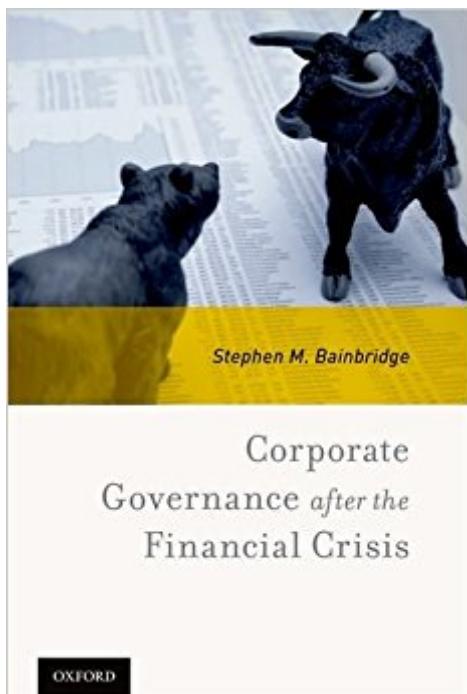


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Corporate Governance After The Financial Crisis



Synopsis

The first decade of the new millennium was bookended by two major economic crises. The bursting of the dotcom bubble and the extended bear market of 2000 to 2002 prompted Congress to pass the Sarbanes-Oxley Act, which was directed at core aspects of corporate governance. At the end of the decade came the bursting of the housing bubble, followed by a severe credit crunch, and the worst economic downturn in decades. In response, Congress passed the Dodd-Frank Act, which changed vast swathes of financial regulation. Among these changes were a number of significant corporate governance reforms. Corporate Governance after the Financial Crisis asks two questions about these changes. First, are they a good idea that will improve corporate governance? Second, what do they tell us about the relative merits of the federal government and the states as sources of corporate governance regulation? Traditionally, corporate law was the province of the states. Today, however, the federal government is increasingly engaged in corporate governance regulation. The changes examined in this work provide a series of case studies in which to explore the question of whether federalization will lead to better outcomes. The author analyzes these changes in the context of corporate governance, executive compensation, corporate fraud and disclosure, shareholder activism, corporate democracy, and declining U.S. capital market competitiveness.

Book Information

Paperback: 308 pages

Publisher: Oxford University Press; Reprint edition (March 24, 2016)

Language: English

ISBN-10: 0190496673

ISBN-13: 978-0190496678

Product Dimensions: 9.2 x 0.9 x 6.1 inches

Shipping Weight: 15.8 ounces (View shipping rates and policies)

Average Customer Review: 3.0 out of 5 stars 1 customer review

Best Sellers Rank: #1,694,503 in Books (See Top 100 in Books) #111 in Books > Law > Business > Banking #619 in Books > Law > Business > Corporate Law #4048 in Books > Law > Administrative Law

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"Stephen Bainbridge is not only an expert on corporate governance and an academic whose ideas and writing have changed the way we think about corporations. Professor Bainbridge is also one of the most perceptive academic commentators on the federal government's regulation of corporate

governance. In *Corporate Governance after the Financial Crisis*, Professor Bainbridge has written an important book for those seeking to understand the theoretical and practical implications of Dodd-Frank, Sarbanes-Oxley and the federal government's foray into corporate regulation. It is a book that for years to come will influence the controversial debate over the federal regulation of corporate governance." --Professor Steven Davidoff N.Y. Times "Deal Professor" "In this important work, Stephen Bainbridge exposes the flaws in the modern notion that corporations should be treated as little democracies, and shows how this erroneous idea influenced the framing of both the Sarbanes-Oxley Act and the Dodd-Frank Act. If there is ever to be a repeal or significant modification of the corporate governance provisions in these destructive laws, it will be driven by the scholarly work in this book." --Peter J. Wallison Arthur F. Burns Fellow in Financial Policy Studies American Enterprise Institute "Stephen Bainbridge's outstanding book, *Corporate Governance after the Financial Crisis*, is a 'must read' not only for corporate scholars, but also (and perhaps more importantly) for federal policy makers. Professor Bainbridge incisively peels away the layers of the onion that encapsulate the complex issues lying at the heart of corporate governance and principles of federalism. This superb work cogently reveals the policy reasons why corporate governance must continue to be purely a matter of internal affairs of the states of incorporation. He argues convincingly why crisis-driven paroxysms of federalization of corporate governance (epitomized by Sarbanes-Oxley and Dodd-Frank) are wrong-headed and must continue to be vigorously resisted at the state and federal levels." --The Honorable E. Norman Veasey Senior Partner, Weil, Gotshal & Manges LLP and former Chief Justice, Delaware Supreme Court "Bainbridge summarizes a wide variety of empirical evidence and gives clear explanations of all relevant legalese...It is extremely well researched, thorough, and persuasive in concluding that the federalization of corporate governance facilitated by Sarbanes-Oxley and Dodd-Frank constitutes 'quack corporate governance regulation.'" --J. Fitzpatrick, SUNY Fredonia Choice, July 2012"Professor Stephen M. Bainbridge's *Corporate Governance After the Financial Crisis* presents a cogent discussion of the congressional and regulatory reaction to two significant economic crises within the past decade and the unprecedented federal expansion into the traditional state bulwark of corporate law that resulted...For those trying to understand the state of corporate governance regulation today and the key debates and tensions that are at work, Bainbridge's book is a must read." --Holly J. Gregory & Rebecca C. Grapsas, Texas Law Review

Stephen M. Bainbridge is the William D. Warren Distinguished Professor of Law at UCLA, where he teaches Business Associations, Advanced Corporation Law and a seminar on corporate

governance. He has also taught at Harvard Law School as the Joseph Flom Visiting Professor of Law and Business, La Trobe University in Melbourne, and at Aoyama Gakuin University in Tokyo. In 2008, Professor Bainbridge received the UCLA School of Law's Rutter Award for Excellence in Teaching. Also, in 2008, he was named by *Directorship* magazine to its list of the 100 most influential people in the field of corporate governance. Professor Bainbridge is a prolific scholar. He has written over 75 law review articles which have appeared in such leading journals as *Harvard Law Review*, *Virginia Law Review*, *Northwestern University Law Review*, *Cornell Law Review*, *Stanford Law Review*, and *Vanderbilt Law Review*. His most recent books include: *The New Corporate Governance in Theory and Practice* (Oxford University Press, 2008); *Securities Law-Insider Trading* (2nd ed., 2007); *Business Associations: Cases and Materials on Agency, Partnerships, and Corporations* (6th ed., 2006) (with Klein and Ramseyer); *Agency, Partnerships, and Limited Liability Entities: Cases and Materials on Unincorporated Business Associations* (2nd ed., 2007) (with Klein and Ramseyer); *Agency, Partnerships & LLCs* (2004); *Corporation Law and Economics* (2002). Professor Bainbridge currently serves on the American Bar Association's Committee on Corporate Laws and on the Editorial Advisory Board of the *Journal of Markets and Morality*.

Prof. Bainbridge's book is a pleasure to read. As usual, he writes clearly and elegantly. And much can be learned about corporate governance in the U.S. But the reader should know that this book is mainly in the nature of a polemic, rather than a dispassionate analysis. Prof. Bainbridge has long supported a director-centric, rather than a shareholder-centric, theory of the corporation. He reminds us that the Board of Directors has three functions (1) monitoring management (2) helping manage the corporation (3) relations with the outside world, including networking, finding resources, and so on. It is pretty clear that he thinks monitoring is a secondary role, subordinate to managing. Indeed, too intense monitoring constrains Directors' discretion, and hampers their ability to help manage the corporation. As a result, he thinks that independence of directors is over-rated, that the roles of CEO and Chairman of the Board can profitably be combined, and so on. Shareholder activism has no role in this model: Shareholders get to endorse the slate of directors that they are presented with, and collect dividends (if the Board feels like declaring them) and that's it. It follows that Prof. Bainbridge finds that most of the corporate governance reforms in Sarbanes Oxley and in Dodd-Frank are wrong-headed and counter-productive -- "quack corporate governance". They are trying to beef up the monitoring function -- and it doesn't need beefing up. Along the way, Prof. Bainbridge does refer to many empirical studies both supporting and opposing his position. But I think that he is overly

kind when evaluating studies that support him, and overly harsh on opposing studies. Finally, he does not hesitate to make a big deal of anecdotes. For example, independence of the audit committee is over-rated -- after all the chair of Enron's audit committee was an accounting professor at Stanford, and that didn't help. Now I share the view that Sarbanes-Oxley was not a success, and that Dodd-Frank is unlikely to be. Both statutes are at once much too detailed and too vague. But that just tells me that we haven't found a solution yet. It does not tell me that we don't have a huge, huge problem at the heart of corporate governance.

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