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# Liberty in Loyalty:

## A Republican Theory of Fiduciary Law

Evan J. Criddle\*

*Conventional wisdom holds that the fiduciary duty of loyalty is a prophylactic rule that serves to deter and redress harmful opportunism. This idea can be traced back to the dawn of modern fiduciary law in England and the United States, and it has inspired generations of legal scholars to attempt to explain and justify the duty of loyalty from an economic perspective. Nonetheless, this Article argues that the conventional account of fiduciary loyalty should be abandoned because it does not adequately explain or justify fiduciary law's core features.*

*The normative foundations of fiduciary loyalty come into sharper focus when viewed through the lens of republican legal theory. Consistent with the republican tradition, the fiduciary duty of loyalty serves primarily to ensure that a fiduciary's entrusted power does not compromise liberty by exposing her principal and beneficiaries to domination. The republican theory has significant advantages over previous theories of fiduciary law because it better explains and justifies the law's traditional features, including the uncompromising requirements of fiduciary loyalty and the customary remedies of rescission, constructive trust, and disgorgement.*

*Significantly, the republican theory arrives at a moment when American fiduciary law stands at a crossroads. In recent years, some politicians, judges, and legal scholars have worked to dismantle two central pillars of fiduciary loyalty: the categorical prohibition against unauthorized conflicts of interest and conflicts of duty (the no-conflict rule), and the requirement that fiduciaries relinquish unauthorized profits (the no-profit rule). The republican theory explains why these efforts to scale back the duty of loyalty should be resisted in the interest of safeguarding liberty.*

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## Introduction

Fiduciary relationships are ubiquitous in American law,<sup>1</sup> but judges and legal scholars have struggled in the past to explain precisely when, why, and how fiduciary duties apply.<sup>2</sup> Conventional wisdom holds that a relationship triggers the fiduciary duty of loyalty whenever one party (the principal) has reposed special trust and confidence in another (the fiduciary), thereby exposing herself or others (the beneficiaries) to a heightened risk of injury.<sup>3</sup> Yet, aside from a handful of well-established fiduciary relationships such as trustee–beneficiary, guardian–ward, and attorney–client, there is considerable uncertainty about just how broadly the duty of loyalty extends.<sup>4</sup> Equally troubling, the nature and scope of the duty of loyalty have become matters of intense debate. Some experts argue that the duty of loyalty requires fiduciaries merely to avoid conflicts of interest and relinquish profits to their principals,<sup>5</sup> while others defend a much more robust conception of loyalty that would include obligations to deliberate and pursue beneficiaries’ interests with affirmative devotion.<sup>6</sup> Scholars disagree, as well, over the

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1. Fiduciary duties arise, for example, in the law governing trusts, agency, corporations, partnerships, pensions, investment banking, bankruptcy, charities and nonprofits, family relationships, guardianship, employment, legal representation, and medical care. *See generally* TAMAR FRANKEL, *FIDUCIARY LAW* (2011) (discussing these and other fiduciary relationships).

2. *See* Paul B. Miller, *Justifying Fiduciary Duties*, 58 MCGILL L.J. 969, 972, 976 (2013) (observing that “we know relatively little about the justification for fiduciary duties” and “[t]he boundaries of fiduciary obligation are poorly defined”).

3. *See, e.g.*, *Burdett v. Miller*, 957 F.2d 1375, 1381 (7th Cir. 1992) (“A fiduciary relation arises only if ‘one person has reposed trust and confidence in another who thereby gains influence and superiority over the other.’” (quoting *Amendola v. Bayer*, 907 F.2d 760, 763 (7th Cir. 1990))).

4. *See* Robert Cooter & Bradley J. Freedman, *The Fiduciary Relationship: Its Economic Character and Legal Consequences*, 66 N.Y.U. L. REV. 1045, 1045 (1991) (observing that “the precise nature of the fiduciary relationship remains a source of confusion and dispute”).

5. *See, e.g.*, MATTHEW CONAGLEN, *FIDUCIARY LOYALTY: PROTECTING THE DUE PERFORMANCE OF NON-FIDUCIARY DUTIES* 59 (2010) (affirming that “fiduciary duties are proscriptive rather than prescriptive”); Stephen A. Smith, *The Deed, Not the Motive: Fiduciary Law Without Loyalty*, in *CONTRACT, STATUS, AND FIDUCIARY DUTY* 213, 213–14 (Andrew S. Gold & Paul B. Miller eds., 2016) (arguing that the duty of loyalty is comprised exclusively of the no-conflict and no-profit rules and that loyalty is not a concern of fiduciary law).

6. *See, e.g.*, Peter Birks, Lionel Cohen Lecture, *The Content of Fiduciary Obligation*, 34 ISR. L. REV. 3, 11–12 (2000) (“[T]he best way into the trustee’s obligation is through the word ‘altruism.’ The trustee is under an obligation to act in the interest of another.”); Stephen R. Galoob & Ethan J. Leib, *Intentions, Compliance, and Fiduciary Obligations*, 20 LEGAL THEORY 106, 107 (2014) (“A fiduciary whose deliberation is not shaped [by the fiduciary obligation to her beneficiary] does not live up to her fiduciary obligation, no matter what else she does.”); Daniel Markovits, *Sharing Ex Ante and Ex Post: The Non-Contractual Basis of Fiduciary Relations*, in *PHILOSOPHICAL FOUNDATIONS OF FIDUCIARY LAW* 209, 220–23 (Andrew S. Gold & Paul B. Miller eds., 2014) [hereinafter *PHILOSOPHICAL FOUNDATIONS*] (citing marriage as the paradigmatic fiduciary relationship because spouses bear robust duties of loyalty to one another that may “evolve, and become more demanding, as circumstances develop”).

extent to which parties may modify or waive the duty of loyalty by contract,<sup>7</sup> and whether the “pulpit-thumping rhetoric” courts use to describe fiduciary duties promotes or undermines the rule of law.<sup>8</sup> These debates are beginning to spill over from academic commentary into judicial decisions, legislation, and uniform laws, sowing inconsistency and uncertainty in American fiduciary law.<sup>9</sup>

This Article argues that the fiduciary duty of loyalty comes into clearest focus when viewed through the lens of republican legal theory.<sup>10</sup> The central message of republican legal theory is that legal norms and institutions are necessary to safeguard individuals from “domination,” understood as subjection to another’s alien control (*arbitrium*).<sup>11</sup> Fiduciary power is dominating in this sense if a fiduciary is capable of acting “without reference to the interests, or the opinions, of” her principal and beneficiaries.<sup>12</sup> Fiduciary law’s classic duty of loyalty combats domination, I argue, by ensuring that a fiduciary’s actions are legally required to track the terms of her mandate and the interests of her beneficiaries.<sup>13</sup>

Although private law scholars have generally neglected the link between republicanism and fiduciary law in the past,<sup>14</sup> the republican foundations of

7. Compare Frank H. Easterbrook & Daniel R. Fischel, *Contract and Fiduciary Duty*, 36 J.L. & ECON. 425, 427 (1993) (arguing that fiduciary duties are fundamentally contractual duties), Henry Hansmann & Ugo Mattei, *The Functions of Trust Law: A Comparative Legal and Economic Analysis*, 73 N.Y.U. L. REV. 434, 447–49 (1998) (arguing that fiduciary duties are default contractual rules), and John H. Langbein, *The Contractarian Basis of the Law of Trusts*, 105 YALE L.J. 625, 655–56 (1995) (asserting that “fiduciary law is contractarian” and fiduciary duties are “default norms imposed in juridical relations”), with Margaret M. Blair & Lynn A. Stout, *Trust, Trustworthiness, and the Behavioral Foundations of Corporate Law*, 149 U. PA. L. REV. 1735, 1780–89 (2001) (arguing for limits on contractual waiver by contending that permitting a fiduciary “to opt out of [the commitment to pursue the beneficiary’s interests and not her own] undermines both the very foundation and the source of the economic value of the concept of a fiduciary relationship”), Melvin Aron Eisenberg, *The Limits of Cognition and the Limits of Contract*, 47 STAN. L. REV. 211, 249 (1995) (“[T]he core duty-of-loyalty rules should not be subject to a general waiver.”), and Melanie B. Leslie, *Trusting Trustees: Fiduciary Duties and the Limits of Default Rules*, 94 GEO. L.J. 67, 71 (2005) (arguing that courts should not enforce broad exculpatory clauses of fiduciary duties).

8. Langbein, *supra* note 7, at 629. Compare CONAGLEN, *supra* note 5, at 107–09 (rejecting moralistic rhetoric in fiduciary jurisprudence as an irrelevant distraction), with Blair & Stout, *supra* note 7, at 1809–10 (defending fiduciary law’s affirmation of moral and social norms).

9. See *infra* subpart II(E).

10. The interpretive methodology employed in this Article is inspired by John Rawls’s concept of “reflective equilibrium,” in that it takes the law’s core features at face value and seeks to distill the basic normative structure underlying them. JOHN RAWLS, A THEORY OF JUSTICE 20 (1971).

11. PHILIP PETTIT, REPUBLICANISM: A THEORY OF FREEDOM AND GOVERNMENT 55 (1997).

12. *Id.*

13. See *id.* (observing that under republican theory “an act of interference will be non-arbitrary,” and accordingly nondominating, “to the extent that it is forced to track the interests and ideas of the person suffering the interference”).

14. By way of illustration, a recent collection of essays on the “philosophical foundations of fiduciary law” does not contain a single reference to republicanism as a normative theory of

fiduciary law have been hiding in plain sight for centuries. Generations of republican judges,<sup>15</sup> political theorists,<sup>16</sup> and legal theorists<sup>17</sup> have invoked

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fiduciary obligation. *See generally* PHILOSOPHICAL FOUNDATIONS, *supra* note 6. In previous writings on public fiduciary theory, Evan Fox-Decent and I have drawn explicit connections between republicanism and fiduciary law. *See, e.g.*, EVAN J. CRIDDLE & EVAN FOX-DECENT, FIDUCIARIES OF HUMANITY: HOW INTERNATIONAL LAW CONSTITUTES AUTHORITY 103–04 (2016) (developing a republican fiduciary theory of international legal norms). To my knowledge, however, this Article is the first to develop these connections systematically and defend republicanism as an alternative to theories of fiduciary law that are premised upon classical liberalism.

15. *See, e.g.*, Taylor v. Beckham, 178 U.S. 548, 577 (1900) (describing public offices as “mere agencies or trusts”); Stone v. Mississippi, 101 U.S. 814, 820 (1880) (“[T]he power of governing is a trust committed by the people to the government.”); Trist v. Child, 88 U.S. (1 Wall) 441, 450 (1874) (“The theory of our government is, that all public stations are trusts, and that those clothed with them are to be animated in the discharge of their duties solely by considerations of right, justice, and the public good.”).

16. *See, e.g.*, 1 MARCUS TULLIUS CICERO, DE OFFICIIS 87 (Walter Miller, trans. 1913) (characterizing the “administration of the government” as “like the office of a trustee” and “must be conducted for the benefit of those entrusted to one’s care, not of those to whom it is entrusted”); THE FEDERALIST No. 46, at 294 (James Madison) (Clinton Rossiter ed., 1961) (affirming that all public institutions serve as “agents and trustees of the people”); THE FEDERALIST No. 65, at 397 (Alexander Hamilton) (Clinton Rossiter ed., 1961) (“The delicacy and magnitude of trust which so deeply concerns the political reputation and existence of every man engaged in the administration of public affairs speak for themselves.”); JAMES HARRINGTON, THE OCEANA AND OTHER WORKS 147 (1656) (“As an estate in trust becomes a man’s own, if he be not answerable for it, so the power of a magistracy not accountable to the People, from whom it was receiv’d, becoming of private use, the Common-wealth loses her liberty.”); JOHN LOCKE, SECOND TREATISE OF GOVERNMENT §§ 142–43, at 75–76 (C. B. Macpherson ed., Hackett Publ’g Co. 1980) (1690) (describing legislative power as a “trust” committed to the legislature for the benefit of the commonwealth); JOHN MILTON, *The Tenure of Kings and Magistrates*, in POLITICAL WRITINGS 3, 10 (Martin Dzelzainis ed., Claire Gruzelić trans., 1991) (1649) (describing “the power of Kings and Magistrates” as “derivative, transferr’d, and committed to them in trust from the People, to the Common good of them all, in whom the power yet remains fundamentally, and cannot be tak’n from them.”); PETTIT, *supra* note 11, at 8 (“The commonwealth or republican position . . . sees the people as trustor, both individually and collectively, and sees the state as trustee: in particular, it sees the people as trusting the state to ensure a dispensation of non-arbitrary rule. . . .”); QUENTIN SKINNER, LIBERTY BEFORE LIBERALISM 109–11 (1998) (discussing “the idea of the state as the name of an artificial person whose representatives are authorized to bear the rights of sovereignty in its name”); 2 JOHN TRENCHARD & THOMAS GORDON, CATO’S LETTERS 267 (Ronald Hamowy ed., Liberty Fund 1995) (1755) (describing government as “[a] great and honourable Trust” in which “Honesty, diligence, and plain sense, are the only talents necessary for the executing of this Trust; and the public Good is its only End”).

17. *See generally, e.g.*, CRIDDLE & FOX-DECENT, *supra* note 14, at 103–04 (developing an interpretive theory of sovereignty under international law as a fiduciary relationship between a state and its citizens); EVAN FOX-DECENT, SOVEREIGNTY’S PROMISE: THE STATE AS FIDUCIARY 112 (2011) (discussing the state–subject fiduciary relationship); Eyal Benvenisti, *Sovereigns as Trustees of Humanity: On the Accountability of States to Foreign Stakeholders*, 107 AM. J. INT’L L. 295, 295–97 (2013) (characterizing sovereigns as trustees of humanity at large); Evan J. Criddle, *Fiduciary Administration: Rethinking Popular Representation in Agency Rulemaking*, 88 TEXAS L. REV. 441, 446 (2010) (arguing that federal administrative law should promote “fiduciary representation,” in which federal officers exercise authority for the benefit of a state’s subjects); Evan J. Criddle, *Fiduciary Foundations of Administrative Law*, 54 UCLA L. REV. 117 (2006) (reframing the problem of agency discretion around the concept of fiduciary duty); Evan J. Criddle,

private fiduciary relationships such as guardianship, agency, and trusteeship to explain by analogy how state authority can be reconciled with individual liberty. Just as fiduciary law prevents private law fiduciaries from exercising arbitrary power over the interests of their beneficiaries,<sup>18</sup> republicans argue that public law safeguards liberty by ensuring that public officials wield their entrusted powers as a “public trust”—i.e., subject to fiduciary norms of loyalty and care.<sup>19</sup> Thus, republican legal theory is premised on the idea that the primary purpose of private fiduciary law—like public law—is to safeguard freedom from domination.

In contrast, most legal scholars and judges today accept as an article of faith that fiduciary law is devoted exclusively to deterring material harm—an idea that resonates with classical liberalism rather than republicanism.<sup>20</sup> The classical liberal theory of fiduciary law holds that there is nothing inherently wrongful about fiduciary self-dealing, provided that conflicted transactions do not harm beneficiaries’ material interests.<sup>21</sup> Viewed from this perspective, fiduciary law prohibits unauthorized conflicts of interest solely as a prophylactic measure to deter harmful opportunism and compensate for

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*Standing for Human Rights Abroad*, 100 CORNELL L. REV. 269 (2015) (arguing that states may employ interstate countermeasures as fiduciaries to protect the human rights of foreign nationals abroad); Evan Fox-Decent, *The Fiduciary Nature of State Legal Authority*, 31 QUEEN’S L.J. 259 (2005) (arguing that the fiduciary character of a state’s relationship with its people provides a justification for its legal authority); Sung Hui Kim, *The Last Temptation of Congress: Legislator Insider Trading and the Fiduciary Norm Against Corruption*, 98 CORNELL L. REV. 845 (2013) (arguing that legislators are fiduciaries to the public for the purposes of insider-trading law); Gary Lawson et al., *The Fiduciary Foundations of Federal Equal Protection*, 94 B.U. L. REV. 415 (2014) (describing the Constitution as a fiduciary document requiring equal protection of all citizens); Ethan J. Leib et al., *Essay, A Fiduciary Theory of Judging*, 101 CALIF. L. REV. 699 (2013) (offering a fiduciary theory of the judicial office); Ethan J. Leib et al., *Translating Fiduciary Principles into Public Law*, 126 HARV. L. REV. F. 91 (2013) (applying fiduciary political theory to redistricting); Ethan J. Leib & Stephen R. Galoob, *Fiduciary Political Theory: A Critique*, 125 YALE L.J. 1820 (2016) (assessing the utility and limitations of fiduciary political theory); Robert G. Natelson, *The Constitution and the Public Trust*, 52 BUFF. L. REV. 1077, 1088–91 (2004) (arguing that the U.S. Constitution is premised on a fiduciary conception of public authority); D. Theodore Rave, *Politicians as Fiduciaries*, 126 HARV. L. REV. 671 (2013) (arguing that political representatives should be treated as fiduciaries for purposes of redistricting).

18. See PETTIT, *supra* note 11, at 31–32 (explaining that for republicans the “great evil” that legal and political institutions must combat is “domination,” defined as “exposure to the arbitrary will of another, or living at the mercy of another”).

19. See Natelson, *supra* note 17, at 1088–91 (listing fiduciary duties potentially applicable to public officials).

20. See *infra* Part II. This Article uses the term “classical liberalism,” to distinguish the theory from other “liberal” theories that are more closely aligned with republicanism. See Alan Ryan, *Liberalism*, in A COMPANION TO CONTEMPORARY POLITICAL PHILOSOPHY 360, 360 (Robert E. Goodwin, Philip Pettit & Thomas Pogge eds., 2d ed. 2012) (emphasizing liberalism’s diversity).

21. See *infra* subpart II(A).

courts' inability to discern whether particular conflicted transactions undermined beneficiaries' interests.<sup>22</sup>

This classical liberal theory of fiduciary law, like the republican theory, boasts a venerable pedigree. It features prominently in *Keech v. Sandford*,<sup>23</sup> the English Chancery Court's celebrated 1726 decision which ushered in the modern era of Anglo-American fiduciary law.<sup>24</sup> It also supplies theoretical ballast for the first major American fiduciary law case, *Davoue v. Fanning*.<sup>25</sup> And it has inspired generations of legal academics in the United States to try to explain and critique fiduciary law from a purely economic perspective.<sup>26</sup> Nonetheless, as an interpretive theory of fiduciary law—one that purports to explain and justify the law's core features from its own internal point of view—the classical liberal theory is unconvincing.

Classical liberalism struggles, in particular, to explain and justify two signature features of the fiduciary duty of loyalty: the categorical prohibition against unauthorized conflicts of interest and conflicts of duty (the “no-conflict rule”), and the requirement that fiduciaries must relinquish profits obtained through conflicted transactions (the “no-profit rule”).<sup>27</sup> As other commentators have observed, there are good reasons to question the consensus among scholars of law and economics that these rules are designed

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22. See, e.g., CONAGLEN, *supra* note 5, at 62 (asserting that “the fiduciary doctrine is prophylactic in its very nature”); Henry E. Smith, *Why Fiduciary Law Is Equitable*, in PHILOSOPHICAL FOUNDATIONS, *supra* note 6, at 261, 261, 263–64 (characterizing fiduciary law's prophylactic rules as an outgrowth of equity); Robert H. Sitkoff, *The Economic Structure of Fiduciary Law*, 91 B.U. L. REV. 1039, 1045–46 (2011) (arguing that “the nature of fiduciary governance as a system of deterrence [is] meant to minimize agency costs”).

23. (1726) 25 Eng. Rep. 223.

24. *Id.* at 223–24.

25. 2 Johns. Ch. 252, 257 (N.Y. Ch. 1816).

26. See, e.g., Richard R.W. Brooks, *Knowledge in Fiduciary Relations*, in PHILOSOPHICAL FOUNDATIONS, *supra* note 6, at 225, 228–35 (discussing the “economics of knowledge” and its importance in explaining the fiduciary relationship); Henry N. Butler & Larry E. Ribstein, *Opting Out of Fiduciary Duties: A Response to Anti-Contractarians*, 65 WASH. L. REV. 1, 29 (1990) (explaining fiduciary duties in the context of contracting problems); Cooter & Freedman, *supra* note 4, at 1074 (applying the economic “principal-agent” model to the concept of fiduciary relationships); Easterbrook & Fischel, *supra* note 7, at 427 (concluding a “‘fiduciary’ relation is a contractual one,” and applying “economic assessments of contractual terms and remedies” to fiduciary duties); Robert Flannigan, *The Economics of Fiduciary Accountability*, 32 DEL. J. CORP. L. 393, 393 (2007) (concluding that when applying the economic perspective to the concept of fiduciary duty, “ancient principle” is confirmed, and does not imply an “alteration of the conventional position”); Oliver Hart, *An Economist's View of Fiduciary Duty*, 43 U. TORONTO L.J. 299, 313 (1993) (applying economic theory to the issue of “the scope of fiduciary duty”); Robert H. Sitkoff, *An Agency Costs Theory of Trust Law*, 89 CORNELL L. REV. 621, 677–83 (2004) (utilizing economic theory, particularly the “principal-agent problem,” and applying agency-cost theory to trust law). See generally Sitkoff, *supra* note 22 (synthesizing economic theory and fiduciary law).

27. See, e.g., *Bray v. Ford* [1896] AC 44 (HL) 51 (Lord Herschell) (appeal taken from AC) (Eng.) (“It is an inflexible rule of a Court of Equity that a person in a fiduciary position . . . is not, unless otherwise expressly provided, entitled to make a profit; he is not allowed to put himself in a position where his interest and duty conflict.”).

to achieve optimal harm minimization.<sup>28</sup> More fundamentally, classical liberalism’s focus on deterrence is an awkward fit with fiduciary law because the paradigmatic fiduciary remedies—constructive trust and disgorgement—are restitutionary remedies, not punitive remedies.<sup>29</sup> Taking classical liberalism’s normative commitments seriously, therefore, would seem to invite legislators and judges to strip fiduciary law down to its foundations and reengineer fiduciary duties and remedies from the ground up.

It should come as no surprise, therefore, that this reengineering process is already well underway in the United States. Inspired by classical liberalism, the Delaware Supreme Court has replaced the no-conflict and no-profit rules in corporate law with an “entire fairness” test that allows corporate directors to conclude self-interested transactions without the consent of either the corporation’s disinterested directors or its shareholders.<sup>30</sup> The past two decades have also seen a growing number of states discard the no-conflict and no-profit rules in agency law and parts of trust law.<sup>31</sup> These departures from fiduciary law’s traditional requirements have been premised on the idea that courts should intervene in fiduciary relationships only as strictly necessary to rescue beneficiaries from material harm.<sup>32</sup>

The republican theory developed in this Article challenges classical liberals’ efforts to dismantle traditional fiduciary rules and remedies. As this Article will demonstrate, the fiduciary duty of loyalty reflects the concerns of republicanism rather than classical liberalism. The republican theory of fiduciary law resonates with the venerable idea that fiduciaries in both private and public law occupy a distinctive office that is constituted, defined, and regulated by law.<sup>33</sup> Unlike classical liberalism, republicanism bolsters the

28. See *infra* subpart II(D).

29. See *infra* subpart II(D).

30. See *infra* text accompanying notes 136–37.

31. See *infra* text accompanying notes 141–47.

32. See Tamar Frankel, *Fiduciary Law*, 71 CALIF. L. REV. 795, 823 (1983) (noting that “courts will intervene in the fiduciary relation by requiring the fiduciary to act with loyalty and skill, in the entrustor’s best interests”).

33. See SHELDON AMOS, *THE HISTORY AND PRINCIPLES OF THE CIVIL LAW OF ROME* 291 (Fred B. Rothman & Co. reprinted 1987) (1883) (observing that under Roman law “[t]he office of guardian . . . was regarded as a service of public moment, and not of mere private convenience or arrangement,” being imposed “as a public burden or duty to be rendered to the State”); 1 CICERO, *supra* note 16, at 85 (“For the administration of the government, like the office of a trustee, must be conducted for the benefit of those entrusted to one’s care, not of those to whom it is entrusted.”); Joshua Getzler, *Rumford Market and the Genesis of Fiduciary Obligations*, in *MAPPING THE LAW* 577, 584–85 (Andrew Burrows & Alan Rodger eds., 2006) (arguing that the English Chancery Court’s introduction of “[t]he idea that profit from [a private fiduciary] should be barred can plausibly be connected to [Chancellor] King’s experience battling the abuses of [public offices] in Chancery”); *id.* at 595–96 (explaining how English legal norms governing private and fiduciary offices developed in tandem during the eighteenth and nineteenth centuries); Jedediah Purdy, *Presidential Popular Constitutionalism*, 77 *FORDHAM L. REV.* 1837, 1847 & n.39 (2009)



traditional duty of loyalty with its associated remedies by showing how fiduciary law neutralizes the domination that would otherwise arise in asymmetric relationships premised upon trust and confidence. A fiduciary's power to exercise entrusted power for and on behalf of her principal (or pursuant to authority entrusted to her by law) would engender domination but for the fact that fiduciary law compels a fiduciary to honor her principal's instructions and her beneficiaries' interests. The republican theory thus frames the fiduciary duty of loyalty as a liberty-enhancing safeguard that denies fiduciaries the formal legal capacity to exercise arbitrary power. To the extent that American law remains committed to the republican ideal of liberty as freedom from domination, legislators and judges today should take care to preserve and reinforce fiduciary law's traditional legal requirements and remedies.

The republican theory also clarifies fiduciary law's proper scope, explaining why some interpersonal relationships that pose a risk of harmful opportunism qualify as fiduciary relationships (e.g., trustee–beneficiary), while others do not (e.g., manufacturer–consumer).<sup>34</sup> In particular, republicanism offers a simple test for identifying fiduciary relationships: *Fiduciary duties apply whenever a party has been entrusted with power over another's legal or practical interests.*<sup>35</sup> The fiduciary duty of loyalty governs relationships that meet this test because without this obligation a fiduciary would have the capacity to work a double wrong: she could both (1) harm her beneficiary's legal or practical interests and (2) violate the trust reposed in her by treating fiduciary power as an instrument for advancing her own purposes. A fiduciary's capacity to commit the second type of wrong—breach of trust—represents a unique form of domination and therefore justifies fiduciary law's distinctive legal obligations and remedies. While other species of private law such as contract, tort, property, and unjust enrichment are capable of neutralizing the domination entailed in a private party's capacity for harmful opportunism in an arm's-length relationship, only fiduciary duties and remedies are calibrated to ensure that fiduciaries lack the capacity to betray trust in a fiduciary relationship.

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(emphasizing how this republican conception of the fiduciary office shaped early American political theory). Scholars of business organization law have observed similarly that Anglo–American corporations began as public entities chartered for public purposes. *See, e.g.*, LAWRENCE M. FRIEDMAN, *A HISTORY OF AMERICAN LAW* 129–30 (3d ed. 2005) (“Banks, insurance companies, water companies, and companies organized to build or run canals, turnpikes, and bridges made up the overwhelming majority of these early corporations.”); JAMES WILLARD HURST, *THE LEGITIMACY OF THE BUSINESS CORPORATION IN THE LAW OF THE UNITED STATES, 1780–1970*, at 17 (1970) (“From the 1780's well into mid-nineteenth century the most frequent and conspicuous use of the business corporation . . . was for one particular type of enterprise, that which we later called public utility . . .”).

34. *See, e.g.*, *Burton v. R.J. Reynolds Tobacco Co.*, 397 F.3d 906, 911–13 (10th Cir. 2005) (holding that cigarette manufacturers are not fiduciaries for consumers under Kansas law).

35. *See infra* subpart III(A).

The remainder of this Article develops the republican theory of fiduciary law in several stages. Part I offers a brief primer on legal republicanism, summarizing the tradition's distinctive conception of liberty as freedom from domination. Part II introduces the classical liberal theory of fiduciary law and explains how the classical liberal theory has shaped the development of English and American fiduciary law. Part II also explains why theories of fiduciary law that are based on classical liberalism—including economic theories—do not offer a persuasive, interpretive account of the duty of loyalty. Lastly, Part III explains how the republican theory both bolsters and clarifies the traditional fiduciary duty of loyalty. In particular, the republican theory offers an interpretively persuasive account of the normative foundations of fiduciary law, it provides a simple test for identifying fiduciary relationships, it clarifies the fiduciary duty of loyalty, and it furnishes a principled justification for judicial deference to fiduciaries' discretionary judgments. In each of these respects, republicanism lays a firm theoretical foundation for fiduciary law's traditional features.

To be clear, although this Article advances the thesis that fiduciary law's traditional structure reflects republican principles, it does not set out to prove that judges in England, the United States, or other former British colonies have deliberately drawn upon republican principles as they have developed contemporary fiduciary law. Nor does it attempt to show that republicanism can explain or justify every statute, regulation, or judicial decision involving fiduciary duties. Some features of American fiduciary law—particularly in the law governing corporations and other business associations—have clearly drifted away from the republican theory. This Article does make the case, however, that the traditional fiduciary duty of loyalty addresses republican concerns about arbitrary power, and it aims to persuade the reader that fiduciary jurisprudence could achieve greater coherence through deeper engagement with the republican ideal of liberty as freedom from domination.

## I. Republican Legal and Political Theory: A Primer

To understand the role that republican theory has played, and might yet play, in fiduciary law, we must first appreciate what makes the republican tradition distinctive. Over the centuries, the term “republicanism” has been used to capture a diverse collection of ideas, including popular sovereignty; representative government; the constitutional separation of legislative, executive, and judicial powers; civic virtue; inclusive public deliberation; and universal citizenship.<sup>36</sup> Indeed, the republican tradition has come to embrace

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36. Cass R. Sunstein, *Beyond the Republican Revival*, 97 YALE L.J. 1539, 1541–42, 1586 (1988); see also Samantha Besson & José Luis Martí, *Law and Republicanism: Mapping the Issues*, in LEGAL REPUBLICANISM: NATIONAL AND INTERNATIONAL PERSPECTIVES 3, 8 (Samantha Besson

so many diverse trends and voices that debates among the tradition's adherents threaten at times to overshadow the tradition's core contribution to legal and political theory.<sup>37</sup> At its heart, however, republicanism offers a distinctive account of the source and purpose of state authority. Specifically, it asserts that all public officials and institutions derive their authority from their people for the purpose of securing individual liberty.<sup>38</sup> The state fulfills its mission to secure liberty when it enacts and enforces laws that protect its people from “domination.”<sup>39</sup>

To fully appreciate the republican ideal of liberty as freedom from domination, it may be helpful to unpack what this term means for republicans. The leading contemporary exponents of republicanism, Philip Pettit and Quentin Skinner, have explained that domination for republicans is subjection to another's “arbitrary power” or “alien control.”<sup>40</sup> If another person can interfere in your choices as they like with impunity, you are dependent on their will and “not *sui juris*—or not ‘your own person’—in the expression from Roman Law.”<sup>41</sup> You are no longer capable of acting as “your own man,” freely exercising “your own right.”<sup>42</sup> Instead, you are “under the power of a master” (*in potestae domini*)—effectively a slave rather than a fully emancipated, self-determining agent.<sup>43</sup>

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& José Luis Martí eds., 2009) (describing some of the core themes of republicanism) [hereinafter LEGAL REPUBLICANISM].

37. For a recent dustup over the meaning of “republicanism,” compare RANDY E. BARNETT, OUR REPUBLICAN CONSTITUTION: SECURING THE LIBERTY AND SOVEREIGNTY OF WE THE PEOPLE 50–51 (2016) (using the term “republicanism” to capture libertarianism), with Jack M. Balkin, *Which Republican Constitution?*, 31 CONST. COMMENT. 31 (2017) (reviewing RANDY E. BARNETT, OUR REPUBLICAN CONSTITUTION: SECURING THE LIBERTY AND SOVEREIGNTY OF WE THE PEOPLE (2016)) (contrasting Barnett's libertarianism with founding-era republicanism based on freedom from domination).

38. See PETTIT, *supra* note 11, at 8 (“The commonwealth or republican position . . . sees the people as trustor, both individually and collectively, and sees the states as trustee . . .”).

39. M. N. S. SELLERS, THE SACRED FIRE OF LIBERTY: REPUBLICANISM, LIBERALISM AND THE LAW 71–72 (1998) (describing James Madison's republican vision of liberty).

40. Philip Pettit, *Republican Freedom: Three Axioms, Four Theorems*, in REPUBLICANISM AND POLITICAL THEORY 102, 102 (Cécile Laborde & John Maynor eds., 2008); Quentin Skinner, *Freedom as the Absence of Arbitrary Power*, in REPUBLICANISM AND POLITICAL THEORY, *supra*, at 83, 84–86; see also PHILIP PETTIT, ON THE PEOPLE'S TERMS: A REPUBLICAN THEORY AND MODEL OF DEMOCRACY 1 (2012) (emphasizing “the evil of subjection to another's will”).

41. PETTIT, *supra* note 40, at 7. The term “*sui juris*” is often translated as “free from power,” meaning not subject to another's domination. *E.g.*, MAX KASER, ROMAN PRIVATE LAW 76 (Rolf Dannenbring trans., 4th ed. 1984).

42. Skinner, *supra* note 40, at 86.

43. Phillip Pettit, *Law and Liberty*, in LEGAL REPUBLICANISM, *supra* note 36, at 39, 44; see also LOCKE, *supra* note 16, § 22, at 17 (asserting that liberty entails not being “subject to the inconstant, uncertain, unknown, arbitrary will of another man”); 2 TRENCHARD & GORDON, *supra* note 16, at 430 (“Liberty is, to live upon one's own terms; slavery is, to live at the mere mercy of another . . .”).

Importantly, republicans contend that domination is wrongful even if the empowered party never affirmatively interferes with the dependent party's choices. The mere fact that the empowered party has the *capacity* for arbitrary interference underscores the dependent party's vulnerability, impressing upon the dependent party's mind the need to remain within the power holder's good graces. The dependent party therefore faces "a continual state of uncertainty and wretchedness," characterized by the need for constant invigilation, self-abasement, and self-censorship.<sup>44</sup> This condition of subservience persists even if the empowered party does not exercise her power in an arbitrary manner. Accordingly, subjection to a virtuous king or benevolent slave master is incompatible with liberty, notwithstanding the fact that the king or slave master may always choose to exercise power altruistically for the benefit of their subordinates. In these relationships, the mere presence of alien control is sufficient to render the subject or slave unfree.<sup>45</sup>

The republican conception of liberty as freedom from domination might appear at first glance to be incompatible with government. Republicans argue, however, that public authority does not constitute "alien control" if the state is properly "checked" to ensure that it does not serve as an instrument of arbitrary control.<sup>46</sup> A state that interferes with private choices on a nonarbitrary basis to secure a regime of secure and equal freedom does not dominate its people. The key question for republicans, therefore, is whether public institutions are hedged by sufficient legal and political safeguards to ensure that they lack the formal and practical capacity to exercise power in an arbitrary manner. If state action is "forced to track the avowed or avowal-ready interests of the interferee," it is not arbitrary in the relevant sense and therefore does not constitute a form of alien control.<sup>47</sup> Thus, republicans assert that the state can make, adjudicate, and enforce laws that constrain individual autonomy without undermining liberty, provided that robust safeguards are in place to guarantee that the state cannot disregard the public interest with impunity.<sup>48</sup>

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44. 2 TRENCHARD & GORDON, *supra* note 16, at 430; *see also* Pettit, *supra* note 40, at 103 (emphasizing that alien control "invigilate[s] the choices of the controlled agent").

45. *See, e.g.*, SELLERS, *supra* note 39, at 71 (observing that James Madison in the *Federalist Papers* "attributed tyranny to an excess of power, even in service of the common good").

46. Pettit, *supra* note 40, at 117–18.

47. *Id.* at 117.

48. Some contemporary republicans, following a strand of republicanism that can be traced back to Aristotle, contend that individuals, to be fully free, must participate in developing the laws that govern them so that these laws can be understood as the product of their own authorship. *See, e.g.*, MICHAEL J. SANDEL, DEMOCRACY'S DISCONTENT: AMERICA IN SEARCH OF A PUBLIC PHILOSOPHY 322–23 (1996) (arguing that current disenchantment with American politics can be alleviated by replacing the liberal, "voluntarist conception of freedom" with a return to republican ideas of self-government and civic engagement); Charles Taylor, *Cross-Purposes: The Liberal-*

Laws that deny public institutions the formal authority to wield alien control are necessary to secure republican liberty, but they are not sufficient to ensure that the state lacks the practical capacity for domination. Robust legal and political institutions are also necessary to reduce the incidence of arbitrary interference *ex ante* and ensure *ex post* that the state cannot exercise alien control with impunity. Republicans therefore emphasize the importance of structural safeguards such as popular elections and inter-branch checks and balances as safeguards for individual liberty.<sup>49</sup> The role of courts within republican theory is to affirm legal rules that formally rule out domination, while enforcing these rules in a manner that minimizes domination in practice. Because courts—like other public institutions—have the practical capacity for arbitrary interference, republicans have argued that judicial intervention should be calibrated to guard against overreach, ensuring that judicial intervention in public governance minimizes overall net domination.<sup>50</sup>

An important lesson of the republican tradition is that individual liberty in the private sphere is also a product of effective institutional design. Republican freedom is “an explicitly political notion of freedom,” Martin Loughlin observes; “rather than being a natural or intrinsic human characteristic, liberty is . . . created through governmental action,” as the state makes and enforces laws to protect individuals from being subject to others’ arbitrary power.<sup>51</sup> Consequently, legal norms and institutions are necessary to protect individuals from domination in the private sphere, just as they are necessary to protect individuals from state domination.<sup>52</sup>

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*Communitarian Debate*, in LIBERALISM AND THE MORAL LIFE 159, 165 (Nancy L. Rosenblum ed., 1989) (“In order to have a free society, one has to replace this coercion with . . . a sense that the political institutions in which [citizens] live are an expression of themselves. The ‘laws’ have to be seen as reflecting and entrenching their dignity as citizens, and hence to be in a sense extensions of themselves.”). However, most republicans consider it “more important *not to have* a master than to *be* a master.” ISEULT HONOHAN, CIVIC REPUBLICANISM 184 (2002). When legal norms and institutions require public officials to exercise their entrusted powers in a manner that is calculated to advance the public interest, republicans contend that these officials relate to the public not as masters but as public servants. *Id.* at 158–61.

49. See, e.g., PETTIT, *supra* note 11, at 100–01 (noting Alexander Hamilton’s assertion that “legislative balances and checks” and “the representation of the people in the legislature by deputies of their own election . . . are means, and powerful means, by which the excellencies of republican government be retained and its imperfections lessened or avoided” (quoting THE FEDERALIST NO. 9, at 72–73 (Alexander Hamilton) (Clinton Rossiter ed., 1961))).

50. See Yasmin Dawood, *The Antidomination Model and the Judicial Oversight of Democracy*, 96 GEO. L.J. 1411, 1418 (2008) (“[A] decision by courts to intervene in the political process should be reconceptualized as a domination-minimizing institutional tradeoff . . . . Not only does this tradeoff result in an overall net minimization of domination, it also constrains judicial intervention to the most serious instances of domination. In this way, the antidomination model guards against the danger of judicial overreaching.”).

51. MARTIN LOUGHLIN, FOUNDATIONS OF PUBLIC LAW 174 (2010).

52. See John Braithwaite & Philip Pettit, *Republicanism and Restorative Justice: An Explanatory and Normative Connection*, in RESTORATIVE JUSTICE: PHILOSOPHY TO PRACTICE 145,

Although republican legal and political theorists have lavished attention on public law, private law's equally vital role in securing freedom from domination has received less scrutiny.<sup>53</sup> The clear implication of republican theory, however, is that private law also may promote liberty by ensuring that individuals are not consigned to live at the mercy of others. As Pettit has explained, contract law is necessary “not just to facilitate voluntary agreements among different agents, but to play a regulative role in disallowing contracts that involve terms under which one party has the possibility of dominating the other.”<sup>54</sup> Tort law duties of care regulate the domination that would arise if private parties could harm their neighbors negligently, recklessly, or intentionally with impunity.<sup>55</sup> Similarly, the law of unjust enrichment arguably responds to the threat of alien control by compelling individuals to restore property in their possession to the rightful owner.<sup>56</sup> Property law likewise can be understood to enshrine rights and duties and supplies remedies to prevent private parties from wielding unilateral control over others' legally protected interests in resources.<sup>57</sup> Thus, viewed from a republican perspective, private law enshrines legal rules that deny private parties the formal capacity for domination, while tasking courts with enforcing these rules in a manner that is calculated to minimize overall net domination in practice.<sup>58</sup>

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149 (Heather Strang & John Braithwaite eds., 2000) (arguing that the “republican ideal of freedom as non-domination” requires “restraining the private power . . . whereby people can be effectively protected, informed and empowered in relation to one another”).

53. See generally, e.g., LEGAL REPUBLICANISM, *supra* note 36 (providing excellent essays on republican approaches to constitutional law, criminal law, and international law, but ignoring private law). Although private law scholars rarely invoke republicanism expressly, David Dyzenhaus observes that republican liberty is “akin to the sense of freedom” defended by Kantian private law theorists such as Ernest Weinrib and Arthur Ripstein. See David Dyzenhaus, *Liberty and Legal Form*, in PRIVATE LAW AND THE RULE OF LAW 92, 95–96 (Lisa M. Austin & Dennis Klimchuk eds., 2014).

54. PETTIT, *supra* note 11, at 165.

55. See David F. Partlett, *The Republican Model and Punitive Damages*, 41 SAN DIEGO L. REV. 1409, 1417–18 (2004) (suggesting that tort law responds to republican concerns about domination).

56. RESTATEMENT (THIRD) OF RESTITUTION AND UNJUST ENRICHMENT, § 1 cmt. b (AM. LAW INST. 2011).

57. See PETTIT, *supra* note 11, at 135 (arguing that nondomination best protects private-property rights).

58. Republicans have debated whether nondomination is best understood as a constraint on an agent's actions or as a value to be maximized. See PETTIT, *supra* note 11, at 97–106 (distinguishing these approaches and defending a consequentialist theory). This Article advances a mixed approach. It endorses the nonconsequentialist view that law, to be legitimate, must respect republican liberty by enshrining formal conduct rules that unequivocally affirm each individual's right to freedom from domination. See *infra* subparts III(A)–(D). Because nondomination must be secured in practice through fallible legislatures and courts, however, the Article asserts that nondomination must also operate as a maximand for the design of decision rules to govern judicial review. See *infra* subpart III(E). A thoroughly consequentialist republican theory might generate different conclusions regarding the optimal design of fiduciary conduct and decision rules.

Generations of republican political theorists have argued that fiduciary duties, in particular, preserve freedom from domination.<sup>59</sup> For example, Pettit asserts that an agent with power of attorney does not dominate her principal because she is permitted to exercise this power “only on condition that the interference promises to further [her principal’s] interests,” and “according to opinions of a kind that [the principal] share[s].”<sup>60</sup> Consequently, an agent does not relate to her principal “as a master,” but rather as an extension of the principal’s own self-mastery.<sup>61</sup> As Part III of this Article explains in greater detail below, the legal requirements of fiduciary loyalty formally rule out alien control in fiduciary relationships by requiring a fiduciary to exercise her entrusted power in a manner that respects the interests of her principal and beneficiaries. The norms and institutions of fiduciary law thus safeguard republican freedom by ensuring that a fiduciary lacks the formal and practical capacity to interfere arbitrarily in the affairs of her principal and beneficiaries with impunity.

In sum, republicanism offers a distinctive theory of the purpose of legal institutions based on the ideal of liberty as freedom from domination. According to republicans, private parties suffer a special wrong whenever their legal interests are subject to another’s arbitrary control, irrespective of whether that control results in wrongful interference.<sup>62</sup> Legal norms and institutions are necessary under republican theory to ensure that the powerful are unable to interfere arbitrarily in others’ affairs with impunity. Fiduciary law thus contributes to the establishment of a free society by emancipating principals and beneficiaries from domination at the hands of those who hold entrusted power over their legal or practical interests.

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59. See sources cited *supra* note 16.

60. PETTIT, *supra* note 11, at 23.

61. *Id.*

62. Republicans disagree about whether noninterference and nondomination are both essential components of republican freedom. See Philip Pettit, *Keeping Republican Freedom Simple: On a Difference with Quentin Skinner*, 30 POL. THEORY 339, 342 (2002) (arguing that republican freedom is concerned solely with domination, while acknowledging Skinner’s claim that republicans historically understood freedom to encompass both nondomination and noninterference). Some theorists argue that nonarbitrary interference does not compromise freedom, see, for example, PETTIT, *supra* note 11, at 75–76 (arguing that “[f]reedom as non-domination is compromised by domination and by domination alone,” not by interference or the “influence of conditioning factors”), while others reject this thesis. See, e.g., Christian List & Laura Valentini, *Freedom as Independence*, 126 ETHICS 1043, 1059 (2016) (criticizing republican theories, like Pettit’s, that recast constraints on freedom as no restriction of freedom, “[c]ontrary to ordinary-language use”); Evan Fox-Decent, *Freedom as Independence* 19–23 (unpublished manuscript) (on file with author) (articulating and defending a version of republican freedom that includes freedom from interference). This Article endorses the view that nonarbitrary interference compromises freedom, but that such interference is wrongful only if it reflects alien control.

## II. Classical Liberalism in Anglo–American Fiduciary Law

Despite the longstanding association between fiduciary concepts and republican legal and political theory, private law scholars today rarely mention republicanism as a possible theoretical framework for explaining, justifying, or critiquing fiduciary law. Although academics and judges often identify factors such as power, trust, dominance, and vulnerability as defining features of fiduciary relationships,<sup>63</sup> they tend to characterize the no-conflict and no-profit rules as “prophylactic” measures that are designed to address the risk of harmful opportunism (per classical liberalism),<sup>64</sup> rather than as liberty-enhancing safeguards that rule out domination (per republicanism).

This Part examines classical liberalism’s enduring influence on Anglo–American fiduciary law. It begins by laying out the tradition’s vision of liberty as freedom from interference. It then considers how classical liberalism has shaped fiduciary law’s development in England and the United States, and it examines how legal scholars today—including leading practitioners of law and economics—have endeavored to explain and justify fiduciary duties and remedies based on the normative commitments of classical liberalism. Lastly, this Part explores several important critiques of classical liberalism as an interpretive theory of fiduciary law, and it explains how the theory’s exclusive focus on wrongful interference has encouraged legislatures and courts to set aside fiduciary law’s traditional no-conflict and no-profit rules in some areas of American fiduciary law.

### A. *Classical Liberalism and Fiduciary Duty*

Contemporary republicans typically present their vision of liberty as an alternative to classical liberalism, which focuses on “freedom as noninterference.”<sup>65</sup> Whereas republicans consider a power holder’s mere *capacity* for arbitrary interference to undermine liberty (whether or not it results in actual interference), proponents of classical liberalism contend that individual freedom is compromised if (and only if) a person’s choices are

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63. See, e.g., *Frame v. Smith*, [1987] 2 S.C.R. 99, 102 (Can.) (Wilson, J., dissenting) (emphasizing unilateral power and vulnerability); Frankel, *supra* note 32, at 809–10 (characterizing “abuse of power” as “the central problem” of fiduciary law); D. Gordon Smith, *The Critical Resource Theory of Fiduciary Duty*, 55 VAND. L. REV. 1399, 1483 (2002) (suggesting that “the strength of [fiduciary law’s] protection varies inversely with the potential for self-help on the part of the vulnerable party”).

64. See, e.g., Smith, *supra* note 22, at 262–71 (describing features of fiduciary law as equitable constraints on opportunism); Smith, *supra* note 63, at 1402 (explaining how the duty of loyalty, which serves as the essential aspect of fiduciary duty, serves to mitigate against opportunistic behavior by fiduciaries).

65. See, e.g., PETTIT, *supra* note 11, at 40–50 (contrasting “liberty as non-domination” from liberty “as non-interference”).



actually constrained by another.<sup>66</sup> According to classical liberals, it is the incidence or risk of choice-constraining interference—not alien control per se—that renders a person unfree. Consequently, a person may be unfree without suffering actual interference only to the extent that another has actually interfered, or is likely to interfere, in their affairs to their detriment.<sup>67</sup>

In some respects, the republican conception of freedom is narrower than the classical liberal conception. Unlike classical liberals, republicans consider an individual's formal subjection to a benevolent slaveholder to be a form of unfreedom even if the slaveholder was disposed to treat the slave well and refrain from interference in the slave's choices.<sup>68</sup> In other respects, however, the classical liberal conception of freedom is narrower than its republican alternative. For example, any interference in matters of personal choice—not just arbitrary interference—compromises freedom under classical liberalism. Accordingly, classical liberals tend to view laws that constrain citizens' choices as limitations on personal freedom even if the laws are necessary to protect all members of society from domination.<sup>69</sup> Although they recognize that legal institutions are often necessary to protect individual autonomy from private interference, classical liberals consider state intervention in the private sphere to be appropriate only to the extent that there is an actual risk of interference in matters of personal choice.<sup>70</sup>

Viewed from the perspective of classical liberalism, fiduciary duties guard against the possibility that fiduciaries may harm their principals and beneficiaries by interfering in their legally privileged choices. Most fiduciaries have a unique capacity for harm because they are enlisted precisely to carry others' choices into execution.<sup>71</sup> Accordingly, classical liberals argue that the duty of loyalty is designed to address the threats of material harm that arise within fiduciary relationships by requiring fiduciaries to respect their principals' choices and their beneficiaries'

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66. See, e.g., MATTHEW H. KRAMER, *THE QUALITY OF FREEDOM* 157 (2003) (identifying freedom simply as the ability to perform an action).

67. Ian Carter, *How Are Power and Unfreedom Related?*, in *REPUBLICANISM AND POLITICAL THEORY*, *supra* note 40, at 58, 61–63; Matthew H. Kramer, *Liberty and Domination*, in *REPUBLICANISM AND POLITICAL THEORY*, *supra* note 40, at 31, 42–44.

68. See Cécile Laborde & John Maynor, *The Republican Contribution to Contemporary Political Theory*, in *REPUBLICANISM AND POLITICAL THEORY*, *supra* note 40, at 1, 4–5 (describing Skinner's and Pettit's arguments that benevolent slave owners still subject their slaves to unfreedom).

69. See, e.g., Carter, *supra* note 67, at 65–66 (arguing that there is no reason to privilege the common interest over one's personal interest when determining what counts as an instance of unfreedom “unless this reason consists in a moral point of view”); Charles Larmore, *A Critique of Philip Pettit's Republicanism*, 11 *PHIL. ISSUES* 229, 234 (2001) (offering taxation as an example of state interference for the common good that results in a loss of individual freedom).

70. See Kramer, *supra* note 67, at 42 (“[T]he soft-hearted dominator's superiority is not in itself a source of unfreedom; everything hinges on what the dominator does with his superiority.”).

71. Frankel, *supra* note 32, at 808–10.

interests.<sup>72</sup> Arguably, the first principle of agency law, for example, is that an agent is required to follow her principal's instructions.<sup>73</sup> Trustees likewise are obligated to honor the terms of their trust agreement,<sup>74</sup> and corporate officers and directors are bound to respect the requirements of their corporate charter and bylaws.<sup>75</sup> When a principal does not give her fiduciary precise instructions, the fiduciary is required to honor the principal's choices by exercising her discretionary powers to advance the principal's objectives and protect beneficiaries' interests.<sup>76</sup> These features of fiduciary law are arguably consistent with classical liberalism's theory of freedom as noninterference.

Proponents of classical liberalism contend that there is nothing inherently wrongful about a fiduciary engaging in conflicted transactions, provided that the transactions are consistent with the principal's objectives and do not undermine the beneficiary's material interests.<sup>77</sup> For example, an investment manager might find that she can maximize profit for an investor-beneficiary by investing in a commercial venture in which she also has a personal financial stake. According to classical liberals, the reason why fiduciary law requires the investment manager to disclose and receive her beneficiary's consent to the conflicted transactions has to do with the challenge of monitoring a fiduciary's performance: it is often difficult for investors and courts to discern whether a particular conflicted transaction was actually the best option available to the fiduciary.<sup>78</sup> Rather than saddle the investor with determining whether a fiduciary's self-dealing has harmed her material interests, the no-conflict rule's categorical prohibition against unauthorized conflicted transactions forces the investment manager to obtain the investor's fully informed consent *ex ante* or face court-ordered rescission or disgorgement *ex post*.<sup>79</sup> Classical liberalism thus presents fiduciary law's

72. See, e.g., CONAGLEN, *supra* note 5, at 32–50, 61–62.

73. RESTATEMENT (THIRD) OF AGENCY § 8.09 (AM. LAW INST. 2006) (requiring an agent to comply with all lawful instructions from the principal).

74. See RESTATEMENT (THIRD) OF TRUSTS § 76(1) (AM. LAW INST. 2007) (requiring the trustee to administer the trust lawfully and diligently in accordance with the terms of the trust).

75. See, e.g., *Henrichs v. Chugach Alaska Corp.*, 250 P.3d 531, 533 (Alaska 2011) (affirming that a corporate director breached his duty of loyalty by, *inter alia*, “refusing to comply with corporate bylaws”).

76. See, e.g., RESTATEMENT (THIRD) OF TRUSTS § 76(2) (requiring the trustee to identify the duties and powers of the trusteeship, and to effect returns and other benefits for the beneficiaries of the trust).

77. See, e.g., CONAGLEN, *supra* note 5, at 108–09, 113–25 (asserting that a fiduciary can breach her duty of loyalty without acting immorally); John H. Langbein, *Questioning the Trust Law Duty of Loyalty: Sole Interest or Best Interest?*, 114 YALE L.J. 929, 934–35 (2005) (arguing that conflicts of interest are not “inevitably harmful”).

78. See, e.g., Langbein, *supra* note 77, at 938 (noting that categorically prohibiting conflicts of interest may be appropriate when abuses are difficult to detect).

79. See CONAGLEN, *supra* note 5, at 120 (asserting that the no-profit rule is a “prophylactic” rule that reflects courts’ recognition “that when a fiduciary has made an unauthorized profit out of his fiduciary position there will *commonly* or *ordinarily* be a conflict between duty and interest”);

traditional no-conflict and no-profit rules as a pragmatic response to the epistemic challenge of discerning whether conflicted transactions actually respect the principal's choices and promote the beneficiary's best interest.

### B. *The Rise of Modern Fiduciary Law*

The classical liberal theory of fiduciary law can be traced back to the English Chancery Court's seminal 1726 decision, *Keech v. Sandford*.<sup>80</sup> At issue in the case was a lease to Rumford Market, which had been devised to a trustee to hold in trust for an infant.<sup>81</sup> When the lease was set to expire, the trustee allegedly sought to renew the lease on the infant's behalf.<sup>82</sup> The lessor refused to renew the lease, however, objecting that he would not be able to defend his interests in court against an infant lessee in the event of the lease's breach.<sup>83</sup> Finding the path to renewing the lease in the infant's favor blocked, the trustee opted to renew the lease on his own behalf.<sup>84</sup> This action had the effect of disrupting the infant beneficiary's "customary, non-legal, but none the less firm entitlement [under the principle of 'tenant's right'] to roll over finite leases and thus maintain possession over long stretches of time across

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R.P. MEAGHER ET AL., *EQUITY: DOCTRINES AND REMEDIES* 186 (5th ed. 2015) (discussing the availability of the remedies of rescission and disgorgement to victims of the breach of fiduciary duties); LEONARD I. ROTMAN, *FIDUCIARY LAW* 279 (2005) (emphasizing the necessity of obtaining the principal's express and informed consent before a fiduciary may enter into a self- or other-interested transaction); cf. Langbein, *supra* note 77, at 964–65 ("An agent who wants to proceed with a conflicted transaction need only persuade the principal to authorize it (which, of course, the principal will resist, unless he or she determines the transaction to be in his or her best interest).").

80. (1726) 25 Eng. Rep. 223; see also Cooter & Freedman, *supra* note 4, at 1045 n.1 (characterizing *Keech* as fiduciary law's "seminal case"). Although this Article does not afford the space for an in-depth look at the history of the fiduciary concept, it bears noting that the republican conception of fiduciary loyalty predates the classical liberty theory. See, e.g., 1 CICERO, *supra* note 16, at 85 (noting that one of Plato's rules for those in charge of public affairs was to "keep the good of the people so clearly in view that regardless of their own interests they will make their every action conform to that"). Indeed, the introduction of formal fiduciary obligations in Roman law arguably enshrined Cicero's republican conception of the fiduciary relationship—albeit long after the demise of the Roman Republic. See R. D. MELVILLE, *A MANUAL OF THE PRINCIPLES OF ROMAN LAW RELATING TO PERSONS, PROPERTY, AND OBLIGATIONS* 187–208 (3d. ed. 1921) (discussing the legal obligations of guardians under Roman law); David Johnston, *Trusts and Trust-like Devices in Roman Law*, in *ITINERA FIDUCIAE: TRUST AND TRUEHAND IN HISTORICAL PERSPECTIVE* 45, 51 (Richard Helmholz & Reinhard Zimmermann eds., 1998) (discussing the Roman law of *fideicommissum*). But see ALAN WATSON, *THE SPIRIT OF ROMAN LAW* 98, 117, 158 (1995) (arguing that Roman law was pragmatic, unsystematic, and untethered from philosophy); Michele Graziadei, *Virtue and Utility: Fiduciary Law in Civil and Common Law Jurisdictions*, in *PHILOSOPHICAL FOUNDATIONS*, *supra* note 6, at 287, 288 (arguing that Roman fiduciary law reflected an "economy of honor").

81. *Keech*, 25 Eng. Rep. at 223.

82. *Id.*

83. *Id.*; see also Joshua Getzler, *Rumford Market and the Genesis of Fiduciary Obligations*, in *MAPPING THE LAW*, *supra* note 33, at 577, 581 (explaining why various causes of action could not be levied against an infant lessee).

84. *Keech*, 25 Eng. Rep. at 223.

lives and generations.”<sup>85</sup> By renewing the lease in his own name and thereby breaking the inter-generational chain of possession, the trustee frustrated the very purpose of this trust.

Responding to these concerns, Chancellor King ordered the trustee to hold all profits from the lease in a constructive trust for the infant.<sup>86</sup> The Chancellor acknowledged the extraordinary nature of his determination that “the trustee is the only person of all mankind who might not have the lease.”<sup>87</sup> Nonetheless, he stressed that “if a trustee, on the refusal to renew, might have a lease to himself, few trust-estates would be renewed to *cestui que* use.”<sup>88</sup> A general prohibition against conflicted transactions was necessary, in other words, to guard against the likelihood that trustees would abuse their positions of trust and confidence for their own gain at the beneficiaries’ expense.<sup>89</sup>

Despite its antiquated facts and terse reasoning, *Keech* continues to be cited widely for the proposition that the fiduciary duty of loyalty operates as a prophylaxis against harmful opportunism.<sup>90</sup> Consistent with Chancellor King’s reasoning, conventional wisdom holds that the no-conflict and no-profit rules are deliberately over-inclusive measures that deter fiduciaries from engaging in opportunism.<sup>91</sup> By prohibiting all self-interested transactions and profit taking without a beneficiary’s informed consent—regardless of a fiduciary’s intent and irrespective of whether the beneficiary has suffered actual harm—fiduciary law eliminates a fiduciary’s incentives to abuse her position for her own gain.<sup>92</sup> The no-conflict and no-profit rules

85. Getzler, *supra* note 83, at 582.

86. *Keech*, 25 Eng. Rep. at 223–24.

87. *Id.* at 223.

88. *Id.*

89. Pleadings in the case suggest that the trustee may have bribed the lessor to deny renewal to the infant beneficiary in favor of the trustee. Joshua Getzler, “*As If.*” *Accountability and Counterfactual Trust*, 91 B.U. L. REV. 973, 984 (2011).

90. See, e.g., CONAGLEN, *supra* note 5, at 121–22 (stating that, after *Keech*, the no-conflict rule “developed into a clear principle of fiduciary doctrine”); ROTMAN, *supra* note 79, at 61–62; Getzler, *supra* note 83, at 586 (describing *Keech* as “the *fons et origo*” of the doctrine prohibiting fiduciary profit taking).

91. See, e.g., R.P. MEAGHER ET AL., EQUITY: DOCTRINES AND REMEDIES 111 (1st ed. 1975) (asserting that *Keech* frames the duty of loyalty as a prophylactic rule that “imposes a duty to avoid a situation of possible conflict between interest and duty”); T.G. Youdan, *The Fiduciary Principle: The Applicability of Proprietary Remedies*, in EQUITY, FIDUCIARIES AND TRUSTS 93, 105 (T.G. Youdan ed., 1989) (arguing that the “twin policies of prophylaxis and of surmounting the evidence problem may justify the finding of personal liability in a fiduciary where his gain is not shown to correspond to any loss to the principal” (footnote omitted)).

92. See *In re Primedia Inc. Derivative Litig.*, 910 A.2d 248, 262 (Del. Ch. 2006) (“[T]he duty of loyalty ‘does not rest upon the narrow ground of injury or damage to the corporation resulting from a betrayal of confidence, but upon a broader foundation of a wise public policy that, for purposes of removing all temptation, extinguishes all possibility of profit flowing from the breach

also prevent a fiduciary from exploiting the fact that she “controls all evidence of the relationship and can easily conceal wrongdoing from the vulnerable party or the court.”<sup>93</sup> Thus, *Keech* “has been received as embodying a policy of prophylaxis, or preventative sanction through profit stripping that takes away all incentive for a fiduciary to consider how he might gain from his position.”<sup>94</sup>

Nearly two centuries after *Keech*, this theory of fiduciary law received perhaps its most iconic expression in *Bray v. Ford*,<sup>95</sup> an 1896 case from the English House of Lords.<sup>96</sup> The defendant in the case was the Vice-Chancellor of Yorkshire College who was found to have violated his fiduciary duty by simultaneously receiving payment for services rendered as the College’s solicitor.<sup>97</sup> In his opinion, Lord Herschell affirmed the “inflexible rule” that a fiduciary may not “put himself in a position where his interest and duty conflict.”<sup>98</sup> Turning to the basis for this rule, Lord Herschell doubled down on Chancellor King’s theory of the no-conflict and no-profit rules as a prophylaxis against harmful opportunism:

It does not appear to me that this rule is, as has been said, founded upon principles of morality. I regard it rather as based on the consideration that, human nature being what it is, there is danger, in such circumstances, of the person holding a fiduciary position being swayed by interest rather than by duty, and thus prejudicing those whom he was bound to protect. It has, therefore, been deemed expedient to lay down this positive rule. But I am satisfied that it might be departed from in many cases, without any breach of morality, without any wrong being inflicted, and without any consciousness of wrong-doing.<sup>99</sup>

The idea that the duty of loyalty operates as a prophylaxis against harmful opportunism also informed the early development of American fiduciary law. In *Davoue v. Fanning*, “the foundational American case recognizing and enforcing the then-recently-settled English [no-profit] rule,”<sup>100</sup> Chancellor Kent explained the rule as follows:

The *cestuy que trust* is not bound to prove, nor is the court bound to judge, that the trustee has made a bargain advantageous to himself. . . .

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of confidence imposed by the fiduciary relation.” (quoting *Guth v. Loft, Inc.*, 5 A.2d 503, 510 (Del. 1939)).

93. Getzler, *supra* note 83, at 586.

94. *Id.*

95. *Bray v. Ford* [1896] AC 44 (HL) 51 (Lord Herschell) (appeal taken from AC) (Eng.).

96. *Id.*

97. *Id.*

98. *Id.*

99. *Id.* at 51–52.

100. Langbein, *supra* note 77, at 944.

There may be fraud, . . . and the party [may] not [be] able to prove it. It is to guard against this uncertainty and *hazard* of abuse, and to remove the trustee from temptation, that the rule does and will permit the *cestuy que trust* to come, at his own option, and without showing actual injury . . . . This is a remedy which goes deep, and touches the very root of the evil.<sup>101</sup>

In sum, these three cases—*Keech*, *Bray*, and *Davoue*—demonstrate that courts in the United Kingdom and the United States have defended the no-conflict and no-profit rules from the very beginning as measures for prophylactically protecting beneficiaries from harm. Courts recognized that fiduciary power posed a serious risk of opportunism because many conflicted transactions would, in fact, undercut beneficiaries’ interests, but that it would often be difficult, if not impossible, for a court to discern after the fact whether this was so in any particular case. Consistent with classical liberalism, therefore, courts sought to explain and justify the no-conflict and no-profit rules based primarily on concerns for safeguarding beneficiaries from harmful interference.

### C. *Classical Liberalism in Contemporary Fiduciary Theory*

Legal scholars today continue to develop theories of fiduciary law that reflect the normative commitments of classical liberalism. Some scholars argue that fiduciary duties are designed to promote fidelity to a principal’s choices.<sup>102</sup> Others emphasize how fiduciary duties prevent harm to beneficiaries’ material interests.<sup>103</sup> What unites these two camps is the shared assumption that the purpose of fiduciary law is to safeguard freedom from interference.

Consider first the idea that fiduciary law promotes fidelity to a principal’s choices. This vision of fiduciary law has been elaborated most extensively in Matthew Conaglen’s monograph with the suggestive title *Fiduciary Loyalty: Protecting the Due Performance of Non-fiduciary Duties*.<sup>104</sup> Conaglen argues that fiduciary duties are “a subsidiary and prophylactic form of protection for non-fiduciary duties”—principally, those that arise via contract.<sup>105</sup> In Conaglen’s view, the duty of loyalty’s

101. *Davoue v. Fanning*, 2 Johns. Ch. 252, 261 (N.Y. Ch. 1816).

102. See, e.g., CONAGLEN, *supra* note 5, at 202 (asserting that the proscriptive nature of fiduciary duties indicates that they are concerned principally with “removing temptations, such as inconsistent interests or duties, which have a tendency to sway the fiduciary away from proper performance of . . . non-fiduciary duties”).

103. See Cooter & Freedman, *supra* note 4, at 1047 (suggesting that fiduciary law serves to protect principals against “two distinct forms of wrongdoing: first, the fiduciary may misappropriate the principal’s asset or some of its value (an act of malfeasance); and second, the fiduciary may neglect the asset’s management (an act of nonfeasance”).

104. See generally CONAGLEN, *supra* note 5.

105. *Id.* at 4.

proscriptive no-conflict and no-profit rules do not codify the requirements of morality; fiduciaries may profit from unauthorized conflicted transactions in a variety of contexts, he argues, without acting immorally.<sup>106</sup> Nonetheless, these rules are necessary as a practical matter, he argues, to prophylactically eliminate temptations that might compromise a fiduciary's faithful performance of her assigned tasks.<sup>107</sup>

A second line of scholarship, which has been particularly influential in the United States, seeks to explain and justify the fiduciary duty of loyalty based on economic theory. Scholars of law and economics argue that the fiduciary duty of loyalty protects beneficiaries from a classic "agency problem": the risk that a fiduciary will harm their interests by misappropriating their assets or profit-making opportunities to their detriment.<sup>108</sup> Early economic theories of fiduciary law claimed that courts used fiduciary duties as gap fillers for incomplete contracts to compensate for parties' inability to design contracts that completely specify their respective obligations.<sup>109</sup> Over time, scholars have refined this contractarian account by characterizing fiduciary duties as "off-the-rack" or "standard form" contractual default rules that protect unsophisticated parties, enhance the efficiency of contract negotiation, and lower beneficiaries' bonding and monitoring costs.<sup>110</sup> Fiduciary duties are good candidates to serve as default rules, these scholars contend, because they are the kind of legal obligations

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106. See *id.* at 106–41 (asserting that "a breach of fiduciary duty may be committed without the fiduciary necessarily acting immorally").

107. See *id.* at 39–40, 61–62 (using the no-conflict and no-profit principles to advance the argument "that fiduciary doctrine is prophylactic in its very nature, as it is designed . . . to neutralise influences likely to sway the fiduciary"); Smith, *supra* note 5, at 224 ("The rationale for [fiduciary duties] is to prevent fiduciaries from breaching their mandates.").

108. See, e.g., Cooter & Freedman, *supra* note 4, at 1047 (applying "the principal-agent model to the fiduciary relationship" and noting that "misappropriation . . . is governed by the duty of loyalty"); Robert H. Sitkoff, *An Economic Theory of Fiduciary Law*, in PHILOSOPHICAL FOUNDATIONS, *supra* note 6, at 197, 198–99, 201 (discussing how the "benefits [of a fiduciary] come at the cost of being made vulnerable to abuse" and analyzing how the duty of loyalty lessens that risk).

109. See, e.g., *Burdett v. Miller*, 957 F.2d 1375, 1381 (7th Cir. 1992) (suggesting that the courts impose fiduciary duties when "it is a reasonable inference that had the parties in advance negotiated expressly over the issue they would have agreed that the agent owed the principal the high duty [of loyalty]"); Easterbrook & Fischel, *supra* note 7, at 426 (suggesting "that the duty of loyalty is a response to the impossibility of writing contracts completely specifying the parties' obligations"); Jonathan R. Macey, *An Economic Analysis of the Various Rationales for Making Shareholders the Exclusive Beneficiaries of Corporate Fiduciary Duties*, 21 STETSON L. REV. 23, 25 (1991) (arguing that "fiduciary duties should properly be seen as a method of gap-filling in incomplete contracts").

110. See Butler & Ribstein, *supra* note 26, at 11 (regarding fiduciary duties as consistent with "an appropriate implied standard form provision that anticipates what the parties would have drafted if they had focused on the situation"); Easterbrook & Fischel, *supra* note 7, at 426–27 (arguing that fiduciary duties lower transaction, monitoring, and specification costs); Brett H. McDonnell, *Sticky Defaults and Altering Rules in Corporate Law*, 60 SMU L. REV. 383, 387 (2007) (describing corporate law as "a convenient set of off-the-rack rules that help solve problems").

that a sophisticated party would demand whenever they repose special trust and confidence in another.<sup>111</sup> By making fiduciary duties default rules, fiduciary law also minimizes information costs to third parties, such as creditors, who transact with a fiduciary.<sup>112</sup>

Scholars who apply economic theory to fiduciary law tend to agree with Conaglen that the no-conflict and no-profit rules are over inclusive, because they deter fiduciaries from pursuing some self-interested transactions that would actually promote their beneficiaries' best interests.<sup>113</sup> Nonetheless, they argue that the "prophylactic" character of these rules is a necessary response to the significant information asymmetries between fiduciaries, beneficiaries, and the judiciary.<sup>114</sup> Thus, in contrast to Conaglen, who focuses on respecting a principal's choices, scholars of law and economics emphasize the duty of loyalty's deterrent and protective function in preventing fiduciaries from harming beneficiaries' material interests.

Despite their different points of departure, these two accounts of fiduciary law both approach the duty of loyalty from a classical liberal perspective. Both assume that fiduciary duties are concerned exclusively with safeguarding parties' freedom from interference. Both characterize the no-conflict and no-profit rules as "over inclusive" because the rules may deter fiduciaries from pursuing some desirable transactions.<sup>115</sup> Accordingly, both endorse Lord Herschell's suggestion that the no-conflict and no-profit

111. See Eric Talley, *Turning Servile Opportunities to Gold: A Strategic Analysis of the Corporate Opportunities Doctrine*, 108 YALE L.J. 277, 280–81 (1998) (classifying standard fiduciary rules as "default mechanism[s]" and arguing that "fashioning a [fiduciary] rule that replicates (at least functionally) the allocation that the parties themselves would have bargained for ex ante . . . should be an important goal of the courts").

112. See John C. Coffee, Jr., *The Mandatory/Enabling Balance in Corporate Law: An Essay on the Judicial Role*, 89 COLUM. L. REV. 1618, 1678 (1989) (arguing that "standardization of contract terms through the use of mandatory legal rules reduces information costs for investors"); Sitkoff, *supra* note 108, at 205 (concluding that fiduciary obligations "minimize third-party information costs").

113. See, e.g., GEORGE GLEASON BOGERT & GEORGE TAYLOR BOGERT, *THE LAW OF TRUSTS AND TRUSTEES* § 543 (2d ed. rev. 1993) ("The principal object of the [no-profit] rule is preventative . . ."); Langbein, *supra* note 77, at 932–33 (arguing that the no-conflict rule results in overdeterrence); Sitkoff, *supra* note 109, at 201 ("[T]he functional core of fiduciary obligations is deterrence.").

114. See, e.g., Cooter & Freedman, *supra* note 4, at 1048 ("Because a fiduciary's misappropriation is profitable and difficult to prove, it is appropriate for fiduciary law to infer disloyalty from its appearance."); Talley, *supra* note 111, at 282 (arguing that fiduciary law's prophylactic rules are justifiable on the basis that "an optimal legal rule in a private-information environment may consciously permit some inefficiencies in order to obviate even greater efficiency losses"); Youdan, *supra* note 91, at 105 (arguing that the "twin policies of prophylaxis and of surmounting the evidence problem may justify the finding of personal liability in a fiduciary where his gain is not shown to correspond to any loss to the principal" (footnote omitted)).

115. See Talley, *supra* note 111, at 282 (noting that "the optimal legal rule will tend . . . to be over-inclusive"); cf. CONAGLEN, *supra* note 5, at 68 (discussing how fiduciary duties can "capture situations in which no true wrong has been committed").



rules “might be departed from in many cases, without any breach of morality, without any wrong being inflicted, and without any consciousness of wrongdoing.”<sup>116</sup> At the end of the day, however, both accounts accept that the traditional duty of loyalty is necessary as a prophylactic measure to minimize the serious risks of harm that arise within fiduciary relationships.<sup>117</sup>

#### D. *Challenges to the Classical Liberal Theory*

Despite classical liberalism’s many virtues as an interpretive theory of fiduciary law, it is not a natural fit with traditional fiduciary rules and remedies. Some key features of fiduciary relationships run at cross-purposes with the ideal of freedom as noninterference, including the discretionary authority that fiduciaries often exercise over their principals’ interests. There are also good reasons to question whether the inflexible no-conflict and no-profit rules offer an optimal strategy for combatting harmful opportunism. Moreover, the traditional fiduciary remedies of constructive trust and disgorgement do not track the optimal deterrence conception of fiduciary loyalty. For these and other reasons, it is unlikely that classical liberalism can offer a complete justification for the traditional duty of loyalty with its associated remedies.

Under classical liberalism, any form of interference in matters of personal choice constitutes a threat to freedom.<sup>118</sup> Yet fiduciary law entrusts many fiduciaries—including guardians and investment managers—with broad discretionary powers to make decisions for and on behalf of their principals.<sup>119</sup> These fiduciaries are not charged solely with carrying their principals’ choices into execution; instead, they make choices *for* their principals and beneficiaries.<sup>120</sup> Indeed, it is no great exaggeration to say that a fiduciary’s intercession in her principal’s domain of personal choice is the entire *raison d’être* for these categories of fiduciary relationships. Fiduciary decision making might be less problematic from a classical liberal perspective when it occurs with a principal’s informed consent. Some fiduciary relationships, however, are established by legislation, judicial decree, or unilateral undertaking, rather than through the parties’ voluntary

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116. *Bray v. Ford* [1896] AC 44 (HL) 51 (Lord Herschell) (appeal taken from AC) (Eng.).

117. See CONAGLEN, *supra* note 5, at 70–71 (asserting that the purpose of fiduciary doctrine is to “provide prophylactic protection” to minimize harm); Sitkoff, *supra* note 22, at 1049 (declaring that “the law requires the fiduciary to be other-regarding” and elaborating that “[w]hat is meant by other-regarding is defined by default fiduciary duties of loyalty”).

118. See *supra* subpart II(A).

119. See, e.g., FRANKEL, *supra* note 1, at 42–53 (examining traditional examples of fiduciary relationships and the responsibilities and discretion in each).

120. *Id.*

choice.<sup>121</sup> These relationships sidestep a principal's decision making by placing her interests under another's power without her consent. They also impose legal duties that constrain the fiduciary's choices.<sup>122</sup> The best argument for these choice-constraining features of fiduciary law, from the perspective of classical liberalism, may be that they are default rules that correspond to the hypothetical bargain that a reasonable fiduciary would make with her principal. As this Article explains in Part III, however, the triggering conditions and terms of this "hypothetical bargain" are best understood as reflecting republican concerns about fiduciaries' capacity for arbitrary interference, rather than the classical liberal ideal of freedom from interference.

Just as classical liberalism struggles to explain fiduciary authority and fiduciary duties, there are good reasons to reject the classical liberal thesis that optimal deterrence can fully explain or justify the duty of loyalty with its associated remedies. Economic theory suggests that successful deterrence depends upon the expected sanction equaling or exceeding the expected gain from a fiduciary's indiscretions.<sup>123</sup> However, the expected value of unauthorized conflicted transactions will always exceed the expected value of disgorged assets. The reasons for this are obvious. Some beneficiaries will never become aware that their fiduciary has engaged in self-dealing. Others will lack a sufficient stake in the matter to justify incurring litigation costs, or they will decline to pursue judicial relief for idiosyncratic personal reasons. As long as the probability of effective judicial enforcement is less than 100%, the traditional fiduciary remedies of rescission, constructive trust, and disgorgement will fail systematically to deter harmful opportunism *ex ante*.<sup>124</sup> Thus, if the no-profit rule were designed as a deterrence mechanism, we would expect it to be backed by harsher penalties than rescission, constructive trust, and disgorgement.

More troubling still, it is unclear as a purely empirical matter whether the no-conflict and no-profit rules actually promote beneficiaries' material interests. Some legal scholars have speculated that these rules are more likely to harm beneficiaries' interests overall by deterring loyal fiduciaries from

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121. See Walter G. Hart, *The Development of the Rule in Keech v. Sandford*, 21 L.Q. REV. 258, 258 (1905) (observing that "a vendor of land is [deemed by law] to be a constructive trustee for the purchaser" between contract formation and conveyance); Miller, *supra* note 2, at 982 n.37 (citing as examples the relationships between parents and children and between a trustee and beneficiary of a declaratory trust).

122. See FRANKEL, *supra* note 1, at 101–77 (examining the duties of fiduciaries, including the duties of care and loyalty).

123. See A. Mitchell Polinsky & Steven Shavell, *The Optimal Use of Fines and Imprisonment*, 24 J. PUB. ECON. 89, 91 (1984) ("An individual will engage in [an] activity if his private gain exceeds the expected sanction.").

124. See Lionel Smith, *Deterrence, Prophylaxis and Punishment in Fiduciary Obligations*, 7 J. EQUITY 87, 91 (2013).

concluding profit-enhancing (or loss-minimizing) transactions.<sup>125</sup> Although the no-conflict and no-profit rules may prevent some self-dealing, critics have argued that it “also reduces—and in all likelihood to a greater extent—the number of instances in which fiduciaries who are inclined to act loyally can act on their inclinations.”<sup>126</sup> Extending this argument, it is possible that the no-conflict and no-profit rules might also frustrate the “due performance of non-fiduciary duties” in some settings by deterring fiduciaries from pursuing transactions that would best satisfy their principals’ instructions.

John Langbein has pursued this critique of the no-conflict and no-profit rules with particular vigor.<sup>127</sup> Langbein characterizes the no-conflict rule as “*Bleak House* law, born of the [English Chancery Court’s] despair” over its inability to distinguish faithful trust administration from fraud.<sup>128</sup>

Today, by contrast, in the wake of fusion and the reform of civil procedure, courts dealing with equity cases command effective fact-finding procedures.<sup>129</sup>

Accordingly, much of the concern voiced by [Chancellor Kent and others]—that without the [no-conflict] rule the beneficiary would be “not able to prove” trustee misbehavior—is archaic.<sup>130</sup>

In Langbein’s view, therefore, the duty of loyalty’s “prophylactic” rules are no longer necessary to protect beneficiaries from fiduciary opportunism and may actually harm beneficiaries’ interests by taking desirable conflicted transactions off the table.

One final critique of the classical liberal theory of fiduciary law merits brief consideration. As other scholars have noted, there is a fundamental conceptual mismatch between classical liberalism’s conception of the no-profit rule as a prophylactic deterrent measure and the paradigmatic remedies for unauthorized profits: constructive trust and disgorgement.<sup>131</sup>

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125. See, e.g., Langbein, *supra* note 77, at 988 (arguing that the present formulation of fiduciary loyalty forsakes the underlying purpose of the duty by ignoring that conflicted transactions sometimes advance a beneficiary’s best interest).

126. Smith, *supra* note 5, at 126 n.15. Melanie Leslie argues that this concern is vastly overstated because fiduciaries would decline to pursue conflicted transactions only in the exceedingly rare cases where the costs of obtaining beneficiaries’ informed consent would outweigh the expected gains. See Melanie B. Leslie, *In Defense of the No Further Inquiry Rule: A Response to Professor John Langbein*, 47 WM. & MARY L. REV. 541, 550 (2005).

127. See Langbein, *supra* note 77, at 951–52 (arguing that the rules result in “overdeterrence”— “[b]y penalizing trustees in cases in which the interest of the trust beneficiary was unharmed or advanced, the rule deters future trustees from similar, beneficiary-regarding conduct”).

128. *Id.* at 947.

129. *Id.*

130. *Id.*

131. See, e.g., Lionel Smith, *Fiduciary Relationships: Ensuring the Loyal Exercise of Judgement on Behalf of Another*, 130 L.Q. REV. 608, 625–31 (2014) (explaining that viewing the no-profit rule as prophylactic is incompatible with the theories behind constructive trusts and disgorgement).

Traditionally speaking, courts have conceptualized disgorgement as a restitutionary remedy rather than a punitive remedy.<sup>132</sup> The purpose of disgorgement is simply to effectuate the return of assets that have been wrongfully withheld.<sup>133</sup> Constructive trust likewise applies when a party has been “unjustly enriched by the acquisition of title to identifiable property at the expense of the claimant or in violation of the claimant’s rights.”<sup>134</sup> Under the classical liberal theory, however, it is unclear why profits generated by conflicted transactions or misappropriated business opportunities would belong, strictly speaking, to beneficiaries rather than to the public fisc. That a beneficiary may suffer harm from the opportunism that generates fiduciary profits is self-evident. Yet compensatory damages, punitive damages, and criminal sanctions would seem to be the appropriate remedies to make a beneficiary whole and deter future indiscretions—not constructive trust and disgorgement.<sup>135</sup> Taking classical liberalism seriously would therefore require an extreme makeover of fiduciary duties and remedies.

#### *E. Classical Liberalism’s Challenge to Fiduciary Law*

These lessons have not been lost on legal scholars, legislators, and judges in the United States. As the mismatch between classical liberalism’s normative commitments and fiduciary law’s rules and remedies has become increasingly apparent, some legal scholars, judges, and legislators have taken steps to reshape American fiduciary law in the image of classical liberalism. Over the past several decades, classical liberal thinking has profoundly shaped the fiduciary law of business organizations, as state legislatures and courts have dismantled key features of the duty of loyalty. For example, under the latest formulation of the Delaware Supreme Court’s “entire fairness” test, corporate directors may authorize self-dealing transactions without obtaining informed consent from either the disinterested directors or the corporation’s shareholders, as long as they can convince courts after the fact that the transactions were substantially fair.<sup>136</sup> Moreover, when a court

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132. *See, e.g.*, *SEC v. First City Fin. Corp.*, 890 F.2d 1215, 1231 (D.C. Cir. 1989) (explaining that disgorgement “may not be used punitively”).

133. *See id.* (“[D]isgorgement primarily serves to prevent unjust enrichment.”).

134. RESTATEMENT (THIRD) OF RESTITUTION AND UNJUST ENRICHMENT § 55(1) (AM. LAW INST. 2011).

135. *See, e.g.*, *Bardis v. Oates*, 14 Cal. Rptr. 3d 89, 100–08 (Cal. Ct. App. 2004) (awarding compensatory and punitive damages, recognizing the availability of disgorgement, and noting the availability of substantial criminal penalties for breach of fiduciary duty). Conaglen has argued that disgorgement can be rehabilitated as a fiduciary remedy if it is conceptualized as a purely prophylactic measure. *See CONAGLEN, supra* note 5, at 76. As Lionel Smith has explained, however, Conaglen’s theory still raises the over-inclusivity and under-inclusivity concerns associated with deterrence accounts. *See Smith, supra* note 124, at 93, 95.

136. DEL. CODE ANN. tit. 8, § 144(a)(3) (2017); *see also Nixon v. Blackwell*, 626 A.2d 1366, 1376 (Del. 1993) (defining the aspects of the entire fairness test as applied to breaches of fiduciary

in Delaware determines that a conflicted transaction violates the entire fairness test, “the remedy is the difference between the fair value determined by the court and the value actually conveyed” (consistent with classical liberalism), rather than full disgorgement of all profits (as required under the traditional no-profit rule).<sup>137</sup> These departures from the traditional duty of loyalty resonate with the classical liberal view that state intervention in the private sphere is warranted only to the extent that it is absolutely necessary to prevent officers and directors from harming a corporation’s material interests.

Drawing inspiration from Delaware corporate law, Langbein has argued that trust law’s no-conflict and no-profit rules should also be reframed as a rebuttable presumption.<sup>138</sup> Under Langbein’s proposed approach, unauthorized conflicted transactions would not be subject to rescission, constructive trust, or disgorgement if a trustee can establish that the transactions promoted her beneficiaries’ best interests relative to other available opportunities.<sup>139</sup> Implicit in this proposal is a simple premise: there is nothing inherently immoral about a fiduciary profiting from a conflicted transaction, provided that the transaction also increases the beneficiaries’ profits (or minimizes losses) relative to other opportunities. After all, why should courts demand that fiduciaries act in the *sole* interest of their beneficiaries if a conflicted transaction would inarguably promote the beneficiaries’ *best* interests? Taking the normative commitments of classical liberalism at face value, it is hard to see why courts must apply the no-conflict and no-profit rules with “[u]ncompromising rigidity.”<sup>140</sup>

Recent developments suggest that Langbein’s critique of the no-conflict and no-profit rules is gaining traction at the state level. For example, the Model Business Corporation Act and the Uniform Business Organizations Code have been revised in recent years to allow fiduciaries to conclude conflicted transactions without their beneficiaries’ approval if they can

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duty); *Weinberger v. UOP, Inc.*, 457 A.2d 701, 711 (Del. 1983) (explaining the entire fairness test as an overall look at whether the transaction met the aspects of fair dealing and fair price, and which factors play into that determination).

137. D. Gordon Smith, *Fiduciary Law and Entrepreneurial Action 3* (unpublished manuscript) (on file with author); *see also Int’l Telecharge, Inc. v. Bomarko, Inc.*, 766 A.2d 437, 440–42 (Del. 2000) (explaining that in a merger action, the court must appraise the actual value of the shares in determining damages); *In re Dole Food Co. Stockholder Litig.*, 2015 WL 5052214, at \*44–46 (Del. Ch. Aug. 27, 2015) (explaining that the damages awarded in a breach of fiduciary duty case can be determined by the difference between the fair value of the shares as determined by the court and the value actually conveyed for said shares).

138. Langbein, *supra* note 77, at 931–33.

139. *Id.*

140. *Meinhard v. Salmon*, 164 N.E. 545, 546 (N.Y. 1928). *But see* Leslie, *supra* note 7, at 72 (arguing that Langbein’s approach “would strike a fatal blow to the duty of loyalty as a moral norm, and would thus increase instances of trustee opportunism, at least at the margins”).

convince courts that the conflicted transactions were objectively “fair.”<sup>141</sup> The Uniform Trust Code likewise no longer presumes that a trustee who purchases investments from related entities has violated her duty of loyalty.<sup>142</sup> Although transactions between a trustee and her relatives, agents, and other close associates are “presumed to be affected by a conflict between personal and fiduciary interests,”<sup>143</sup> this presumption can be rebutted “if the trustee establishes that the transaction was not affected by a conflict between personal and fiduciary interests.”<sup>144</sup> Similarly, the Uniform Power of Attorney Act and the Uniform Probate Code no longer apply the no-conflict rule to principal–agent relationships.<sup>145</sup> Dozens of states and the District of Columbia have embraced these changes, implicitly endorsing the classical liberal idea that if beneficiaries have suffered “no harm” there is “no foul” requiring judicial relief.<sup>146</sup> As long as a fiduciary has acted “with care, competence, and diligence for the best interest of the [beneficiary],” the thinking goes that the beneficiary has no cause to complain.<sup>147</sup>

The classical liberal theory of fiduciary loyalty is also beginning to shape federal law. Over the past year, the fiduciary status of investment advisers has become a topic of heated political debate following the Department of Labor’s (DOL) promulgation of a final rule designating certain retirement investment advisers as fiduciaries (the “Fiduciary Rule”).<sup>148</sup> Under intense lobbying from the financial services community, majorities of both houses of Congress voted to revoke the Fiduciary Rule in 2016, only to see the measure vetoed by President Barack Obama.<sup>149</sup> Several

141. See MODEL BUS. CORP. ACT § 8.61(b)(3) (AM. BAR ASS’N 2005) (providing that conflicted transactions need “to have been fair to the corporation”); UNIF. BUS. ORG. CODE § 8-507 (UNIF. LAW COMM’N 2011) (providing that a conflicted transaction is not voidable if “the covered party shows that the transaction is fair to the trust”).

142. UNIF. TRUST CODE § 802(f) (UNIF. LAW COMM’N 2010). Commentary accompanying this provision states that it “creates an exception to the [no-conflict and no-profit rules] for trustee investment in mutual funds.” *Id.* § 802 cmt.

143. *Id.* § 802(c).

144. *Id.* § 802 cmt.

145. UNIF. PROB. CODE § 5B-114(d) (UNIF. LAW COMM’N 2010); UNIF. POWER OF ATT’Y ACT § 144(d) (UNIF. LAW COMM’N 2006). *But see* RESTATEMENT (THIRD) OF AGENCY §§ 8.01–06 (AM. LAW INST. 2006) (retaining the traditional no-conflict rule).

146. On business organizations, see, for example, 7 COLO. REV. STAT. § 7-108-501(2)(c) (2016); 29 D.C. CODE § 29-1205.07 (2016); ME. REV. STAT. ANN. tit. 13–C § 872(2)(C) (2016); 47 S.D. CODIFIED LAWS § 47-1A-861.1(3) (2007). On principal–agent relationships, see, for example, ARK. CODE ANN. 28-68-114(d) (West 2017); DEL. CODE ANN. tit. 12 § 49A-114(d) (West 2014); 13 OHIO REV. CODE ANN. § 1337.34(D) (West 2016); VA. CODE ANN. § 64.2-1612(D) (2012).

147. UNIF. POWER OF ATT’Y ACT § 114(d).

148. Definition of the Term “Fiduciary”; Conflict of Interest Rule—Retirement Investment Advice, 81 Fed. Reg. 20,946, 20,997 (Apr. 8, 2016) (codified at 29 C.F.R. § 2510.3–21 (2016)) [hereinafter *Fiduciary Rule*].

149. See Tammy Duckworth, Opinion, *Isn’t Honesty the Best Policy?*, N.Y. TIMES (June 10, 2016), [https://www.nytimes.com/2016/06/11/opinion/isnt-honesty-the-best-policy.html?\\_r=0](https://www.nytimes.com/2016/06/11/opinion/isnt-honesty-the-best-policy.html?_r=0)

lawsuits were later filed against DOL,<sup>150</sup> including one in which the U.S. Chamber of Commerce and other industry groups sought to prevent the Fiduciary Rule's enforcement on the grounds that the rule creates "unwarranted burdens and liabilities" for financial advisers.<sup>151</sup> To date, none of these legal challenges to the Fiduciary Rule have been successful.<sup>152</sup> In the meantime, however, congressional Republicans introduced a bill to delay the Fiduciary Rule's effective date for two years.<sup>153</sup> Incoming President Donald Trump also issued a memorandum, instructing DOL to review the Fiduciary Rule for possible revision or rescission.<sup>154</sup> White House representatives and some congressional leaders defended the President's move, arguing that reconsideration was justified because in their view the Fiduciary Rule threatened to limit the investment choices available to retirement investors and increase management costs.<sup>155</sup> Although this

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[<https://perma.cc/68DM-TKGF>] (stating "Republican majorities in the House and Senate pushed through a bill to block the Department of Labor's rule. On Wednesday [June 8th, 2016], President Obama rightly vetoed it.").

150. See Jacklyn Wille, *Labor Department Faces Five Lawsuits Over Fiduciary Rule*, BLOOMBERG BNA (June 9, 2016), <https://www.bna.com/labor-department-faces-n57982073912/> [<https://perma.cc/K5YT-FGED>] (describing lawsuits).

151. Complaint at 2, *Chamber of Commerce v. Perez*, No. 16-cv-1476 (N.D. Tex. June 1, 2016), [http://www.financialservices.org/uploadedFiles/FSI\\_Content/Advocacy\\_Action\\_Center/DOL/DOL-Fiduciary-Rule-Complaint.pdf](http://www.financialservices.org/uploadedFiles/FSI_Content/Advocacy_Action_Center/DOL/DOL-Fiduciary-Rule-Complaint.pdf) [<https://perma.cc/4K2T-4N92>].

152. *Chamber of Commerce v. Hugler*, No. 16-cv-1476, 2017 WL 514424, at \*1 (N.D. Tex. Feb. 8, 2017).

153. See David Trainer, *The Truth Behind the Push To Delay Fiduciary Rule*, FORBES (Jan. 17, 2017), <http://www.forbes.com/sites/greatspeculations/2017/01/17/the-truth-behind-push-to-delay-fiduciary-rule/#e9cc79d4b100> [<https://perma.cc/6LVH-E98L>] (discussing the bill introduced by Representative Joe Wilson and providing a link to it).

154. Presidential Memorandum on Fiduciary Duty Rule, Memorandum for the Secretary of Labor § 1(b) (Feb. 3, 2017), <https://www.whitehouse.gov/the-press-office/2017/02/03/presidential-memorandum-fiduciary-duty-rule> [<https://perma.cc/MQ8U-X3GY>] [hereinafter TRUMP MEMORANDUM]. At the time of this writing, the press has reported that the President intends to take action to delay implementation of the Fiduciary Rule to facilitate this review. See *The Trump Administration Reportedly Plans To Delay the 'Fiduciary' Rule for 180 Days*, FORTUNE (Feb. 10, 2017), <http://fortune.com/2017/02/10/trump-administration-labor-department-fiduciary-rule-delay/> [<https://perma.cc/3PH5-8BNS>] (discussing these developments).

155. See Press Release, House Fin. Servs. Comm., Statement from Hensarling and Wagner on President Trump's Action to Delay Harmful Fiduciary Rule (Feb. 3, 2017), <http://financialservices.house.gov/news/documentsingle.aspx?DocumentID=401458> [<https://perma.cc/LG8C-NWPB>] (quoting Financial Services Committee Chairman Jeb Hensarling as claiming that eliminating the Fiduciary Rule would "empower Americans to make their own financial decisions" and lower management costs for retirement investors); Jonnelle Marte, *Trump Calls for Review of Long-Awaited Rule Meant To Protect Retirement Savers*, WASH. POST (Feb. 3, 2017), [https://www.washingtonpost.com/news/get-there/wp/2017/02/03/trump-to-target-long-awaited-rule-meant-to-protect-retirement-savers/?tid=a\\_inl&utm\\_term=.6206b3a7ee55](https://www.washingtonpost.com/news/get-there/wp/2017/02/03/trump-to-target-long-awaited-rule-meant-to-protect-retirement-savers/?tid=a_inl&utm_term=.6206b3a7ee55) [<https://perma.cc/P7EC-2FX5>] (citing comments of White House Press Secretary Sean Spicer that the rule would have limited the amount of financial services available to the public); Press Release, White House Office of the Press Sec'y, Remarks by President Trump at Signing of Executive Order on Fiduciary Rule (Feb. 3, 2017), <https://www.whitehouse.gov/the-press-office/2017/02/03/remarks-president-trump-signing-executive-order-fiduciary-rule>

characterization of the Fiduciary Rule's impact is controversial, to say the least,<sup>156</sup> the critical point for present purposes is what it reveals about the terms of contemporary debates over fiduciary loyalty. Without exception, critics of the Fiduciary Rule presume that classical liberal values—investor choice and private wealth maximization—are the only relevant normative considerations.

Some fiduciary law scholars in the United States have expressed consternation about the growing movement to rein in the fiduciary duty of loyalty.<sup>157</sup> By and large, however, they have defended fiduciary law's traditional rules and remedies without challenging the normative commitments of classical liberalism.<sup>158</sup> Consequently, debates over the wisdom of preserving and extending fiduciary law's no-conflict and no-profit rules have become mired in empirically contested claims about whether fiduciary duties and remedies optimally deter opportunism.<sup>159</sup> The republican tradition offers a more promising theoretical foundation for explaining, justifying, and defending fiduciary law's conventional rules and remedies. To build upon this foundation, however, courts and policy makers will have to set aside some cherished myths about the purpose and function of fiduciary duties, including Chancellor King's oft-repeated dictum that the duty of loyalty is an over-inclusive prophylactic rule. In the discussion that follows, this Article shows how the republican theory of fiduciary law furnishes an interpretively compelling alternative to classical liberalism. The republican theory supports the traditional features of fiduciary loyalty, including the proscriptive no-conflict and no-profit rules, and it justifies fiduciary law's distinctive remedies.

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[<https://perma.cc/QV2Y-ZX7K>] (quoting Representative Ann Wagner's comment: "What we're doing is we are returning to the American people . . . their control of their own retirement savings").

156. Contrary to the protestations of its critics, the Fiduciary Rule does not limit investor choice in any meaningful sense; it merely requires investment advisers to obtain investors' informed consent to particular conflicts of interest. *See generally* Fiduciary Rule, *supra* note 148. Supporters observe, moreover, that the Rule promotes investors' interests because "conflicted advice" from retirement-investment advisers "lowers investors' returns by as much as 1 percentage point a year—a loss of \$17 billion annually for IRA investors alone." Eileen Ambrose, *New Rules to Improve Retirement Investing*, AARP BULL., May 2016, <http://www.aarp.org/money/investing/info-2016/rules-protect-retirement-investments.html> [<https://perma.cc/S3LF-PS2T>] (citing figures from the White House Council of Economic Advisers).

157. *See, e.g.*, Melanie B. Leslie, *Common Law, Common Sense: Fiduciary Standards and Trustee Identity*, 27 CARDOZO L. REV. 2713, 2742–43 (2006) (arguing that modifying or eliminating fiduciary rules undermines beneficiaries' interests).

158. *See, e.g.*, Leslie, *supra* note 126, at 544 (challenging amendments to the Uniform Trust Code on the grounds that they would harm future beneficiaries rather than challenging classical liberalism itself).

159. *Compare* Langbein, *supra* note 77, at 940–41 (arguing that some traditional fiduciary rules and remedies were suboptimal in the context of trust law), *with* Leslie, *supra* note 7, at 70–71 (defending traditional fiduciary rules and remedies).



### III. A Republican Theory of Fiduciary Law

Unlike classical liberalism, republicanism persuasively explains and justifies the traditional features of contemporary fiduciary law. As this Part will show, the juridical structure of American fiduciary law reflects republican principles, from the idea that “breach of trust” constitutes a distinctive legal wrong<sup>160</sup> to courts’ reliance on equitable remedies that are calibrated precisely to neutralize domination.<sup>161</sup> Although classical liberalism has chipped away at traditional fiduciary rules and remedies over the past several decades—particularly with respect to the fiduciary duties of business associations<sup>162</sup>—American fiduciary law as a whole continues to reflect republicanism’s normative commitment to freedom from domination.

Republican themes also appear in contemporary fiduciary law scholarship. As fiduciary legal theory has matured in recent years, some theorists have pushed back against classical liberalism, arguing that fiduciary duties cannot be fully apprehended from the perspective of preventing harmful interference. Some have suggested that fiduciary duties and remedies reflect formal juridical features of fiduciary relationships.<sup>163</sup> Others have emphasized the need to protect vulnerable parties from subjection to fiduciaries’ unilateral power.<sup>164</sup> Still others have emphasized the

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160. See, e.g., CAL. PROB. CODE § 16440 (West 2005) (describing a trustee’s violation of the duty of loyalty as a “breach of trust”); *United States v. Carter*, 217 U.S. 286, 306 (1910) (emphasizing that if a fiduciary “acquires any interest adverse to his principal without a full disclosure, it is” actionable as “a betrayal of his trust and a breach of confidence”); *Pure Power Boot Camp, Inc. v. Warrior Fitness Boot Camp, LLC*, 813 F. Supp. 2d 489, 521–22 (S.D.N.Y. 2011) (emphasizing the betrayal of trust in fiduciary disloyalty).

161. See, e.g., *Lewis v. Pension Benefit Guarantee Corp.*, 2016 WL 3676099, at \*6–7 (D.D.C. July 6, 2016) (affirming disgorgement as a remedy for breach of fiduciary duty); *In re Opus East LLC*, 528 B.R. 30, 106–07 (Bankr. D. Del. 2015) (emphasizing that constructive trust is an appropriate remedy for breach of fiduciary duty); *Holliday v. Weaver*, 2016 WL 3660261, at \*2 (mem. op.) (Tex. App.—Dallas 2016, no pet.) (“Where there has been a clear and serious violation of a fiduciary duty, equity dictates not only that the fiduciary disgorge his fees, but also all benefit obtained from use of those fees.”).

162. See *supra* notes 136–37, 141–47 and accompanying text.

163. See, e.g., Paul B. Miller, *The Fiduciary Relationship*, in PHILOSOPHICAL FOUNDATIONS, *supra* note 6, at 63, 67 (noting that “fiduciary duties *have* historically been ‘necessarily referable to a relationship’”); Lionel D. Smith, *Can We Be Obligated to Be Selfless?*, in PHILOSOPHICAL FOUNDATIONS, *supra* note 6, at 141, 141–42 (discussing the idea that the legal requirement of loyalty should not be called a duty).

164. See, e.g., ROTMAN, *supra* note 79, at 84 (analyzing *Frame v. Smith*, [1987] 2 S.C.R. 99, 99 (Can.) (Wilson, J., dissenting)); Deborah A. DeMott, Essay, *Relationships of Trust and Confidence in the Workplace*, 100 CORNELL L. REV. 1255, 1259–60 (2015) (commenting that fiduciary relationships “require or engender trust by the beneficiary with a correlative potential for abuse by the fiduciary, often . . . effected through deceptive or disingenuous means”); Smith, *supra* note 64, at 1483 (noting that “[t]he law provides protection against opportunistic behavior, and the strength of that protection varies inversely with the potential for self-help on the part of the vulnerable party”); Ernest J. Weinrib, *The Fiduciary Obligation*, 25 U. TORONTO L.J. 1, 4–5 (1975) (“The wide leeway afforded to the fiduciary to affect the legal position of the principal in effect puts

“entrustment” of other-regarding power as a defining feature of fiduciary relationships.<sup>165</sup> Each of these contributions gestures toward a republican theory in which fiduciary duties and remedies are calculated to safeguard parties’ freedom from domination. Nonetheless, the fact that judges and private law scholars have not expressly connected fiduciary law to republicanism’s distinctive conception of legal order has impeded previous efforts to develop a coherent interpretive theory of fiduciary law.

This Part shows how republicanism can explain fiduciary law’s traditional duties and remedies while also supplying a robust normative justification for these features. The republican theory furnishes answers to some of the most important and controversial questions in fiduciary theory today, including: (A) the normative foundations of fiduciary law; (B) the distinguishing features of fiduciary relationships; (C) the requirements of fiduciary loyalty; (D) the theoretical basis for fiduciary law’s traditional remedies; and (E) the theoretical basis for fiduciary law’s divergent conduct and decision rules. Taking a step back, however, the republican theory’s most important contribution may be to situate fiduciary law within a rich philosophical account of the relationship between public institutions, private relationships, and private law.<sup>166</sup> As this Part will show, private fiduciary theory has much to learn from public law theory. Whereas private law theory has underscored the interpersonal nature of fiduciary relationships and has provided the most granular analysis of the duty of loyalty’s applications, public law theory offers the sharpest account of what it means to hold a fiduciary office properly, which is to say, subject to republican norms of nondomination.<sup>167</sup>

#### A. *The Normative Foundations of Fiduciary Law*

The republican theory posits that fiduciary law *empowers* principals, while also *emancipating* principals, beneficiaries, and fiduciaries alike from domination. Fiduciary law is concerned not merely with promoting the performance of non-fiduciary obligations or preventing material harm, as

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the latter at the mercy of the former, and necessitates the existence of a legal device which will induce the fiduciary to use his power beneficently.”)

165. FRANKEL, *supra* note 1, at 4–6; *see also* J. C. SHEPHERD, *THE LAW OF FIDUCIARIES* 35 (1981) (describing as essential to a fiduciary relationship the acquisition and use of power by one person on the condition that it be used in the best interests of another); Matthew Harding, *Trust and Fiduciary Law*, 33 *OXFORD J. LEGAL STUD.* 81, 82–87 (2013) (arguing that “thick” trust, which is characterized by the entrustment of discretionary power, characterizes some types of fiduciary relationships).

166. Whether fiduciary duties can successfully eliminate domination in practice depends, of course, on whether they are implemented through legal and political institutions that are congenial to nondomination. This Article discusses some implications of this challenge in subpart III(E) below.

167. I am grateful to Evan Fox-Decent for suggesting this formulation.

some theorists have assumed. Rather, it secures freedom from domination by affirming that all people are *sui juris*—free and equal agents whose legal and practical interests are entitled to respect.

*1. Empowerment.*—Fiduciary law empowers principals in several different ways. First, it enables principals to extend their agency through fiduciaries who exercise legal powers and assert legal rights on their behalf.<sup>168</sup> A principal may decide to entrust a fiduciary with authority to conclude transactions on her behalf with third parties (agency);<sup>169</sup> manage and distribute her assets upon her death (testamentary trusts);<sup>170</sup> distribute her assets to unspecified third parties for charitable purposes (charitable trusts);<sup>171</sup> participate in a commercial enterprise (corporations);<sup>172</sup> or tend to the physical, emotional, educational, and religious upbringing of her children (guardianship).<sup>173</sup> In each of these settings, fiduciary law makes vicarious representation possible by empowering a principal to authorize another party to exercise legal rights and assume obligations on her behalf.

Fiduciary law also empowers principals in situations where they lack the legal or practical capacity to designate a fiduciary to act on their behalf. For example, children generally lack legal capacity to assert their own legal rights, and they are unable to designate an adult to exercise these rights on their behalf.<sup>174</sup> Fiduciary law addresses this dilemma by providing legal mechanisms whereby adults (e.g., guardians) are assigned to serve as fiduciaries until children reach adulthood.<sup>175</sup> Consider also how fiduciary

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168. Cf. Robin Kar, *Contract as Empowerment*, 83 U. CHI. L. REV. 759, 761 (2016) (arguing that contract law “aims to empower people to use promises as tools to influence one another’s actions and thereby to meet a broad range of human needs and interests”).

169. RESTATEMENT (THIRD) OF AGENCY § 1.01, §§ 2.01–2.02 (AM. LAW INST. 2006).

170. See RESTATEMENT (THIRD) OF TRUSTS § 2 (AM. LAW INST. 2007) (defining a trust as a category of fiduciary relationships); *id.* § 17 (discussing the creation of testamentary trusts).

171. See *id.* § 28 (listing the purposes for which a charitable trust may be established as such).

172. See Note, *Incorporating the Republic: The Corporation in Antebellum Political Culture*, 102 HARV. L. REV. 1883, 1894 (1989) [hereinafter *Incorporating the Republic*] (quoting John Quincy Adams’s 1832 defense of the corporation as a “truly republican institution” that enabled broad participation in capitalist enterprise in a society where “[v]ery few, scarcely any, individuals had command of wealth and credit competent to the formation of [manufacturing] establishments” (quoting 8 CONG. DEB. app. at 84 (1832) (statement of John Quincy Adams))).

173. See, e.g., COLO. REV. STAT. § 15-14-202(1) (2017) (“A guardian may be appointed by will or other signed writing by a parent for any minor child the parent has or may have in the future.”).

174. See Frederic B. Rodgers, *Court-Appointed Counsel in Civil Cases*, 40 JUDGES’ J., Winter 2001, at 22, 23 (“Children lack legal capacity to sue and be sued, and courts have the power to appoint a guardian or next friend to defend their interests in civil suits.”).

175. See *id.* It may seem counterintuitive to characterize fiduciary law as “empowering” children, given that the law does not ordinarily require guardians to follow the choices of children under their care. Children would be disempowered indeed, however, if their guardians lacked the capacity to serve as fiduciary representatives to exercise their legal rights on the children’s behalf.

law responds when a ship runs aground, imperiling cargo that does not belong to the shipmaster. Although shipmasters do not ordinarily have contractual relationships with cargo owners, courts have held that shipmasters who are unable to communicate with cargo owners may sometimes sell the cargo to a third party, acting as an agent of necessity for the cargo owners, in order to protect the goods' value.<sup>176</sup> In such cases, fiduciary law empowers principals by ensuring that their legal rights can be exercised on their behalf even when they lack the legal or practical capacity to select their own fiduciary.

In other settings, fiduciary law empowers private parties by enabling them to benefit from the exercise of legal powers that they do not independently possess. For example, when multiple investors commit assets to a pooled investment fund, each retains an equitable interest in the profits generated by the fund, but no particular investor has the right to decide unilaterally how the fund will be distributed.<sup>177</sup> Accordingly, when an investment manager winds up a pooled fund and distributes assets, she exercises a power that none of the contributing investors can claim independently. Although the investment manager's authority to resolve investors' competing claims to pooled funds is called into existence by investors' mutual consent, it is not derived from investors' independent legal powers; instead, it is constituted and regulated by fiduciary law itself.<sup>178</sup>

Similarly, when parties appoint an arbitrator to resolve a dispute, the arbitrator exercises a legal power that neither party would have the right to exercise independently under the general principle that no private party is authorized to serve as judge and party to the same cause (*nemo iudex in sua causa*).<sup>179</sup> Like the investment manager for a pooled fund, an arbitrator's authority to resolve disputes is called into existence by the parties' common consent, but it involves the exercise of a power that private parties do not

176. See, e.g., *The "Gratitude"* (1801) 165 Eng. Rep. 450, 455–56; 3 C. Rob. 240, 255–58 (holding that a shipmaster may pledge cargo as collateral to finance the ship's repairs "in cases of instant and unforeseen and unprovided [sic] necessity," where "the character of agent [of the cargo's owner] . . . is forced upon [the shipmaster]"); *Australasian Steam Navigation Co. v Morse* [1872] 8 Moore PC (NSW) 482, 491–92 (Austl.) (holding same, provided the communication with the cargo owner is impossible); *China Pacific SA v. Food Corp. of India* [1981] 3 All ER 688 (HL) 693 (Lord Diplock) (appeal taken from AC) (Eng.); see generally CRIDDLE & FOX-DECENT, *supra* note 14, at 132–34 (discussing fiduciary duties in the context of emergencies).

177. See RESTATEMENT (THIRD) OF TRUSTS § 65(1) (AM. LAW INST. 2007) (providing for the termination of a trust if all beneficiaries consent); *id.* § 79 (providing that the trustee of a pooled investment has a duty to the beneficiaries of the trust that governs the trustee's investments, not a duty to any one particular investor).

178. See *id.* § 90 cmt. a (noting that trustees have a duty to "preserve the trust property . . . and to make it productive," but failing to enumerate duties to a particular investor).

179. See *Gutierrez de Martinez v. Lamagno*, 515 U.S. 417, 428 (1995) (characterizing this principle as "a mainstay of our system of government"); *Calder v. Bull*, 3 U.S. (3 Dall.) 386, 388 (1798) (opinion of Chase, J.) (identifying "certain vital principles in our free Republican governments," including the prohibition against "a law that makes a man a Judge in his own cause").

independently possess.<sup>180</sup> This power to arbitrate among the rivalrous claims of multiple beneficiaries is quintessentially fiduciary in nature.<sup>181</sup>

Fiduciary law thus reflects an implicit normative commitment to individual empowerment. By allowing principals to designate fiduciaries to act on their behalf, fiduciary law empowers beneficiaries to accomplish purposes that they could not achieve as easily—or could not achieve at all, legally or practically speaking—without a fiduciary’s assistance. This commitment to individual empowerment is consistent with republicanism’s respect for individual agency<sup>182</sup> as long as it does not compromise others’ equal freedom.<sup>183</sup>

Fiduciary law also empowers fiduciaries but in a very different way than it empowers principals. It empowers fiduciaries in the limited sense that they receive authorization to exercise legal rights that they would not otherwise be entitled to exercise in their personal capacity. Fiduciary law authorizes a fiduciary to exercise fiduciary power solely in an institutional or official capacity—as holder of an office that is constituted and regulated by law—for a prescribed, other-regarding purpose.<sup>184</sup> Fiduciary power is categorically different from principals’ power because fiduciaries are not free to pursue their own ends; a constitutive feature of fiduciary power is that the law permits its exercise only in a manner that is faithful to the fiduciary’s mandate and solicitous of beneficiaries’ legal and practical interests.<sup>185</sup> Fiduciary law thus confers power on fiduciaries to act in a manner that affects others’ legal

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180. See James Allsop, *The Authority of the Arbitrator*, 30 ARB. INT’L 639, 648 (2014) (describing the power of the arbitrator, which, while derived from the agreement of the parties, necessarily encompasses authority the parties themselves do not have, such as the power to determine the parties’ rights in the dispute).

181. See *Atkins v. Bert Bell/Pete Rozelle NFL Player Retirement Plan*, 694 F.3d 557, 569 (5th Cir. 2012) (explaining that “a trustee deadlock over [the Employment Retirement Income Security Act (ERISA)] eligibility matters . . . must be submitted to [an arbitrator as fiduciary]” (quoting *NLRB v. Amax Coal Co.*, 453 U.S. 322, 338 (1981)); U.S. DEP’T OF LABOR, ADVISORY OP. 79-66A, at 1–3 (Sept. 14, 1979) (concluding that an arbitrator who decides the question of a participant’s entitlement to ERISA plan benefits acts as a fiduciary); cf. Leib et al., *supra* note 17, at 718–19 (arguing that the judicial office should be understood as a public trust).

182. A commitment to individual empowerment is not unique to republicanism. This feature of fiduciary law is compatible with classical liberalism and a variety of other normative theories.

183. Republicanism thus supports liberty-reinforcing constraints on individual empowerment, including reasonable antitrust regulations. See *Incorporating the Republic*, *supra* note 172, at 1893–902 (discussing nineteenth-century debates over whether the corporation, “with its potential for dominant market power,” was congenial to republican freedom).

184. See CRIDDLE & FOX-DECENT, *supra* note 14, at 18–19 (discussing the institutional, purposive, and other-regarding characteristics of fiduciary power); Getzler, *supra* note 83, at 585 (observing that Chancellor King’s “idea that profit from office should be barred [in fiduciary relationships] can plausibly be connected to [his] experience battling [corruption of public offices]”).

185. See SHEPHERD, *supra* note 165, at 35 (defining fiduciary power as conditioned on using such power in the best interests of another).

and practical interests, while constituting that power juridically in a manner that formally rules out alien control.

2. *Emancipation.*—As a practical matter, of course, fiduciaries are creatures of flesh and blood and therefore susceptible like all humankind to the deadly sins of greed and sloth. Under republican theory, therefore, it is not enough for fiduciary law to prescribe legal rights and duties that affirm a universal right to freedom from domination in the abstract. To secure liberty in a practical sense, the law must also furnish appropriate causes of action and effective remedies to protect beneficiaries against a fiduciary’s self-dealing and waste.<sup>186</sup> Legal sanctions that deter fiduciaries from abusing trust may be particularly valuable as checks against domination. But perfect deterrence is not a prerequisite for republican liberty. A legal system can secure freedom from domination even if it does not prevent all abuses from occurring *ex ante*, as long as it supplies robust accountability mechanisms to defuse domination *ex post* by guaranteeing that fiduciaries are unable to exercise arbitrary control with impunity.<sup>187</sup>

Fiduciary duties emancipate principals by ensuring that their liberty is not compromised by fiduciary power. Whenever the law entrusts a party with power over others’ legal or practical interests, the duty of loyalty prevents this power from being held in a manner that engenders domination. A fiduciary does not dominate her principal if the law requires her to exercise entrusted power in a manner that tracks the principal’s “avowed or avowal-ready interests,” to borrow Pettit’s formulation.<sup>188</sup> A fiduciary must follow her principal’s “avowed interests,” as reflected in her express instructions, and she must act with reasonable diligence and prudence to achieve her principal’s “avowal-ready interests,” as reflected in her broader objectives and purposes.<sup>189</sup> Focusing on a principal’s “avowed or avowal-ready interests” in this manner respects a principal’s independent agency by requiring that exercises of fiduciary power be interpretable always as empowering a principal to accomplish her own purposes. The duty of loyalty thus safeguards a principal’s liberty by ensuring that she remains in a position of formal self-mastery with respect to her fiduciary’s exercise of entrusted power.

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186. See, e.g., CONAGLEN, *supra* note 5, at 254–68 (discussing judicial applications of fiduciary principles and theories for determining whether fiduciary duties should be recognized and enforced by the law).

187. See CRIDDLE & FOX-DECENT, *supra* note 14, at 271 (characterizing impunity as “domination institutionalized”).

188. Pettit, *supra* note 40, at 117.

189. See CONAGLEN, *supra* note 5, at 104 (noting that some view the core fiduciary duty as acting in the best interests of the beneficiary, under the tacit assumption that such interests may be either express or implicit).

Fiduciary duties also protect beneficiaries from domination. Absent the duty of loyalty, a fiduciary would have the capacity to subject beneficiaries' equitable interests to her own arbitrary control by exercising fiduciary power in a manner that was indifferent to these interests. Beneficiaries would therefore interact with their fiduciaries from an unequal position of vulnerability and subservience.<sup>190</sup> In appreciation of the fiduciary's dominating power, beneficiaries would be forced to maintain constant vigilance against the threat of fiduciary misconduct. They might feel the need to engage in self-abasement or self-censorship in order to remain within the trustee's good graces. Indeed, they might feel compelled to offer kickbacks or other material inducements as security against the risk of fiduciary self-dealing.<sup>191</sup> The duty of loyalty rescues beneficiaries from this position of abject vulnerability by arming them with legal claims that affirm their equitable interest in fiduciaries' fidelity to the principal's instructions and purposes.

Modern fiduciary law also safeguards fiduciaries from domination, ensuring that the requirement to pursue others' purposes and interests does not enslave fiduciaries to their principals and beneficiaries. Most fiduciary relationships today are established through a voluntary undertaking, with fiduciaries receiving handsome remuneration for services performed.<sup>192</sup> And fiduciaries are generally free to exit the relationship if they become dissatisfied with the terms under which they labor.<sup>193</sup> Thus, while fiduciary law demands that fiduciaries exercise fiduciary power exclusively for other-regarding purposes, it does not safeguard the liberty of principals and beneficiaries at the expense of fiduciaries' equal freedom.

Skeptics might object that the republican tradition's focus on domination—the mere capacity for arbitrary interference—devotes too little attention to a fiduciary's wrongful *exercise* of power and the material *harm* that may result from this exercise. The republican theory developed in this Article recognizes, however, that domination is not the only threat to freedom that justifies legal regulation; a fiduciary also wrongs her principal and

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190. See, e.g., Nat'l Westminster Bank PLC v. Morgan [1985] AC 686 (HL) 609 (Lord Scarman) (appeal taken from AC) (Eng.) (asserting that fiduciary relations arise where one party is subject to another's dominating influence).

191. See, e.g., Hylton v. Hylton (1754) 28 Eng. Rep. 349, 350; 2 Ves. Sen. 548, 548–49 (suggesting that if courts did not apply the no-conflict rule, trust beneficiaries might feel compelled to offer kickbacks to secure a smooth transfer of the estate).

192. See Talley, *supra* note 111, at 300 (observing that “no one is *required* to become a corporate fiduciary; she consents to do so voluntarily, and only then in exchange for compensation that makes entering such a relationship worthwhile”).

193. A court-ordered constructive trust is an exception to this rule, but this relationship generally functions as a “restitutionary proprietary remedy” rather than a free-standing fiduciary relationship. LAC Minerals Ltd. v. Int'l Corona Resources Ltd., [1989] 2 S.C.R. 574, 577–80 (Can.).

beneficiaries if she exercises entrusted power in a manner that is indifferent to their interests. In previous writings, Evan Fox-Decent and I have described the arbitrary exercise of fiduciary power as “instrumentalization,” and we have argued that the Kantian principle of noninstrumentalization complements the principle of nondomination in specifying the normative requirements of a republican legal order.<sup>194</sup> Both noninstrumentalization and nondomination are essential benchmarks for evaluating whether a legal system meets the normative requirements of a republican legal order. By ruling out a fiduciary’s formal capacity for arbitrary control and providing remedies responsive to the actual exercise of arbitrary control, fiduciary law satisfies both the principle of nondomination and the principle of noninstrumentalization.

Contrary to the classical liberal theory, however, fiduciary law’s formal structure is not devoted to protecting beneficiaries from material harm. A fiduciary who treats entrusted power as a means to her own ends wrongs her beneficiaries even if her actions do not harm their interests—for example, when an investment manager purchases highly profitable investments for a client, but, in the process, also receives undisclosed kickbacks without the client’s consent. Conversely, a fiduciary may harm her beneficiaries’ interests without committing any wrong—for example, when an investment manager selects prudent investments, but the investments unexpectedly lose value. Consistent with the republican theory, the fiduciary duty of loyalty prohibits fiduciaries from subjecting entrusted power to their own alien control; it does not fully insure beneficiaries’ interests against harm.

Republicanism thus clarifies the fiduciary relationship’s unique threat to liberty. What distinguishes fiduciary relationships from ordinary arm’s-length relationships is that a fiduciary receives power in “trust” (*fides*) for another.<sup>195</sup> The power entrusted to a fiduciary is, by definition, not her own; rather, she receives entrusted power in an official capacity on the condition that she exercise the powers associated with her office in a manner that is consistent with her purposive mandate. The fiduciary mandate circumscribes the outer limits of a fiduciary’s authority to hold and exercise entrusted power. Accordingly, an agent who treats fiduciary power as a means to advance her own ends dominates her principal by arbitrarily displacing the principal’s decisions concerning how her own legal rights and powers will be exercised. Similarly, a trustee who treats fiduciary power as a means to advance her own ends wrongs her beneficiaries by asserting alien control over their legal and practical interests. This corruption of the fiduciary office

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194. CRIDDLE & FOX-DECENT, *supra* note 14, at 78.

195. See Lyman P.Q. Johnson, *Faith and Faithfulness in Corporate Theory*, 56 CATH. U. L. REV. 1, 28 (2006) (“The Latin root of fiduciary—‘fides’—means ‘faith,’ as in trust, reliability, or faithfulness . . .”).



constitutes a distinctive form of domination—the betrayal of trust—that justifies fiduciary law’s distinctive duty of loyalty with its associated remedies.

The idea that “betrayal of trust” lies at the heart of fiduciary loyalty resonates with the familiar refrain in American jurisprudence that fiduciary relationships are distinguished by “trust and confidence.”<sup>196</sup> All fiduciary relationships involve trust and confidence in the strictly formal, legal sense that fiduciaries exercise powers that are entrusted to exercise. Parties to fiduciary relationships may also subjectively trust one another to meet their respective obligations,<sup>197</sup> but “the fact that one person subjectively trusted another—is neither necessary for nor conclusive of the existence of a fiduciary relationship.”<sup>198</sup> In determining whether or not a relationship is fiduciary, courts do not ask whether the parties actually trust one another in a subjective sense; instead, they simply ask whether a party has received power over another’s legal or practical interests in “trust and confidence”—i.e., on the condition that the power be exercised exclusively for the other’s benefit.<sup>199</sup> Within such relationships, the fiduciary duty of loyalty ensures that fiduciaries cannot expose their principal and beneficiaries to domination by subjecting entrusted power to their own alien control.

Some scholars argue that the primary purpose of fiduciary law is to inculcate social norms, encouraging fiduciaries to practice loyalty and care out of a sense of moral obligation.<sup>200</sup> The implicit corollary of this view is

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196. *E.g.*, *Advocare Int’l LP v. Horizon Labs., Inc.*, 524 F.3d 679, 695–96 (5th Cir. 2008) (noting that the court below had instructed the jury that “a fiduciary duty may arise informally from a ‘relationship of trust and confidence’”); *Amendola v. Bayer*, 907 F.2d 760, 763 (7th Cir. 1990) (observing that even in the absence of a formal fiduciary relationship, a constructive trust may be recognized by the court where a relationship of “trust and confidence” exists); *see also* *Gerdes v. Estate of Cush*, 953 F.2d 201, 205 (5th Cir. 1992) (characterizing “the position of trust” as the fiduciary relationship’s distinguishing feature).

197. *See* *Harding*, *supra* note 165, at 84–85 (emphasizing this feature of fiduciary relationships).

198. *Hosp. Prods. Ltd. v U.S. Surgical Corp.* (1984) 156 CLR 41, ¶ 69 (Austl.). Parties to relational contracts often exercise trust in one another, yet a fiduciary relationship is not triggered unless one of the parties has conferred power on the other on the condition that the power be held and exercised exclusively for other-regarding purposes. *See id.* (using the example of the contractor–subcontractor relationship to illustrate this point).

199. *See* *Evans v. Taco Bell Corp.*, 2005 WL 2333841, at \*12 (D.N.H. Sept. 23, 2005) (explaining that “‘confidence’ in this context does not equate with simple reliance on another to perform a bargained-for service, but denotes a ‘special confidence reposed in one who . . . is bound to act in good faith and with due regard to the interests of the one reposing the confidence’” (quoting *Lash v. Cheshire Cty. Sav. Bank*, 474 A.2d 980, 982 (1984))).

200. *See, e.g.*, Melvin A. Eisenberg, *Corporate Law and Social Norms*, 99 COLUM. L. REV. 1253, 1266 (1999) (noting that “[a]lthough the regulatory function of these legal rules is important, the social norm of loyalty that the legal rules support and define is critical to the efficient operation of the duty of loyalty”); Lyman Johnson, *Counter-Narrative in Corporate Law: Saints and Sinners, Apostles and Epistles*, 2009 MICH. ST. L. REV. 847, 857 (identifying fiduciary duties as “broad standards,” which are “all-encompassing” as moral obligations “pervasively to act loyally, in good

that fiduciary law could be discarded in a world where all fiduciaries could be trusted to refrain from opportunism.<sup>201</sup> The republican theory challenges this view. Fiduciary virtue might be desirable, but it is not strictly necessary to preserve freedom from domination. As long as legal norms and institutions ensure that a fiduciary cannot engage in opportunism with impunity, a fiduciary's motivations for loyal or disloyal behavior are legally and practically irrelevant.<sup>202</sup> Nor is a fiduciary's commitment to social norms sufficient to secure liberty. The classic examples of the virtuous king and benevolent slave master illustrate that domination can be present even if a power holder's intentions and actions are above reproach.<sup>203</sup> Even if all fiduciaries were angels, fiduciary law would still be necessary as a formal matter to affirm that loyalty and care are *legal* obligations and not merely social conventions that depend for their fulfillment on a fiduciary's unilateral discretion, personal morality, or good will.

Republicanism thus offers a robust interpretive account of the normative basis for fiduciary loyalty. Under the republican theory, the duty of loyalty is not merely a subset of contractual obligations or property rules, as some scholars have suggested.<sup>204</sup> It is not a prophylactic requirement intended to promote the performance of non-fiduciary obligations.<sup>205</sup> Nor is its primary purpose to lower transaction costs in private bargaining,<sup>206</sup> provide a framework for optimal deterrence,<sup>207</sup> or promote voluntary adherence to social norms.<sup>208</sup> Instead, the requirements of fiduciary loyalty serve primarily

faith, and with due care"); Edward B. Rock, *Saints and Sinners: How Does Delaware Corporate Law Work?*, 44 UCLA L. REV. 1009, 1016 (1997) (comparing Delaware courts' opinions on fiduciary duties to sermons and parables which serve as a form of instruction to practitioners).

201. See Eisenberg, *supra* note 200, at 1274 ("[I]f all corporate actors fully internalized the social norm of loyalty and gave full effect to that norm, the costs of both legal sanctions and monitoring and bonding systems would be unnecessary . . .").

202. See SELLERS, *supra* note 39, at 67 (noting John Adams's observation that in a republican system liberty may flourish "even among highwaymen").

203. See Pettit, *supra* note 43, at 44 ("From the earliest Roman days, the republican tradition insisted that being under the power of a master—in *potestate domini*—meant being un-free, even if that master was quite benevolent and allowed you a great deal of leeway.").

204. See, e.g., Avihay Dorfman, *On Trust and Transubstantiation: Mitigating the Excesses of Ownership*, in PHILOSOPHICAL FOUNDATIONS, *supra* note 6, at 339 (discussing the duty of loyalty as arising out of property rules); Easterbrook & Fischel, *supra* note 7, at 426 (arguing that fiduciary loyalty is a subset of contract obligations); Langbein, *supra* note 7, at 657–59 (contending that fiduciary loyalty is fundamentally contractarian); cf. Smith, *supra* note 63, at 1402 (asserting that fiduciary loyalty is based on the respect of a "critical resource belonging to the beneficiary").

205. See CONAGLEN, *supra* note 5, at 4 (articulating a theory that fiduciary duties are "designed to assist with ensuring proper performance of non-fiduciary duties").

206. See, e.g., Butler & Ribstein, *supra* note 26, at 28–30 (describing how fiduciary obligations reduce the need for contracting parties to negotiate over remote contingencies).

207. See, e.g., Cooter & Freedman, *supra* note 4, at 1052 (analyzing deterrence problems in the context of fiduciary obligations).

208. See, e.g., Rock, *supra* note 200, at 1016 (describing fiduciary duties as standards meant to influence the social behavior of directors, officers, and lawyers).

to emancipate private parties by defining and regulating fiduciary power in a manner that formally precludes domination from corrupting the fiduciary relationship.

### B. *Identifying Fiduciary Relationships*

Private law theorists have struggled in the past to devise principled criteria for distinguishing fiduciary relationships from non-fiduciary relationships.<sup>209</sup> Courts have held that certain categories of private relationships always trigger fiduciary duties, including agent–principal, trustee–beneficiary, guardian–ward, director/officer–corporation, attorney–client, and doctor–patient.<sup>210</sup> Other categories of private relationships, such as employer–employee, are sometimes held to trigger fiduciary duties, but sometimes not, depending upon case-specific features of the relationships between specific parties.<sup>211</sup> Legislatures and courts have not always been clear and consistent, however, in their efforts to explain which relationships qualify as “fiduciary.” As a result, fiduciary law’s borders remain theoretically and doctrinally nebulous.

In recent years, legal scholars have proposed a variety of tests for distinguishing fiduciary relationships from non-fiduciary relationships. Some have argued that fiduciary duties are a product of contractual agreement or voluntary undertaking.<sup>212</sup> As discussed previously, however, the voluntarist theory struggles to account for fiduciary relationships that arise without parties’ express or implied consent. Rather than consider the parties’ actual intentions, courts tend to ascribe fiduciary duties to specific relationships based on whether one of the parties has reposed special “trust and confidence” in the other.<sup>213</sup> Where this feature is present, courts commonly hold that the duty of loyalty applies even if the party who holds entrusted power persistently rejects the implication that she bears fiduciary

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209. See, e.g., Deborah A. DeMott, *Beyond Metaphor: An Analysis of Fiduciary Obligation*, 1988 DUKE L.J. 879, 923–24 (concluding that fiduciary relationships lack a common theoretical basis). See generally Miller, *supra* note 2 (reviewing theories based on contract, property, and vulnerability, and offering a legal-formalist alternative).

210. See DeMott, *supra* note 164, at 1258 (observing that “fiduciary-duty analysis usually proceeds categorically”).

211. See *id.* (explaining that assessments of ad hoc fiduciary status in the employment context depend “on fact-specific inquiries”); Matthew T. Bodie, *Employment as Fiduciary Relationship*, 104 GEO. L.J. (forthcoming 2017) (analyzing employer fiduciary duties based on the specific facts of an employment relationship).

212. E.g., Easterbrook & Fischel, *supra* note 7, at 427 (concluding that a fiduciary relationship “is a contractual one”); James Edelman, *When Do Fiduciary Duties Arise?*, 126 L.Q. REV. 302, 310–13 (2010) (arguing that voluntary undertaking is a necessary condition for fiduciary obligation); Hansmann & Mattei, *supra* note 7, at 447–49 (arguing that fiduciary duties are default contractual rules).

213. See sources cited *supra* note 196.

duties.<sup>214</sup> While classical liberals might welcome a rule that would make consent a prerequisite for the assumption of fiduciary duties, this approach has not gained traction in the courts.

Another theory of the fiduciary relationship, advanced most forcefully by Paul Miller, posits that fiduciary relationships share a distinctive juridical structure.<sup>215</sup> In Miller's view, what makes fiduciary relationships special is the fiduciary's discretionary power over another party's legally protected rights.<sup>216</sup> Because the legal rights that a fiduciary exercises belong to the beneficiary rather than fiduciary, "[t]he fiduciary may not treat fiduciary power as an unclaimed means or as a personal means."<sup>217</sup> Instead, the fiduciary must treat her beneficiary always as entitled to all benefits generated by her exercise of the entrusted power.

Miller's juridical theory offers a powerful framework for identifying some fiduciary relationships, but it struggles to make sense of other relationships that are universally accepted as fiduciary. As Miller's theory predicts, many fiduciaries do hold discretionary power to exercise another's legal rights, including trustees, corporate officers, guardians, and investment managers.<sup>218</sup> In these relationships, it is certainly plausible to think that the fiduciary duty of loyalty reflects the principle that beneficiaries are legally entitled to the full fruits of any exercise of their own rights. Returning to examples discussed previously, however, it is hard to make the case that an arbitrator exercises the parties' respective legal rights when she renders a judgment or that an investment manager exercises investors' legal rights when she winds up a pooled fund, although in both contexts the fiduciary's actions may limit her beneficiaries' subsequent choices in ways that impact their legal interests.<sup>219</sup> Equally problematic for Miller's theory, courts have also held that advisers may qualify as fiduciaries even if they lack formal

214. See SHEPHERD, *supra* note 165, at 66 (observing that when "fiduciary duties are attached by operation of law," they apply even "in the face of express rejection of those very same duties by the fiduciary").

215. See Miller, *supra* note 163, at 69–75.

216. Miller uses the term "[p]ersonal legal capacity" rather than rights, but the message is essentially the same. *Id.* at 71.

217. Miller, *supra* note 2, at 1021.

218. See Miller, *supra* note 163, at 71 (observing that fiduciaries may be entrusted with power, *inter alia*, to "enter into legally binding relationships for another . . . ; acquire, invest, use, administer, or alienate property owned by or held for another; . . . to make decisions relating to the health and personal welfare of another; [and] to institute legal proceedings to enforce or seek vindication of legal rights for another").

219. Miller might respond that a fiduciary in these contexts wields rights that beneficiaries possess collectively, even though they cannot claim these rights individually. But this response begs the question: why can groups of beneficiaries claim rights that their members do not possess individually?

authority to exercise their advisees' legal rights.<sup>220</sup> Thus, while Miller may be correct that a person is a fiduciary if she has discretionary power to exercise another's legal rights, it does not necessarily follow that a person *must* hold such authority to qualify as a fiduciary.

Some other scholars and judges have argued that what distinguishes fiduciary relationships from other relationships is a fiduciary's discretionary power over beneficiaries' interests, a power which renders beneficiaries uniquely vulnerable to opportunism.<sup>221</sup> This emphasis on power, vulnerability, and opportunism resonates with fiduciary law's historical roots in equity.<sup>222</sup> The trouble with basing fiduciary duties on such vague concepts as power, vulnerability, and the threat of opportunism, however, is that these factors are present in *all* private relationships. Hence, some further limiting principle is needed to prevent the fiduciary concept from swallowing all of private law. To fill this void, we need a theory of the fiduciary relationship that is capable of justifying fiduciary duties without imposing these duties indiscriminately as a one-size-fits-all solution to every threat of opportunism that arises in the private sphere.

The republican theory advanced in this Article furnishes a simple definition of the fiduciary relationship that is distinct from the contractarian, legal-formalist, and generic-opportunism accounts. Under the republican theory, *a party is a fiduciary if she has been entrusted with power over another party's legal or practical interests*. For the sake of clarity, it may be helpful to break this definition down into its various component parts to allow for closer inspection.

*1. Entrustment.*—A defining feature of any fiduciary relationship is entrusted power.<sup>223</sup> Power is “entrusted” if it does not belong to a party by right but is nonetheless committed to her administration. Power may be entrusted to a fiduciary by a voluntary assignment from a principal (e.g., attorney), by judicial appointment (e.g., receivership), or by the independent operation of law (e.g., agent of necessity). The power may belong by right

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220. See, e.g., *SEC v. Capital Gains Research Bureau, Inc.*, 375 U.S. 180, 191–92 (1963) (finding a fiduciary relationship between investment advisers and clients).

221. See, e.g., *Frame v. Smith*, [1987] 2 S.C.R. 99, 102 (Can.) (Wilson, J., dissenting) (asserting that indicia of a fiduciary relationship include: “(1) The fiduciary has scope for the exercise of some discretion or power. (2) The fiduciary can unilaterally exercise that power or discretion so as to affect the beneficiary’s legal or practical interests. (3) The beneficiary is peculiarly vulnerable to or at the mercy of the fiduciary holding the discretion or power.”); DeMott, *supra* note 164, at 1259 (“Fiduciary relationships stem from or create disparities of power and information, such that the relationship’s beneficiary is or becomes vulnerable to the [fiduciary].”).

222. See, e.g., Flannigan, *supra* note 26, at 393 (“The conventional function of fiduciary regulation is to control opportunism in limited access arrangements. That function has never been disputed.”); Smith, *supra* note 22, at 261 (“Equity as anti-opportunism explains not only the general tenor, but the overall structure and particular features of fiduciary law.”).

223. See FRANKEL, *supra* note 1, at 4–5 (emphasizing entrustment as a distinguishing feature of fiduciary relationships).

to the principal (e.g., agency) or to a beneficiary (e.g., guardianship), or it may be called into existence by the independent operation of law (e.g., arbitration). Regardless of the mechanism that triggers the entrustment of fiduciary power, the critical feature of entrusted power is held *in trust*; it is not committed to the unilateral discretion of the one who holds it. Entrustment is a necessary feature of fiduciary relationships under the republican theory because it facilitates the distinctive form of domination that fiduciary loyalty is designed to neutralize: a party's capacity to betray trust by exercising alien control over entrusted power.

2. *Power.*—Fiduciary power is a form of authority. It may be de jure or de facto. A fiduciary holds de jure power if her mandate authorizes her to exercise another's legal rights or powers (e.g., agency) or other powers conferred by law (e.g., arbitration). A fiduciary holds de facto power if she is in a position, as a practical matter, to dictate how another's legal rights or powers will be exercised (e.g., investment adviser). Fiduciary power may be limited to purely nondiscretionary ministerial tasks, or it may entail authorization to make discretionary judgments. As this Article will explain further below, bringing nondiscretionary power within the ambit of fiduciary loyalty is important under the republican theory because fiduciary law's distinctive remedies are necessary to remedy the domination entailed in a fiduciary's infidelity to a nondiscretionary mandate.<sup>224</sup>

3. *Over Another Party's Legal or Practical Interests.*—A relationship is fiduciary only if a person holds power relative to another person's legal or practical interests. Under the republican theory, it is a fiduciary's empowered position relative to her principal and beneficiaries that raises the threat of alien control.<sup>225</sup> A fiduciary's power to set aside the choices of her principal and disregard the legal and practical interests of her beneficiaries would constitute domination, but for fiduciary law's emancipating intervention.<sup>226</sup>

4. *Some Applications.*—The republican theory's definition of the fiduciary relationship elucidates the scope of fiduciary law's domain in a variety of respects.

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224. See *infra* section III(C)(2).

225. Frankel asserts:

The [fiduciary] relation may expose the entrustor to risk even if he is sophisticated, informed, and able to bargain effectively. Rather, the entrustor's vulnerability stems from the *structure* and *nature* of the fiduciary relation. The delegated power that enables the fiduciary to benefit the entrustor also enables him to injure the entrustor, because the purpose for which the fiduciary is allowed to use his delegated power is narrower than the purposes for which he is capable of using that power.

Frankel, *supra* note 32, at 810.

226. See *Nat'l Westminster Bank PLC v. Morgan* [1985] AC 686 (HL) 709 (Lord Scarman) (appeal taken from AC) (Eng.) (asserting that fiduciary relations arise where one party is subject to another's dominating influence).

The republican theory confirms the conventional wisdom that some categories of private relationships always satisfy the republican theory's criteria. For example, all trustees are entrusted with power over others' legal or practical interests. Although some trustees hold more discretionary power than others, all bear a fiduciary duty of loyalty because the office of trustee, by definition, involves the entrustment of power over others' legal or practical interests.<sup>227</sup> Other fiduciary relationships that always satisfy these criteria include agent–principal, officer/director–corporation, partner–partner, guardian–ward, and attorney–client.<sup>228</sup> Because these relationships always meet the republican theory's criteria, they are suitable for categorical treatment as “status-based fiduciary relationships” under the republican theory.<sup>229</sup>

The republican theory also explains why generations of republican judges, politicians, and political theorists have confidently asserted that public officials and institutions are fiduciaries.<sup>230</sup> Like fiduciaries under private law, public officials and institutions are entrusted with power over the legal and practical interests of their people.<sup>231</sup> Consequently, they bear fiduciary obligations to exercise their entrusted power in a manner that satisfies the requirements of fiduciary loyalty.

In addition, the republican theory supports recognizing investment advisers as fiduciaries for their clients. Formally speaking, many investment advisers are not legally authorized to choose investments for their clients.<sup>232</sup> Nonetheless, courts have held that investment advisers are fiduciaries because they hold themselves out to their clients as experts who will act in clients' best interests, thereby inducing their clients to entrust them with responsibility to assist them in an official advisory capacity.<sup>233</sup> This line of cases is difficult to square with theories of the fiduciary relationship that focus exclusively on a fiduciary's exercise of de jure authority,<sup>234</sup> but they

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227. See *Trustee*, BLACK'S LAW DICTIONARY (10th ed. 2014) (defining “trustee” as “[s]omeone who stands in a fiduciary or confidential relation to another; esp., one who, having legal title to property, holds it in trust for the benefit of another and owes a fiduciary duty to that beneficiary”).

228. See Evan J. Criddle & Evan Fox-Decent, *A Fiduciary Theory of Jus Cogens*, 34 YALE J. INT'L L. 331, 349 (2009) (listing and detailing different types of fiduciary relationships).

229. Paul B. Miller, *A Theory of Fiduciary Liability*, 56 MCGILL L.J. 235, 241–42 (2011).

230. See sources cited *supra* notes 15–16.

231. See generally CRIDDLE & FOX-DECENT, *supra* note 14 (covering the fiduciary duty of public officials under international law); FOX-DECENT, *supra* note 17.

232. Arthur B. Laby, *Advisers as Fiduciaries 1* (unpublished manuscript) (on file with author).

233. See, e.g., *SEC v. Capital Gains Research Bureau, Inc.*, 375 U.S. 180, 191–94 (1963) (describing the fiduciary relationship between investment advisers and clients and confirming Congress's designation of investment advisers as fiduciaries).

234. See, e.g., *Hodgkinson v. Simms*, [1994] 3 S.C.R. 377, 386 (Can.) (Sopinka, McLachlin & Major, JJ., dissenting) (arguing that an investment adviser is not a fiduciary because the advisee formally “retains the power and ability to make his or her own decisions”).

harmonize easily with the republican theory's insight that fiduciary law is equally concerned with domination that arises in relationships involving de facto power. Although an investment adviser's client retains formal control over her investment decisions, the investment adviser receives entrusted de facto power to guide and shape those decisions.<sup>235</sup> Under the republican theory, therefore, the investment adviser–advisee relationship triggers fiduciary obligations to provide “disinterested” advice and receive informed consent to any conflicted transactions.<sup>236</sup>

The republican theory thus explains why the current arguments for setting aside DOL's Fiduciary Rule are unpersuasive.<sup>237</sup> Under the republican theory, fiduciary duties apply to retirement-investment advisers not for the purpose of achieving optimal deterrence of harm (as reflected in a conventional cost–benefit analysis)<sup>238</sup> but rather to neutralize the domination that would arise if investment advisers had the capacity to wield alien control over their clients' legal and practical interests. Fiduciary law's traditional no-conflict and no-profit rules are strictly necessary, under republican legal theory, to prevent domination from corrupting adviser relationships that are premised on trust and confidence.<sup>239</sup>

Some fiduciaries exercise a combination of de jure and de facto power over their beneficiaries' interests. For example, when a patient authorizes a surgeon to operate on her body, making discretionary decisions as the operation unfolds, the surgeon exercises de jure power entrusted by the patient herself. The surgeon therefore assumes fiduciary obligations to honor the patient's instructions and purposes, act with solicitude toward the patient's avowed or avowal-ready interests, and exercise the care and skill expected of members of her profession. Even before surgery begins, however, the surgeon is a fiduciary for her patient when she provides advice on possible treatment options. Although the surgeon–adviser does not wield formal control over her patient's choices, the structure of the advisement relationship is one in which the patient entrusts the surgeon with de facto

235. See, e.g., *Burdett v. Miller*, 957 F.2d 1375, 1381 (7th Cir. 1992) (explaining a fiduciary relationship arises when “one person has reposed trust and confidence in another who thereby gains influence and superiority over the other,” and that such a relationship is seen when “the agent has . . . expert knowledge the deployment of which the principal cannot monitor” (quoting *Amendola v. Bayer*, 907 F.2d 760, 763 (7th Cir. 1990))).

236. *Capital Gains*, 375 U.S. at 188–92.

237. See *supra* notes 153–57 and accompanying text.

238. This is not to say, however, that the Fiduciary Rule cannot survive cost–benefit analysis. See *Chamber of Commerce v. Hugler*, No. 16-cv-1476, 2017 WL514424, at \*32–35 (N.D. Tex. Feb. 8, 2017) (concluding that DOL's assessment of the Fiduciary Rule's costs and benefits was reasonable); *Fiduciary Rule*, *supra* note 148, at 20,949–52, 20,952 tbl.1 (explaining how the Fiduciary Rule “will mitigate conflicts, support consumer choice, and deliver substantial gains for retirement investors and economic benefits that more than justify its costs”).

239. The Fiduciary Rule exempts investment advice that is merely incidental to certain arm's-length transactions. *Fiduciary Rule*, *supra* note 148, at 20,948.



power to shape and constrain her choices regarding her own medical care. The surgeon is a fiduciary for her patient, therefore, regardless of the fact that the patient retains both the formal right and the practical capacity to reject her advice. Focusing on the threat of arbitrary control in this manner explains not only when and how fiduciary duties apply to physicians but also to other relationships such as attorney–client that combine de jure powers with the provision of professional advice.

An increasingly important type of de facto power that may generate fiduciary duties is access to confidential information.<sup>240</sup> Private parties often entrust confidential information to a fiduciary within the context of a broader fiduciary relationship—for example, when a criminal defendant shares inculpatory information with her defense attorney or a patient allows a physician to collect sensitive data concerning her physical or emotional health. When attorneys, physicians, counselors, and clerics accept confidential information, they are entrusted with de facto power over the practical interests of the party who shares the information, with the expectation that they will use the information exclusively for the benefit of the sharing party.<sup>241</sup> As such, these relationships of trust and confidence activate the fiduciary duty of loyalty, requiring the recipient to use confidential information solely to advance her beneficiaries’ avowed or avowal-ready interests.<sup>242</sup> Conversely, when parties share confidential information in contexts that do not involve the expectation that the recipient will use the information to promote the other’s best interests (e.g., sharing confidential business data during arm’s-length merger negotiations), fiduciary duties do not apply.<sup>243</sup>

Fiduciary relationships formed solely by the entrustment of power over confidential information are an example of what courts and commentators

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240. See Brooks, *supra* note 26, at 239–40 (describing “information fiduciaries” as having both an affirmative duty to collect and use personal information as well as a duty to observe confidentiality standards). See generally Jack M. Balkin, Lecture, *Information Fiduciaries and the First Amendment*, 49 U.C. DAVIS L. REV. 1183 (2016) (discussing the tension between “personal privacy in the digital age” and companies’ interest in collecting, analyzing, and distributing customers’ personal information).

241. See, e.g., DeMott, *supra* note 209, at 882 (“[A] fiduciary’s duties go beyond mere fairness and honesty; they oblige him to act to further the beneficiary’s best interests.”); Smith, *supra* note 63, at 1402, 1441 (explaining that “fiduciary relationships form when one party . . . acts on behalf of another party . . . with respect to a *critical resource* belonging to the [second party],” for example, confidential information in doctor–patient, attorney–client, and clergy–parishioner relationships).

242. See RESTATEMENT (THIRD) OF THE LAW GOVERNING LAWYERS §§ 16, 49, 60 (AM. LAW INST. 2000) (discussing lawyers’ fiduciary duties to keep confidences); MARK A. HALL ET AL., MEDICAL LIABILITY AND TREATMENT RELATIONSHIPS 169–97 (3d ed. 2013) (discussing the duty of patient confidentiality).

243. See, e.g., *Dirks v. SEC*, 463 U.S. 646, 662 n.22 (1983) (citing with approval *Walton v. Morgan Stanley & Co.*, 623 F.2d 796, 798–99 (2d Cir. 1980) (holding that the possession of confidential information within the context of an arm’s-length merger negotiation is not sufficient to generate a fiduciary relationship and that liability would not attach in the event of its disclosure)).

have sometimes described as “ad hoc”<sup>244</sup> or “informal”<sup>245</sup> fiduciary relationships. Ad hoc fiduciary relationships arise when a particular relationship does not fall within a status-based category of fiduciary relationships (e.g., agency, trust) but nonetheless qualifies for the duty of loyalty based on features specific to the relationship.<sup>246</sup> The republican theory suggests that courts should identify ad hoc fiduciary relationships by asking a simple question: does a party hold entrusted power over another’s legal or practical interests?

This test confirms current jurisprudence in a variety of respects. Consistent with established case law, the republican theory affirms that used car dealers are not ordinarily fiduciaries for their customers,<sup>247</sup> cigarette manufacturers are not ordinarily fiduciaries for their consumers,<sup>248</sup> and restauranteurs are not ordinarily fiduciaries for their patrons.<sup>249</sup> Although each of these relationships involves significant information asymmetries, generating a risk of opportunism, the relationships are all presumptively arm’s-length; none by definition involves an entrustment of power from one party to another to be exercised under a purposive and other-regarding mandate.<sup>250</sup> Consequently, these relationships do not ordinarily render either party vulnerable to the specific type of opportunism that triggers fiduciary duties and remedies. The injuries that arise within these relationships can be remedied, instead, through other regimes such as contract law, tort law, property law, and criminal law.<sup>251</sup>

244. *E.g.*, *Galambos v. Perez*, [2009] 3 S.C.R. 247, 276 (Can.); *DeMott*, *supra* note 164, at 1261.

245. *E.g.*, *Advocare Int’l, LP v. Horizon Labs., Inc.*, 524 F.3d 679, 695 (5th Cir. 2008).

246. *See, e.g.*, *Burdett v. Miller*, 957 F.2d 1375, 1381 (7th Cir. 1992) (“[F]iduciary duties are sometimes imposed on an ad hoc basis . . . [when] a person solicits another to trust him in matters in which he represents himself to be expert as well as trustworthy and the other is not expert and accepts the offer and reposes complete trust in him . . . .” (citations omitted)).

247. *Cf. Guenther v. Snap-On Tools Corp.*, No. 90 C 4436, 1995 WL 137061, at \*2–4, \*9 (N.D. Ill. Mar. 28, 1995) (“While the law recognizes certain relationships . . . as being fiduciary, the relationship between franchisor and franchisee is not among them.”), *vacated in part* by 1996 WL 84182 (N.D. Ill. Feb. 22, 1996).

248. *See Burton v. R.J. Reynolds Tobacco Co.*, 397 F.3d 906, 911–13 (10th Cir. 2005) (concluding that “ordinary transactions for the sale of cigarettes do not, as a matter of Kansas law, create fiduciary relationships”).

249. *See Evans v. Taco Bell Corp.*, No. Civ. 04CV103JD, 2005 WL 2333841, at \*13 (D.N.H. Sept. 23, 2005) (concluding it is “obvious” that no fiduciary relationship exists between fast-food restaurants and their customers).

250. *See, e.g.*, *Carey Elec. Contracting, Inc. v. First Nat’l Bank of Elgin*, 392 N.E.2d 759, 763 (Ill. App. Ct. 1979) (“Normal trust between friends or businesses, plus a slightly dominant business position, do not operate to turn a formal, contractual relationship into a confidential or fiduciary relationship.”).

251. *See, e.g.*, *Engle v. Ligett Group, Inc.*, 945 So. 2d 1246, 1276–77 (Fla. 2006) (denying class certification to a large group of tobacco plaintiffs, but allowing the individual plaintiffs to proceed with suit based on injuries resulting from the use of tobacco products); *Taco Bell Corp.*, 2005 WL 2333841, at \*5–12 (discussing the application of negligence and strict liability causes of action to

Harder cases for the republican theory include mechanic–client and contractor–homeowner—i.e., relationships in which a property owner commits their property to another’s care with the expectation that the latter will improve the property for the owner’s benefit. Courts have concluded that auto mechanics and home contractors are not ordinarily fiduciaries for their clients because their services “occasion no fiduciary-like trust or equivalent reposing of faith.”<sup>252</sup> Some commentators have questioned the accuracy and coherency of this conclusion, arguing that clients do, in fact, entrust auto mechanics and home contractors with de jure and de facto power over their property interests, much as patients entrust physicians with de jure and de facto power over their bodies.<sup>253</sup> Although this Article does not afford the space necessary to resolve this debate definitively, the republican theory suggests that auto mechanics and home contractors qualify as fiduciaries only if these relationships are conditioned, in actual practice, on the understanding that the service providers receive authority *in trust* for their clients’ exclusive benefit. If property owners do not “entrust” their property to mechanics and contractors in this robust sense, the fiduciary duty of loyalty does not apply.

### C. *The Requirements of Fiduciary Loyalty*

Fiduciary relationships trigger a number of legal duties, including the duty of care, the duty to keep and render accounts, and the duty to furnish critical information,<sup>254</sup> but the heart of fiduciary law is its distinctive duty of loyalty. Despite its centrality to the theory and practice of fiduciary law, the concept of fiduciary “loyalty” remains ambiguous and contested. As Andrew Gold has demonstrated, courts have employed a variety of different conceptions of fiduciary loyalty, including honoring a hypothetical bargain, fidelity to the instructions and purposes, affirmative devotion to

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injuries the plaintiff allegedly suffered from consuming food prepared by a Taco Bell employee with Hepatitis A); *United States v. Sullivan*, 498 F.2d 146, 149–50 (1st Cir. 1974) (upholding the embezzlement conviction of a union employee who “possessed [a] fiduciary obligation with respect to union funds and assets”); Karl A. Boedecker & Fred W. Morgan, *Strict Liability for Sellers of Used Products: A Conceptual Rationale and Current Status*, 12 J. PUB. POL’Y & MARKETING 178, 179–84 (1993) (reviewing cases involving strict liability claims for sales of used cars and discussing the rationales behind the holdings).

252. *Thompson v. Wis. Cty. Mut. Ins. Corp.*, No. 95-3107-FT, 1996 WL 330363, at \*1 (Wis. Ct. App. June 18, 1996) (per curiam); see also *Guenther*, 1995 WL 137061, at \*9 (rejecting the idea in dicta that “disparity of knowledge . . . would make an auto mechanic or home-repair contractor the fiduciary of his less knowledgeable customer”). But see *Council on Am.-Islamic Relations Action Network, Inc. v. Gaubatz*, 31 F. Supp. 3d 237, 257–61 (D.D.C. 2014) (holding that if an individual obtained an internship with an organization in order to take compromising video of the organization, the individual would owe a fiduciary duty of confidentiality if he “understood himself to be bound by and violating a duty of confidentiality and non-disclosure”).

253. See, e.g., *Smith*, *supra* note 5, at 227–28.

254. See RESTATEMENT (THIRD) OF TRUSTS §§ 76–84 (AM. LAW INST. 2007) (enumerating and discussing the specific duties owed by a trustee to the beneficiaries of the trust).

beneficiaries' interests, fairness and evenhandedness, and the avoidance of conflicts.<sup>255</sup> Taking into account the many fields where the duty of loyalty applies and the powerful remedies available for its breach, it is no great exaggeration to suggest that clarifying the requirements of fiduciary loyalty ranks among the most important challenges for private law theory today.

The republican theory of fiduciary law offers new tools for addressing this challenge. By grounding fiduciary loyalty in freedom from domination, the republican theory helps to explain and justify the duty of loyalty's traditional requirements of fidelity to instructions and purposes, affirmative devotion to beneficiaries' interests, avoidance of conflicts of interest, and fair and evenhanded treatment of beneficiaries.<sup>256</sup> The republican theory thus supports the conventional American view that the duty of loyalty has both proscriptive and prescriptive dimensions,<sup>257</sup> and it calls into question recent efforts to dismantle the categorical no-conflict and no-profit rules in favor of flexible presumptions and standards that reflect the normative commitments of classical liberalism.

*1. Fidelity to Instructions and Purposes.*—Consider first the suggestion that the duty of loyalty requires a fiduciary to “be true” to her principal's instructions and purposes.<sup>258</sup> According to the republican theory, a fiduciary may exercise entrusted power only in a manner that is consistent with the instructions and purposes enshrined in her official mandate.<sup>259</sup> To safeguard principals and beneficiaries from domination, the fiduciary must respect instructions and purposes that communicate the principal's avowed and avowal-ready interests.<sup>260</sup> Hence, a fiduciary's acceptance, assertion, or exercise of entrusted power over another's legal or practical interests automatically triggers a legal requirement to be true to the terms of the trust reposed.

The republican theory rejects the popular view that the duty of loyalty does not apply in the absence of discretion.<sup>261</sup> Under the republican theory,

255. Andrew S. Gold, *The Loyalties of Fiduciary Law*, in PHILOSOPHICAL FOUNDATIONS, *supra* note 6, at 176, 178–83.

256. As Lionel Smith has explained, the “duty of loyalty” is best understood as a legal requirement that applies to the exercise of fiduciary power—rather than, strictly speaking, a legal duty. Smith, *supra* note 124, at 142.

257. In contrast, Australian courts have held that fiduciary duties are exclusively proscriptive. *Pilmer v Duke Grp. Ltd.* (2001) 207 CLR ¶ 74 (Austl.); *Breen v Williams* (1996) 186 CLR 71, 113 (Austl.).

258. Gold, *supra* note 255, at 180–82.

259. See, e.g., *US Sprint Commc'ns Co. v. Thompson*, Civ. A. No. 91-2089-O, 1992 WL 350233, at \*2 (D. Kan. Oct. 2, 1992) (holding that an agent “violated his fiduciary duty to follow explicit instructions” by entering unauthorized transactions).

260. See Harding, *supra* note 165, at 93–95 (arguing that the no-conflict rule rests on “the requirements of respect . . . [which] forbid using other people as means to one's own ends”).

261. See, e.g., Miller, *supra* note 163, at 72 (“[P]owers are ordinarily considered fiduciary only if they are *discretionary*.”); DeMott, *supra* note 209, at 901 (“If the relationship . . . does not confer

a person is a fiduciary if she holds entrusted power over another's legal or practical interests, even if that entrusted power does not involve discretionary judgment.<sup>262</sup> For example, an agent who is given a purely ministerial charge to deposit money in her principal's bank account is entrusted with de jure power to act on her behalf. If the agent instead absconds with the money and invests it for her own profit, she breaches her fiduciary duty of loyalty.<sup>263</sup> The agent is liable not only for breach of contract and conversion of her principal's property but also for breach of the duty of loyalty. Accordingly, a court may order rescission of the agent's transactions, or it may order the agent to hold the purchased investments in constructive trust and disgorge any profits she accrued through her self-dealing pursuant to fiduciary law's no-profit rule.<sup>264</sup> While contract law and property law are capable of redressing the harm caused by the agent's wrongful interference with her principal's choices, only fiduciary law is designed to redress the breach of trust entailed in the fiduciary's opportunistic instrumentalization of her entrusted power.<sup>265</sup> Thus, the duty of loyalty applies regardless of whether a fiduciary exercises discretionary or nondiscretionary power.

2. *Affirmative Devotion to Beneficiaries' Interests.*—The republican theory also supports a requirement that fiduciaries pursue the best interests of their beneficiaries with affirmative devotion.<sup>266</sup> Fiduciary relationships are distinct from ordinary contractual relationships, as Daniel Markovits has explained, because a contract promisor is required only to “honor her contract,” while a “fiduciary must take the *initiative* on her beneficiary's behalf” and “make new sacrifices in the face of unforeseen developments.”<sup>267</sup>

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discretion on the ‘fiduciary,’ then his actions are not subject to the fiduciary constraint.”); Weinrib, *supra* note 164, at 4 (asserting that “the fiduciary must have scope for the exercise of discretion”). *But see* Arthur B. Laby, Book Review, 35 L. & PHIL. 123, 130–34 (2016) (reviewing PHILOSOPHICAL FOUNDATIONS, *supra* note 6) (criticizing the “discretionary power” theory of fiduciary relationships).

262. *See* Laby, *supra* note 261, at 132 (arguing that there are “many instances when courts impose fiduciary duties on persons and firms shorn of discretionary power over another,” such as investment advisers, lawyers, and physicians who are acting in an advisory capacity).

263. *See* IT Corp. v. Gen. Am. Life Ins. Co., 107 F.3d 1415, 1421–22 (9th Cir. 1997) (observing that nondiscretionary “control over assets” is sufficient to trigger fiduciary duties under ERISA); McDermott v. Party City Corp., 11 F. Supp. 2d 612, 627 (E.D. Pa. 1998) (explaining that “an agent who embezzles from his principal may be in breach of . . . the [fiduciary] duty imposed by operation of law”).

264. *See* RESTATEMENT (THIRD) OF RESTITUTION AND UNJUST ENRICHMENT § 51 cmt. b, illustr. 2 (AM. LAW INST. 2011) (observing that such remedies are available in a similar scenario where embezzled funds are used to purchase real property).

265. *See* RESTATEMENT (THIRD) OF TRUSTS §§ 93, 100 (AM. LAW INST. 2007) (defining breach of trust and trustee liability for such a breach).

266. Evan Fox-Decent and I refer to this requirement elsewhere as the principle of “solicitude.” *See* CRIDDLE & FOX-DECENT, *supra* note 14, at 98 (describing the principle of solicitude as concern for the other's “legitimate interests”).

267. Markovits, *supra* note 6, at 216, 222.

The duty of loyalty thus requires a fiduciary to tailor her actions to advance her beneficiaries' best interests.

A number of courts have asserted that the requirement of affirmative devotion requires alignment between a fiduciary's intentions and her beneficiaries' interests.<sup>268</sup> In *Stone v. Ritter*,<sup>269</sup> for example, the Delaware Supreme Court famously took the position that a corporate "director cannot act loyally towards the corporation unless she acts in the good faith belief that her actions are in the corporation's best interest."<sup>270</sup> Fiduciary loyalty therefore demands that a fiduciary exercise entrusted power in a manner that she believes will promote the best interests of her beneficiaries.<sup>271</sup>

Purely as a matter of interpersonal ethics, the logic of *Stone v. Ritter* is unassailable: a fiduciary does not act loyally if she does not believe her actions advance her beneficiaries' best interests. But should affirmative devotion be enshrined as a legal obligation? The republican theory suggests that the answer is "yes." This conclusion may not seem particularly surprising, given the emphasis that republicans place on the importance of cultivating civic virtue.<sup>272</sup> But the reasons why affirmative devotion is a *legal* requirement require further elaboration.

Under the republican theory, the legal requirement of affirmative devotion is not concerned with elevating a fiduciary's moral rectitude for its own sake, nor is it merely a means for reducing the likelihood of harm to beneficiaries' interests. Fiduciaries are required to give due regard to their beneficiaries' interests because this approach safeguards beneficiaries' freedom from domination.<sup>273</sup> A fiduciary who reserved the right to exercise entrusted power based on reasons unrelated to her mandate and the interests of her beneficiaries would subject the interests of her principal and

268. See, e.g., *Stone v. Ritter*, 911 A.2d 362, 370 (Del. 2006) (explaining that the fiduciary duty of loyalty encompasses an obligation to act in good faith, which requires a fiduciary to act "in the good faith belief that her actions are in the corporation's best interest"); *In re Walt Disney Co. Derivative Litig.*, 906 A.2d 27, 67 (Del. 2006) ("The good faith required of a . . . fiduciary includes not simply the duties of care and loyalty . . . but all actions required by a true faithfulness and devotion to the interests of the [beneficiary].").

269. 911 A.2d at 362.

270. *Id.* at 370 (quoting *Guttman v. Huang*, 823 A.2d 492, 506 n.34 (Del. Ch. 2003)).

271. Smith, *supra* note 124, at 148.

272. See, e.g., Besson & Marti, *supra* note 36, at 22–24 (extolling civic virtues such as "respect for and loyalty to the law [and] the republic's institutions, . . . respect for pluralism and for others' preferences and opinions[,] and the pursuit of "the common good . . . through political participation" as necessary to enable and promote the political participation of an active and motivated citizenry required by republican liberty). See generally PHILIP PETTIT, *THE ROBUST DEMANDS OF THE GOOD: ETHICS WITH ATTACHMENT, VIRTUE, AND RESPECT* (2015) (developing these themes).

273. See Evan J. Criddle & Evan Fox-Decent, *Keeping the Promise of Public Fiduciary Theory: A Reply to Leib and Galoob*, 126 YALE L.J. F. 192, 199 (2016) ("[F]iduciary rules and remedies in the United States . . . reflect the republican principle of non-domination.").

beneficiaries to alien control.<sup>274</sup> The republican theory thus supports the Delaware Supreme Court's view that a fiduciary's affirmative devotion to her beneficiaries' best interests is an indispensable requirement of fiduciary loyalty.

Contrary to the views of some fiduciary scholars, however, the duty of loyalty does not require that a fiduciary's motives for action be wholly uncompromised by self-regarding interests.<sup>275</sup> Recall that the purpose of private law, under the republican theory, is to ensure that a private party's legal and practical interests are not subject to another's arbitrary control. The loyalty requirement of affirmative devotion safeguards freedom from domination, in part, by obligating a fiduciary to act in a manner that she reasonably believes in good faith will maximize her beneficiaries' interests. When a fiduciary satisfies this requirement, her solicitude to the interests of her beneficiaries ensures that she does not exercise alien control. From the beneficiaries' perspective, it does not matter whether the fiduciary's primary motivation for acting loyally is a desire for remuneration, fear of legal sanctions, or other self-regarding considerations.<sup>276</sup> As long as the fiduciary exercises her entrusted authority in a manner that she reasonably believes will advance her principal's directives and her beneficiaries' best interests, the principal and beneficiaries cannot complain that they are subject to domination.<sup>277</sup> From the perspective of republican legal theory, therefore,

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274. See, e.g., Miller, *supra* note 2, at 993 (asserting that a breach of fiduciary duty may be conceptualized as a harmful interference with the beneficiary's personal interests).

275. But see Lionel Smith, *The Motive, Not the Deed*, in RATIONALIZING PROPERTY, EQUITY AND TRUSTS 53, 69 (Joshua Getzler ed., 2003) ("The fiduciary obligation of loyalty requires the fiduciary to act with a particular motive: in general, she must act (or not act) in what she perceives to be the best interests of the person to whom the duty is owed."); Leib & Galoob, *supra* note 17, at 1835–38 (asserting a conscientious- motivation requirement such that "certain ways of conforming to fiduciary duties do not count as living up to fiduciary norms" if not based in the best interests of the principal). Smith, in particular, argues that the no-conflict and no-profit rules are necessary to compensate for courts' inability to surmount the inscrutability of a fiduciary's true motivations. See Smith, *supra*, at 74 ("The prophylactic rules are triggered by situations in which it may be especially difficult to know with what motive the fiduciary acted, because the fiduciary is subject to conflicting motivational pressures.").

276. See Criddle & Fox-Decent, *supra* note 273, at 203 ("As long as a fiduciary performs her entrusted duties with due regard for her principal's instructions and her beneficiaries' best interests, the law does not care [what] the reasons motivating her actions are. . . . As long as the . . . fiduciary does not assert the prerogative to wield entrusted power in a manner that is indifferent to her beneficiaries' interests, she does not subject her beneficiary to instrumentalization or domination."). This is not to suggest, of course, that a fiduciary's motivations are unimportant from the perspective of republican *ethics*. See PETTIT, *supra* note 272, 44–48 (arguing that republican virtues impose robust ethical demands).

277. See PETTIT, *supra* note 11, at 212 (quoting John Trenchard's observation that people "are Free, where their Magistrates . . . act by Rules prescribed them by the People: And they are Slaves, where, their magistrates choose their own Rules, and follow their Lust and Humours").

the better view is that fiduciary loyalty is concerned with a fiduciary's actions and intentions, not her motivations.<sup>278</sup>

The requirements of fidelity and affirmative devotion do not apply in equal measure to all fiduciary relationships. As Gold and Miller have observed, some fiduciaries are entrusted with power primarily for the purpose of advancing the interests of designated beneficiaries (e.g., guardianships), while others receive broad purposive mandates that do not specify discrete beneficiaries (e.g., charitable trusts).<sup>279</sup> When fiduciary relationships fall on the latter end of the spectrum, the requirement of fidelity to instructions will predominate over the requirement of affirmative devotion to beneficiaries' best interests in some aspects of a fiduciary's performance. The relative salience of fidelity and affirmative devotion thus depends upon the purpose and design of particular fiduciary relationships.

3. *Fairness and Evenhandedness.*—The duty of loyalty also emancipates beneficiaries from domination by ensuring that they are treated fairly and evenhandedly in fiduciary relationships involving rivalrous beneficiary claims. For example, when investors commit their resources to a hedge fund, they face not only the threat that the manager might engage in self-dealing but also the possibility that the manager might arbitrarily confer a disproportionate share of the profits on some favored investors to the detriment of others. In such cases, “the discrete fiduciary duty of loyalty is necessarily transformed into duties of fairness and reasonableness.”<sup>280</sup> This requirement of fair and evenhanded treatment emancipates beneficiaries with rivalrous interests by requiring fiduciaries to exercise entrusted power in a manner that respects the beneficiaries' formal equality.

4. *Conflict Avoidance.*—The republican theory of fiduciary law also provides a strong counterpoint to classical liberalism's argument for diluting the duty of loyalty's uncompromising no-conflict and no-profit rules. As discussed in Part II, classical liberalism posits that there is nothing inherently immoral about a fiduciary profiting from a conflicted transaction, as long as the transaction also benefits the principal. Accordingly, classical liberalism characterizes the no-conflict and no-profit rules as prophylactic checks

278. See Markovits, *supra* note 6, at 220 (“Legal obligations—both contractual and fiduciary—turn on intentions not motivations.”).

279. Paul B. Miller & Andrew S. Gold, *Fiduciary Governance*, 57 WM. & MARY L. REV. 513, 517 (2015).

280. FOX-DECENT, SOVEREIGNTY'S PROMISE, *supra* note 17, at 34–35; see also RESTATEMENT (THIRD) OF TRUSTS § 79(1)(a) (AM. LAW INST. 2007) (providing that “the trustee must act impartially and with due regard for the diverse beneficial interests created by the terms of the trust”); P.D. Finn, *The Forgotten “Trust”*: *The People and the State*, in EQUITY: ISSUES AND TRENDS 131, 138 (Malcolm Cope ed., 1995) (“It is uncontroversial fiduciary law that where a fiduciary serves classes of beneficiaries possessing different rights, . . . the fiduciary is . . . required to act *fairly* as between different classes of beneficiary in taking decisions which affect the rights and interests of the classes *inter se*.”).



against opportunism: by prohibiting all self-interested transactions and profit taking without a principal's consent—regardless of a fiduciary's intent or whether the beneficiary has been harmed—fiduciary law eliminates a fiduciary's incentives to abuse her position and lowers the principal's monitoring and bonding costs. Experts have argued that these rules also correct for information asymmetries by preventing a fiduciary from exploiting the fact that she “controls all evidence of the relationship and can easily conceal wrongdoing from the vulnerable party or the court.”<sup>281</sup> Yet, as Langbein has argued, in theory these concerns can all be addressed in a less onerous way: by placing the burden squarely on fiduciaries to demonstrate that unauthorized conflicted transactions maximized beneficiaries' profits (or minimized losses) relative to other available opportunities.<sup>282</sup>

The republican theory of fiduciary law flatly rejects this reasoning. According to the republican theory, an agent, trustee, or corporate director has no legal authority to use fiduciary power in the service of her own ends and, accordingly, may not retain any profits that result from transactions associated with the fiduciary office.<sup>283</sup> The other-regarding character of the fiduciary office requires a fiduciary to reserve any surplus generated by conflicted transactions for the benefit of her principal.<sup>284</sup> A fiduciary's withholding of this surplus to any degree constitutes a betrayal of trust that is inimical to the other-regarding character of the fiduciary relationship. This abuse of trust is wrongful even if it does not harm the beneficiaries' material interests.<sup>285</sup> Accordingly, a party who holds fiduciary power may not use that power to advance her own self-interest unilaterally (i.e., without informed consent), *even if such action indisputably promotes her beneficiaries' interests.*

Significantly, if a fiduciary truly believes that a conflicted transaction will best promote her beneficiaries' interests, the no-conflict and no-profit

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281. Getzler, *supra* note 83, at 586.

282. Langbein, *supra* note 77, at 981.

283. See ERNEST VINTER, A TREATISE ON THE HISTORY AND LAW OF FIDUCIARY RELATIONSHIP AND RESULTING TRUSTS 11 (3d ed. 1955) (reviewing the history of the no-conflict and no-profit rules of fiduciary duty). The no-conflict and no-profit rules do not, however, preclude a fiduciary from receiving reasonable fees for services rendered pursuant to contract or with judicial approval.

284. See Melvin A. Eisenberg, *The Disgorgement Interest in Contract Law*, 105 MICH. L. REV. 559, 563 (2006) (“A fiduciary who wrongfully makes a personal gain through the use of his position, or of property or information that he holds through his position, must disgorge that gain to his beneficiary even if the beneficiary has suffered no loss from the wrong.”).

285. For a helpful discussion of the distinction between wrongs and harms, see ARTHUR RIPSTEIN, FORCE AND FREEDOM: KANT'S LEGAL AND POLITICAL PHILOSOPHY 30–56 (2009).

rules do not actually preclude the transaction from taking place;<sup>286</sup> the fiduciary need only take whatever steps are necessary to prevent the potential conflict from introducing domination. The fiduciary may disclose the potential conflict and obtain beneficiaries' advance consent to the transaction's terms, thereby authorizing her to withhold profits acquired in a personal capacity through the transaction.<sup>287</sup> Or she may voluntarily relinquish all profits accrued in her personal capacity in order to satisfy her fiduciary obligation to reserve all surplus generated by the transaction for her beneficiaries.<sup>288</sup> Either choice would eliminate the conflict of interest, defuse the fiduciary's capacity for alien control, and thereby satisfy the fiduciary duty of loyalty. There is no inherent conflict, therefore, between a fiduciary acting in her beneficiaries' "sole interest" while also advancing their "best interests."

The republican theory thus opposes classical liberalism's call to scale back or eliminate fiduciary law's traditional no-conflict and no-profit rules. In particular, it shows how Delaware's "entire fairness" test, which permits corporate directors to engage in self-interested transactions without informed consent, subjects corporations (and thereby, indirectly, their shareholders) to domination.<sup>289</sup> It also explains why recent efforts to scale back the duty of loyalty in agency and trust law should be resisted in the interest of safeguarding liberty.

5. *The Mandatory Core.*—Although this Article cannot address every aspect of the duty of loyalty, one final contribution of the republican theory merits brief consideration: the theory's novel justification for fiduciary law's "mandatory core."<sup>290</sup> Some scholars of law and economics have argued that all fiduciary duties are contractual default rules and therefore should be freely waivable with beneficiaries' informed consent.<sup>291</sup> Others have asserted,

286. See RESTATEMENT (THIRD) OF TRUSTS § 78 cmt. c (AM. LAW INST. 2007) (explaining the specific exemptions to the no-conflict rule, including transactions allowed by consent of all beneficiaries).

287. See RESTATEMENT (THIRD) OF AGENCY § 8.06(1) (AM. LAW INST. 2006) (providing that an agent may obtain a material benefit arising out of her position when she obtains her principal's consent).

288. *Id.* § 8.02 cmt. e (describing available remedies when an agent obtains a material benefit arising out of her position without having secured her principal's consent).

289. Compare DEL. CODE ANN. tit. 8, § 144(a)(3) (2016) (explaining the "entire fairness" test, where a corporate director may engage in conflicted transactions without informed consent of beneficiaries), with PETTIT, *supra* note 11, at 31–41 (discussing the republican tradition and its association with nondomination).

290. Sitkoff, *supra* note 22, at 1046.

291. See, e.g., Butler & Ribstein, *supra* note 26, at 71–72 (arguing for a new concept of the corporation that recognizes the power of private ordering, market forces, and "private controls on managerial conduct," while deemphasizing the role of fiduciary duties); Easterbrook & Fischel, *supra* note 7, at 427, 431–32 (theorizing that "a 'fiduciary' relation is a contractual one" and that courts "setting out to protect principals from their agents *must* use the hypothetical contract

however, that economic theory can support treating some loyalty requirements as mandatory rules.<sup>292</sup> In arguably the most sophisticated economic defense of mandatory rules, Robert Sitkoff asserts that the duty of loyalty's "mandatory core" serves two functions: (1) it "insulates fiduciary obligations that the law assumes would not be bargained away by a fully informed, sophisticated principal";<sup>293</sup> and (2) it provides "clean lines of demarcation across types of legal relationships, among other things to minimize third-party information costs."<sup>294</sup> Viewed from this perspective, classical liberalism can support mandatory rules as autonomy-reinforcing safeguards that address the risks of harm that arise in fiduciary relationships.

The republican theory offers a different justification for fiduciary law's mandatory core. Although republicanism generally supports allowing principals to structure fiduciary relationships in ways that deviate from fiduciary law's baseline rules, this concession to individual choice has a nonnegotiable limit: Fiduciary relationships may not be structured in a manner that subjects beneficiaries' legal or practical interests to a fiduciary's unfettered alien control.

This bedrock nondomination principle explains and justifies the current features of fiduciary law's mandatory core. It supports the rule that a principal may not authorize a fiduciary to act in bad faith or otherwise violate the terms or purposes of the fiduciary relationship.<sup>295</sup> Nor may beneficiaries waive the fiduciary duty to provide information relevant to informed consent.<sup>296</sup> The nondomination principle also reinforces courts' common practice of construing waivers of fiduciary duties narrowly to ensure that consent is fully informed.<sup>297</sup> These features of contemporary fiduciary law

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approach" to determine whether fiduciary duties apply); Langbein, *supra* note 7, at 658 (observing that fiduciary duties are prevailingly, if not obviously, contractarian; "[c]ontract is there, but not always at first glance"); Sitkoff, *supra* note 22, at 1046 ("[V]arious fiduciary duties are for the most part *default rules* that apply unless the parties have agreed otherwise.").

292. See, e.g., Sitkoff, *supra* note 22, at 1046 (theorizing "mandatory rules" of the "fiduciary obligation that cannot be overridden by agreement").

293. Sitkoff, *supra* note 108, at 205.

294. *Id.*; see also Coffee, *supra* note 112, at 1624 ("[T]hird-party effects justify a certain minimum level of judicial paternalism . . .").

295. See *Sample v. Morgan*, 914 A.2d 647, 663–64 (Del. Ch. 2007) (holding that stockholder ratification is not a "blank check" for conflicted transactions that cannot plausibly be interpreted as advancing the corporation's best interests); RESTATEMENT (THIRD) OF TRUSTS § 96(1)(a) (AM. LAW INST. 2007) (providing that an exculpation clause is unenforceable if it purports to relieve a trustee "of liability for a breach of trust committed in bad faith or with indifference to the fiduciary duties of the trustee, the terms or purposes of the trust, or the interests of the beneficiaries").

296. See, e.g., *Sample*, 914 A.2d at 664–67 (holding that director ratification cannot preclude a claim for breach of fiduciary duty if the directors failed to disclose material facts).

297. See Deborah A. DeMott, *Defining Agency and its Scope (II)*, in *COMPARATIVE CONTRACT LAW: BRITISH AND AMERICAN PERSPECTIVES* 396, 398 (Larry A. DiMatteo & Martin Hogg eds., 2016) ("[A] principal's consent to conduct that would otherwise breach a fiduciary duty requires

are necessary to prevent principals and beneficiaries from placing their legal and practical interests under fiduciaries' "uncontrolled discretion."<sup>298</sup> Just as courts will not enforce contracts in which one person consents to become another's slave or involuntary servant,<sup>299</sup> principals and beneficiaries may not contract to subject their legal or practical interests to a fiduciary's alien control through general waivers of fiduciary duties.

#### D. *Understanding Fiduciary Remedies*

Another important contribution of the republican theory is the link it forges between the formal legal character of fiduciary power and the remedies that courts have traditionally offered to address breaches of the duty of loyalty. Fiduciary theorists who embrace classical liberalism tend to characterize traditional fiduciary remedies, such as constructive trust and disgorgement, as supracompensatory measures that deter opportunism.<sup>300</sup> In contrast, the republican theory suggests that these remedies are appropriate to support the principle that a fiduciary is legally incapable of holding or exercising fiduciary power except in trust for her principal and beneficiaries.<sup>301</sup>

The republican theory's account of fiduciary remedies closely tracks Paul Miller's juridical theory of fiduciary remedies.<sup>302</sup> In a series of path-breaking publications, Miller has argued that the distinctive feature of fiduciary relationships is that a fiduciary "stands in substitution for the beneficiary or a benefactor in exercising a legal capacity that is ordinarily derived from the beneficiary or benefactor's legal personality."<sup>303</sup> Because in Miller's view the legal rights exercised by a fiduciary are vested in the

specificity."); Miller, *supra* note 2, at 1006 (observing that "broad waivers or contractual clauses purporting to completely exclude fiduciary liability are usually read down or held void").

298. *In re Will of Allister*, 545 N.Y.S.2d 483, 486 (N.Y. Sup. Ct. 1989).

299. See U.S. CONST. amend. XIII, § 1 ("Neither slavery nor involuntary servitude, except as a punishment for crime . . . , shall exist within the United States, or any place subject to their jurisdiction.").

300. See, e.g., Daniel Fischel & John H. Langbein, *ERISA's Fundamental Contradiction: The Exclusive Benefit Rule*, 55 U. CHI. L. REV. 1105, 1115–16 (1988) (discussing how stricter fiduciary rules help "deter conduct by the fiduciary that is inconsistent with the . . . welfare of the beneficiaries"); Smith, *supra* note 64, at 1404 ("[F]iduciary law can be justified on the grounds that it deters opportunistic behavior."); cf. James J. Edelman, *Unjust Enrichment, Restitution, and Wrongs*, 79 TEXAS L. REV. 1869, 1876 (2001) (asserting that courts apply "disgorgement damages" to fiduciary relationships because "there is a profound need for deterrence not fulfilled by compensatory damages").

301. See, e.g., SHEPHERD, *supra* note 165, at 93 ("The essence of this theory of fiduciary relationships is that powers are a species of property, which can be beneficially owned by one person while being exercised by another person, who may be referred to as the legal owner of the power.").

302. See Miller, *supra* note 163, at 69 (defining "[a] fiduciary relationship [as] one in which one party (the fiduciary) exercises discretionary power over the significant practical interests of another (the beneficiary)").

303. *Id.* at 70–71.

principal or beneficiary rather than the fiduciary, “[t]he fiduciary may not treat fiduciary power as an unclaimed means or as a personal means.”<sup>304</sup> Instead, the fiduciary must treat her beneficiary always as the exclusive beneficiary of her exercise of entrusted power. Miller argues that disgorgement is an appropriate remedy for fiduciary disloyalty, because within a fiduciary relationship “[n]o one is entitled to gain from the execution of a fiduciary mandate save the beneficiary; to the extent that there are such gains, they belong to the beneficiary.”<sup>305</sup> In Miller’s view, therefore, the no-profit rule reflects the simple principle that a beneficiary is entitled to enjoy the full benefits of the exercise of her own legal powers.<sup>306</sup>

The republican theory refines Miller’s juridical account of fiduciary remedies by elucidating its implicit normative underpinnings. Consistent with Miller’s account, fiduciary remedies affirm that fiduciaries may not dominate their beneficiaries by treating entrusted fiduciary power as an instrument for advancing their own interests without beneficiaries’ consent.<sup>307</sup> Giving beneficiaries the option to seek rescission of unauthorized conflicted transactions promotes freedom from domination by affirming that fiduciaries lack the legal capacity to use fiduciary power for their own benefit unilaterally. If beneficiaries conclude that an unauthorized conflicted transaction was, in fact, the best option for maximizing their own profits (or minimizing losses), they may elect to leave the transaction intact and compel the fiduciary to hold, and ultimately disgorge, any profits generated by the transaction.<sup>308</sup> Constructive trust and disgorgement thus prevent the fiduciary from dictating unilaterally the terms under which profits generated by a conflicted transaction will be divided between herself and her beneficiaries. Collectively, these traditional fiduciary remedies prevent a fiduciary from wielding alien control over her beneficiaries’ legal and practical interests.

The republican theory clarifies why disgorgement is justified in settings where fiduciary disloyalty produces gains that principals and beneficiaries would not be entitled to generate for themselves. Consider the case of a fiduciary who accepts bribes from a third party. Courts routinely hold that public officials who accept bribes violate their duty of loyalty and must relinquish bribes to their government employers.<sup>309</sup> Disgorgement of bribes

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304. Miller, *supra* note 2, at 1021.

305. Paul B. Miller, *Justifying Fiduciary Remedies*, 63 U. TORONTO L.J. 570, 616 (2013).

306. *Id.* at 616–17.

307. *See, e.g., id.* at 585 (noting that a fiduciary is subject to fiduciary liability when the fiduciary allows his own interests or those of a third party to “actually or potentially . . . conflict with the interests of the beneficiary”).

308. *See* MEAGHER ET AL., *supra* note 79, at 186.

309. *See, e.g.,* United States v. Carter, 217 U.S. 286, 306 (1909) (requiring an agent to account to his principal for any benefit received in “violation of his duty”); United States v. Drumm, 329

exposes a tension within Miller’s juridical account of fiduciary law because a public official cannot be understood in any meaningful sense to have been entrusted with authority to collect bribes.<sup>310</sup> Moreover, as Deborah DeMott has observed, even if the concept of entrusted power

is defined more broadly, perhaps as the power to deal with third parties on the principal’s behalf, the facts that the power was used for an illegal end, and thus that the principal could not itself directly use the power to the same end, make it hard to explain why the proceeds of the transaction belong to the principal.<sup>311</sup>

Federal courts wrestled with this question during the late 1980s, when they were asked to decide whether bribery constituted a form of fraud under the federal mail fraud statute.<sup>312</sup> In *McNally v. United States*,<sup>313</sup> the Supreme Court reversed the conviction of a Kentucky state official who had participated in a self-dealing patronage scheme because the jury in the case had not been asked to decide whether the official had defrauded the state of any money or property.<sup>314</sup> The Court based its decision, in part, on the idea that the state lacked an ownership interest in kickbacks from government contractors.<sup>315</sup> Justice Stevens conceded this point in his dissent, but he argued that the defendant, as a state official, was duty bound to deliver anything he received “as a result of his violation of a duty of loyalty to the principal.”<sup>316</sup> He therefore asserted that “[t]his duty may fulfill the Court’s ‘money or property’ requirement in most kickback schemes.”<sup>317</sup> Following *McNally*, however, lower federal courts overwhelmingly rejected Justice

F.2d 109, 113 (1st Cir. 1964) (holding an agent accountable for “all profits in excess of his lawful compensation”); *United States v. Project on Gov’t Oversight*, 572 F. Supp. 2d 73, 75–77 (D.D.C. 2008) (noting that an agent with two “paymasters” necessarily creates a conflict of interest and that failing to disclose and seek approval for the additional payment constituted a breach of fiduciary duty warranting disgorgement); *Jersey City v. Hague*, 115 A.2d 8, 11–15 (N.J. 1955) (allowing the recovery of money taken wrongfully from the principal by the agent through restitution, thus preventing the “unfaithful public official” from wrongfully profiting).

310. Compare Miller, *supra* note 163, at 70–71 (suggesting that fiduciary power derives from a beneficiary’s legal capacities), with Miller, *supra* note 305, at 600 (asserting that disgorgement of bribes can be justified based on a beneficiary’s “quasi-proprietary” right to fiduciary loyalty itself).

311. DeMott, *supra* note 209, at 912–13.

312. 18 U.S.C. § 1341 (2012); see also *id.* § 1346 (defining “scheme or artifice to defraud” as including a “scheme or artifice to deprive another of the intangible right of honest services”).

313. 483 U.S. 350 (1987).

314. *Id.* at 360–61.

315. *Id.* at 351, 360.

316. *Id.* at 365–66, 377 n.10 (Stevens, J., dissenting) (quoting RESTATEMENT (SECOND) OF AGENCY § 403 (AM. LAW INST. 1958)).

317. *Id.* Justice O’Connor joined all of Justice Stevens’s dissent except the concluding section that contained this proposal. *Id.* at 362.

Stevens's duty-based theory.<sup>318</sup> Following Judge Posner's lead,<sup>319</sup> several circuits reasoned that disgorgement of bribes might be justified under fiduciary law as a deterrence measure, but they flatly rejected the idea that this remedy could be based on a governmental property interest in bribes.<sup>320</sup>

The republican theory developed in this Article offers a different justification for fiduciary law's disgorgement remedy and, in so doing, clarifies why the government is entitled to demand disgorgement of bribes as a civil remedy for breach of fiduciary duty. Consistent with Miller's juridical theory, the republican theory takes disgorgement on its own terms as a remedy for wrongful withholding of property rather than as a prophylactic or compensatory measure. The republican theory avoids the implausible suggestion that the government has a property right in bribes. Instead, the disgorgement remedy tracks the other-regarding character of the fiduciary office itself: when acting within the scope of her office, a fiduciary is legally incapable of accepting assets except in trust for her beneficiaries.<sup>321</sup> As the Supreme Court has explained in another landmark corruption case, *United States v. Carter*,<sup>322</sup> disgorgement "results not from the subject-matter but from the fiduciary character of the one against whom it is applied."<sup>323</sup> Hence, disgorgement is not dependent upon a finding that the government would be entitled to receive bribery payments in the absence of a public official's disloyalty, nor is it contingent upon a finding or presumption that the

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318. See, e.g., *United States v. Walgren*, 885 F.2d 1417, 1422–24 (9th Cir. 1989) (rejecting the "duty of loyalty" theory that would make a government employee guilty of mail fraud against his employer for accepting bribes); *United States v. Shelton*, 848 F.2d 1485, 1491–92 (10th Cir. 1988) (en banc) (holding that the constructive trust theory is not sufficient to sustain a mail fraud conviction for lost intangible rights); *United States v. Ochs*, 842 F.2d 515, 525–27 (1st Cir. 1988) (noting that the Supreme Court effectively rejected Justice Stevens's argument in *McNally* and that the courts may not "recharacterize every breach of fiduciary duty as a financial harm"); *United States v. Holzer*, 840 F.2d 1343, 1346–48 (7th Cir. 1988) (finding that the placement of bribe money into a constructive trust does not make it government property for the purpose of a mail fraud conviction). But see *United States v. Runnels*, 833 F.2d 1183, 1186–88 (6th Cir. 1987) (holding that bribes are "a benefit which properly belongs to the [state], which is the principal, rather than the official, officer, or employee, who is merely a fiduciary-agent"), *rev'd and vacated en banc*, 877 F.2d 481 (6th Cir. 1989).

319. See *Holzer*, 840 F.2d at 1348 (Posner, J.) ("A constructive trust is imposed on the bribes not because [a public servant] . . . failed to account for money received on the state's account but in order to deter bribery by depriving the bribed official of the benefit of the bribes.").

320. *Walgren*, 885 F.2d at 1422–24; *Shelton*, 848 F.2d at 1491–92.

321. See RESTATEMENT (SECOND) OF AGENCY § 403 (AM. LAW INST. 1958) ("If an agent receives anything as a result of his violation of a duty of loyalty to the principal, he is subject to a liability to deliver it, its value, or its proceeds, to the principal."); RESTATEMENT (FIRST) OF RESTITUTION § 197 (AM. LAW INST. 1937) ("Where a fiduciary in violation of his duty to the beneficiary receives or retains a bonus or commission or other profit, he holds what he receives upon a constructive trust for the beneficiary.").

322. 217 U.S. 286 (1910).

323. *Id.* at 306.

government suffered financial or other material harm from the bribery.<sup>324</sup> Under the republican theory, the fact that a public official's entrusted position of authority enables him to obtain bribes is enough to trigger the requirement that he hold the assets in trust and relinquish them to his employer for the public's benefit. The violation of this requirement wrongs a fiduciary's beneficiaries by betraying the other-regarding terms of the fiduciary's entrusted power, irrespective of whether beneficiaries suffer material harm.<sup>325</sup> Disgorgement in this context thus affirms the fiduciary character of public offices by ensuring that "[t]he citizen is not at the mercy of his servants holding positions of public trust."<sup>326</sup>

### *E. The Divergence of Fiduciary Conduct and Decision Rules*

The republican theory also helps to explain the deferential standards of review that courts have applied across many fields of fiduciary law. Although courts often assert that fiduciaries must pursue their principals' objectives with "utmost good faith," observing "the highest standards of honor and honesty,"<sup>327</sup> they rarely find a breach of fiduciary duty absent evidence of egregious abuse. Perhaps the best known example of this phenomenon is corporate law's "business judgment rule," which requires courts to accept business decisions that disinterested directors have made deliberatively and in good faith—even if those decisions ultimately harmed the interests of the corporation or its stockholders.<sup>328</sup> Corporate law is hardly unique, however, in its deferential approach to fiduciary decision making. Courts also apply a healthy measure of deference to fiduciaries' discretionary

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324. See *Hawaiian Int'l Fins., Inc. v. Pablo*, 488 P.2d 1172, 1175 (Haw. 1971) (stating that the rule against a fiduciary retaining a bonus, commission, or other profit from third parties "is applicable although the profit received by the fiduciary is not at the expense of the beneficiary" (quoting RESTATEMENT (FIRST) OF RESTITUTION § 197 cmt. c (AM. LAW INST. 1937))).

325. See *Bos. Deep Sea Fishing & Ice Co. v. Ansell* [1888] 39 Ch. D. 339 at 357 (Eng. & Wales) (Cotton, L.J.) (concluding that "where an agent . . . without the knowledge or assent of [the] principal, receives money from the person with whom he is dealing, he is doing a wrongful act" and must relinquish the money to the principal).

326. *Driscoll v. Burlington-Bristol Bridge Co.*, 86 A.2d 201, 222 (N.J. 1952).

327. *Grossberg v. Haffenberg*, 11 N.E.2d 359, 360 (Ill. 1937); see also *Smith v. Van Gorkom*, 488 A.2d 858, 872 (Del. 1985) (defining a director's duty of loyalty as an "unyielding fiduciary duty to [pursue the purposes and interests of] the corporation and its shareholders"), *overruled on other grounds*, *Gantler v. Stephens*, 965 A.2d 695 (Del. 2009); *Guth v. Loft, Inc.*, 5 A.2d 503, 510 (Del. 1939) (describing the duty of loyalty as a "rule that demands of a corporate officer or director, peremptorily and inexorably, the most scrupulous observance of his duty, . . . affirmatively to protect the interests of the corporation").

328. See D. Gordon Smith, *The Modern Business Judgment Rule*, in RESEARCH HANDBOOK ON MERGERS AND ACQUISITIONS 83, 83 (Claire A. Hill & Steven Davidoff Solomon eds., 2016) (describing the traditional business judgment rule as a mechanism to shield corporate directors from liability for "honest mistakes" when the directors made the decision in a careful, loyal, and good-faith manner).



judgments in other contexts, including trust law<sup>329</sup> and bankruptcy law.<sup>330</sup> These deferential standards of review have produced a stark divergence between the legal “conduct rules” that formally regulate fiduciary performance (e.g., diligence, affirmative devotion) and the deferential “decision rules” that govern judicial review in some contexts (e.g., negligence, intentional malfeasance).<sup>331</sup>

The republican theory lends support for the idea that a fiduciary’s “duty of the finest loyalty” is a genuine legal obligation rooted in the fiduciary relationship itself, and not merely an aspirational moral or social norm.<sup>332</sup> The strict conduct rules that flow from this general obligation (e.g., fidelity to instructions, affirmative devotion to beneficiaries, and fairness and evenhandedness) safeguard liberty by ensuring that a fiduciary lacks the formal legal capacity to use entrusted power as a form of alien control over the legal or practical interests of her beneficiaries. These conduct rules pervasively regulate fiduciary power, constituting fiduciary relationships juridically in a manner that formally rules out domination.

At the same time, the republican theory is sensitive to the fact that formal conduct rules are not sufficient to secure freedom from domination in practice. Recall that for republicans, liberty is constituted not only by liberty-affirming conduct rules but also by effective legal and political institutions. The republican theory’s success depends in no small part, therefore, on courts implementing fiduciary law in a manner that promotes liberty.

The challenge for republicans is that judges, like other fiduciaries, have the practical capacity to exercise arbitrary power.<sup>333</sup> To guard against the threat of judicial domination, courts must calibrate fiduciary law’s decision rules to prevent judicial oversight from increasing overall net domination in

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329. *E.g.*, *Crabb v. Young*, 92 N.Y. 56, 66 (N.Y. 1883) (“[W]hile trustees are . . . held to great strictness in their dealings with the interests of their beneficiaries, the court will regard them leniently when it appears they have acted in good faith, and if no improper motive can be attributed to them, the court have even excused an apparent breach of trust, unless the negligence is very gross.”).

330. *See, e.g.*, *In re Healthco Int’l, Inc.*, 136 F.3d 45, 50 n.5 (1st Cir. 1998) (“[The] judge . . . is not to substitute her judgment for that of the [bankruptcy] trustee, and the trustee’s judgment is to be accorded some deference.” (quoting *In re Moorhead Corp.*, 208 B.R. 87, 90 (B.A.P. 1st Cir. 1997))).

331. *See, e.g.*, Melvin Aron Eisenberg, *The Divergence of Standards of Conduct and Standards of Review in Corporate Law*, 62 *FORDHAM L. REV.* 437, 437–38 (1993) (commenting on the variance between “standards of conduct” that set forth how to perform an activity and “standards of review” that govern the associated litigation in corporate law); Julian Velasco, *The Role of Aspiration in Corporate Fiduciary Duties*, 54 *WM. & MARY L. REV.* 519, 521–22 (2012) (“Courts often opine on the relatively demanding standard of conduct, but their judgments must be based on the more forgiving standard of review.”).

332. *Meinhard v. Salmon*, 164 N.E. 545, 546 (N.Y. 1928).

333. *See Getzler, supra* note 83, at 598 (noting Peter Birks’s concern that moralistic formulations of fiduciary loyalty may “descend into a formless anarchy of opinion,” serving as “a prelude to power-mongering and tyranny”).

fiduciary relationships.<sup>334</sup> Yasmin Dawood refers to this approach to judicial oversight as the “antidomination model” of judicial review.<sup>335</sup>

Under the republican theory’s antidomination model and consistent with prevailing practice, judicial deference to fiduciary judgments turns on two considerations. First, courts should respect the fact that in a variety of contexts the law entrusts fiduciaries with discretionary authority to decide what particular measures will best advance their principals’ purposes and their beneficiaries’ interests.<sup>336</sup> Second, courts should take into account that they are poorly equipped to evaluate whether some fiduciary decisions satisfy the duty of loyalty. How much judicial deference is appropriate in a particular context depends upon the interplay between these two considerations.

Whenever a fiduciary exercises entrusted discretionary power, the republican theory supports highly deferential decision rules. For example, courts wisely apply a strong form of deference when they review guardians’ discretionary judgments regarding the interests of their wards.<sup>337</sup> The law entrusts guardians with sweeping responsibility to ascertain and develop strategies to advance the best interests of their beneficiaries.<sup>338</sup> By virtue of their regular contact with their wards, guardians are typically in a better position than judges to discern what measures will maximize their wards’ idiosyncratic preferences.<sup>339</sup> Corporate law’s business judgment rule reflects similar concerns. Courts defer to corporate directors’ discretionary business decisions because directors are primarily responsible to decide what measures will best advance their corporation’s purposes, and courts usually lack the information and expertise necessary to second-guess those decisions.<sup>340</sup> Were courts to conduct *de novo* review of such decisions, they

334. See Dawood, *supra* note 50, at 1418 (arguing that the purpose of judicial intervention is “to prevent the *most* dominating . . . action with judicial intervention that is the *least* dominating”).

335. *Id.*

336. See, e.g., UNIF. POWER OF ATT’Y ACT § 114(d) (UNIF. LAW COMM’N 2006) (providing that, as long as the fiduciary acts in the best interests of the principal, the fiduciary is not subject to liability).

337. See, e.g., J.A. *ex rel.* Atkins v. Ja-Ru, Inc., No. 08 Civ. 3640 (DAB)(KNF), 2011 WL 990167, at \*2 (S.D.N.Y. Mar. 15, 2011) (“A court’s role in reviewing a proposed infant compromise is to ensure the settlement is ‘fair and reasonable and in the infant plaintiff’s best interests.’” (quoting Edionwe v. Hussain, 777 N.Y.S.2d 520, 522 (N.Y. App. Div. 1996))).

338. See, e.g., Stahl v. Rhee, 643 N.Y.S.2d 148, 153 (N.Y. App. Div. 1996) (“In a case where reasonable minds may legitimately differ, the judgment of the infant’s natural guardian should prevail.”).

339. See, e.g., Parham v. J.R., 442 U.S. 584, 602 (1979) (explaining that the law has historically recognized that “natural bonds of affection” result in parents acting in their children’s best interests); *Atkins*, 2011 WL 990167, at \*3 (giving “significant [judicial] deference” to the infant–plaintiff’s mother regarding what settlement proposal was in the best interests of her son).

340. See *Smith v. Van Gorkom*, 488 A.2d 858, 872 (Del. 1985) (observing that “[t]he business judgment rule exists to protect and promote the full and free exercise of the managerial power granted to Delaware directors”).

would substitute more dominating judicial review for less dominating fiduciary decision making. Accordingly, courts may safeguard liberty most effectively in these contexts by giving fiduciaries a wide berth and interceding only when beneficiaries present clear and convincing evidence of abuse or neglect.<sup>341</sup>

What if a decision has not been entrusted to a fiduciary's discretionary judgment, but the fiduciary possesses expertise that is relevant to the inquiry and superior to that of the court? Consider, for example, the case of a corporate director who is accused of failing to pursue her corporation's best interests in good faith.<sup>342</sup> Courts are usually poorly equipped to second-guess a corporate director's testimony that she actually believed in good faith that her actions would advance the corporation's best interests.<sup>343</sup> In such cases, the republican theory counsels that courts should offset their own capacity for arbitrary interference by according respectful consideration to a fiduciary's judgments. But courts should not retreat too far. At a minimum, they should require a corporate director to demonstrate that her decision-making process was not unreasoned, uninformed, patently irrational, or intentionally or recklessly indifferent to the corporation's interests. As the Delaware Supreme Court has explained, "[t]he presumptive validity of a business judgment is rebutted in those rare cases where the decision under attack is 'so far beyond the bounds of reasonable judgment that it seems essentially inexplicable on any ground other than bad faith.'"<sup>344</sup> By placing the burden on a fiduciary to articulate a nonarbitrary rationale for her decisions, courts can protect beneficiaries from being dominated by their fiduciaries while simultaneously minimizing their own capacity to exert alien control over the fiduciary relationship.

Conversely, when neither of the two considerations favoring deference applies, courts should not hesitate to enforce fiduciary law's "unbending and inveterate" conduct rules without according any special deference to the fiduciary.<sup>345</sup> De novo review is the appropriate standard, therefore, when evaluating whether a trustee or corporate director has engaged in fraud or

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341. See, e.g., *In re Beidel Estate*, 13 Pa. D. & C.2d 29, 31 (Pa. Orphans' Ct. 1958) ("It is . . . the task of the guardian in the performance of its duties to determine whether a proposed expenditure is necessary for the care, maintenance or education of the minor. The Court should not be asked to perform the guardian's function.").

342. See, e.g., *In re Walt Disney Co. Derivative Litig.*, 906 A.2d 27, 66–67 (Del. 2006) ("A failure to act in good faith may be shown . . . where the fiduciary intentionally acts with a purpose other than that of advancing the best interests of the corporation . . ." (quoting with approval *In re Walt Disney Co. Derivative Litig.*, 907 A.2d 693, 755 (Del. Ch. 2005))).

343. See, e.g., *In re PSE & G S'holders Litig.*, 801 A.2d 295, 315 (N.J. 2002) (accepting board member testimony denying any negligence in the absence of contradictory evidence).

344. *Parnes v. Bally Entm't Corp.*, 722 A.2d 1243, 1246 (Del. 1999) (quoting *In re J.P. Stevens & Co., Inc. S'holders Litig.*, 542 A.2d 770, 780–81 (Del. Ch. 1988)).

345. *Meinhard v. Salmon*, 164 N.E. 545, 546 (N.Y. 1928).

self-dealing in violation of their duty of loyalty.<sup>346</sup> Such matters are not entrusted to a fiduciary’s discretionary judgment, and judges are better qualified to resolve them in a nonarbitrary manner. Hence, *de novo* review of these issues is the best approach for minimizing overall net domination.

Determining the optimal degree of separation between fiduciary law’s conduct and decision rules is obviously a very complex, context-sensitive challenge that this Article cannot fully work out in the limited space that remains.<sup>347</sup> For present purposes, the critical point to appreciate is simply that the republican theory offers resources for tackling this problem. In particular, it underscores that judicial standards of review must account for the comparative threats that fiduciary power and judicial power pose to freedom from domination. Although the republican theory affirms that fiduciary law’s uncompromising conduct rules are genuine legal obligations, it supports deferential decision rules in many settings to ensure that judicial review does not increase overall, net domination in the fiduciary relationship. The republican theory thus clarifies how legislatures and courts should design judicial standards of review to maximize freedom from domination.

## Conclusion

Fiduciary law is predicated on the idea that “[n]o man can serve two masters”: “the same person cannot act for himself, and at the same time, with respect to the same matter, as agent for another, whose interest might be in conflict with his’; nor can he be allowed to profit by his own wrong, even if such be only constructive wrong.”<sup>348</sup> For nearly three centuries, jurists throughout the common law world have tried to justify this fundamental precept based on classical liberalism’s vision of freedom as noninterference, arguing that fiduciary law serves a prophylactic function, deterring fiduciary self-dealing and redressing the material harm caused by fiduciary opportunism. Yet, as scholars who operate within this tradition have begun to recognize, classical liberalism does not offer a particularly compelling justification for preventing a fiduciary from serving two masters—her beneficiaries and herself—in transactions where both sides demonstrably

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346. See, e.g., *Scrushy v. Tucker*, 70 So. 3d 289, 312–13 (Ala. 2011) (holding that Delaware’s business judgment rule does not apply to fraud or other illegal activity).

347. I take up this challenge in a forthcoming essay. See Evan J. Criddle, *Fiduciary Law’s Mixed Messages*, in *RESEARCH HANDBOOK ON FIDUCIARY LAW* (Andrew S. Gold & D. Gordon Smith eds., forthcoming 2018).

348. *City of Minneapolis v. Canterbury*, 142 N.W. 812, 814 (Minn. 1913) (quoting *Stone v. Bevans*, 92 N.W. 520, 520 (Minn. 1902)); see also *Pepper v. Litton*, 308 U.S. 295, 311 (1939) (stressing that a director “cannot by the intervention of a corporate entity violate the ancient precept against serving two masters”).

stand to profit.<sup>349</sup> Nor can classical liberalism credibly explain why constructive trust and disgorgement are appropriate remedies for fiduciary disloyalty. Viewed purely from the perspective of classical liberalism, therefore, it is tempting to dismiss fiduciary law's signature features as outdated relics of equity's *Bleak House* era.<sup>350</sup>

This Article has explained why the classical liberal critique of traditional fiduciary duties and remedies is unpersuasive. Fiduciary law's unique structure reflects a republican commitment to freedom from domination. Fiduciaries are not entitled to serve two masters—their beneficiaries and themselves—because fiduciary power would compromise beneficiaries' liberty if it were not exercised for their exclusive benefit. When fiduciaries engage in conflicted transactions without their beneficiaries' informed consent, they may or may not *harm* their beneficiaries' material interests, but they always *wrong* their beneficiaries by treating their office as an instrument for advancing their own unilateral interests in breach of the trust reposed in them. The traditional fiduciary remedies of rescission, constructive trust, and disgorgement are perfectly suited to rectify this kind of wrong and thereby eliminate the domination that would otherwise plague fiduciary relationships. Fiduciary law thus safeguards liberty in relationships of trust and confidence by empowering private parties and emancipating them from domination.

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349. See Langbein, *supra* note 77, at 934–35 (disputing Bogert's assertion that “[i]t is *not possible* for any person to act fairly in the same transaction on behalf of himself and in the interest of the trust beneficiary”).

350. See *supra* note 128–30 and accompanying text.