our topic today: restoring trust. We have a large trust deficit—one that may rival the federal deficit in size—and we need ideas for rebuilding our trust capital as surely as our banks need to replenish their financial capital. We have a distinguished panel representing many different sectors in society with diverse responsibilities and diverse vantage points. All of us, with one exception, work in the private sector. The one who does not work in the private sector is Chancellor Chandler, but most of what he does addresses conduct in the private sector. So he, too, has views on the private sector.

The private sector is where the loss of trust now lies, and one question is whether it, too, can be a place where solutions are developed. We hope to touch on how, going forward, various actors within the private sector itself might take steps to reform practices in their own cultures as a way to enhance public trust. Without that, the burden will fall solely to the government to bolster trust. Surely, new regulation is a necessary measure, something that Jack Coffee may speak to, but one can rightly doubt whether it is sufficient.

Let me briefly identify our panel members, and then I will introduce them more fully. We have Professor Jack Coffee from Columbia, Lizanne Thomas from the Jones Day law firm, Professor Rakesh Khurana from the Harvard Business School, and Chancellor Bill Chandler from the Delaware Court of Chancery. Our format today is that each of the speakers will speak in turn. We will then assemble as a panel and have some in-panel discussion, and then, time permitting—and I hope this is the case—we will open it up for audience questions and answers.

Our first speaker is John Coffee,[6] who is the Adolf A. Berle Professor of Law at the Columbia University Law School. I think Jack is perhaps the leading corporate law and securities law commentator in the U.S. today. He provided testimony to Congress last week on his thoughts about proposed new financial regulation.[7] Jack practiced with the law firm of Cravath, Swaine & Moore for several years before he entered academia. He has served as Reporter on a number of august bodies. He is a Fellow of the American Academy of Arts and Sciences, and he has been listed by the *National Law Journal* as one of "The 100 Most Influential Lawyers in the

6. Columbia Law School: Full Time Faculty, John C. Coffee, http://www.law.columbia.edu/fac/John_Coffee (last visited May 22, 2009).

7. *Enhancing Investor Protection and the Regulation of Securities Markets: Hearing Before the S. Comm. on Banking, Housing, and Urban Affairs*, 111th Cong. (2009) (statement of John C. Coffee).

United States." He has a casebook on securities regulation[8] and a casebook on corporations[9] and he now knows how to run PowerPoint.

Our second speaker brings the point of view of a corporate lawyer. Lizanne Thomas[10] is a partner at Jones Day, an international law firm. She is the partner in charge of the Atlanta office, and she also heads the firm's global corporate governance team.

Lizanne represents a number of publicly-traded companies and businesses throughout the United States, Europe, and Asia. She is actively involved in advising boards of directors and their committees on corporate governance, shareholder activism, and director liability issues. She has been involved in a number of special committees involving transactions, investigations, and litigation. She is a recurring panelist for the Directors' Institute, sponsored by the Conference Board. She lectures at seminars sponsored by the National Association of Corporate Directors, the Practicing Law Institute, and the American Bar Association. She has lectured throughout the world on matters of corporate governance and I am happy to say that she is also a graduate of Washington and Lee Law School. Her advice is not only lawyerly, but sage.

Our third speaker brings yet a different vantage point: the perspective of a judge. The Honorable William Chandler III,[11] was appointed Chancellor of the Delaware Court of Chancery in 1997. He served as Vice Chancellor from 1989 until his appointment as Chancellor. He now has been on the bench for twenty years. Prior to that, he practiced corporate law with the Delaware firm of Morris, Nichols, Arsht & Tunnell, and he served as legal counsel to former Governor Pete duPont.

I think it is fair to say that Bill, although he is a very humble man—and a man I like a great deal—is definitely the most influential judge in America on corporate law issues. He has addressed issues involving countless major U.S. corporations. Last month, he ruled on a case involving Citigroup,[12] and this month he was prepared to hear the trial in the Dow Chemical acquisition of Rohm & Haas. Fortunately for us, and probably for him, too, that case settled. Bill speaks widely across the country. He teaches at various law schools; he taught my class at St. Thomas two years ago.

Now, a word about the Court of Chancery: In our legal system, historically, we had a law side of the court and we had an equity side.[13] This

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8. John C. Coffee, Jr., Joel Seligman & Hillary A. Sale, Securities Regulation: Cases and Materials (10th ed. 2007).

9. Jesse H. Choper, John C. Coffee, Jr. & Ronald J. Gilson, Cases and Materials on Corporations (7th ed. 2008).

10. Lizanne Thomas: Professional Biography, http://www.jonesday.com/lthomas/ (last visited May 22, 2009).

11. Judges of the Delaware Court of Chancery, Chancellor William B. Chandler III, http://courts.delaware.gov/Courts/Court%20of%20Chancery/?jud_off.htm (last visited May 22, 2009).

12. *In re* Citigroup Inc. Shareholder Derivative Litigation, 964 A.2d 106 (Del. Ch. 2009).

13. *See* Dan B. Dobbs, Law of Remedies § 2.1(1) (2d ed. 1993).

grows out of Aristotle's conception of justice and equity.[14] This continued through English jurisprudence and on into this country until many decades ago when, in most states, law and equity merged.[15] The Court of Chancery in Delaware, though, remains a separate court. It is an equity court, and some people think that equity is sometimes a little bit hard to understand, and so I thought I would share a humorous anecdote about equity.

A student came to a law school dean one time wanting to study equity. The dean told him sternly, "First you must study law," and sent the student away. Three years later the student returned. "I studied law as you insisted," he said. "It was a worthless endeavor. The law is unjust, formalistic, nonsensical, and hopelessly confused. I have never been so frustrated in my life as in the last three years." "Now you are ready to study equity," said the dean.

Our final speaker brings yet a different perspective. Rakesh Khurana[16] is the Marvin Bower Professor of Leadership Development at the Harvard Business School. Professor Khurana's research uses a sociological perspective to focus, for example, on the processes by which elites and leaders are selected and developed. He has written extensively about the CEO labor market with a particular interest on the factors that lead to vacancies in the CEO position.

Professor Khurana's most recent book is one I highly recommend to you. I have just finished it. It is called *From Higher Aims to Hired Hands: The Social Transformation of American Business Schools and the Unfulfilled Promise of Management as a Profession*.[17] He chronicles the evolution of management as a profession with particular focus on the institutional development of the MBA. It is not without stinging criticism of graduate business education. He is very insightful, and does not pull punches. This book won the Max Weber Award in 2008 for outstanding contribution to scholarship in the past two years.[18]

Professor Khurana is a frequent commenter for *Business Week*, *Fortune*, *The Wall Street Journal*, *The New York Times*, *Newsweek*, and many other outlets. He has been recognized by the *London Times* as one of the Thinkers 50,[19] a list of the fifty most influential management thinkers in the world.

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14. ARISTOTLE, NICOMACHEAN ETHICS 97–100 (Hippocrates G. Apostle trans., Peripatetic Press 1984) (350 B.C.E.).

15. *See* DOBBS, *supra* note 13, § 2.6(1).

16. Harvard Business School Faculty Biography, Rakesh Khurana, http://dor.hbs.edu/fit/public/facultyInfo.do?facInfo=bio&facEmId=rkhurana%40hbs.edu (last visited May 22, 2009).

17. RAKESH KHURANA, FROM HIGHER AIMS TO HIRED HANDS (2007).

18. American Sociological Association, Recipients of 2008 Section Awards, http://www.asanet.org/cs/root/leftnav/awards/recipients_of_2008_section_awards (last visited May 22, 2009).

19. The Thinkers 50, 2007 Global Ranking of Business Thinkers, http://www.thinkers50.com/?page=2007 (last visited May 22, 2009).

The months ahead will bring the Obama administration's proposals for regulatory reform. These will be debated in Congress and in the broader society, as we all seek ways to improve regulatory gaps and shortcomings in the public sector. The program today, however, is a bracing reminder that, just as many problems started in the private sector, so too private sector institutions must reform themselves if they are to regain the public trust.