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TOO BIG TO FAIL, TOO BIG NOT TO KNOW: FINANCIAL FIRMS AND CORPORATE SOCIAL RESPONSIBILITY

Z. JILL BARCLIFT*

"WHAT HAPPENS ON WALL STREET HAS REAL CONSEQUENCES ACROSS THE COUNTRY, ACROSS OUR ECONOMY."1

In 2008, the U.S. financial markets experienced a series of cataclysmic events that continue to dominate the economic news two years later.2 The financial crisis began with the collapse of the mortgaged-backed securities market, which led to the failure of several Wall Street financial firms.3 The financial markets reacted to these events by freezing credit, which contributed to U.S. and global recessions.4 In unprecedented actions, the federal government injected capital into the financial markets by providing loans and equity to financial firms in order for these institutions to avoid

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2 See Shahien Nasiripour, Financial Crisis Investigators Looking at Wall Street, THE HUFFINGTON POST, Feb. 26, 2010, http://www.huffingtonpost.com/2010/02/26/financial-crisisinvestig_n_478520.html ("Goldman Sachs and others helped inflate the housing bubble by funding and securitizing junk mortgages, selling them off to investors and pocketing the fees — while at the same time placing contrary bets in the expectation that the market would eventually crash.").

3 See CHARLES R. MORRIS, THE TRILLION DOLLAR MELTDOWN 107–36 (PublicAffairs 2008) (describing that the subprime crisis was just the beginning of the crisis in the summer of 2007); see also Shawn Tully, What's Wrong With Wall St. and How to Fix It, 157 FORTUNE 7, at 70–76 (Apr. 14, 2008) (explaining how things would be different following the government “clean up” of the subprime mortgage “mess”); see also Allan Sloan & Doris Burke, On the Brink of Disaster, 157 FORTUNE 7, at 78–84 (Apr. 14, 2008) (discussing the subprime mortgage failures at Bear Stearns); see also Roddy Boyd & Doris Burke, The Last Days of Bear Stearns, 157 FORTUNE 7, at 86–89 (Apr. 14, 2008) (describing how it only took a few days for the Bear Stearns investment bank to collapse).

4 See MORRIS, supra note 3, at 128–33 (concluding that there is and will continue to be a decline in the availability of credit); see also Carrie Mollenkamp et al., Lehman’s Demise Triggered Cash Crunch Around Globe, WALL ST. J., Sept. 29, 2008, at A1 (giving insight into the panic and lack of trust in the U.S. and global markets during the few days that Lehman dissolved); Press Release, U.S. Dep’t of the Treasury, Testimony by Sec’y Henry M. Paulson, Jr. Before the Senate Banking Committee on Turmoil in U.S. Credit Markets: Recent Actions Regarding Gov’t Sponsored Entities, Investment Banks and other Financial Institutions (Sept. 23, 2008) (on file with author), available at http://www.ustreas.gov/press/releases/hp1153.htm (explaining the severity of financial market being frozen).
serious financial losses or bankruptcy. Many contend that the recession fueled by the financial crisis is nearing an end; however, its underlying causes and responses are still debated.

The federal government initiated a multi-agency investigation into the conditions that caused the financial meltdown. The Treasury Department concluded that the primary triggers precipitating the financial crisis were the lack of regulatory oversight, the risky bets of many Wall Street firms, and transparency in the selling of collateralized debt obligations and mortgage-backed securities by banks, investment banks, and other financial institutions.

The Treasury Department announced as a regulatory priority the assessment of systemic risks in the financial markets; and it began

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5 See Deborah Solomon et al., U.S. Seals Bailout Deal, WALL ST. J., Sept. 29, 2008, at A1 (detailing the specifics of the bailouts and giving justification for this bill); see also Alan Murray, Fixing Global Finance, WALL ST. J., Dec. 14, 2009, at R1 (suggesting ways to strengthen the financial institutions, including a demand for each institution to hold more capital).

6 See Bradford Cornell, The Fundamental Nature of Recessions: A Contracting and Restructuring Perspective, 6 ECON. VOICE 1 (2009), available at http://www.bepress.com/ev/vol6/iss9/art6 (stating that "economic interaction is managed not through markets, but through personal plans, commitments [such as career decisions], relationships, and contracts [including implicit contracts]," and explaining how many of these plans are long term, resulting in a recession when these relationships were unable to quickly respond to the changes in the financial and housing markets); see also Lucian A. Bebchuk, A Better Plan for Addressing the Financial Crisis, 5 ECON. VOICE 1 (2008), available at http://www.bepress.com/ev/vol5/iss5/art6 (critiquing proposed emergency legislation); David O. Beim, Good Bailouts and Bad, 5 ECON. VOICE 1 (2008), available at http://www.bepress.com/ev/vol5/iss5/art8 (evaluating whether or not the recent bailout plant was good or bad); Economic Outlook: Hearing Before the J. Econ. Comm., 111th Cong. (2008) (statement of Chairman Ben S. Bernanke), available at http://www.federalreserve.gov/newsevents/testimony/bernanke20080924a.htm (discussing how "[t]he downturn in the housing market has been a key factor underlying both the strained condition of financial markets and the slowdown of the broader economy" and how to respond to the situation); Luigi Zingales, Plan B, 5 ECON. VOICE 1 (2008), available at http://www.bepress.com/ev/vol5/iss6/art4 (explaining Treasury Secretary Hank Paulson’s Plan B, and how it will not work).


8 See Press Release, Financial Stability Plan, supra note 7 (outlining the events that led to the turmoil of the U.S. credit markets); see also MORRIS, supra note 3, at 83–85 (discussing the history of various financial breakdowns); Press Release, Financial Markets Update, supra note 7 (setting forth some of the root causes of the strain to U.S. and global financial markets); Russell Roberts, How Little We Know: The Challenges of Financial Reform, 6 ECON. VOICE 1, 3 (2009), available at www.bepress.com/ev/vol6/iss11/art3 (discussing the financial crisis).
identifying financial institutions it deemed "too big to fail" by establishing procedures for a stress test on such institutions. A financial institution is deemed "too big to fail" if its collapse or bankruptcy would disrupt the capital markets in such a catastrophic way that it would push the U.S. economy into recession or depression.

Congress is currently debating legislation to increase transparency and regulations over financial institutions. Omitted, however, from the assessment of systemic risks is an evaluation of a financial firm's corporate governance. Government stress tests do not evaluate a financial firm's obligation to engage in good corporate governance; nor do they evaluate a financial institution's corporate social responsibility.

Although a discussion of the corporate social responsibility of financial firms seems to reengage a debate that is settled, it is a discussion worth reconsidering in light of Wall Street's role in the current financial crisis. Many would argue that because Wall Street firms only have a duty to maximize shareholder wealth, there is little need to address issues of societal harm caused by the sale of products and financial securities, such as subprime mortgage loans. Yet, over the years, the role of corporate social responsibility as a measure of good corporate governance has increased as economic globalization has come to serve as the incentive.

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9 See Press Release, Financial Stability Plan, supra note 7 (explaining the stress test used as part of a comprehensive Capital Assistance Program designed to offset financial institutions' losses).

10 See id. (discussing the capital assistance program providing large financial institutions with "capital buffer" to absorb losses); see also GARY H. STERN & RON J. FELDMAN, TOO BIG TO FAIL: THE HAZARDS OF BANK BAILOUTS 9 (2009) (establishing that "too big to fail is a problem of credibility," in that "creditors of large banks do not believe that the government will make them bear all their losses from bank failure").

11 See Press Release, Remarks by the President, supra note 1 (addressing two bills within the Senate and House regarding financial reform); see also David M. Herszenhorn, Bill Passed in Senate Broadly Expands Oversight of Wall St., N.Y. TIMES, May 20, 2010, available at http://www.nytimes.com/2010/05/21/business/21regulate.html (discussing a bill passed by the Senate that will "touch virtually every aspect of the financial industry").


13 See Halina Ward, Corporate Social Responsibility in Law and Policy, in PERSPECTIVES ON CORPORATE SOCIAL RESPONSIBILITY 8, 14 (Nina Boeger, Rachel Murray & Charlotte Villiers eds., 2008) (discussing how the mainstream CSR agenda is focused on the role of market actors "to ensure that economic globalization is supportive of social and environmental progress"); see also DAVID MILMAN, NATIONAL CORPORATE LAW IN A GLOBALISED MARKET: THE UK EXPERIENCE IN PERSPECTIVE 146 (Edward Elgar Publ'g Ltd. 2009) (expressing the need for social moral responsibility); Cynthia A. Williams, Corporations Theory and Corporate Governance Law: Corporate Social Responsibility in an Era of Economic Globalization, 35 U.C. DAVIS L. REV. 705, 720–21 (2002) (discussing transnational economic activity in the globalizing economy).
Several Wall Street financial firms have significant corporate social responsibility initiatives focused on philanthropy and the environment.14 However, the financial crisis has brought into sharper focus the connection between Wall Street and Main Street by demonstrating the link between financial firms’ products and societal well-being. As the President’s recent comments indicate, what happens on Wall Street has broader consequences for our economy.

This article reconsiders the debate over the role of corporate social responsibility as a governance tool to monitor the behavior of management in financial firms that have been identified by the federal government as “too big to fail.” Financial institutions deemed critical to the economy must have corporate governance processes in which board and management decision-making is not only reliable and transparent, but is also engaged in the utmost rigor in assessing profitability and economic viability in financial markets and the communities in which they compete.

Part one of this Article explores the link between products sold by Wall Street financial firms and broader societal harm, particularly to local communities. Part one examines the meaning of “too big to fail” and the criteria by which the government identifies a financial institution as critical to the economy. This part also looks at the role of sub-prime mortgage lending in the financial crisis, and explores how Wall Street firms enabled sub-prime mortgage lending in communities. Part one further examines the negative effects of securitization and sub-prime mortgages on local communities, and evaluates the connection between Wall Street financial products and societal harm. Additionally, part one examines the litigation surrounding sub-prime mortgages and the effort to hold various parties involved in sub-prime mortgage lending legally accountable. This part

14 See, e.g., Corporate Social Responsibility at Citi, http://www.citibank.ro/en/desprenoi/responsabilitate-sociala-la-citi.html (last visited June 25, 2010) (“Citi has long been committed to making the communities in which it operates better,” focusing on microfinance and microentrepreneurship, small and growing businesses, education, financial education, asset building, and the environment, and engaging in Global Community Day and Volunteer Program in Romania); Wells Fargo in the Community, https://www.wellsfargo.com/about/csr/ (last visited June 25, 2010) (giving hope by providing an average of $553,425 per day to nonprofits and donating 1.23 million employee volunteer hours in 2009); Citizenship: Corporate Engagement., http://www2.goldmansachs.com/citizenship/index.html (last visited July 18, 2010) (stressing the firm’s commitment to assisting communities worldwide through financial support to areas such as small businesses, education, and the environment); About Bank of America: In the Community, http://www.bankofamerica.com/index.cfm?page=about (last visited July 18, 2010) (discussing how Bank of America is “investing in our communities and our economy”); see also What Does the Future Hold For This Country, http://www.bankofamerica/global/hs_home/pdf/CSR_Brochure_Final.pdf (discussing Bank of America’s CSR initiatives); Phil Mattern, Corporate Social Irresponsibility, DIRT Diggers DIGEST, May 17, 2010, http://www.southernstudies.org/2010/05/corporate-social irresponsibility.html (discussing companies that claim to have enlightened policies on environmental and social policies).
suggests that the increasing amount of litigation against parties involved in the securitizations is a wake-up call for financial firms to not only properly document their loans, but to engage in greater scrutiny of the supply chain for consumer mortgages in order to understand moral hazard risks.

Part two explores the efficacy debate over corporate social responsibility's role in corporate governance. This part explores the evolution of corporate social responsibility as a corporate governance tool and examines the limitations of corporate social responsibility in effectuating corporate governance changes. This part also argues that the lack of a concise meaning for corporate social responsibility has allowed financial firms to define corporate social responsibility as the completion of good deeds or a moral checklist for corporate conduct. As financial firms have focused on philanthropy and the environment to assess corporate social responsibility, they have failed to address a more meaningful corporate social responsibility in which products sold and societal harm are evaluated and disclosed to shareholders.

Part three calls for a concise definition of corporate social responsibility for financial firms deemed critical to the U.S. economy. This part argues for mandatory corporate social responsibility compliance and disclosures. Further, part three of the article examines how the financial crisis has changed the regulatory environment for financial institutions. This part identifies ways in which the new regulatory regime presents an opportunity to implement corporate social responsibility as part of good corporate governance for financial firms critical to economic stability. The article concludes by recommending a corporate social responsibility definition for "too big to fail" financial firms and by suggesting mandatory compliance via disclosure. It argues for improved disclosure of corporate social responsibility accounting.

I. "TOO BIG TO FAIL" AND THE "STRESS TEST"

The phrase "too big to fail" refers to a banking or financial organization so large that the federal government must support and prevent the collapse of the institution because its failure poses a significant risk to the entire financial and economic systems.15 Although economists disagree whether

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15 See STERN, supra note 10, at 1, 12 (noting that big banks "play an important role in a country's financial system and economic performance" and that their failure is "seen as posing significant risks to ... the financial system as a whole ... "); see also David Cho, Banks 'Too Big to Fail' Have Grown Even Bigger, WASH. POST, Aug. 28, 2009, available at http://www.washingtonpost.com/wp-dyn/content/article/2009/08/27/AR2009082704193.html?sid=ST2009090801107 (expressing that "[w]hen the credit crisis struck last year, federal regulators pumped tens of billions of dollars into the
government protection of creditors for economic loss is warranted, the policy behind government bailouts of large financial institutions is to reduce the risk of bank failures or capital market freezes, which may result from the collapse of a large financial institution.\textsuperscript{16}

The purpose of the Treasury Department’s Financial Stability Plan is to identify financial institutions whose collapse would have negative effects on capital markets.\textsuperscript{17} Key points of the Treasury Department’s stress test call for increased transparency, accountability, and monitoring of financial institutions receiving federal funds.\textsuperscript{18} After identifying major financial institutions, the government proposes to determine whether the financial institutions have the capital to lend and absorb losses in the event of a severe economic downturn.\textsuperscript{19}

Financial institutions passing the stress test will be permitted to access a government funded capital buffer.\textsuperscript{20} The capital buffer serves as a “contingent equity” providing financial firms with access to capital in the nation’s leading financial institutions because the banks were so big that officials feared their failure would ruin the entire financial system.”).

\textsuperscript{16} See STERN, supra note 10, at 1, 12 (stating that “[d]etermining the appropriate policy response to an important failing bank has long been a vexing public policy issue,” and that “[t]he failure of a large banking organization is seen as posing significant risks to other financial institutions . . . and possibly to the economic and social order;” because there is a “chance that one bank’s failure can spill over and threaten the viability of other banks”); see also Cornell, supra note 6, at 2–3 (discussing why there is reason to be pessimistic about “whether the government can do anything to speed the restructuring process or reduce its cost”); Bebchuk, supra note 6, at 1–2 (critiquing the U.S. Treasury Department’s proposed emergency legislation to purchase “troubled assets” from financial institutions); Beim, supra note 6, at 1–2 (describing good bailouts versus bad bailouts, and how it is hard to tell whether the current bailout plans are good or bad); Zingales, supra note 6, at 1–2 (setting forth the possible problems of bailing out Wall Street); Luc Laeven & Fabian Valencia, Systemic Banking Crises: A New Database 3–4 (Int’l Monetary Fund, Working Paper No. WP/08/224, 2008) (discussing how “choosing the best way of resolving a financial crisis and accelerating economic recovery is far from unproblematic,” and how empirical research shows that “providing assistance to banks and their borrowers can be counterproductive, resulting in increased losses to banks, which often abuse forbearance to take unproductive risks at government expense.”).

\textsuperscript{17} See Press Release, Financial Stability Plan, supra note 7 (“To address the financial crisis, the Financial Stability Plan is designed to attack our credit crisis on all fronts . . . To be successful, we must address the uncertainty, troubled assets and capital constraints of our financial institutions as well as the frozen secondary markets that have been the source of around half of our lending for everything from small business loans to auto loans.”).


\textsuperscript{19} See Press Release, Financial Stability Plan, supra note 7 (articulating that through the “stress test” the government will assess “whether major financial institutions have the capital necessary to continue lending and to absorb the potential losses that could result from a more severe decline in the economy than projected”).

\textsuperscript{20} See id. (noting that “a financial institution that has undergone a comprehensive ‘stress test’ will have access to a Treasury provided ‘capital buffer’”).
event that lending conditions worsen. Additionally, in order to address the freezing-up of lending in secondary markets and securitizations, the government designed a lending program to provide financing to private investors so to help unfreeze lending markets and improve consumer lending.

The Treasury Department’s stress test will likely identify future institutions engaged in risky lending practices or those with risky assets on their books. Implementation of the stress tests may also prevent the failure of individual financial institutions and minimize the cascade of failures in the capital market. Yet, the current financial crisis had many accelerative events, which resulted in risky lending practices for financial institutions. Sub-prime mortgage lending and securitization are identified as key accelerants of the financial crisis. They have had the most direct impact on consumers and together provide the most demonstrative link between Wall Street products and local community well-being.

A. The Financial Crisis – Securitization and Sub-prime Lending

The risky bets of Wall Street firms have had a dramatic effect on our communities in many ways. In the process known as securitization, financial firms purchased mortgages from mortgage brokers, banks, and other lenders, and bundled the mortgages into securitized assets. Financial firms’ insatiable appetite for the securitized assets created a

21 See id. ("[T]he Financial Stability Trust will provide a capital buffer that will: [o]perate as a form of “contingent equity” to ensure firms the capital strength to preserve or increase lending in a worse than expected economic downturn.").
22 See Press Release, Financial Stability Plan, supra note 7 (discussing how “[t]he Consumer and Business Lending Initiative will support the purchase of loans by providing the financing to private investors to help unfreeze and lower interest rates . . . ”).
23 See Press Release, Financial Markets Update, supra note 7 (noting that the Department of the Treasury plans to use more oversight in the future).
24 See id. (stating that part of the strategy of the Emergency Economic Stabilization Act “is designed to mitigate financial market disruption when a bank fails”).
25 Senator Charles E. Schumer, Sheltering Neighborhoods from the Subprime Foreclosure Storm, Special Report by the Joint Economic Committee (2007), available at http://jec.senate.gov/archive/Documents/Reports/subprimelapr2007revised.pdf (discussing how “it has become increasingly clear that irresponsible subprime lending practices have been contributing to a wave of foreclosures that are hitting homeowners and rattling the housing markets.”).
26 See id. (highlighting the current financial effects of the subprime mortgage crisis).
27 See Adam B. Ashcraft & Til Schuermann, Understanding the Securitization of Subprime Mortgage Credit, FED. RES. BANK N.Y. STAFF REP. NO. 318, at 2–3 (2008) (discussing how “the securitization of mortgage loans is a complex process that involves a number of different players.”); see also Taylor D. Nadauld & Shane M. Sherlund, The Role of the Securitization Process in the Expansion of Subprime Credit 2 (Fin. & Econ. Disc. Series, Working Paper No. 2009-28, 2009) (on file with author) (commenting that banks were not stupid when making subprime loans: “they passed the buck to other people” by securitizing them).
morally hazardous environment where fraud and unscrupulous mortgages increased as Wall Street financial firms continued to look for mortgage loans to sell in the secondary market.²⁸

Securitization is the process of pooling consumer mortgages and selling the pooled mortgages as a separate security.²⁹ The underlying consumer mortgage is separated from the security instrument sold by financial firms in the secondary securitization market.³⁰ A trustee is ultimately the owner of record of the consumer mortgage.³¹

Securitization of loans is highly profitable for financial institutions.³² The lenders and financial institutions involved in the securitization process reaped financial rewards for originating consumer mortgages, servicing, or selling the bundled assets to other financial firms.³³ Because financial firms had to sell the securitized assets, the originator of the loan held no responsibility for the quality of the loan, and the ultimate owner of the consumer mortgage had no concern for the consequences of the loan on the consumer.³⁴ Moreover, the financial institution selling the mortgage-backed securitized asset took no responsibility for the terms of the underlying loan, and no one in the securitization chain cared about whether the consumer could ultimately afford or repay the loan.³⁵ The financial

²⁸ See Nadauld, supra note 27 (stating how banks were making dubious loans); see also Michael G. Crouhy et al., The Subprime Credit Crisis of 07, 5, 7, 11 (July 9, 2008) (unpublished manuscript, on file with author), available at http://ssm.com/abstract=1112467 (suggesting that the process of securitization led many loan originators to commit fraud and other questionable acts); see generally The Joint Economic Committee, Subprime Mortgage Market Crisis Timeline (2007), available at http://www.criminallawlibraryblog.com/subprime crisis_timeline.pdf.

²⁹ See Ashcraft, supra note 27, at 6 (highlighting how the “pool of mortgage loans is sold by the originator to a bankruptcy-remote trust, which is a special-purpose vehicle that issues debt to investors.”); see also Nadauld, supra note 27, at 49 (discussing how “[p]ools of subprime loans are originated by retail banks or mortgage brokers and subsequently sold to private financial intermediaries,” often “Wall Street firms . . .”).

³⁰ See Ashcraft, supra note 27, at 6 (mentioning how a credit risk transfer “protects investors from bankruptcy of the originator or arranger . . . .’); see also Nadauld, supra note 27, at 49 (noting how pools of loans are put into remote bankruptcy trusts, which is a separate legal entity).

³¹ See Ashcraft, supra note 27, at 6 (noting how the “pool of mortgage loans is sold by the originator to a bankruptcy-remote trust’’); see also Nadauld, supra note 27, at 49 (noting the presence of a trustee due to the bankruptcy remote trust).

³² See Ashcraft, supra note 27, at 6–7 (stating that “the trust protects both the originator and arranger from losses on the mortgage loans”). See generally MORRIS, supra note 3, at 59–85, 87–105 (discussing the current cost and profit of subprime mortgages as well as the value of the United States dollar).

³³ See Ashcraft, supra note 27, at 5 (“[T]he originator might sell a portfolio of loans with an initial principal balance of $100 million for $102 million, corresponding to a gain on sale of $2 million. The buyer is willing to pay this premium because of anticipated interest payments on the principal.”); see also Nadauld, supra note 27, at 21 (explaining how regulatory capital arbitrage generates profits for lenders and financial institutions).

³⁴ See Crouhy et al., supra note 28, at 5 (discussing how originators did not care about the value of the loans because they passed on the losses to the trusts).

³⁵ See Ashcraft, supra note 27, at 11–12 (explaining how the various frictions between the parties
incentives in the securitization processes rewarded volume, thereby exacerbating the moral hazard problem.\textsuperscript{36}

\textbf{B. Sub-prime Lending}

In order to meet the demands for mortgages that could be sold to Wall Street financial firms, lenders increasingly designed loan products for sub-prime borrowers so as to increase the pool of consumer mortgages that could be securitized.\textsuperscript{37} Sub-prime mortgages are loans to borrowers with low credit scores or limited credit history.\textsuperscript{38} Sub-prime mortgages carry higher interest rates and are typically tied to adjustable rate mortgages.\textsuperscript{39} A federal report indicates that sub-prime mortgage loans were more involved in the subprime mortgage market allowed for predatory borrowing, predatory lending, and the abandonment of due diligence; \textit{see also} Nadauld, \textit{supra} note 27, at 6 (noting that “the prospect of selling loans to secondary markets reduces lenders’ incentives to screen borrowers carefully”); Crouhy et al., \textit{supra} note 28, at 5 (explaining how each party in the securitization chain avoided or absorbed the losses from defaulted subprime loans).

\textsuperscript{36} \textit{See} Ashcraft, \textit{supra} note 27, at 74 (“The parties involved at ComFed exaggerated property values to increase the volume-oriented commissions that they received for originating loans. To increase underwriting volumes still more, ComFed employees granted loans to unqualified borrowers by concealing the fact that these obligors had financed down payments with second-lien mortgages.”); \textit{see also} Crouhy et al., \textit{supra} note 28, at 11 (explaining how the compensation package for brokers was based on the volume of loans originated); John M. Quigley, \textit{Compensation and Incentives in the Mortgage Business}, \textit{ECON. VOICE} 1 (2008), \textit{available at} http://www.bepress.com/ev/vol15/iss6/art2 (“[E]ach specialized party to the mortgage had fee-based compensation that motivated a large volume of transactions with little or no concern about the performance of the mortgages.”).

\textsuperscript{37} \textit{See} Ashcraft, \textit{supra} note 27, at 2 (explaining a table that illustrates the increases in subprime origination and issuance during the years that an increased amount of these loans were sold to investors); \textit{see also} Nadauld, \textit{supra} note 27 app. § 1a (pointing out that subprime loans used to represent a small portion of total mortgage originations until Wall Street firms began buying them); Crouhy et al., \textit{supra} note 28, at 4, 5 (explaining how subprime mortgages were in demand, tracking the marketshare growth of subprime mortgages, and stating that there was pressure to increase the supply of subprime mortgages as a result of investor demand).

\textsuperscript{38} \textit{See} Ashcraft, \textit{supra} note 27, at 14 (“The 2001 Interagency Expanded Guidance for Subprime Lending Programs defines the subprime borrower as one who generally displays a range of credit risk characteristics, including one or more of the following: \{\textit{t}\}wo or more 30-day delinquencies in the last 12 months, or one or more 60-day delinquencies in the last 24 months; \{\textit{j}\}udgment, foreclosure, repossession, or charge-off in the prior 24 months; \{\textit{b}\}ankruptcy in the last 5 years; \{\textit{r}\}elatively high default probability as evidenced by, for example, a credit bureau risk score (FICO) of 660 or below (depending on the product/collateral), or other bureau or proprietary scores with an equivalent default probability likelihood; and/or, \{\textit{d}\}ebt service-to-income ratio of 50 percent or greater; or, otherwise limited ability to cover family living expenses after deducting total debt-service requirements from monthly income.”); \textit{see also} Nadauld, \textit{supra} note 27, app. § 1a (describing the basic characteristics of a subprime mortgage); Crouhy et al., \textit{supra} note 28, at 50 n.1 (“The term ‘subprime’ refers to mortgages who are unable to qualify for prime mortgage rates. Reasons for this include poor credit histories (payment delinquencies, charge offs, bankruptcies, low credit scores, large existing liabilities, high loan to value ratios.”).

\textsuperscript{39} Chris Mayer & Karen Pence, \textit{Subprime Mortgages: What, Where, and to Whom?} 2 Fin. & Econ.

predominate in low-income communities.\textsuperscript{40}

Low income communities and communities of color were more likely to be the victims of fraudulent and unscrupulous mortgage broker practices, including the selling of sub-prime mortgage loans and predatory lending.\textsuperscript{41} These practices resulted in increased foreclosures, as families could no longer afford their homes when adjustable interest rate loans increased their mortgage payments to excessive levels.\textsuperscript{42} Sub-prime mortgage foreclosures make up a significant percentage of foreclosures, further fueling the financial crisis.\textsuperscript{43}

Foreclosures harm families by decreasing family stability, harming credit ratings, and decreasing a significant source of family wealth.\textsuperscript{44} Not only do individual families directly experience the devastation of foreclosure, but communities suffer as well. Communities with a high percentage of subprime mortgage loans also experience high rates of foreclosure.\textsuperscript{45}

\textsuperscript{40} See U.S. Dep’t of Housing & Urban Dev., \textit{Unequal Burden: Income and Racial Disparities in Subprime Lending in America} (2000), available at http://www.huduser.org/portal/publications/fairhsg/unequal.html ("The data clearly demonstrate the rapid growth of subprime lending during the 1990’s and, further, the disproportionate concentration of such lending in the nation’s minority and low-income neighborhoods."); see also John C. Coffee Jr., \textit{What Went Wrong? A Tragedy In Three Acts}, 6 U. St. Thomas L.J. 403, 405 (2009) (stating that "[b]etween 2001 and 2006, the availability of mortgage funds increased sharply, with most of this increase being channeled to poorer communities").

\textsuperscript{41} See Mayer, supra note 39, at 1–2 (discussing the results of research on subprime mortgages, including findings that these mortgages are concentrated in locations with high proportions of black and Hispanic residents); see also U.S. Dep’t of Housing & Urban Dev., \textit{supra} note 40 ("Since subprime lending often operates outside of the federal regulatory structure, it is a fertile ground for predatory lending activities, such as excessive fees, the imposition of single premium credit life insurance and prepayment penalties. The recent acceleration in predatory lending activity has accompanied the growth in subprime lending over the past decade."); Schumer, \textit{supra} note 25 (discussing subprime mortgages and how studies show that they are most prevalent in lower-income neighborhoods with high concentrations of minorities; for instance, in 2005, 53 percent of African Americans and 37.8 percent of Hispanic borrowers took out subprime mortgages, and subprime mortgages were 5 times more likely to be found in predominately black neighborhoods than predominately white neighborhoods); Jennifer E. Bethel et al., \textit{Legal and Economic Issues in Litigation Arising From the 2007-2008 Credit Crisis}, 16 Harvard Law Sch. Program on Risk and Reg., Discussion Paper No. 08-5 (2008), available at http://ssrn.com/abstract=10965582 (setting forth evidence that “at least some mortgage bankers and brokers may have submitted false appraisals and financial information to qualify otherwise unqualified households for subprime mortgage loans”).

\textsuperscript{42} See U.S. Dep’t of Housing & Urban Dev., \textit{supra} note 40 (cautioning that “predatory lending can have disastrous consequences for the unknowing borrower,” such as equity being stripped from the home or even having the home stripped from its owner altogether).

\textsuperscript{43} See U.S. Dep’t of Housing & Urban Dev., Office of Pol’y Dev. & Res., \textit{Report to Congress on the Root Causes of the Foreclosure Crisis}, vi (2010), available at http://www.huduser.org/Publications/PDF/Foreclosure_09.pdf (“Most of the initial increase in foreclosures was driven by subprime loans, both due to the fact that these inherently risky loans had come to account for a much larger share of the mortgage market in recent years and because the foreclosure rates among these loans were rising rapidly.”).

\textsuperscript{44} See Schumer, \textit{supra} note 25, at 14 (discussing the costs of foreclosures on families).

\textsuperscript{45} See U.S. Dep’t of Housing & Urban Dev., \textit{supra} note 40 (noting that foreclosure is a relatively more “egregious” case); see also SCHUMER, \textit{supra} note25, at 14 (listing some of the negative effects of foreclosures).
Neighborhoods with increased foreclosed properties experience an overall decline in home values, safety, and community continuity. Increased foreclosures in neighborhoods likewise negatively impacts cities. Foreclosures put downward pressure on housing prices, which results in significant costs to cities and local governments. Neighborhoods with significant foreclosures experience an overall drop in home prices.

In neighborhoods with high foreclosure rates, a phenomenon known as "spillover" occurs, in which home values decrease for the entire community. Additionally, in low-income communities where there are a greater percentage of multi-family buildings, many rent-paying families face eviction when their apartment rentals are foreclosed.

C. Sub-prime Litigation

A variety of lawsuits have been filed by a host of different plaintiffs seeking relief from the consequences of the mortgage meltdown. This has increased the litigation risks of subprime mortgages and securitizations. Securitization servicers, trustees, loan originators, and guarantors have been the targets of lawsuits by investors, homeowners, and political groups seeking to protect homeowners or tenants from eviction. Several cities have also sued originators seeking accountability for the epidemic

46 See Schumer, supra note 25, at 15–16 (discussing the costs of foreclosures on families, businesses, city and local governments, and neighboring homeowners).

47 See id. at 15 (noting, as an example, that foreclosures lead to cities losing tax revenue).

48 See id. (discussing how costly foreclosures can be for city and local governments, especially when the foreclosures result in property vacancies).

49 See id. at 15 (explaining how home foreclosures negatively affect the prices that neighboring homeowners can get for their properties, and noting that "[a] recent study calculated that a single-family home foreclosure lowers the value of homes located within one-eighth of a mile (or one city block) by an average of 0.9 percent, and more so in a low to moderate-income community (1.4 percent.").

50 See id. at 15–16 (noting that "the bulk of the spillover costs of foreclosure are concentrated among the nation’s most vulnerable households").

51 See The Annie Casey Foundation, Building Family Economic Success: Foreclosure 1 (August 2009) (indicating that "40 percent of families facing eviction are renters").

52 See George S. Oldfield, Expanding Subprime Mortgage Crisis Increases Litigation Risks, THE BRATTLE GROUP, 1, 3 (2008), available at http://www.brattle.com/_documents/UploadLibrary/Upload667.pdf (discussing how originators, servicers, guarantors, and securitizers of subprime loans face increased exposure to legal actions, and how "[s]everal hundred private actions related to alleged problems with subprime mortgages have been initiated in the last year").

53 See Robert J. Coughlin, Caught in the Cross-fire: Securitization Trustees and Litigation During the Subprime Crisis (Sept. 18, 2009) http://www.nixonpeabody.com/linked_media/publications/securitization_litigation_subprime_crisis.pdf (addressing Amendola v. Deutsche Bank, a complaint filed in 2008 in Southern California, where homeowners facing foreclosure included the securitization trustee along with the loan originator and loan servicer as defendants in an action to enjoin foreclosure and recover damages, based primarily on alleged truth in lending action and RESPA violations); see also Oldfield, supra note 52, at 1 (explaining that this exposure to legal action is a result of these loans being major sources of collateral for securitized deals held by various types of investment funds).
foreclosures in communities. Insurance companies have sued as well, seeking to nullify mortgage pool policies issued on home equity loan securitizations. The many lawsuits filed in connection with sub-prime mortgages and securitizations are fact specific with fact specific outcomes. The issues involve either violation of securities laws or breach of contract claims between sophisticated contracting parties.

D. Lenders

In an example of litigation by a lender, Chase Bank sued Advanta for breach of federal securities laws and breach of contract in Chase Manhattan Mortgage Corp. v. Advanta Corp. Chase purchased sub-prime mortgage loans originated by Advanta. The bank then alleged that Advanta failed to disclose certain delinquency information required by contract. Awarding Chase damages for a breach of contract claim, the court concluded that as a sophisticated contracting party, Chase had failed to engage in its own due diligence regarding the sub-prime loans it purchased. Indeed, commentators agree that courts are unlikely to find a duty or reliance by sophisticated parties in an arm’s-length securitization contract.

54 See Coughlin, supra note 53 (discussing the Whittaker case, filed in the Northern District of Ohio, which was a class action suit against a securitization trustee, the servicers, and the servicers’ legal counsel, alleging that defendants engaged in a pattern and practice of seeking and obtaining foreclosure judgments by filing foreclosure actions without first recording the mortgage assignments).

55 See Oldfield, supra note 52, at 3 (outlining the insurance problems that resulted from the subprime mortgage crisis and the disputes that are arising from these problems); see also Coughlin, supra note 53, at 5 (discussing Radian Insurance, Inc. v. Deutsche Bank National Trust Company, an action brought by a mortgage pool insurer seeking to nullify mortgage pool policies that it used in a series of home equity loan securitizations).


57 See id. at 9 (elaborating on the court’s holding in Chase Manhattan Corp. v. Advanta Corp.); see also Oldfield, supra note 52, at 3 (discussing the types of litigation that have arisen from the subprime mortgage crisis).


59 Id. at *2 ("Advanta sold, and Chase purchased, the residential interests in 30 Advanta-Sponsored Closed-End Mortgage Securitizations").

60 Id. at *16 ("Chase alleges that Advanta did not adequately disclose all advances on zero balance loans because Advanta did not disclose delinquent interest advances, one type of advance on zero balance loans . . . ").

61 Id. at *17 ("A party such as Chase, sophisticated in investor accounting, could be expected to understand that the chart on the first page does not purport to show delinquent interest advances, being that delinquent interest advances are different from the escrow advances or corporate advances disclosed in the chart.").

62 See Murray, supra note 56, at 11 ("[C]ourts normally will not attribute either duty or reliance by the parties to a securitization contract, due to an arm’s length nature of the transaction and
A potential obstacle for lawsuits against mortgage servicers or lenders is the recently enacted Helping Families Save Their Home Act of 2009, which provides a safe harbor from litigation to mortgage servicers who agree to loan modifications in compliance with the Act. The Act will likely limit lawsuits against servicers and trustees.

E. Mortgage Insurers

Mortgage insurers have also found it difficult to hold the originators of subprime loans responsible for mortgage defaults. In United Guaranty Mortgage Indemnity Co. v. Countrywide Financial Corp., an insurer of securitized sub-prime mortgages sought recovery against the mortgage lender and the securitization trustee. Countrywide obtained mortgage insurance from United Guaranty on a series of securitized mortgage loans. Countrywide purchased the mortgage insurance to shift some of the risk of default from Countrywide to United Guaranty. Such mortgage insurance would cover Countrywide’s losses in the event of foreclosure and sale of a mortgaged property. United Guaranty argued that it relied on information provided by Countrywide to decide whether to insure the mortgages. Eleven of the policies insured by United Guaranty were sub-prime mortgage loans originated by Countrywide. United Guaranty alleged that Countrywide falsely represented the underwriting standards for policies with sub-prime loans and sought recovery based on negligence, sophistication of the parties which . . . are almost always both financial institutions."

(citing Robert M. Abrams, Securitization Disputes – Negligence/Fraud/Negligent Misrepresentation, 8 BUS. & COMM. LITG. FED. CTS. § 90:13 (2d ed.) (2007)).


See Coughlin, supra note 53, at 8 (discussing Greenwich Financial Services Distressed Mortgage Fund 3, LLC and QEB LLC v. Countrywide Financial Corporation, Countrywide Home Loans Inc. and Countrywide Home Loans Servicing LP, in which a federal judge in New York rejected an argument by Countrywide that the Act essentially precludes the plaintiffs from trying to assert their rights under MBS contracts).


66 Id. at 1169 (“In the securitizations, Countrywide affiliates conveyed a pool of mortgages to a first trustee. In exchange for the mortgages, this first trustee issued debt instruments that represent a right to proceeds from trust assets (such as incoming mortgage payments by homeowners or, perhaps, mortgage insurance proceeds).”).

67 Id. (“Countrywide and a second trustee, BNY Trust, obtained mortgage insurance on a subset of the securitized loans from United Guaranty.”).

68 See id. at 1171 (“Mortgage insurance covers the difference between the lender’s loss ‘after foreclosure and sale’ of mortgaged property.”).

69 Id. at 1172 (referencing United Guaranty’s Amended Complaint, which stated that as a result of its “delegated model” for underwriting Countrywide loans, United Guaranty relied on Countrywide to represent information on the loans being insured).

70 Id. (providing background information on the eleven insurance policies at issue in the lawsuit).
negligent misrepresentation, and fraudulent inducement, as well as other breach of contract claims.\textsuperscript{71} The court concluded that this case involved sophisticated parties to a contract who negotiated to handle various risks. Thus, since the contract agreed upon between United Guaranty and Countrywide provided remedies for claims of fraud and negligence,\textsuperscript{72} the court denied United Guaranty's contract, tort, and statutory claims.\textsuperscript{73}

Further, an interesting complaint filed by a mortgage insurer sought a declaratory judgment stating that the mortgage pool insurer was entitled to rescind each of the mortgage insurance policies as a result of materially false representations and warranties made concerning the quality of the mortgage pool, which induced it to issue the insurance policies.\textsuperscript{74}

**F. Shareholders/Investors**

Shareholders/investors have had some success in bringing securities fraud claims against lenders and originators. In \textit{In re Countrywide Financial Corp. Derivative Litigation}, a shareholder derivative action and class action alleged breaches of fiduciary duty and other violations.\textsuperscript{75} Shareholders alleged that the defendant breached securities laws by making false and misleading statements in proxy documents concerning mortgage-backed securities.\textsuperscript{76} In allowing the securities fraud claims to proceed, the court concluded that the shareholders raised enough strong inferences with respect to certain directors for violation of federal securities laws and that the requirements for demand futility were satisfied.\textsuperscript{77}

However, shareholders/investors must satisfy the high standards for pleading scienter in securities litigation. In \textit{In re Radian Securities Litigation}, a group of investors who purchased securities backed by sub-

\textsuperscript{71} Id. at 1170, 1172 (outlining the allegations and claims in United Guaranty's Amended Complaint).

\textsuperscript{72} Id. at 1188 ("Here, sophisticated business entities agreed to contractually handle claims fraud by the insured. These contract terms therefore subsume any tort remedy for claims fraud.").

\textsuperscript{73} Id. at 1170 (dismissing United Guaranty's claims for fraudulent inducement, negligent misrepresentation, negligence, and rescission, with prejudice as to all defendants).

\textsuperscript{74} Radian Ins., Inc. v. Deutsche Bank Nat'l Trust Co., No. 08-2993, 2009 U.S. Dist. LEXIS 92197, at *3 (E.D. Pa. Oct. 1, 2009) (stating the action requested by the plaintiff that this decision addresses); see Coughlin, supra note 53, at 5 (discussing the plaintiff's request for relief in \textit{Radian Insurance, Inc.}).

\textsuperscript{75} 554 F. Supp. 2d 1044, 1049 (C.D. Cal. 2008) (noting that the plaintiffs' complaint was entitled "Consolidated Shareholder Derivative Action and Class Action Complaint for Breaches of Fiduciary Duty, Aiding and Abetting Breaches of Fiduciary Duty, and Violations of the California and Federal Securities Laws").

\textsuperscript{76} Id. at 1053–54 (noting that plaintiffs' complaint alleges that defendants made false and misleading claims in press releases and conference calls, SEC filings, proxy statements, and statements about Countrywide's position).

\textsuperscript{77} Id. at 1083 (discussing which claims were granted and which claims were denied).
prime mortgage assets alleged the Radian Group had engaged in securities fraud. Dismissing the complaint, the court concluded that the plaintiffs had failed to demonstrate the elements of securities fraud, including scienter.

G. Homeowners

Homeowners also have had limited success in bringing claims against parties involved in subprime lending and securitization. In Pontiflet-Moore v. GMAC Mortgage, a homeowner who was foreclosed upon sought relief, alleging she was defrauded into refinancing her home. The homeowner claimed that the loan officer of a mortgage brokerage solicited and defrauded her by convincing her to take out a loan to refinance her home. The homeowner alleged various violations of state and federal consumer lending laws with respect to the sub-prime mortgage. The homeowner's complaint was dismissed based primarily on poorly drafted pleadings.

H. Municipalities

In City of Cleveland v. Ameriquest Mortgage Securities, Inc., the cities of Cleveland and Buffalo sued mortgage brokers seeking to recover for harm caused by foreclosures under a variety of theories, including violation of public nuisance laws. The defendants successfully moved to dismiss the complaint. The district court held that since the cities permitted and encouraged sub-prime mortgage lending by government regulation, they could not later claim such products were a public nuisance.

A likely outcome from the flood of litigation involving securitized sub-prime mortgage assets is that originators, servicers, lenders, homeowners, and investors will improve documentation by all those involved in the securitization process. Some of these lawsuits may serve to improve

79 Id. at 623 ("The plaintiffs have not met their burden under PSLRA of alleging a strong inference of scienter . . . . The plaintiff's inference of scienter is neither cogent, nor compelling, nor strong in light of competing inferences, and a reasonable person would not deem the inference of scienter cogent and at least as compelling as any nonculpable inference.").
81 Id.
82 Id.
83 Id. at *6-9, *11 (discussing the various shortcomings of plaintiffs' complaint).
84 621 F. Supp. 2d 513 (N.D. Ohio 2009); see Coughlin, supra note 53, at 4 (explaining Cleveland's claim of public nuisance).
85 Id. at 536.
86 See Eugene R. Licker, Subprime Mortgage Meltdown Litigation - A Look Ahead (2008),
corporate governance at all financial institutions as firms seek to manage litigation risk. However, managing litigation risk does little to improve proactive management of the risk of moral hazard.

The connection between the products sold by financial firms derived from consumer mortgages, and the ultimate foreclosure crisis in low-income communities has not only fueled a recession, but has harmed families and neighborhoods alike. Because the market for mortgaged-backed securities lacked regulatory transparency, institutions and regulators had no idea of the potential domino effect that the collapse of the sub-prime market would have on the economy. Management and directors of financial firms approved the purchase and selling of mortgaged-backed products because they were highly profitable for financial firms. There was no corporate governance mechanism requiring financial firms to focus on the risk posed to the communities being targeted for sub-prime lending.

Corporate social responsibility offers the opportunity to address the corporate governance failures at “too big to fail” financial institutions. A corporate social responsibility strategy, in which financial products based on consumer loans are assessed for their impact on communities, ties a financial firm’s profitability to its long-term viability. If financial firms properly analyze the risks of their financial products from a corporate social responsibility perspective, they can potentially reduce not only financial losses and litigation risks, but also societal harm.

http://www.metrocorpcounsel.com/current.php?artType=view&artMonth=April&artYear=2008&EntryNo=8116 (noting how some lawsuits will claim that those holding interests did not properly assess the value of the securities). See generally, Raymond H. Brescia, Tainted Loans: Towards a Mass Torts Approach to Subprime Mortgage Litigation (2009), available at http://works.bepress.com/cgi/viewcontent.cgi?article=1003&context=raymond_brescia (discussing the use of mass torts litigation as a means to correct the subprime mortgage crisis and how one of the problems that caused the crisis was people being given loans without proper documentation).


88 See Richard E. Mendales, Collateralized Explosive Devices: Why Securities Regulation Failed to Prevent the CDO Meltdown, and How to Fix It, 2009 U. ILL. L. REV. 1359, 1361 (2009) (finding that the crisis began and was powered by the ratings not being worth their face amounts, due to the common failure in transparency of securities law, which was an underlying issue that led to the financial market meltdown).

89 See id. at 1389–91 (comparing the current CDO market to earlier junk bond markets that collapsed due to risky investments made by portfolio managers in return for high yield returns).

social responsibility and business profitability are not mutually exclusive, and can benefit financial institutions.

II. CORPORATE SOCIAL RESPONSIBILITY & CORPORATE LAW

Corporate Social Responsibility (CSR) is a broad concept describing a business’s obligation to interact with society in a socially responsible manner. The legal debate over CSR has evolved from a much-criticized effort to hold corporate managers accountable to stakeholders other than shareholders, and from a more nuanced discussion of the realities of CSR in a global economy, including its limits in holding management accountable for societal harms.

The early debates on corporate social responsibility have been attributed to Adolf A. Berle and E. Merrick Dodd. These scholars debated the duties of directors and the role of corporations in society. Over the years, the debate over whether a corporation is private, public, or quasi-public property has continued, with its popularity often tied to the public social or economic issues of the time.

Much like the current climate, in which anger over the conduct of Wall Street financial firms has energized a movement against perceived greed and excessiveness, CSR was reinvigorated during the 1970s as many
argued that corporations had attained too much power in society, thus warranting government intervention to curtail corporate power and make firms more accountable to society. A variety of efforts to increase corporate social responsibility emerged, including shareholder voting, proxy requirements, independent directors (public interest directors), and disclosure and accounting of corporate social responsibility. Notwithstanding the ebb and flow of proponents of corporate social responsibility to seek greater accountability of corporations for societal harm, the ultimately predominant view of corporate social responsibility is the shareholder-centered model, in which managers manage the corporation for the benefit of shareholders and have a primary duty to maximize shareholder wealth.

International and U.S. corporate laws make it difficult to enforce CSR by means other than guidelines and market forces. Corporate law, through the enforcement of director fiduciary duties, requires management to act in the best interest of the corporation and its shareholders. While corporate law gives directors some latitude to consider the interests of stakeholders other than shareholders, such consideration is limited; shareholders’ interests take priority. Nevertheless, corporate law in general, as well as the lawyers that advise corporate management, encourages careful consideration of the concerns of other constituents. Thus, CSR is subject not only to the legal requirements applicable to corporate fiduciaries, but

96 See Branson, supra note 12, at 1211–12 (noting activists’ concerns that corporations had grown so large, and affected so many, that they should be regarded as public or quasi-public institutions, and regulated as such).
97 See id. at 1211–15 (discussing the corporate social movement and proposals).
98 See Williams, supra note 13, at 712-15 (explaining, in addition, that the interests of other corporate stakeholders should be protected by methods other than participation in corporate governance).
99 See id. at 724 (discussing the limits of laws); see also Wells, supra note 92, at 123–24 (explaining how Milton Friedman believed that replacing market mechanisms with political mechanisms when determining how resources should be allocated was inefficient and immoral). See generally Charlotte Villiers, Corporate Law, Corporate Power and Corporate Social Responsibility, in PERSPECTIVES ON CORPORATE SOCIAL RESPONSIBILITY 85, 100 (Nina Boeger et al. eds., 2008) (noting the global challenge to corporate social responsibility).
101 See Wells, supra note 92, at 126–27 (noting the onset of corporate constituency statutes in the 1980s); see also Nobel, supra note 92, at 1260 (discussing what directors are allowed to do, and the consensus that “a corporation must consider the interests of all stakeholders (and not simply shareholders)
102 See Wells, supra note 92, at 126–27 (discussing anti-takeover defenses and corporate constituency statutes); see also Nobel, supra note 92, at 1260 (clarifying what directors are allowed to do, and how under a long-term view, even profit maximizing might demand that a corporation consider an optimal combination of all contributing factors).
also the requirement of promoting corporate profit-making – sometimes at the expense of socially desirable goals.¹⁰³

A. Corporate Social Responsibility & Business Strategy

In the U.S and internationally, CSR is now recognized as a part of overall corporate business strategy, as evidenced by the many organizations and companies touting CSR as an appropriate business model, the increased number of consultants advising businesses on the appropriate CSR focus, and the number of companies advertising CSR initiatives.¹⁰⁴ Business leaders have embraced CSR as a moral imperative because corporations have significant economic and political power in society.¹⁰⁵ Firms are expected to utilize corporate powers in a socially responsible way.¹⁰⁶ The basic assumption of CSR is that a corporation is obligated not only to recognize its effects on society, but to work towards reducing any negative impact of corporate activities.¹⁰⁷

Thus, despite the law’s constraints on CSR, corporate social responsibility is embraced by prestigious U.S. and international organizations. The United Nations identifies several standards for assessing a corporation’s CSR efforts.¹⁰⁸ Other international organizations also have identified CSR as a key to the success of multinational corporations in the increasingly global economy.¹⁰⁹

¹⁰³ See Williams, supra note 13, at 724–25 (noting the limiting nature of a corporation’s organizational design in effectively translating legal requirements into actions at all levels of the organization).

¹⁰⁴ See Villiers, supra note 99, at 89 (highlighting the CSR consulting businesses and the six categories of CSR initiatives: “international instruments, nationally based standards, certifications schemes, voluntary initiatives, mainstream financial indices, and tools, meetings and other initiatives”); see also Bryan Horrigan, Fault Lines in The Intersection Between Corporate Governance and Social Responsibility, 25 U. N.S.W. L.J. 515, 518 (2002) (arguing that the corporate mindset is changing to decision-making based on a wider set of integrated interests such as “ecological integrity, effective decision-making, and social cohesion”).

¹⁰⁵ See Horrigan, supra note 104, at 518–21 (discussing global and ideological debates); see also Villiers, supra note 99, at 88 (emphasizing how much power corporations have, including the ability to “crush a local economy” and “provide a living or not for individuals”).

¹⁰⁶ See Villiers, supra note 99, at 88 (stating that the connection between power and responsibility shows that corporate power naturally demands a form of corporate responsibility).

¹⁰⁷ See id. at 85 (setting forth CSR advocates’ assertion “that corporations are to be made accountable for their activities and for how they exercise their power and that CSR should lead to corporations having a positive effect on society and the environment”).

¹⁰⁸ See id. at 89 (noting that there are 200 such standards and initiatives).

¹⁰⁹ See id. (discussing a UN report which makes clear “that the existence of so many initiatives reflects a recognition on the part of a broad range of actors that corporate activity must be monitored and controlled in order to protect society and the environment”); see also Vogel, supra note 91, at 6–8 (exploring the resurgence of corporate social responsibility, its growing reach, and how organizations such as the United Nations, the World Bank, and the Organization for Economic Cooperation and Development “actively promote CSR”).
In the U.S., many companies embrace CSR in order to obtain positive corporate rankings. For example, some U.S. companies obtain rankings of their CSR efforts through the Dow Jones Sustainability Indexes (DJSI) and promote positive DJSI rankings as part of a CSR strategy. Other firms also seek rankings for their CSR efforts through prestigious certifications by international agencies. Notwithstanding the increased focus on corporate social responsibility, its effectiveness in improving corporate governance has been limited.

Much of the difficulty in achieving greater acceptance of CSR by businesses is based on the fact that there is no agreement on the meaning of CSR. The limits of CSR in improving corporate governance are attributable not only to the legal boundaries of corporate law, but also to a lack of a concise meaning of what constitutes corporate social responsibility.

The meaning of CSR suffers from a definition that is too broad and vague to be successfully implemented by businesses. The result is that companies are often not clear on what is expected of them to achieve good CSR. CSR means different things to different companies, industries, and countries, and it becomes whatever a corporation defines as its efforts to be socially responsible. Corporations are thus left to select CSR agendas ranging from the elimination of poverty to the creation of environmentally-sustainable products. Corporations use CSR to promote human rights initiatives, environmental and sustainability programs, diversity and other

110 See Dow Jones Sustainability Index, http://www.sustainability-index.com (last visited on June 26, 2010) (indicating that the DJSI are "the first global indexes tracking the financial performance of the leading sustainability-driven companies worldwide"); see also Kerr, supra note 100, at 864 (listing the main business benefits to an organization of having a defined corporate responsibility policy).
111 See Villiers, supra note 99, at 89 (surveying existing CSR initiatives).
112 See id. (discussing the limits of CSR); see also Williams, supra note 13, at 724–25 (suggesting that "constraints are insufficient fully to address the concerns of corporate social responsibility in the context of a globalizing economy").
113 See Villiers, supra note 99, at 91 (discussing how the CSR definition is problematic, and how the problem is further exacerbated in a globalized context).
114 See id. (stating that the voluntariness of CSR allows companies to "set their own CSR agenda without fear of significant challenge").
115 See id. (explaining how "the same term . . . may carry different implications among various parties regarding the legitimacy, obligations and impact of corporate social responsibility standards").
116 See id. at 90 (stating that "[c]ompanies are left confused as to what is expected of them").
117 See id. at 91 (noting that a major weakness in the CSR agenda is that the voluntary approach apparent in most definitions gives companies the power to set their own CSR agendas without fear of significant challenge).
118 See id. (asserting that such agendas can be established without challenge); see also Michael E. Porter & Mark R. Kramer, Strategy & Society: The Link Between Competitive Advantage and Corporate Social Responsibility, 84 HARV. BUS. REV. 78, 81 (2006) (claiming that this often results in a "hodgepodge of uncoordinated CSR").
workplace improvement efforts, philanthropic contributions, and community outreach programs.\textsuperscript{119} What seems consistent among the various definitions of CSR is that companies must conduct business in a way that satisfies minimal legal requirements and identifies social or economic issues that are sustainable for long-term profit.\textsuperscript{120}

Shareholders and consumers are increasingly looking at a variety of indexes to measure a corporation’s corporate social responsibility.\textsuperscript{121} In addition, a variety of industry consultants are advising corporations on how to design CSR plans.\textsuperscript{122} There are also many international efforts to define CSR, including a United Nations Report identifying a range of standards for measuring corporate social responsibility.\textsuperscript{123} These standards include national assessments and certifications, as well as various voluntary initiatives, such as codes of conduct and other published policies and directives focused on corporate efforts to improve society and the environment.\textsuperscript{124}

Over the years, various other organizations have also attempted to define CSR. In 1981, The Business Roundtable released a statement on corporate social responsibility:

Balancing the shareholder’s expectations of maximum return against other priorities is one of the fundamental problems confronting corporate management. The shareholder must receive a good return but the legitimate concerns of other constituencies (customers, employees, communities, suppliers and society at large) also must have the appropriate attention... [Leading managers] believe that by giving enlightened consideration to balancing the legitimate claims of all its constituents, a corporation will best serve the interest of its shareholders.\textsuperscript{125}

\textsuperscript{119} See Villiers, \textit{supra} note 99, at 89 (listing examples of such “good corporate deeds”).

\textsuperscript{120} See id. at 92 (stating that corporations should operate “in a manner that at least meets legal requirements and that respects social and economic interests so that economic progress is sustainable rather than merely short-term”).


\textsuperscript{122} See Villiers, \textit{supra} note 99, at 89 (“There exists a large CSR industry and consultants, accountants, lawyers and others will advise companies on how to direct their CSR strategies and how to present them).

\textsuperscript{123} See id. (listing the six categories of the standards and initiatives relevant to corporate social responsibility).

\textsuperscript{124} See id. (listing the six categories of the standards and initiatives relevant to corporate social responsibility).

The World Business Council on Sustainable Development defines CSR as "the commitment of business to contribute to sustainable economic development, working with employees, their families, the local community and society at large to improve their quality of life." The Business for Social Responsibility states:

While there is no single, commonly accepted definition of . . . CSR, it generally refers to business decision-making linked to ethical values, compliance with legal instruments, and respect for people, communities and the environment . . . [and] operating a business in a manner that meets or exceeds the ethical, legal, commercial and public expectations that society has of business.

Finally, the Working Group of the ISO noted that a commonality of CSR definitions "revolve[s] around the concept of the ‘triple-bottom line’ . . . which is a framework for measuring and reporting corporate performance against economic, social and environmental parameters."

Notwithstanding the efforts of international organizations to define CSR agendas and promote CSR as part of business decision-making, there are no broad patterns of corporations adopting CSR strategies in order to improve corporate behavior. CSR’s effect on improving corporate governance will not be perceived until management is required to identify the link between profit-making and society’s economic viability, and, in turn, develop products designed to improve both. “Too big to fail” financial institutions must operate with a concise definition of CSR in which compliance is mandatory.

III. CSR AND “TOO BIG TO FAIL” FINANCIAL FIRMS – A MEANINGFUL DEFINITION

For financial firms deemed “too big to fail” by the federal government, a few fundamental concepts of corporate social responsibility require

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127 Id. (alteration to original).
128 Id. at 93 (alteration to original); see Porter, supra note 118, at 82 (setting forth the elements of triple bottom lines and problems implementing them); see also Horrigan, supra note 104, at 518–19 (discussing the "'quadruple bottom line' emphasis for companies [which] focuses on the dynamic interaction between components which cover financial, socioeconomic, and environmental concerns, as well as governance and regulatory concerns").
129 See Villiers, supra note 99, at 89 (noting the public outcry for CSR initiatives).
130 See Porter, supra note 118, at 83–84 (discussing integration of business and society).
adjusting. Furthermore, a definition of CSR is needed under which philanthropic initiatives are required and CSR is mandatory for “too big to fail” financial firms.\footnote{See Kerr, supra note 100, at 848–55 (arguing that CSR needs a better definition, and what the definition should contain).}

The recent financial crisis has demonstrated that systemic risks are posed to the capital markets when financial firms sell products that fuel economic instability and inflict negative social consequences. The subprime mortgages sold in communities, the process of securitization (and its corresponding moral hazard dilemma), and, ultimately, the global economic recession are directly linked to the business decisions of financial firms on Wall Street.

By designating financial firms as “too big to fail,” the federal government has implicitly acknowledged that certain financial institutions produce products that are so interwoven into society’s economic stability that their collapse must be either prevented or managed in order to limit the negative consequences to financial markets and the economy. As a result of the federal government’s intervention to stabilize financial markets for certain institutions, the call for improved corporate social responsibility for these institutions differs from previous movements to push a corporate social responsibility agenda.\footnote{See Branson, supra note 12, at 1217 (exploring the “new corporate social responsibility movement,” and how it differs from previous CRS movements).} Because “too big to fail” financial firms have the economic power to influence society, such firms must be obliged to minimize harm to it.

By requiring “too big to fail” institutions to engage in CSR strategies, the federal government would communicate an overarching policy that embraces CSR as not only the morally responsible thing to do, but also the right business decision. It is critical that corporations be required to include a corporate social responsibility agenda in their corporate governance; and one under which such corporations will consider the risks of financial products on communities.\footnote{See Horrigan, supra note 104, at 521–28 (emphasizing the importance of linking socioeconomic interests to corporate governance, because “[n]either organisations nor individuals are likely to take corporate social responsibility seriously as part of their core business unless it is effectively integrated within corporate governance”).}

Financial firms important to the flow of capital should be required to assess the future economic consequences of the mortgaged-based products they sell in the communities they serve. Financial firms that are deemed vital to the stability of the U.S. economy and that require government funding in the event of financial instability should be required to know the effects of their...
financial products (which are derived from consumer mortgages) on communities.

Generally, it is argued that there are four justifications for businesses to engage in CSR. They include moral obligation, sustainability/environment, license to operate, and reputation. Such justifications, however, are criticized as being weak, on the grounds that they are generic strategies that do little to assist a company in identifying and prioritizing major social issues. A more persuasive argument in support of firms’ implementation of CSR strategies is rooted in the interrelationship between corporations and society. Financial firms and other businesses need society to have stable economic conditions in which to sell goods and services, while society needs such companies to prosper in order to provide economic well-being for its citizens. Thus, “too big to fail” financial institutions must embrace CSR strategies that identify the point where business and societal needs intersect.

The current collapse of the mortgaged-backed securities market fueled by subprime mortgages highlights this intersection of business and societal interests.

Due to the increasing popularity of CSR strategies as a point of firm differentiation, many financial firms have CSR statements. Yet, these CSR strategies do little more than identify a moral checklist on corporate philanthropy. A CSR strategy can and should be more. For CSR to be accepted by boards and management as a profitable way to do business, it must be responsive to business and societal needs. As one scholar writes, CSR must unlock “shared value by investing in social aspects of context

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134 Porter, supra note 118, at 81 (outlining the four justifications).
135 Id. at 81–83 (defining moral obligation as companies having “a duty to be good citizens and to ‘do the right thing;’” sustainability as emphasizing “environmental and community stewardship;” license to operate as deriving “from the fact that every company needs tacit or explicit permission from governments, communities, and numerous other stakeholders to do business;” and reputation as being used “by many companies to justify CSR initiatives on the grounds that they will improve a company’s image, strengthen its brand, enliven morale, and even raise the value of its stock”).
136 See id. at 83 (finding that most of the CSR strategies make no meaningful impact).
137 See Horrigan, supra note 104, at 521–28 (discussing the important connection between social responsibility and corporate governance).
138 See Porter, supra note 118, at 83–84. There are two forms of intersection. Inside-out linkages are when “a company impinges upon society through its operations in the normal course of business,” while outside-in linkages are when external social conditions influence corporations. Id. at 84.
139 See id. at 81 (noting that 64% of the 250 largest multinational corporations published CSR reports in 2005); see also supra note 14 and accompanying text.
140 See Sarah A. Altschuller, Distinctions with Differences: The Lawyer’s Role in Distinguishing CSR and Corporate Philanthropy, 39 INT’L L. NEWS 11 (2010) (stating that CSR and corporate philanthropy – which contain many differences that lawyers should advise clients about – “are often used interchangeably in the popular media and in business publications: most frequently, specific instances of corporate philanthropy are deemed to be representative of a company’s commitment to CSR”).
that strengthen company competitiveness. A symbiotic relationship develops: The success of the company and the success of the community become mutually reinforcing.”

By integrating business and societal needs, companies are better able to identify social needs and prioritize them based on their importance to business operations. A strategically focused CSR allows financial firms to integrate business needs with societal needs.

“Too big to fail” financial institutions should continue to let market forces generate product ideas and develop creative business solutions to meet market voids. However, each product must not only demonstrate its profitability for the firm and the individual, but management must also judge the product’s success by how much it lessens harmful consequences to communities. Good corporate governance requires the board of a “too big to fail” financial institution to identify and consider factors such as societal and individual moral hazards, concentrations of products in low-income communities, and the potential negative effects of such products. Such governance will arm the board with improved decision-making tools, which, in turn, will allow it to better predict any potential harmful consequences.

Boards and management informed by CSR data on its financial products must then be required to address product issues and report any possible harmful consequences to regulators and shareholders. If CSR is not a zero-sum game, then management’s efforts to embrace a multi-dimensional bottom line can provide greater transparency to shareholders and promote improved corporate governance.

In order to effect changes in management behavior, CSR must be mandatory and monitored by regulatory bodies responsible for systemic risk assessment. To be successful, CSR must implement ways “to find shared value in operating practices and in the social dimensions of competitive context . . . . [G]overnments and companies must stop thinking in terms of ‘corporate social responsibility’ and start thinking in terms of ‘corporate social integration.’” Thus, the definition of corporate social responsibility applicable to financial institutions deemed

141 Porter, supra note 118, at 89.
142 See id. at 91 (explaining how organizations will distance themselves from the pack when they make the right choices and build focused, proactive, and integrated social initiatives in concert with their core strategies).
143 See id. (emphasizing that “[w]hat needs to be measured is social impact”); see also Horrigan, supra note 104, at 548 (finding that the best interests of a corporation and its shareholders need not be exclusively framed in financial or continuous profit-maximization terms).
144 Porter, supra note 118, at 92.
“too big to fail” by the federal government focuses only on those institutions posing a systemic risk to the financial system. Such a definition is a reasonable solution to the problems posed by overly broad and unworkable definitions facing other businesses in other industries.  

In addition to its definitional challenges, CSR is also limited by the fact that most corporate CSR activities are currently voluntary. Voluntary CSR compliance is said to promote best practices by allowing companies to design CSR programs that meet specific business or industry needs and permitting market forces to set standards. Critics of voluntary CSR argue that without enforcement, CSR will continue to be taken seriously by only a handful of companies. Moreover, critics of voluntary CSR point out that:  

[V]oluntary approaches are generally implemented, not out of altruism, but in response to consumer and community pressures, industry peer pressure, competitive pressures or the threat of new regulations or taxes . . . . [T]he danger is that reliance on business arguments leads to debate based on costs/benefits rather than on moral rights and wrongs so further emphasizing ad hoc coverage and undermines the moral force of arguments so eventually weakens the threat to reputation.  

Others suggest that by separating CSR from competitive advantages, companies simply miss the opportunity to separate the moral imperative from the business case for CSR, thus weakening its use strategically to improve business goals.  

A. Voluntary versus Mandatory CSR  

Without mandatory CSR requirements set by the federal government, “too big to fail” financial firms will continue to rely on rankings and a moral checklist for CSR compliance. Mandatory CSR is necessary in order

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145 See id. at 91 (stating that Whole Foods, Sysco, and General Electric have been exposed to criticism and government regulation).  
146 See id. at 80–81 (noting that companies awoke to corporate responsibility after the public responded to certain corporate practices).  
147 See Villiers, supra note 99, at 96 (stating that the voluntary approach encourages best practice and continual improvement through codes that have the flexibility to be tailored to the characteristics and circumstances of each business).  
148 See id. at 97 (noting that “despite the perceived benefits of . . . voluntary initiatives, the evidence suggests that, in reality, CSR has hardly moved [past its] starting point”).  
149 Id. at 98 (alteration to original).  
150 See Porter, supra note 118, at 91 (finding that companies should envision creating shared value as a long-term investment in the company’s future competitiveness).
to evince the seriousness of such institutions' failure to financial markets. Mandatory CSR is also needed so that less reliance is placed on voluntary compliance. More importantly, mandatory CSR recognizes the role of government and financial firms in achieving regulatory objectives to provide stability to financial markets in times of crisis.151

Mandatory CSR also improves disclosure of the CSR efforts of all financial institutions,152 as well as the dialogue of management by broadening its scope to focus not only on product profitability for the firm, but also the firm's effect on society and communities. Requiring disclosure of firms' CSR efforts not only improves transparency, but also allows the government to better assess and prevent financial market systemic risks, since the government has the relevant data.153 The new regulatory regime brought about by the financial crisis offers the best opportunity for imposing stricter corporate social responsibility requirements on financial firms.

B. A New Regulatory Environment for Financial Firms (Investment Banks)

Investment banks, through their purchase and sale of securitized debt, are viewed as key impetus leading to the financial meltdown.154 The financial crisis has led to bankruptcy as well as institutional changes in the way investment banks are regulated and in the regulatory structure of financial firms.155

151 See Villiers, supra note 99, at 99 (cautioning that "the emphasis on voluntarism risks understating or marginalizing the law's role, rendering it as seemingly irrelevant").

152 See Michael R. Siebecker, Trust & Transparency: Promoting Efficient Corporate Disclosure Through Fiduciary-Based Discourse, 87 WASH. U. L.R. 115, 121–23 (2009) ("While steadfast reliance on static disclosure standards would undermine efficiency despite providing predictability, a common law duty of disclosure based on encapsulated trust would provide flexible standards for corporate communication that evolve as market preferences change. In the end . . . encapsulated trust . . . could lead to enhanced ethical practices by corporate actors and their counsel.").

153 See Cynthia A. Williams, The Securities and Exchange Commission and Corporate Social Transparency, 112 HARV. L. REV. 1197, 1200–03 (1999) (discussing whether the SEC has the power to require social as well as financial disclosure, and how social disclosure would promote "'social transparency' in the capital markets comparable to the financial transparency that [already] exists").


The Federal Reserve now has regulatory authority over traditional banks and investment banks. Upon the collapse of Lehman Brothers, the remaining traditional investment banks either converted to bank holding companies or merged with other financial institutions. Prior to the financial crisis, banks such as Wells Fargo and Citibank were subject to regulatory review by the Federal Reserve. Traditional investment banks such as Goldman Sachs and Morgan Stanley were subject to regulatory review by the SEC. The SEC’s regulatory oversight of investment banks did not include an assessment of capital structures or debt levels. Since the financial crisis, the two remaining investment banks that were not purchased or already owned by a traditional bank voluntarily converted to bank holding companies subject to the regulatory review of the Federal Reserve.

See Sorkin, supra note 153 (quoting Loyde C. Blankfein, who was the Chairman and Chief Executive of Goldman Sachs, as saying “[w]e believe that Goldman Sachs, under Federal Reserve supervision, will be regarded as an even more secure institution with an exceptionally clean balance sheet and a greater diversity of funding sources”); see also Schroeder, supra note 154 (setting forth Blankfein’s statement that “[w]hile accelerated by market sentiment, our decision to be regulated by the Federal Reserve is based on the recognition that such regulation provides its members with full prudential supervision and access to permanent liquidity and funding”); Sushinsky, supra note 155 (“Goldman Sachs and Morgan Stanley are now bank-holding companies, and along with the advantages of being able to ease investors’ concerns about capital, they are also now subject to oversight from the Federal Reserve.”).

See Sorkin, supra note 153 (“Goldman Sachs and Morgan Stanley, the last big independent investment banks on Wall Street, will transform themselves into bank holding companies... JPMorgan Chase acquired Bear Stearns this spring in a fire sale brokered by the federal government, while Bank of America has agreed to buy Merrill Lynch for $50 billion.”); see also Schroeder, supra note 154 (“The Fed’s move is the latest milestone in a jaw-dropping couple of weeks for Wall Street and American business. Goldman and Morgan were the last two independent investment banks, following the filing for bankruptcy of Lehman Brothers and the acquiring of Bear Stearns by JPMorgan this spring. Bank of America, meanwhile, is buying Merrill Lynch.”); Roddy Boyd, The Last Days of Bear Stearns, CNN MONEY, March 31, 2008, available at http://money.cnn.com/2008/03/28/magazines/fortune/boyd_bear.fortuneindex.htm (giving a brief synopsis of JPMorgan Chase’s acquisition of Bear Stearns).


See The Investor’s Advocate: How the SEC Protects Investors, Maintains Market Integrity, and Facilitates Capital Formation, SECURIITIES & EXCHANGE COMMISSION, http://www.sec.gov/about/whatwe.shtml (“The SEC oversees the key participants in the securities world, including securities exchanges, securities brokers and dealers, investment advisors, and mutual funds.”).

See id. (listing the main purposes behind Congress’s establishment of the SEC in 1934).

See Sorkin, supra note 153 (discussing the greater regulations that new bank holding companies will be subject to); see also Schroeder, supra note 154 (explaining the costs and benefits to Goldman Sachs and Morgan Stanley of becoming holding companies, which are subject to stricter federal
The move to become bank holding companies is an acknowledgment by investment banks that a lack of regulatory oversight places these firms at greater financial risk. A lack of regulatory oversight and capital requirements has allowed traditional investment banks to take on too much leverage and engage in risky bets on financial products derived from consumer mortgages.163

With a new regulatory landscape, traditional banks, their investment bank subsidiaries, and stand alone investment banks are now subject to new regulatory standards. In addition to new capital and disclosure obligations, the financial markets will have greater transparency into the types of financial instruments sold by banks (through their investment bank subsidiaries) and investment banks. Recent congressional efforts to further regulate financial firms mark the opportunity for banks and investment banks to reengage their CSR strategies in meaningful ways. Financial firms can identify and correct the moral hazards of their financial products by understanding the effect of consumer-based financial products on society.

In order to establish the overall safety and soundness of financial institutions, banks have traditionally disclosed a range of financial data to regulators. The new regulatory regime affords “too big to fail” institutions the opportunity to develop improved financial data, which links the products sold to communities and improves the long-term profitability

oversight).

162 See Sorkin, supra note 153 (quoting John J. Mack, who was the Chairman and Chief Executive of Morgan Stanley, as saying that “[t]his new bank holding structure will ensure that Morgan Stanley is in the strongest possible position— with the stability and flexibility to seize opportunities in the rapidly changing financial marketplace”); see also Schroeder, supra note 1554 (setting forth Goldman Sachs’s Blankfein’s statement that “[w]e believe that Goldman Sachs, under Federal Reserve supervision, will be regarded as an even more secure institution with an exceptionally clean balance sheet and a greater diversity of funding sources”); MORRIS, supra note 3, at 50–51 (inerring the increased financial risk associated with the previous investment schemes, which required little or no collateral).

163 See Sorkin, supra note 153 (“For decades, firms like Morgan Stanley and Goldman Sachs thrived by taking bold bets with their own money, often using enormous amounts of debt to increase their profits, with little outside oversight.”); see also Schroeder, supra note 154 (noting the movement of the last two independent investment banks toward higher regulation, resulting in a speculative increase in the security of those institutions); MORRIS, supra note 3, at 50–51 (explaining how these firms competed to provide leverage loans on extraordinarily generous terms and demanded limited information on loan specifics).

164 See FEDERAL RESERVE, REGULATIONS, http://www.federalreserve.gov/bankinforeg/reglisting.htm (highlighting the regulation under the Federal Reserve); see also Jaffee, supra note 154, at 3–4 (explaining the current investment banking regulation and what it should look like in the future).

165 See FEDERAL RESERVE, supra note 164 (listing all the federal regulations); see also supra note 11 (discussing the passing of a Senate bill that broadly expanded the federal oversight of the financial sector).

166 See FEDERAL RESERVE, FINANCIAL STATEMENT, http://www.federalreserve.gov/reportforms/CategoryIndex.cfm?WhichCategory=1 (listing the extensive financial statements required by the Federal Reserve).
of financial firms, while at the same time demonstrating that the right CSR strategy can both increase profits and minimize the harm to society. The time is right, as financial firms have acknowledged the inseparable connection between financial products derived from consumer mortgages and the harm to communities and broader society. Also, the current regulatory environment affords financial firms the opportunity to take on a leadership role in designing strategies that embrace sound financial decisions focused on long-term growth.

Wall Street and Main Street are not parallel lines, but rather are connected paths intersecting at critical junctures in the economy. The new climate of regulatory reform makes it the right time for financial institutions to develop CSR practices that bring meaningful changes to the way financial firms interact with the communities they serve.

In order to assist financial firms in designing CSR initiatives that are more meaningful than a moral checklist, a precise definition of CSR is needed in order to avoid the lack of cohesion faced by many companies in defining its CSR efforts. A CSR definition for "too big to fail" financial firms must go beyond broad descriptors for ethical conduct, philanthropic efforts, or environmental initiatives. The proper definition must identify the connection between profitability and societal needs. CSR can offer opportunities for financial firms deemed "too big to fail" to reconcile their financial products with potential effects on society. In particular, an optimal CSR strategy would link the interdependence of corporate goals and societal needs in ways that demonstrate the consequences of failed business decisions on communities. Mandatory compliance is necessary to hold financial firms accountable. Corporate social responsibility must be disclosed to shareholders and investors.

C. Disclosures and SEC Enforcement

Financial firms should engage in mandatory reporting that requires a corporation to understand how its products and policies impact not only its shareholders, but its societal stakeholders as well. Thus, a question

167 See Porter, supra note 11818, at 91 (suggesting a model of corporate organization that supports corporate social responsibility).

168 See Rosabeth Moss Kanter, From Spare Change to Real Change: The Social Sector as Beta Site for Business Innovation, in 77 HARV. BUS. REV. 122, 124 (1999) (discussing how companies have "learned that applying their energies to solving the chronic problems of the social sector powerfully stimulates their own business development").

169 See Hess, supra note 90, at 47 (discussing social reporting and how its use in regulating corporate social responsibility would permit meaningful public scrutiny); see also Siebecker, supra note 152, at 121-23 (examining the shareholder interest in corporate social responsibility).
emerges: what information should “too big to fail” financial firms be required to disclose to satisfy their corporate social responsibilities?

D. Disclosures

Mandatory disclosures should require social accounting and reporting. Social audits and reports require a firm to evaluate the societal impact of its decisions on stakeholders and others. Social reporting involves more than mere disclosure of a code of ethics; it includes an assessment of a firm’s social performance and how the firm makes responsible corporate governance decisions.172

The need for the federal government to regulate “too big to fail” financial firms presents the appropriate opportunity to legislate corporate social reporting. Business leaders embrace corporate social responsibility as the right thing to do, yet find it difficult to determine the best approach to pursue profits while still achieving socially responsible objectives. When defining corporate social responsibility for financial firms as requiring such firms to directly link products to societal impact, financial firms must understand social responsibility and be responsive to it. Thus, in order to analyze what is socially responsible, a financial firm must gather information so it can determine social consequences, and then develop a decision-making process that management must reflect on before acting. Once a financial firm has implemented a corporate decision-making process that identifies social consequences, management must be responsive to the social issues identified.

The financial firm must respond to social issues in much the same way it identifies the needs of stakeholders (including shareholders) when making

170 See Hess, supra note 90, at 43 (“To control corporate behavior, the necessary . . . approach is social accounting, auditing, and reporting . . .”).
171 See id. (“Stakeholders include all individuals and groups who are affected by, or can affect, the organization.”); see also Larry E. Ribstein, Accountability and Responsibility In Corporate Governance, 81 NOTRE DAME L. REV. 1431, 1466 (2006) (discussing current accountability methods).
172 See Hess, supra note 90, at 43 (noting that “a social report is similar to a corporate financial audit, but concerns a company’s social performance”).
173 See id. at 47 (identifying factors to consider when determining the appropriate time to implement corporate social reporting).
174 See Hess, supra note 90, at 51–52 (“[W]hat does it mean to be ‘socially responsible’? Scholars studying this question have found that the idea of social responsibility can be understood best if divided into two distinct concepts: corporate social responsibility and corporate social responsiveness.”).
175 See id. at 51–55 (discussing CSR and responsiveness).
176 See id. at 53 (outlining the decision process that corporations should go through before acting).
177 See id. (claiming that for a corporation to be responsible, it must act as a responsible person would).
business decisions. Corporate social responsibility must be a part of governance and the matrix of issues that financial firms consider when designing financial products. Such a decision-making process involves more than just assigning a moral value judgment about what is the right thing to do; the process comprises the financial firm’s understanding of the connection between the financial products sold and the potential broader economic risks. The firm implements a process to understand internal and external product risks.

Framing corporate social responsibility as reflexive law, Professor Hess maintains that, in addition to mandatory reporting, social reporting must require internal procedures and policies that are regularly updated and define specific stakeholders and goals. Corporate social reports must also be subject to verification by external auditors and publicly disclosed.

E. Disclosure and SEC Enforcement

Mandatory disclosure of corporate social responsiveness and reporting could be accomplished under the current reporting requirements of the federal securities laws. The SEC could require financial firms to disclose the results of corporate social audits or corporate social responsiveness through proxy disclosures or regularly required disclosures.

Financial firms have admitted that the previous regulatory environment exposed the entire financial industry to systemic risks. The SEC could require these firms to disclose corporate social audits and responsiveness as part of Sarbanes-Oxley disclosure requirements for internal controls.

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178 See id. at 54 (noting that “social responsiveness” refers to the “‘capacity of a corporation to respond to social pressures’”) (quoting William C. Frederick, From CSRsub1 to CSRsub2: The Maturing of Business-and-Society Thought, 33 BUS. & SOC’Y 150 (1994)).
179 See Porter, supra note 118, at (surveying the concept of corporate social responsiveness).
180 See Hess, supra note 90, at 60–61 (discussing “other constituency” statutes).
181 See id. at 67–68 (suggesting that a corporation should create and update a statement of values).
182 See id. at 69–70 (stating that an independent and accredited auditor must verify the social report).
183 See id. at 71–72 (noting that disclosure is a key requirement for providing information to the market).
184 See Williams, supra note 153, at 1200–04 (stating that the SEC is authorized to “promote regulations requiring expanded social disclosure in [an] annual proxy statement”).
185 See id. at 1299–1300 (discussing models for expanded social disclosure).
187 See Williams, supra note 153, at 1207 (identifying types of disclosure the SEC might require); see also Hess, supra note 900, at 47 (discussing the need for expanding audits to include all aspects of a firm’s social performance).
Improved disclosures would increase market transparency for financial products by providing information on systemic risks to the industry and identifying potential economic harm to communities that are targeted for loan products. Greater market disclosures also provide shareholders and investors enhanced information on corporate social responsibility, as well as a basis for litigation in the event disclosures violate federal securities laws.

**CONCLUSION**

Is it too much to ask the management of "too big to fail" financial institutions, which design products for personal and corporate profit, to identify their financial products that are likely to harm the economy and the very communities that provide the basis for their income? If select financial firms must use taxpayer money in order to avoid dire economic consequences, then the federal government should require such firms to know of the possible negative consequences of their business decisions. CSR offers a framework for "too big to fail" financial firms to maintain heightened standards of corporate governance and social responsibility.188

If a financial firm is "too big to fail," it is also too big to not know of the consequences of its financial decisions on the communities vital to its financial success.189 Even in the midst of repaying billions of dollars in bailout funds, Wall Street appears to be headed for new record profits and bonuses for employees.190 However, the downstream communities harmed by the financial instruments fueling financial firms' growth continue to receive little attention by Wall Street.191 If, as a requirement for effective corporate social responsibility, firms must identify downside or moral hazard risks to society and disclose such risks to investors and the markets, regulators and markets will be better able to identify society harm as a

188 See Horrigan, supra note 1044, at 517 (suggesting starting points highlighting the importance of CSR).

189 See Porter, supra note 1188, at 83 (explaining the interrelationship between a corporation and society).

190 See Zachery Kouwe, Wall Street on Track for Record in Profits, N.Y. TIMES., Nov. 18, 2009, available at http://www.nytimes.com/2009/11/18/business/18wall.html (“In a report released . . . by Thomas P. DiNapoli, the comptroller of New York State, Wall Street profits in 2009 are on track to exceed the record set three years ago, at the height of the credit bubble . . . In turn, the profits are contributing to a resurgence of bonuses on Wall Street. Six of the top American bank holding companies set aside $112 billion for salaries and bonuses, including deferred payments, in the first nine months, Mr. DiNapoli reported. The six banks are Bank of America, Citigroup, Goldman Sachs, JPMorgan Chase, Morgan Stanley and Wells Fargo.”).

191 See generally Gurria, supra note 18 (exploring how companies can improve upon public governance).
potential consequence of consumer products.

Financial firms determined by the federal government to be critical to the economy must take moral responsibility for the harm their financial products cause to communities and must also be held to high standards of corporate governance and corporate social responsibility. Experts within financial firms that design products for personal and corporate profit ought to know if the products sold are likely to harm the economy and the very communities that provide the basis for their income.