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Klaus J. Hopt / Gunther Teubner

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Foreword

This book on Corporate Governance is an attempt to learn from confrontation. In the pages that follow, we confront different intellectual approaches to private government with each other for the purpose of mutual enrichment. This confrontation occurs in three dimensions: first, as an exchange of diverse national experiences, notably in the form of comparative studies; second, as a debate between diverse theoretical and ideological approaches; and third, as a comparison of concepts and models developed in different disciplines, undertaken here by means of interdisciplinary cooperation. We expect that in all three dimensions this volume will contribute to the international discussion on these topics.

As for the exchange of different national experiences with corporate governance and specifically with corporate social responsibility, the volume represents a European as well as a transatlantic enterprise. This permits a confrontation between the European structural approaches to corporate governance and the American liability approach. Here, we can only allude to the multitude of national approaches: mechanisms based on disclosure, concepts of fiduciary duties, co-determination, outside representation, and governmental controls. To be sure, a transplantation of one national approach to another country is not easily achieved, since the various approaches to corporate social responsibility are intimately connected to national economic and social structures and to political and cultural traditions. However, it might still be possible for each country to learn something from the others: with each country avoiding misjudgments made, or implementing, where feasible, ideas developed in other countries by carefully adapting the diverse national experiences to their own particular institutional traditions.

Corporate social responsibility is an excellent vehicle for demonstrating the multitude of diverse theoretical and ideological approaches to corporate governance. The contributions to this book reveal a whole range of competing and conflicting theoretical and ideological positions. The critical question is, whether beyond a benevolent pluralist tolerance – if not to say indifference – toward one another a dialogue might be possible which would permit translation from one theory language to the other, thereby avoiding a frontal clash of seemingly insurmountable ideological differences. The diverse theoretical approaches selected here can be represented by the social mechanisms on which they primarily rely: market-mechanisms with duties, liabilities and disclosure as their legal prototypes, state-interventionist controls, and decentralized participatory mechanisms. The interesting point is that many of the contributors to this book do not advocate adherence to pure models, but rather incline toward innovative combinations of different mechanisms for the control of corporate behavior. We see in this tendency good prospects for ongoing developement and unconditional and frank dialogue, which we need today more than ever.

The third, perhaps the most important and probably the most difficult confrontation is that between different disciplines, mainly law, economics, sociology and political science. It is interesting to note that all those disciplines have contributed considerably to the debate on corporate social responsibility, with an astonishingly similar perspective, i.e. a common goal of designing institutional devices which are geared to increasing the responsiveness of economic organizations. However, there exist at present only exceptional cases in which an attempt is made to transfer theoretical insights, empirical research results, conceptual constructs and institutional designs from one field to the other. In this book, several contributions attempt to achieve this transfer. The authors ask certain key questions time and again: What are the normative (political and legal) implications of a theoretical construct in the social sciences? How can economic or social strategies be translated into legal norms? What are the social and economic consequences of certain legal and institutional changes? What are the theoretical concepts underlying legal doctrinal considerations?

All in all, we do not think that a synthesis made up out of these differences of opinion is feasible or even desirable. The ambition of our enterprise is more modest. Much is gained if a simple transfer of knowledge – or better, a transfer of educated guesses – enriches argumentation in different fields with the goal of reinserting theory into social reality, in a plurality of social experiments for increasing the responsiveness of economic institutions.

The substantive topic of this book – corporate governance – is a key problem of the 1980's. To be sure, the topic is as old as the corporation itself; moreover, a thoroughly modern discussion on corporate power had been held already in the second half of the last century between politicians, lawyers and economists. It is nonetheless remarkable to see the revival of the topic in the past several years, not just in a few countries, but internationally as well, and not only among lawyers, but also in other disciplines as well as in the more general public.

This renewed attention and interest has many roots. The strongest may be an increased awareness of market failures at the same time as the regulatory crisis, and an increasing appreciation of other values than mere economic profit. Another, though more symptomatic one, is represented by a series of widely known corporate scandals such as the foreign bribery cases, the Love Canal episode, the Nestlé milk story and others. Furthermore, the stiffer economic situation in the 1970's led to dramatic corporate difficulties and outright failures, even of big corporations and highly reputed banks. These affairs did not only disclose grave managerial mistakes, but also improper activities of directors and other top corporate executives. This resulted in a host of civil, criminal and bankruptcy proceedings and, beyond the single cases, in a wave of governmental and private studies in different countries, which shed new light on the already well-known reality of corporate impact and power.

In the *United States*, Edward S. Herman, Professor of Finance at the Wharton School, came up with his study on "Corporate Control, Corporate Power" for the Twentieth Century Fund of which the late Adolf A. Berle was the long-time chairman. One of his findings was that the power of government to restrict or limit corporate action is generally exaggerated. In *West Germany*, the Monopolies Commission has collected data about the relevance of interlocking directorates, the influence of banks on governing boards, and the economic concentration of corporations, and a Comission to Study the Reform of Enterprise Law presented a lengthy report after many years of work. In *France*, Sociologists have discovered for the French scene how French corporate governing boards recruit themselves and how corporate decision-making is quite independent from the influence of shareholders, outside directors and the State, even in nationalized companies – which for France seems to be quite shocking. In *Great Britain*, Professor Gower has been given the responsibiliy by the Government to take a new look into investor protection. In *Switzerland* and other countries the overhauling and remodeling of the Corporation Acts are under way.

While renewed interest in the topic of corporate governance is common in all of these countries, the policies implemented or advocated by them are vastly different. One idea, more along traditional lines, is to increase further the legal requirements imposed on the behaviour of directors. This approach seems to be pursued with more verve in the United States than elsewhere. One reason for this may be linked to the development of the concepts of trust and fiduciary responsibility in Anglo-saxon law, and their strict application in the United States to corporate law, directors and shareholders. The absence of this concept from continental law beyond mere principles of agency has been a major handicap for German and other continental corporation law as they attempt to get a grip on the specific problems of modern public corporations. The refinement of definitions of the director's duties of care and loyalty, the requirements of disclosure and the attention given in American law to conflicts of interest are extraordinary. All this is bolstered by ingenious – as well as controversial – means of enforcement such as the shareholder's derivative suit, or procedural devices such as the quorum litis. The concept of trust leads naturally to the question: "Trustee for whom?", which may be one of the reasons why the American discussion on corporate and director's responsibilities to others than the shareholders becomes especially broad and rich. This is not to diminish the importance of the field of investor protection, but rather opens new perspectives for it. Investor protection then is to be seen as not contrary to, but as a part, and even an important part, of corporate social responsibility. Together with this systematic realignment goes a new function: experiences with devices for investor protection may teach lessons for dealing with corporate social responsibility, and the concern about directors' conflicts of interest becomes now even more acute, for the sake of investors as well as of other members of the organization and of a more general public.

In France and Belgium, where this particular tradition of trust law is lacking, another interesting instrument has been developed of late: the "*action en comblement du passif*", a legal proceeding for repayment of the corporate deficit. This action can be brought against directors of a bankrupt company and may result in holding them personally liable in the case of their clear negligence (whatever that may be) not only for specific damages, but for all or part of the corporate deficit. The underlying idea is that under certain conditions the real corporate actors should not be able to claim "the privilege of incorporation with limited liability", but should be required to back up their actions with their personal wealth. In different legal contexts this basic idea can also be found in English and German corporate law. In a number of the countries the approach is to make changes not only with a view to this last stage of enterprise failure, but to try to set up certain structures in the decision-making process itself which may then result in an improvement of corporate responsibility. Especially Germany, but also Sweden and the Netherlands, have introduced far-reaching systems of labour co-determination in the boardroom. While co-determination may result in individual conflicts of interest, it is expected that on the whole it will appease ideological conflicts between capital and labour and help to integrate labour into the processus of running the enterprise efficiently, all in the best interests of the society at large, and not just those of the shareholders. How realistic an evaluation this may be, and whether the actors in the German situation – especially the German trade unions – are really as different from other countries as is sometimes maintained, will certainly be a topic of further discussion. For the moment we want simply to stress this difference in approaches, which is also reflected in the different parts of this volume.

However, apart from all differences in theory, ideology and policy recommendations, there is one line of thought which in one way or another, many of the contributors to this volume in common: It is an explicit or implicit shift from a merely substantive to a more procedural orientation in the institutionalizing of corporate social responsibility. As the example of co-determination shows, a new structural approach using worker representatives has been used to change the boardroom. Co-determination law turns out not only to change the distribution of power and influence within the corporation but also tends to modify the goal structure of the organization itself. The so-called "profit test" is no longer the only normative touchstone of this organization. Since the corporate structure has lost a clear-cut guide-line, the law itself cannot be labelled any longer as merely result-oriented, if one has in mind an outcome which is dependent on the negotiating process within intra-organizational decision-making on the board level. But a new function of law – beyond traditional formal law and substantive law – is emerging, a function of shaping the negotiation processes among conflicting interest groups. The formulas are "consensus through dialogue" or "negotiation in the shadow of the law".

The contributions to this volume were discussed before their finalization in a Colloquium on "*Corporate responsibility – Directors' Duties and Liabilities*" which we organized at the Law Department of the European University Institute in Florence, Italy, from April 13–16, 1983. The participants cam from various European countries and from the United States.

Unfortunately, the two colleagues invited from France and Belgium had to cancel their participation at a late date, which left the voices of these countries missing from the concert. In editing there were different choices of how to assemble the various pieces. One possibility would have been to arrange according to styles (analytical-legal, theoretical-econo-sociological). We finally opted, well aware of certain overlappings, for a more problem and response oriented sequence since we think that this facilitates the access for those who deal with these problems in the real world and, by the same token, challenges them to let themselves be engaged by multi-style and interdisciplinary efforts.

We thank here all those colleagues and friends who attended the conference and who by their contributions and participation made it a memorable and fruitful undertaking. We would also like to mention and thank Thomas Abeltshauser, Regina Etzbach, Robert Helm, Constance Meldrum, Peter Mülbert for their help in editing and Brigitte Schwab, the Publications Officer of the Institute, for coordinating the publication. Their assistance and support throughout the publication process was in invaluable.

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Gunther Teubner

Table of Contents

Chapter IV: Disclosure and Social Reporting

Chapter V: Outside Representation on the Boards: Conflicts of Interest

Annex:

Chapter I

Theoretical Framework and Legal Foundations

The Legal Development of Corporate Responsibility

For Whom Will Corporate Managers Be Trustees?

Lord Wedderburn of Charlton
London

Contents

I. Introduction

The celebrated exchange between Professors Adolf Berle and E. Merrick Dodd fifty years ago on the issue (to use Dodd's title) "For Whom are Corporate Managers Trustees?" is still central to the modern problem of corporate "responsibility" (Berle, 1931; 1932; Dodd, 1932; 1935). Twenty years later Berle himself summed up that debate by saying that he had argued that

> "corporate powers were powers in trust for the shareholders, while Professor Dodd argued that these powers were held in trust for the entire community. The argument has been settled (at least for the time being) in favor of Professor Dodd's contention." (Berle, 1954: 169).

Later writers saw these two warriors as differing largely in "emphasis" (Weiner, 1964: 1465), partly on the question whether the enforcement of such "trusts" against those in control of large corporation was practicable, especially when management seemed to have acquired its new independence. The original debate coincided of course with the advent of the "managerialist" analysis of increasingly concentrated capital aggregations, the brilliant work by Berle and Means, *The Modern Corporation and Private Property* of which the central theme

"– that ownership and control in the large corporation have been separated with effective discretionary power in the hands of the active management rather than stockholders – has become part of the conventional wisdom accepted by conservatives like H. G. Manne, liberals like R. A. Gordon and J. K. Galbraith and even Marxists like Paul A. Baran and Paul M. Sweezy" (Herman, 1981: 9).[1]

Herman's remarkable recent re-assessment of the American business corporation today has revealed that its controlling managers have indeed become (as Berle and Means (1932: 356) thought "conceivable") a separate "technocracy" firmly in control but *not* one which can ignore profit in the pursuit of status or growth, *nor* one which is wholly divorced from the stockholder interest acting, as they had predicted, as a "purely neutral technocracy". Rather it is interlocked with restricted groups of "owners" of blocks of share capital (many of them in turn corporate), part of centralised groups managing the ever more concentrated capital formations in corporate form with the privileges of limited liability. There has arisen

"an internalisation of profitable growth criteria in corporate psyches and in the rules of large managerial corporations" (Herman, 1981: 112; and see Chs. 3, 4, 6).

Twenty-five years before Herman wrote, it had been argued that the "executives" and the "rich" (including stockholders) were not two distinct groups but "very much mixed up in the corporate world of property and privilege" (Mills, 1956: 119). Some traditionalist critics rejected the complete managerial analysis because it ignored the "passive control" still enjoyed by "owners" (Beed, 1966), while radical commentators felt on similar grounds that Berle and Means had disclosed "at best a half truth" (Bottomore, 1964: 73–76; see now Pahl and Winkler, 1974: Ch. 6). "Half-truth" or not, few analysts of the corporation and the "responsibility" of those within it have since 1932 been able to ignore Berle and Means.

[1] "Acceptance" may be too strong a word for Manne (1962; see Berle's response 1962 – and Manne, 1973), though Herman cites a different work (Manne, 1965: 110–112). So too, Baran and Sweezy hardly "accept" the analysis, though they are heavily influenced by it (1966: Chs. 2, 8). The present writer has reservations concerning the concept of "ownership" ("divorced from control") in the Berle and Means thesis; but space prevents elaboration in this paper. Similar qualifications are offered by Herman (1981). But their incisive analysis of the facts was attractive to many different ideologies, including those with more authoritarian implications (Burnham, 1942).

How far managerialist capitalism sets aside profit-maximization in place of "satisfacing" of profits (Marris, 1964), or whether really "the second half of the twentieth century law and practice had developed to make profit a subordinate aspect" in such enterprises (Hurst, 1970: 110) is less important to our purpose here than the legacy bequeathed to modern company law by the two contemporaneous events: the new managerialist *description* of modern corporations, originating with Berle and Means, and the new *prescription* that those in control pursue new goals because "public opinion" would demand that the business corporation should become

> "an economic institution which has a social service as well as a profit-making function" (Dodd, 1932: 1148).

Again:

> "Most fundamental to the new picture of economic life must be a new concept of business enterprise as concentrated in the corporate organisation . . . . The control groups . . . have placed the community in a position to demand that the modern corporation serve not alone the owners or the control but all society" (Berle and Means, 1932: 352, 356; 1968: 309, 312).

This conception of wider responsibility ultimately afflicted the corporate *legal* system with a trauma from which it has not yet recovered. The object of this chapter is to examine mainly British legal developments of "corporate responsibility" (such as they are) in the setting of the much more extensive discussion in the United States and of some dimensions which are, in turn, present in the West European, but, so far, largely absent understandably from the American debate.

II. Corporate Powers in Trust?

A. The Basis of British Company Law

The fundamental model of Bristish company law – together with most comparable systems – remains that of the shareholders' "city state". When the student learns that directors must, by reason of their fiduciary duties, avoid a "conflict of duty and interest", and must always act

> "*bona fide* in what they consider, not what a court may consider, is in the interests of the company and not for any collateral purpose" (Greene M. R. *Re Smith and Fawcett* 1942: Ch. 304, 306, C. A.)

he also learns that company law understands the "interests of the company" to be, not a balance or congeries of varied economic factors, but the interests

> "of present and future members [i.e. *shareholders*] of the Company . . . [balancing] . . . a long-term view against short term interests of present members", (Milner Holland Q. C., 1954: 16 (known as "Savoy Hotel Report"); Gower, 1979: 577–578).

That means the interests of profit – albeit on a long-term basis. Moreover, directors are allowed to shed their fiduciary garb and enter the shareholders' meeting bearing the votes attached to their shares. These they may cast as rights of property.[2] At this point the British and many Commonwealth systems have remained closer to the pure doctrine – or more old-fashioned – than most American corporation laws:

"The shareholders are not trustees for one another and, unlike directors they occupy no fiduciary position and are under no fiduciary duties. They vote in respect of their shares which are property . . . to be enjoyed and exercised for the owner's personal advantage. . . . The "company as a whole" is a corporate entity consisting of all the shareholders" (per Dixon J. *Peters' American Delicacy Co. Ltd.* v. *Heath* (1939) 61 C.L.R. 451, 504, 512, Aus. H.Ct.).

That at least is still the starting point of the English law, both in precedent and statute. We return to its modern problems below. But already in 1945 it had been observed that the

"illusory nature of the control theoretically exercised by shareholders over directors has been accentuated by the dispersion of capital among an increasing number of small shareholders" [and by the] "growth of investment trust companies and of unit trusts" ("Cohen" Committee, 1945: paras. 7, 124; so too "Jenkins" Committee, 1962: para. 105).

The Berle and Means analysis had reached England *de lege ferenda.* But the five Companies Acts of 1948, 1967, 1976, 1980 and 1981 scarcely show its imprint. Their model is still the shareholders' democracy of the nineteenth century joint stock company. That no major change in this basic company law structure has occurred in Britain does not, however, derive from the indolence or ignorance of the legislature – though Parliamentary debates on our Companies Bills might well provoke that explanation. The slow pace of change has been caused by the central tension which social and economic developments have implanted in the very system of company law and practice itself. The "Jenkins" Committee in 1962 noted the "illusory" nature of shareholder control in large companies; encouraged shareholders – especially the "institutional investors" – to use their legal powers; but added:

"If directors are to manage their company efficiently they must, within broad limits, have a free hand to do what they consider best in the interests of the company" (ibid., para. 109).

But in the classical doctrine, the same "interests of the company" are the interests of the present and future *shareholders* including a balance between the varied interests of different classes. The directors' "free hand" must point in the last resort in the direction of those interests. By the completion of this circle, British company law incorporates into its model a central

[2] *Pender* v. *Lushington* (1877) 6 Ch. D. 70; even on issues affecting them as directors: *North-West Transportation Co. Ltd. v. Beatty* (1887) 12. App. Cas. 589, P. C.

obligation for the directors of a trading or industrial corporation – within the purposes for which it is founded – which is broadly a duty to maximise benefits to shareholders, i.e. to *maximise profits*. No doubt "long-term" profits allow for an eye to growth; but as Professor Gower put it in 1959:

> "Directors who subordinate the long-term interests of shareholders to those of the consumers, the nation and the employees, are likely to fall foul of the law." (The Times, 30 January, 1959, after the Savoy Hotel Report; quoted in Goyder, 1961: 20).

British law still starts there, even after the 1980's legislation.[3]

B. Berle and Means: "Managerialism" and its Critics

But the centrality – or at any rate, the ultimate dominance – of the pursuit of profit-maximization is denied by the prescriptive limb of "managerialism" as interpreted by most adherents after Berle and Means. This approach sees the "director or manager" standing

> "at the point of convergence of a number of interests involved in the operation of his firm; shareholders, employees, customers, dealers, suppliers of materials and equipment, the community at large: None of these interests is primary or overriding. The director's business is to satisfy them all . . . Profit for owners and directors (*sic*) remains one consideration and a very important one . . . But it is one among others, not a unique guiding light" (Fogarty, 1965: 8–9).

The director's "free hand" is here freed from the dominance of profit so as to conjure out of the corporate hat a rabbit fit to feed all comers.

Such new principles are the roots of a continuing crisis in the law governing British corporate responsibility, one that reaches deep into the "black letter" principles of the system. That is not only by reason of their fuzzy intellectual character. They jettison the overriding test of profit, planting the directors in a new land either helplessly lost or (some fear) rulers of all they survey. Little wonder that the classical school's answer has repeatedly been to return to profit-maximization, sometimes in words that now echo with irony:

> "Obey Friedman's law, and make a profit. That will create jobs and that is the most revolutionary concept there is" (Bradshaw, 1974: 31).

American writers who have perceived their role to be a resolute defence of the private enterprise system against Protean forms of attack that utilise the managerialist analysis have accused Berle and Means of "undermining public confidence in capitalism's arch-typical institution, the large cor-

[3] The Companies Acts 1980 and 1981 have *decreased* many dimensions of disclosure, especially "social disclosure" enforced upon companies after the Act of 1967. The issue of the "disclosure philosophy" at the heart of British company law cannot be tackled in this paper; but a return to profit orientation and away from social disclosure is apparent in the 1980's (see Wedderburn, 1981a). Voices now call for a major re-examination and abandonment of disclosure (Sealy, 1981a; 1981b).

poration" (Manne, 1971:3); and asserted that *any* responsibility for corporate officials "other than to make as much for their stockholders as possible" is a "fundamentally subversive doctrine" and could "thoroughly undermine the very foundations of our free society" (Friedman, 1962: 133). Proposals based upon appeals to the Constitution to control corporate power ("gross exaggerations", anyway) are likened to "justifying Idi Amin's regime on First Amendment grounds" (Winter, 1978: 67). More moderately: "once the profit-maximizing conception of the corporation is abandoned it is not easy to construct an attractive and logical new framework to guide and legitimate management" (Vagts, 1967: 48). To deprive the directors of the star of profit-maximization is to leave them with an "ambiguous amalgam" of guides "in carrying out their public trusteeship for the economic system as a whole" (Rostow, 1959b: 71). It is curious that the American literature does not give prominence – often does not cite – one writer who has had pervasive recent influence in Britain and other parts of Europe, one who has pushed forward the logic of the classical position. Friedrich Hayek's forty years of ideological crusade against collectivism has taken on the managerialists though he rarely deigns to cite them. He rejects popular prejudice against the "big" corporation: but he notes the real "danger":

> "So long as the management has the one overriding duty of administering the resources under its control as trustees for the shareholders and for their benefit, its hands are largely tied; and it will have no arbitrary power to benefit this or that particular interest. But once the management of a big enterprise is regarded as not only entitled but even obliged to consider in its decisions whatever is regarded as the public or social interest, or to support good causes and generally to act for the public benefit, it gains indeed an uncontrollable power – a power which . . . would inevitably be made the subject of increasing public control" (1982: Vol. III, 82).

Indeed, if this were to happen the only way to guard against the resultant dangers would be to deprive *government* "of the power of benefiting particular groups" (ibid.). As with von Mises, the defence of the market takes priority for Hayek over the powers of democratic government. The job of government is to "protect the market against encroachment" (von Mises, 1949: 239). The problem for them is that the world refuses to spin as they command, for the "markets" have had to cope with Berle and Means. But the British contributor to this debate in 1983 is compelled to confess that the star of Hayek currently shines so brightly in his country as to blind – at least for the present – the rulers and the ruled.

At the level of theory, the phillipics of Hayek and of Friedman were partly directed to answer Marxists and other radical critics. For the former, the joint stock company rendered the rentier 'owner' functionless, allowing capital to relate externally to production in contradiction to productive forces "from the manager down to the last day labourer". Resemblance to Berle and Means at this point is clear, for the capital-owner becomes a *mere* owner, "a mere, money capitalist" (Marx, 1959: Vol. III, 427–430); but the managers are still subordinated to finance capital.[4] Many writers have found defects in this schema, and the legally more sophisticated 'revisionist' attempts that followed (e.g. Kahn-Freund, 1949; 1976). They were felt, for example, to confuse capital as a social relation with rights of property *as* such; and the failure to investigate the specific effects produced by the legal-economic forms was notable, especially in the case of the limited liability company in England after 1855 (Hirst, 1979: 5; Cutler *et al.*, 1977). But all of the writers within this genre attach a social interest to the forms of organisation assumed by capital; and that assertion at least was shared by Berle and Means. In the same breath, however, they and other managerialists have tended to discover a mechanism for social responsibility within the engines of capital concentration itself, the modern corporation and its controllers.

The main strength in practical terms of the continuing classical case, however, is the absence of clear guidelines for management in any such new framework. Milton Friedman characteristically recruits even the democratic imperative to his case:

> "If businessmen do have a social responsibility other than making maximum profits for stockholders, how are they to know what it is? Can self-selected private individuals decide what the social interest is? . . . Is it tolerable that these public functions of taxation, expenditure and control be exercised by the people who happen at the moment to be in charge of particular enterprises, chosen for their posts by strictly private groups?" (Friedman, 1962: 133–134).

For Friedman – like Hayek – the solution is simple: "The Social Responsibility of business is to increase its Profits". (Friedman, 1977: 168–174).

One might reply that, tolerable or not, those who wield the power of the giant corporation do indeed today exercise all those social functions, and often transnationally at that. One of the most striking features of Herman's recent examination is the extent to which the gigantic concentrations of capital that are today's corporations have resisted governmental encroachment – both as legislator and as business competitor, leading to an "immobilization of the state", even though simultaneously "business clamors for government protection" (Herman, 1981: 185–186, and generally Ch. 5). Even so, it has to be accepted that no markers of parallel clarity to that of the profit test have yet been offered to modern management by government or by society. There is no new "consensus on a value system" (Berle, 1969: 262); "no criteria to replace the standards which the economists have painfully developed during the last century or so" (Rostow, 1959: 238).

That is at the root of legal events which appear, especially in the English courts, to be technical anomalies and illogicalities in the principles of com-

[4] This is a distinction that makes Herman's careful analysis of importance (1981: Chs. 4, 6).

pany law, above all in the responsibilities of directors and the lines of duties and rights within the enterprise. The present writer does not share the thesis that all we need to do is return to obedience to "Friedman's law". But a rejection of that 'law' cannot alone solve the problems for company law structure. Before turning further to the positive English law, however, it is convenient and instructive here to touch again upon the American debate.

III. The Social Responsibility of the Corporation: Aspects of the United States Debate

The British observer is immediately struck by two features of the recent debate about corporate "social responsibility" in the United States: first, its immense quantity and rich texture; second, the virtual absence of certain themes which are necessary constituents in any equivalent British, and perhaps European, debate. From the first he may have much to learn. From the second phenomenon he draws new questions.

A. Corporate Social Responsibility and Profit-Maximization

In all these countries, the classical school can still be found, vociferously asserting profit-maximization, sometimes condemning the very idea of social obligations for the private sector corporation as "pure and unadulterated socialism" (Friedman, 1972: 177). But it is more commonly thought that "all – except the most devout free market economists – embrace the notion of *some* social responsibility, in the sense of incurring uncompensable costs for socially desirable but not legally mandated action" (Brudney, 1982: 604–605). The question is how much and when? Already in 1957 it was said" there can be no return to laissez faire"; on the new technocracy of managers could be built the business "conscience" that would serve all interests by "the best possible series of compromises" (Hamilton, 1957: 166, 138). "The modern corporation is the soulful corporation" (Kaysen, 1957). For Berle himself the emergence of the corporate "conscience" was, at this period of his thinking, the final answer (Berle, 1954; 1959).

Even the supporters of the Friedman ethic frequently, on inspection, allow for elements of corporate action inspired by "social responsibility", fitting them into the jig-saw of profit-maximization as just another "social cost": "engaged in for good business reasons and merely claimed as corporate altruism" (Manne, 1973: 722; Manne and Wallich, 1972: 4–6). Similarly, those ranked as exponents of non-profit "social obligations" often dilute their case by suggesting that in community service, philanthropic enterprises, or employee and environmental concerns, the corporation's acts would "produce long-term benefit for the firm and its stockholders" and "experiment with some relatively cost-free ways of meeting social norms" (McKie, 1974: 14). *Quibus dictis cadit quaestio.* That too has been the customary British route to a gentlemanly silence on the problem. So too, others saw "social expenditure" as "necessary" for the corporations, making them less vulnerable to takeover at the hands of "Ethical Investors", who were alleged to be concerned with corporate policies on pollution, black workers, training programmes and the like.[5] Others found "corporate altruism" to be essential for the preservation of a capitalist economic system with diversified investment (Baumol *et al.*, 1970: 39–55). Having it both ways is a natural human desire; and it may be permissible often; but not always.

The primary response of positive law was to remove major difficulties that might lie in the path of management's power to put into practice its recognition of "social responsibility", especially in respect of donations of corporate funds. Although it seems the courts will still not tolerate management's making "altruistic motives painfully explicit" to the exclusion of profit,[6] the break-through decision of *A. P. Smith Mfg. Co.* v. *Barlow* (13 N. J. 145 (1953)) established that today "conditions require that corporations acknowledge and discharge social as well as private responsibilities" (ibid., 147; appeal dismissed 346 US 861 (1953)). Thereafter the business judgment test has protected management in respect of most gifts so long as indirect benefit to the corporation could be somehow envisaged. Perhaps the last legal dam was broken when courts extended management's power by validating gifts which bore even such indirect benefit to the corporation as "providing justification" for the private enterprise system – especially if it involved young people when "a large segment of youth is alienated even from parents who are not entirely satisfied with our present social and economic system" (*Theodora Holding Corpn.* v. *Henderson*, 257 A 2d 398, 406 (1969 Del. Ch.)) – a judgment which seems to incorporate the theses of Henry Wallich. Doubts were wholly put to rest by State legislation validating traditional corporate charitable or similar contributions (Engel, 1979: 14–15, "48 States and the District of Columbia"; Blumberg, 1970: 192–202 and App. 208–210).

Although no parallel tax concessions exist on such donations, the English development, we shall see, was similar, if more conservative. But, in the United States, very large "voluntary" payments in lieu of taxes have been held valid under statute and judicial precedent, payments made out of the "self-interest" which the corporation has not only in future savings but also its "responsibility to the communities in which it was established" (*Kelly* v. *Bell*, 266 A 2d 878 (1970)). In such cases, the classical school claims

[5] Manne and Wallich (1972: 37–40, 71–74); Simon *et al.* (1971), especially at 171, where a set of priorities is elaborated.

[6] Engel (1979: 16, 51) discussing Henry Fords' activity; *Dodge* v. *Ford Motor Co.*, 204 Mich. 459 (1919).

that Berle was wrong to see the activity as "social" or "altruistic"; major industrial firms are such powerful institutionalized social forces that they will participate in social arrangements, whatever name is given to their activity (Friedman, 1957: 161–162); that "reflects a tactical judgment as to the most advantageous manner" to conduct the business in the current "climate of opinion" (Baumol, 1970: 207). Indeed, those who begin by accepting totally the legitimacy of the political and social system, seem able to give their benediction (after convoluted reasoning of no little opacity) only to a highly restricted range of "social" corporate activity – mainly to voluntary disclosure of information and voluntary observance of the law and forbearance from "interference" with certain political processes, and then only when the corporation receives a "clear signal" from a broad, social consensus (see Engel, 1979).

But the very place and "increasing importance of corporations in our lives" tells us that their dimensions have outgrown models – or, at least, prescriptions – which are restricted to this "city State" of stockholders who control managing agents for profit subject only to the rare "signal" to which by obscure osmosis those managers will, Engel tells us, respond (Stone, 1980: 1; and see Herman, 1981). The predictions and descriptions of Berle and Means themselves, of Marx[7], of Keynes[8] all foresaw concentrations of *social* power coming to be employed by the new administrators, able to "impoverish communities" and determine the fate of political and social bodies (Sommer, 1976: 872). Society now is greatly moulded by "the primacy of corporate initiatives" (Herman, 1981: 295).

B. "Managerialism" – Some Consequences in American Law[9]

To the British lawyer, interest quickens at the effect which the "managerialist" debate has had on American judges, though not always in the same direction of policy. On the one hand, judicial limits placed upon transfers of stockholders' "controlling interests" owe something to this debate. Berle's view that "control" is a corporate asset (1932: 244; 1965) failed to win acceptance. But the more elusive limits placed on the majority in such decisions as *Perlman* v. *Feldman* (219 F. 2d 173 (1955), cert. den. 349 U. S. 952), *Honigman* v. *Green Giant Co.* (208 F. Supp. 754 (1961), cert. den. 372 U.S. 941) or *Jones* v. *H. F. Ahmanson & Co.* (1 Cal 3d 93 (1969)) relate openly to these non-legal sources in formulating controllers' duties.[10]

[7] Marx, whatever else, predicted the enormous expansion of the scale of production and of concentration, and the transformation of the "capitalist" into a "manager" and the "owner of capital" – transnationally – into a "mere owner" (1959: 427, Ch. XXVII).

[8] Keynes saw "owners of capital, i.e. the shareholders" in large enterprises becoming "dissociated from the management" (1951: 314).

[9] On the position of the American law see also Teubner (infra this volume pp. 151 et seq.).

[10] See sources in Brudney and Chirelstein (1979: 594 et seq.).

So too, critical decisions on the "property" element in "corporate opportunities" and information disclose a reliance on parallel literature (e.g. *Diamond* v. *Oreamuno*, 287 NYS 2d 300, 303 (1968) citing Schotland, 1967; affirmed 24 NY 2d 494, 500–501 (1969) citing Israels, 1968). The parallel judicial debate in Britain discloses no case in which any "non-legal" sources are discussed.[11]

On the other hand, the developments in the American "business judgment" principle seem to owe much, though in more concealed fashion, to the concept of management as "independent". The recent emergence, for instance, of an "offensive" dimension to what was thought to be only a "defensive" shield is startling, especially when it leads courts to dismiss derivative suits at the behest of the business judgment of committees of "independent" directors (*Auerbach* v. *Bennett*, 47 N.Y. 2d 619 (1979); *Burks* v. *Lasker*, 441 U.S. 471, 485; *Lewis* v. *Anderson*, 615 F. 2d 778 (1979), cert. den. 449 U.S. 869). Even if the courts are willing to add their own evaluation of "reasonableness" and the validity of the business judgment (*Zapata Corpn.* v. *Maldonado*, 430 A 2d 779 (1981 Del. Sup. Ct.)) the derivative action, a major legal engine of managerial accountability in the United States – effective, in great measure, as Professor Loss has often observed "as a practical matter" (Loss, 1961–69: Vol III, 1622–1623) because of the class action and the contingency fee system combined[12] – could be at risk of extinction in that role (Coffee and Schwarz, 1981). Even so, despite the fact that many of the recent cases arose out of illegal or "questionable" payments, some voices encourage the courts to succumb to temptations to allow directorial committees to determine the fate of corporate litigation like "independent arbitrators".[13] All this is part of the courts lying back as far from interfering with management as they did twenty years ago.[14] And the treatment of directors' obligations by courts, in the 1960's had led commentators to ask despairingly whether state courts at any rate, saw them as holding their powers "in trust" at all (Israels, 1964; Marsh, 1966).

It is, in parenthesis, fascinating to observe how shocking much of this is to a system of law which has never even known the concept of "fiduciary obligation". French company law sees the equivalent of the derivative suit as within the control of each shareholder. The majority members cannot

[11] See for example all the decisions in Gower (1979: Chs. 23–26).

[12] A tiny step in a similar direction is detectable in the English courts' willingness to award costs in a shareholder's derivative action if an "independent board" would have launched proceedings: *Wallersteiner* v. *Moir* (no. 2) [1975] Q.B. 373 C.A.. See on this subject also Boyle (infra this volume p. 268 et seq.).

[13] Beyer (1982: 263–264); and on "independence" see Brudney (1982: 607–627): "miniscule likelihood" of liability in independent directors.

[14] Bishop (1972; 1968). For two possible exceptions see Brudney (1981: 614 n. 50).

obstruct its use; and any attempt by the board to block such a suit "is denied *sub silentio*" (Tunc, 1982a: 772).

As for the Securities and Exchange Commission, it is significant that one of its chairmen has departed from the classical "market" model sufficiently to say: "the large corporation has ceased to be private property – even though theoretically owned by its shareholders" (H. Williams quoted by Sommer, 1980: 215). And it is notable that two advocates of a cost – benefit appreciation of SEC administration complain that the ten-year programme to codify the crucially important securities laws may not be asking the basic question "whether the rules being codified were doing what they were intended to do" (Phillips and Zecher, 1981: 120). Are they intended to settle the pattern of powers and trust-duties of management? Or are they still addressed to the important, but different goal once graphically summed up by Loss: "I suppose a cynic might say, if you're going to run a casino, let's have an honest casino" (Loss, 1976: 70)?

Where stockholding interests of investors are involved, however, one finds no uniform acceptance in the United States of managerial independence bounded only by "business judgment". In take-overs, for example, whilst the law accepts many managerial strategies to defeat a bid, the view is vigorously advanced by some that the decision must be left to the shareholders of the target company unaffected by management which should remain "passive" (Gibson, 1981; Easterbrook and Fischel, 1981; Gelfond and Sebastian, 1980; but see Lipton, 1979). It is convenient to note that in Britain, within the City Code, directors of target companies have, if not a free hand, a very wide power to "defend" the company against a bid (Danzinger, 1983; Council for the Securities Industry, 1981: City Code, general principles 4, Rule 38).

C. Legal Avenues to Corporate Social Responsibility

Legal solutions for the responsibility conundrum are not, however, easy to find. Those aimed at making shareholder surveillance work through enhanced powers and capabilities (Eisenberg, 1976), if need be through Federal legislation[15], seem unduly limited. The "social responsibility" campaigns of the 1960's and 1970's do not suggest that adjustments of stockholders' legal powers could easily enforce new agreed norms of responsibility. Nothing that is said here is meant to detract from the very real social gains that have no doubt been derived from a determination by U.S. Steel to clean up Pittsburgh, or the placement of minority representatives on boards, or such policies as "Shell Protects the Countryside". But at a legally more institutionalised level, the well known shareholder 'social action' proposals, such as those attempting to use proxy regulations to stop produc-

[15] An emotive issue despite the careful treatment by Cary (1974).

tion of napalm for human killing by Dow Chemical (see especially Chirelstein, 1974: 54–63) or the "Campaign GM" to force public interest directors and "constituency" directors on to the board (Herman, 1981: 264–267, 257–260 on GM) or the campaigns for "ethical" investment, bans on South African involvement, efforts to stop damage to Third World Markets like the "Infant Formula" milk campaign (ibid., 268–277) – all these suggest that combined social and legal action by shareholders may win a battle but, even with new weapons, could hardly win the war to transform corporate responsibility. It must be acknowledged that American courts will recognise stockholders' concern with, for instance, the environment as "rational", and the "so-called ethical investors" (*Natural Resources Defense Council Inc.* v. *SEC*, 389 F. Supp. 689, 700 (1974)); but that does not take one very far.

On the other hand, rough-hewn schemes for "client group participation" (Eisenberg's phrase (1969: 16)), with "membership" in law extended from stockholders to employees, suppliers, dealers, and the like (Chayes, 1959: 40–45) raise the prospect of boards with multiple constituencies – and perhaps even multiple derivative actions by "employees and customers", or even "citizens' suits" (Conard, 1976: 405–406). In such a system the risk would be that courts, far from genuflecting to directors' business judgment, would be called upon to administer corporate policy by choosing between the different versions of the "reasonable balance" of interests in practice – something English judges certainly would not do, and are not equipped to do: "it is not the business of the courts to manage the affairs of the company" (per Scrutton L. J., *Shuttleworth* v. *Cox* [1927] 2 K. B. 9, 24). As Chirelstein aptly concluded:

> "The difficulty of reconstructing the framework of business law so as (1) to encourage corporate responsibility while at the same time (2) limiting management's freedom to pursue its own version of the public interest thus seems very great. Interest-group representation on company boards is perhaps the only proposal which purports to aim in both directions at once; but the problems of definition and practicability that are instantly foreseeable . . . have discouraged support . . ." (1974: 56).

Great ingenuity has, however, now gone into proposals for remodelling the American corporate structure and almost no colour in the possible spectrum seems to be missing, including the remarkable idea of "voteless" corporations (Manning, 1958). Recent attention, though, appears to have concentrated upon reforms in the composition of the board. Boards in the United States normally contain far more "non-executive" or "outside" directors than their British equivalents.[16] It was perhaps natural , that the so-called "confessional period" of 1974–1977, bringing disclosure of widespread

[16] Compare Herman (1981: 31–38); Mace (1971; 1981); Brudney (1982), with British Institute of Management (1972: Parts 1, 5); "Bullock" Committee (1977); Brookes (1979: 5–6, Ch. 2, 36–39).

corporate political payoffs, external bribery and similar scandals, saw renewed calls for more "outside" directors, "audit committees" and "public policy" committees, alongside the increased disclosure requirements of the SEC after the corrupt practices legislation of 1977.[17] Unhappily, the record on "disclosure" shows that "when the corporate interest is important enough, counterpublicity is intensified . . . and in the end, disclosure is of little more effect than an appeal to mangement's social conscience" (Herman, 1981: 280). Nor does experience with SEC disclosure used as a means of ensuring the "integrity" of management suggest any great measures of success (Ferrara, 1980).

A former Chairman of the SEC has called for more "truly independent" characters to be placed inside the board itself, in order to "monitor and change" management (Herman, 1981: 282), others for a preponderance of such "outsiders" (Neal, 1981). But experience with investment companies where such directors by law constitute 40 per cent of the board, with the variable record of independence on the part of "outside" directors – e.g. controlling questionable practices, the stifling of awkward litigation, or in other failures to "monitor" the insiders – is not encouraging (see Herman, 1981: 281–283). Indeed, Professor Brudney in his authoritative treatment of "Independent Directors" has argued persuasively that an increase in such representatives, all drawn from the same socio-economic strata as the 'insiders', is likely to have no more than a modest effect at best in making the corporation more responsive to "public needs"; and that such developments cannot, and must not, be seen as a replacement for public guidance and governmental regulation to protect the interests either of investors or of society (Brudney, 1982: 639–659 and passim). Other recent evidence suggests that members of a board are easily susceptible to "group-think" as directors, not least in multinational corporations, whatever their originating constituency (International Management, 1983), a finding which should not be forgotten when we come to consider the representation of new constituencies on boards (such as employees or consumers).

Perhaps the most idiosyncratic plan for reform of the board – and one of special interest for comparative purposes in Europe – is that put forward by Stone (1975). Diagnosing the problem of "responsibility" as capable of solution only by "intrusion" into the boardroom, largely because corporations do not respond to external legal or other stimuli, every large corporation should, he contends, have a minority of members appointed to its board by a federal agency, though they would be removable by unanimous vote (or by special majority for cause). Experience of such minority Government directors under the Communications Satellite Act 1962 or in Union Pacific Railways has not, however, been a significant success (Her-

[17] Brudney (1982: 636, 647) and SEC Reports cited. Also Coffee (1977: 1118–1278), on SEC internal tensions.

mann, 1981: 289–292); and the parallel British debate about Government-appointed directors was to a great degree snuffed out by Crosland's aphorism that

> "government nominees on a private board must either 'go native' or remain suspect, and in neither case will do their duty properly" (Crosland, 1956: 358).

Stone's other, more modest, if ingenious, proposal is for "special public directors" appointed by a court in a variety of circumstances – for example law violations of a continuing character – to promote more "thoughtful" conduct. Their "authority" would be limited to that appropriate to the situation – a proposal which is modest enough to be acceptable, if somewhat grudgingly, to the 'classical' school (Winter, 1978: 57–58). Such thinking leads naturally to a much wider questioning of the categories of "public" and "private" generally (Stone, 1982).

The most extensive plan for wholesale reform of the board along the lines of "constituency" or "client" representation has come from Ralph Nader and his associates. All large corporations should require not only a State but a Federal charter imposing a variety of employment, antitrust, and other social conditions (Nader *et al.*, 1976). This would redress the unacceptable situation where the "Constitution of the United States", which deals with so much else, "does not mention the business corporation" (Nader, 1977: 22). This debate about the "case for federal chartering" is of course a specifically American dimension to the issues. But it is not new; its pedigree "goes as far back as 1855" (Loss, 1961–1969: 107); and two decades ago critics demanded that Congress occupy the field of corporate law, left in the grip of directors by the "collapse" of state laws, "to restore the basic theory of corporate powers as powers in trust to full health and vigour" (Friendly, 1964: 86).

Each member of the nine-man board envisaged by Nader would represent an area: employee welfare; consumers; environment and community; shareholders; law-enforcement; marketing etc.; finance; planning and research; and "management". Nader is insistent that the objectives of this restructuring cannot be met by depending merely "on the social responsibility of business managers to act in the public interest", any more than U.S. Steel fully lived up to its pre-war claim to be the "Corporation with a Soul". Just as Brudney insists that voluntary reform by use of more independent outside directors is no substitute for government regulation, so the Nader school sees 'social responsibility' as merely an adjunct to a legal redesign of the board, which will "strengthen the legal rights" of shareholders, employees, consumers, taxpayers and the neighbouring community.

It is not difficult to demonstrate that Nader does not solve – scarcely addresses – the critical question of the multi-constituency board: what guidelines (other than "decency" and "reasonableness") will conduct the board to a decision on conflicting interests? It is easy to show that the traditional "fiduciary duty" – owed through the corporation to shareholders, or in the United States on occasion owed direct to the latter – could not survive intact; and that, it is said, would ironically cause the "discretion of corporate management . . . to increase rather than diminish" (Winter, 1978: 50). But that argument is only an indirect way of reasserting the priority of profit.

D. The American Debate and its European Counterpart

It is precisely at this point that the American debate seems to run into the sand – and the European debate – sparse though its thoughts are by comparison in the area so far considered – opens into fresh, if surprising pastures. The idea of a board which openly accommodates representatives of constituencies other than shareholders tends to be dismissed by scholars of different viewpoints as based on "economic naiveté", "profoundly ignorant", or even inspired by "punitive" interests (Winter, 1978: 52–53); or productive of boards that are "towers of Babel" operating by "logrolling", with goals subject to "periodic shifts" based upon "coalition bargaining" (Herman, 1981: 284–285). It is characteristic of the literature surveyed that the argument does not pause at this point to ask how far *existing* boards disclose "logrolling" of different interests, nominee directors representing sectional interests, leaning towers that sway with shifts of power in controlling groups. But those two authors – Herman and Winter – have been chosen for another reason. They, unlike many others, *do* advert briefly, though not altogether accurately, to European experience (mainly Swedish and German) on "industrial democracy". But that experience has more to offer than an assumption that multi-representational boards must be impaled on the dilemma of conflicting loyalties.

The impasse which appears to have been reached in the American debate about "corporate responsibility", for all its many intellectual riches, relates, it is submitted, to three factors, none of them *per se* virtues or vices, but elements which do distinguish the socio-economic and cultural scene in the United States from that in Britain and, to a degree, Western Europe.

First, each main school, whether it favours a Federal takeover of corporate law or not, advances its solution in order that "the competitive enterprise system can be made to work equitably and efficiently". That was Nader; but it could have been Friedman. Nader recommends his plan as "the precise opposite of socialism" (Nader, 1976: 262). In the United States government powers to appoint directors would require "a major political struggle" not likely to succeed (Herman, 1981: 294). Contrast equivalent thinkers in France. Even the apparently parallel proposals of such writers as Bloch-Lainé (1963), advocating control through three constituencies, shareholders, employees and public authorities, take on a distinctly un-American flavour when the surveillance of an independent *magistrature* is added, with a power of Government to ensure the contribution of the business to the national Plan. Such contrasts between the United States and Europe were quickly noticed in the "changing style" of post-war private enterprise economics (Shonfield, 1965: Ch. XV).

Second, though it is perhaps only a wider perception of the preceding point, the line of thought deep in Western European culture, leading to the "expropriation" of the private shareholder – not necessarily a "socialist" or even "corporatist" programme in character – whereby some system of "public" corporations is seen, in whole or in part, as an *alternative* to or development from a private "competitive enterprise system", has little place in the United States debate.[18] In the European discussions "planning" at least raises the issue of the property basis of society. Such planning as is judged necessary does not put that item on the agenda of Rostow, Galbraith or Nader, not even in the "regulated" industries of the United States.

Thirdly, varied trade union movements of Western Europe are in origin and central traditions fundamentally different from the business "labor unions" of the United States (Bok, 1971; Gould, 1982: 2–8; Kendall, 1975: Chs. 1–7; Wedderburn, 1971: Chs. 1,7; Kennedy, 1980). Not only is their density of membership and influence in the workforce as a whole generally higher than declining American unions, (with, exceptionally, "density" not rising much higher in Germany and "membership" as such not functionally comparable in France). Their culture and rhetoric – again with the arguable exception now of Germany – contains still a challenge to the basic property-relations of the societies in which they live and work. In the era since 1945 this has been the mainspring of a debate that came to be called "industrial democracy", which appears to have no real counterpart, and is infrequently understood in America. Indeed a comparative understanding of the basic differences between working-class organisations is as important to corporation law as to labour law (see Kahn-Freund, 1977; Schmidt, 1972 Ch. 1). It is therefore logical, perhaps essential, for an appreciation of "Corporate Control, Corporate Power" in the United States *not* to "address" trade unions, which have

> "made no serious effort to obtain direct control or to participate in the broad decision processes of large companies", [being] "oriented to bread and butter gains via bargaining" (Herman, 1981: 338, 288).

We note later the recent footnote exceptions to this overall picture. For the moment, it is submitted that these three factors do divide the European and the American perceptions – and not always to the advantage of either side. Just as the American lawyer finds the European debate on "industrial democracy" hard to follow, in his dreams (or nightmares) the British jurist

[18] See, e.g. Abel (1970: Ch. 11) on the United States as against Friedmann and Garner (1970), on the United Kingdom (Part 1), on Western Europe (Part 2); Posner and Woolf (1967); Shonfield (1965: Chs. V, VIII, IX).

cannot envisage one of *his* judges knowing, let alone citing, Berle or Galbraith to state – even in a dissenting judgment – such "political" propositions as:

"The modern, super-corporations, of which Dow is one, wield immense, virtually unchecked power. Some say they are 'private governments' whose decisions affect the lives of us all. The philosophy of our times, I think, requires that such enterprises be held to a higher standard than that of the "morals of the market place" which exalts a single-minded, myopic determination to maximize profits." (Justice Douglas, dissenting, *SEC* v. *Medical Committee for Human Rights*), 404 U.S. 403, 409–410 (1972)).

IV. Corporate Responsibility in Britain[19]

A. The Social and Legal Evolution of Responsibility

The essays in *The Corporation in Modern Society* (Mason, 1959) through which the up-dated Berle-Dodd debate reached a wider audience, did include a chapter from Britain. Revealingly, however, it was concerned with "The Private and Public Corporation in Great Britain", written by Crosland (1959: Ch. XIII.). That is, it was not about the managerialist debate, but about managerial similarities in "private" sector companies and "public" sector, nationalised corporations. Crosland the "democratic socialist" shared, there and in his book of 1956, the sentiments- almost the words – of Dahl (1972) that "no moral or philosophical basis" could be found for the assumption that investors had some special right to govern firms (Crosland, 1956: 356). But neither that nor his partial acceptance of the managerial analysis led him to "corporate reform":

"The shareholders who retain the sole nominal power, have little real power and the real power of the other parties in no way depends on their being represented on the Board . . .".

Real power lay in "the State"; some power with unions when the labour market allowed it; some with the "consumer"; much with directors. There was no point in changing "company law":

"if we stick to the real object, which is a certain redistribution of effective power, we see that a change in the law [of companies], logical though it might be, would make no difference to the underlying reality" (ibid., 362).

[19] It has not been possible in this paper to deal with the impact of the Stock Exchange Regulations and the Council for the Securities Industry (especially the Code on Take-overs and Mergers of the City Panel) on corporate responsibility of public companies. See Johnson (1980); Lee (1981). The requirements of the Listing Agreement and of the Code are, of course, of primary importance, but they relate mainly to "disclosure" and to equal treatment of shareholders. Within its limitations, this self-regulatory machinery tends to be criticised less than the slender administrative control which the Department of Trade can exercise by way of investigation. See Hadden (1977: Ch. 8; 1980) arguing for a "company law enforcement commission". But see the increased powers for Dept. of Trade investigations in Secs. 86–92 of the Companies Act 1981.

Crosland there gives the flavour of the British debate, though today the priorities between "planning", fiscal reform, nationalisation of industries and services and direction of investment are different for a new generation of socialists (e.g. Holland, 1975; Aaronovitch, 1981) who do not see Britain, as Crosland did then, "on the threshhold of mass abundance", able to disregard "questions of growth and efficiency" (1956: 515).[20] The battle, therefore, was about the "reality" of "*power*" – and the other side agreed. For they were concerned about the "tyranny" that *must* accompany "State planning" (Hayek, 1944; 1982; esp. Vol. III, Ch. 17); and in most respects, the latter philosophy has proved stronger today than many expected (Wedderburn and Murphy, 1983: Ch. 1). If therefore we contrast the post-war position of the classical crusaders for "shareholders' democracy", we find a clear distinction: in the United States Emerson and Latcham (1954) faced trusts and managerialism; but in Britain Hargreaves Parkinson confronted nationalisation, and instigators of "class warfare" who "set out deliberately to depress the investor class" (Parkinson, 1951: 104). The issues of power and reponsibility in Britain were more directly "political". They went to the *legitimacy* of property and of management in a qualitatively different way.

While the analysis of Berle and Means was well-known in post-war Britain and had even been incorporated into new economic theories of the enterprise (e.g. Marris, 1964), it was put to use in legal debates not about rearranging the "constituencies" in the corporate machinery (though that did come later) but about the consequences and the possibilities of their being replaced by controllers appointed by a Minister after nationalisation (Robson, 1960: Chs. VI, VIII, IX). This was another "political" issue. Two decades later, the same concepts were being critically employed to show both that "public ownership" might be preferable to "managerial ownership", but that even in such public corporations, management did not appear to be evolving any acceptable "conscience" (Sloman, 1978: 107, 148–150). By the economists Berle and Means often received almost ritual acknowledgment as they recorded a rate of concentration of capital in Britain which outstripped that of United States industry (Hart and Clarke, 1980: xi; Hannah and Kay, 1977: Ch. 1; Department of Prices and Consumer Protection, 1978: Ch. 3, Annex. A). Meanwhile a Royal Commission on Wealth (1975) disclosed that a far higher proportion – nearly 40 per cent – of shares was owned by institutional investors in Britain than in the United States (15 per cent). In 1959, institutional shareholdings had accounted for only 30 per cent in large companies (Feinstein and Revell, 1960). By 1980 it was 52 per cent in companies generally ("Wilson" Committee, 1980: para. 250 *et seq*). The "concentration" described by Berle and Means was more than evident in Britain, even if the scale of 'institutional' investment

[20] After all, Crosland like many others thought that "full employment . . . has largely cured the depression psychosis" (1956: 394).

led to modifications of their thesis of 'separation' in a manner not dissimilar to that now put forward by Herman (1981) in the United States (see King, 1977: 35–41, 197, 290–298). In 1963 private investors held 59 per cent of all ordinary shares; in 1975 it was 37 per cent and falling (Johnson, 1980: 120; Central Statistical Office, 1979). Moreover, until relatively recently, even the institutional investor in Britain was customarily rather "passive", content to let control be with directors and management; 'voting trusts' were almost unknown; and 'ginger groups' rare (Afterman, 1970: 31–33; Midgley, 1975: 60–85; Pickering, 1965: 251–263). The managerial revolution seemed complete. Even the imperial claims of a further "unseen revolution", alleged to have taken place through large shareholdings of employees' pension funds (Drucker, 1976), were shown to have few clothes by the discovery that most funds were really managed by the orthodox financial institutions (Minns, 1980); and the autonomy of the British financial sector contributed to a picture again remarkably similar to the modifications put upon Berle and Means by Herman (Longstreth, 1979; de Vroey, 1975).

Mangement certainly seemed to have achieved independent status in company law by 1960 as evidenced by the law concerning "gifts" of company assets. As in the United States, an early legal test of the new "realities" naturally arose here. The law ascribed an implied power to make donations to the trading company whenever it would derive from them direct *or indirect* benefit:

> "There are to be no cakes and ale except such as are required for the benefit of the company" (per Bowen L. J., *Hutton* v. *West Cork Rlwy. Co. Ltd.* (1883) 25 Ch. D 654, 672).

Although that requirement was thought to restrain company gifts within a "not very philanthropic garb", the understanding of "indirect benefit" was extended to legitimate gifts for educational, and, indeed any other charitable, welfare or even "political" purposes.[21] Certainly it was the practice of companies to make such donations, a large proportion of the funds going to "education, research, general social welfare and public amenities".[22] Labour Party circles complained that in 1956 industry gave over £ 3 million to re-equip the science laboratories of the independent ("public") schools which feared competition from improving State schools (Labour Party, 1957: 52). Statute later compelled companies to disclose charitable and political donations over a stated[23] amount (Sec. 19 of the Companies Act 1967). But in 1962 the courts re-entered the fray and, as so often in English company

[21] *Evans* v. *Brunner Mond* [1921] 1 Ch. 359; and see "Jenkins" Committee (1962), which said gifts to charities would be accepted by courts even where "no direct interest" to the company if regarded by businessmen as needed to "preserve goodwill" (para. 52).

[22] See the surveys in Shenfield (1969; 1971: Ch. 4).

[23] Currently over £ 200 a year.

law, placed modern limits on managerial rule by use of classical doctrine. Directors of a company gradually going out of business wished to give the proceeds of the sale of its main asset (a newspaper) to the employees becoming redundant; but the court granted an injunction to a shareholder to stop these "gifts". It was argued that although the directors' "prime duty" was to shareholders, they must also consider directly the "interests of employees in these days". To this Plowman J. responded:

> "no authority to support that proposition as a proposition of law was cited to me: I know of none, and in my judgment such is not the law" (*Parke* v. *Daily News Ltd.* [1962] Ch. 927, 963).

The gifts were, therefore, *ultra vires* the company – and a breach of the directors' own fiduciary duties to the company in their not having properly considered its "interests" (see too *Re Roith* [1967] 1 W.L.R. 432; Wedderburn, 1967).

To this it must be added that the courts have subsequently made it clear that if a company's memorandum included an *express* object to make any gifts it chose to give, no question of *ultra vires* could arise (*Re Horsley and Weight Ltd.* [1982] 3 W.L.R. 431 C.A.) unless, at any rate, the donations were not a "genuine" exercise of the power and amounted in reality to a disguised return of capital to shareholders, unauthorised by the court (*Re Halt Garage* [1982] 3 All E.R. 1016). The complexities of the interactions of the doctrines of *ultra vires*, fiduciary duties, majority shareholders' rights and maintenance of "capital" are considerable (see Wedderburn, 1983a). They reveal the tensions of courts caught in a web of legal rules based upon "shareholders' democracy" against which the social facts rebel. The judges are unwilling – or maybe in our system unable – to adjudicate such issues in the light of the "delicate questions of social policy and accountability" that are at least recognised in American cases (Wedderburn, 1962: 146). The issues are left ensnared in a tangle of technical legalism.

B. Current Legal Problems

1. The Positive Law in the Courts

Before examining other British developments further, it is worth noting some of these areas of "technical" law which directly raise the "trusteeship" issue much as Berle and Dodd envisaged it, where policy is not based in English courts on social analysis. It is unclear for example whether the *ultra vires* doctrine still prevents a company from having an object to do "every mortal thing you want"[24]; or whether creditors and members are protected

[24] It is argued that would amount to having no object at all.

by the doctrine at all (Gower, 1979: 167; *Re Introduction Ltd.* [1970] Ch. 199, 209–211 C.A.).[25]

It is from this treatment of the director as a "trustee" or "quasi-trustee", to use the dangerous terms of the older cases (*Re City Equitable Fire Insurance Co.* [1925] Ch. 407, 426) that the tensions of the British system emerge. In his handling of the corporate assets the director is truly a "constructive trustee" (*International Sales and Agencies* v. *Marcus* [1982] 3 All E.R. 551); but otherwise he is under a personal 'fiduciary duty' to the company. As Frankfurter J. insisted, to say that he is "a fiduciary", is only a beginning: "It only gives direction to further inquiry" (*SEC* v. *Chenery Corpn.*, 318 U.S. 80, 85 (1943)). Yet it is through the personal fiduciary duty that the trust was placed upon directors under the early equitable concepts, a level of duty somewhat in conflict with the need to treat them as "commercial men managing a trading concern for the benefit of themselves and all the other shareholders" (*Re Forest of Dean Coal Mining Co.* (1879) 10 Ch. D 451, 453).

It is also a duty internally fraught with tension. The old equity notions of "trusteelike" duties are strict. But the beneficiaries can by consent transform them by ratification; the shareholders can pardon the directors for many, perhaps most of their breaches of duty. In this way many 'social' or *public* elements in the rigorous pre-industrial duties of 'trust' can be removed through the wholly *private* mechanisms of the shareholders' general meeting. American courts, by measuring the limits both of duty and of ratification by greater reference to "fairness" have been able to build in a factor of even greater flexibility which can include social expectations of a wider character, demanding that controllers do not take "undue advantage" and act "fairly".[26]

That is indeed one way to resolve the difficulty involved in the treatment of directors by the law as, on the one hand, akin to trustees but, on the other, businessmen. But it does so at great expense to the fiduciary principle. The curious feature here of the private law doctrines of "trust" is their incorporation into modern company law by way of fiduciary duties which, although in positive terms owed privately to the company or sometimes (more often in the United States) to shareholders, carry within them norms relating to high ethical standards which are at least as important to society at large as to those beneficiaries. This need not surprise us if we recall Maitland's insistence that "the connection between Trust and Corporation is very ancient" (Maitland, 1936: 214). The absence of the fiduciary concept from many Continental systems creates special problems for company law

[25] Recent decisions demonstrate that Sec. 9 of the European Communities Act 1972 (enacting the First Directive of the EEC) has not settled fundamental problems of the *ultra vires* principle (Wedderburn, 1983a).

[26] *Boss* v. *Boss*, 200 A 2d 231 (1964); *Irwin* v. *Pre-stressed Structures*, 420 S.W. 2d 491, 495 (1967); *Burt* v. *Burt Boiler Works Inc.*, 360 So. 2d 327, 331–2 (1978).

and has been said to be "a serious lacuna" in French law (Tunc, 1983b: 13). That judgment reflects the public interest which suffers most from such a gap in private law. These considerations are not always heeded when "business judgment" is given precedence, in Britain or the United States, over fiduciary obligation.

No such escape route, though, has been found by the English courts from the traditional tension of the doctrines. The English fiduciary duty prohibits the director from making *any* "secret" profit from his office, even *bona fide*, and whether or not the company could have acquired an equivalent benefit (*Regal (Hastings) Ltd.* v. *Gulliver* [1942] 1 All E.R. 378 H.L.; *Industrial Development Consultants Ltd.* v. *Cooley* [1972] 1 W.L.R. 443). The duty is strict; yet, it is "trite law" that directors can seek "absolution" of their "sins" by a mere ordinary resolution in a shareholders' meeting (*Bamford* v. *Bamford* [1970] Ch. 212 C.A.; *North West Transportation* v. *Beatty* (1887) 12 App. Cas. 589 P.C.). Such "ratification" – to which English courts have clung closely in classical models of shareholders' control – is not available if the directors have acted in bad faith or taken "money, property or advantages" belonging to the company or defrauded the minority in that respect (*Burland* v. *Earle* [1902] A.C. 83, 93 P.C.), in which case the minority shareholder is afforded the right to bring a "derivative action" (*Wallersteiner* v. *Moir* (No. 2) [1975] Q.B. 373 C.A.). But in respect of breach of fiduciary duty standing alone the minority shareholder has no *locus standi* by reason of the "Rule in *Foss* v. *Harbottle*", because here it is for the majority to decide whether to take action (Wedderburn, 1957); and in the large corporation that means that the directors – proxies and all – are usually safe. None of the efforts of commentators to make sense of this jungle of case law has really succeeded (see Gower, 1979: 23–26; Beck, 1974; 1975; Prentice, 1976: 65; Wedderburn 1957; 1978a), not least in regard to the question whether *all* corporate "opportunities" or "information" become "property" belonging to the company. As in the United States the answer to that question involves deep social policy choices.[27] But none of that has found a place in the British discussion. Indeed the English-style approach may allow the shareholders to approve even prospectively serious breaches of duty (*Winthrop Investments Ltd.* v. *Winns Ltd.* [1975] 2 N.S.W.L.R. 666). So dominant, however, is technical principle in our company law that the habit has now grown up of authors making merely a token reference to Berle and Means, and then passing on to resume the technicalities.[28] For American courts

[27] The issue is especially important for the large "public" company, which should probably be treated separately as demonstrated by Brudney and Clark (1981).

[28] See for a remarkable recent example Shepherd (1981: 360) on trading in "corporate control", an area where some of the social facts and American literature are normally used by British lawyers to advocate a return to "shareholder control" (Pickering, 1965: 272–275).

"it is no longer seriously debated that majority stockholders owe a duty to at least act fairly to the minority interests and the majority cannot avoid that duty merely because the action taken is legally authorised" (*Burt* v. *Burt Boiler Works Inc.*, 360 So 2d 327, 331 (1978)).

Such a general principle allows not only for relaxation of technical barriers (such as, in that case, stockholder ratification); it could also permit consideration of some social factors within the model of corporate responsibility.[29] Despite the efforts of leading commentators to commend it (e.g. Gower, 1979: 625–630; Beck, 1975), no such general principle has overtaken English law (Joffe, 1977). American courts apply their freedom, it seems, in a way that offends those who see departure from certain standards with a *public* content as unsatisfactory – the "race for the bottom" of the State corporation laws (Cary, 1974) – as opposed to those who prefer maximum "yield to shareholders generally" albeit at the cost of "self-dealing or mismanagement" (Winter, 1978: 15). A functional justification of the move from strict trustee-like duties to a "fairness" standard is found by some in that the trustees'

"economic function is . . . wholly dissimilar to that performed by corporate management . . . Trustees do not maximize profit in the context of the competitive market. They do not concern themselves with innovation in products . . . Most important trustees need not fear that beneficiaries may sell their interest to entrepreneurs who will install new trustees . . ." (Winter, 1978: 33)

This school of thought may paint a somewhat academic "shareholders-market" picture, one that appears to reflect reality no more accurately by reason of having become fashionable. American courts, moreover, may not have settled such issues. But in Britain there is not even any equivalent debate. Indeed, despite its background of equity and trust law, the British debate about company law has hardly appreciated the need for any "public interest" element – or even an overall market assessment – in approaching majority and minority 'private' corporate rights. That is one reason why no-one has any idea even now what the legislature "meant" when it told the courts to protect minority shareholders from "oppression" (Sec. 210 of the Companies Act 1948) or, now, "unfair prejudice" (Sec. 75 of the Companies Act 1980). In Britain, internal responsibilities in the corporation, with new patterns of rights between controllers and the minority shareholders, require a framework of overall norms for corporations in society, one which appears to be attainable only by or through Parliament. Yet such issues are barely confronted even in the ragged discussion of "self-regulation" by City institutions.

Again British courts suffer perplexity on the question: who controls corporate litigation? As we have seen in touching on the "offensive" use of

[29] E.g. how far doctrine should be modified in the face of a "family-type" corporation in respect of corporate opportunities (*Sladen* v. *Rowse*, 347 A 2d 409 (1975)).

the business judgment principle, this is of current interest in the United States. In Britain management enjoys its powers to manage not by reason of statute but because in the "contract" constituted by the articles of association the shareholders have "agreed" not to interfere with the exercise of their delegated management powers (*Automatic Self-Cleansing Filter Syndicate Co.* v. *Cunninghame* [1906] 2 Ch. 34 C.A.). So the question whether particular articles, giving management the right to "manage", gives the right to use the corporate name in litigation to the directors or leaves it with the shareholders' meeting has caused great anxiety and no clear approach in modern cases. The nature of the problem can be judged when we espy a judge as robust as Megarry V.C. in one case deliberately avoiding the whole issue, with the comment: "there are deep waters here" (see Wedderburn, 1976: 329; *Re Argentum Reduction (UK) Ltd.* [1975] 1 All E.R. 608, 610) but in another prepared severely to curtail majority shareholders' rights (*Estmanco (Kilner House)* v. *G.L.C.* [1982] 1 W.L.R. 2). The problem of "control of corporate litigation" has revived the question in British law whether management's right to manage – currently resting rather quaintly on a pre-managerial consensual theory – ought to be stated in statute. Oddly, that problem has received greatest attention in the debate about "industrial democracy"; for in any statutory scheme for new corporate constituencies, powers of management would have to be dealt with by the legislation. Once again, the public interest factor in the issue is obvious; but there is no route by which that can come into the courts' considerations. Some would say it should not because, given their training, English judges, though highly skilled technicians, are not socio-legal craftsmen. That, however, even if accurate, seems a counsel of despair.

2. *Uncertainties in the Legislation*

Nor has Parliament had an intelligible policy in modern British company law in respect of such matters. Traditionally it clung to a system of shareholders' control plus disclosure in order to ensure that management maintained unstated levels of behaviour which all gentlemen were no doubt expected to understand. But when it supported the former by an absolute statutory right for a simple majority of shareholders to dismiss directors (Sec. 184 of the Companies Act 1948) Parliament must surely have known about the ways in which directors of companies of any size normally have little to fear from shareholders' meetings – especially with our proxy arrangements. In the 1960's Parliament did begin to realise that mere disclosure by directors would not satisfy modern social standards. But the failure of nerve of the "Jenkins" Committee on company law reform[30] helped to stunt the growth of the law.

[30] As a result it not only rejected disclosure of individual director's fees – contrary to "the traditions of this country" – but generally refused to consider the "broader economic and social" problems (Wedderburn, 1965: 4, Part 4).

Take directors dealings in their company's securities. Disclosure has long been required, but the extent of disclosure, gradually widened after 1948 (to include immediate family interests), is now more patchy (see Secs. 27–30 of the Companies Act 1967 as amended in 1981; Secs. 13, 16 and Sched. 3 paras. 39–40, Companies Act 1981). Suddenly however, the legislature made criminal the taking of a "put" or "call" option by a director (or his immediate family) in securities of his own company if it was listed on the Stock Exchange (Secs. 25, 30 of the Act of 1967). Why just those options? They, it is said, are "gambling". No doubt; but are they the only ways for directors to bet on their own company's shares?

Again, after "sporadic discussion for over 40 years" (Gower, 1979: 631) City resistance to legislation on "insider dealing" finally broke down in 1972, permitting legislation in Part V of the Companies Act 1980, whereby insider dealing is an offence – though no civil liability is created. But such are the provisions of the new Act that the prosecution faces almost insurmountable burdens of proof against alleged "insiders" – especially in regard to the *mens rea* required (Secs. 68–70) – such that the legislation is likely to be less a base for criminal convictions than "a fertile source of examination questions for years to come" (Gower, 1980: 636–638). No doubt the arguments with which the Supreme Court rejected the proposition that the Securities Exchange Act's fraud provisions impose a fiduciary duty of "fairness" on all corporate controllers towards minorities might be criticised as inadequately reflecting overall public interest (*Santa Fe Inds. Inc.* v. *Green,* 430 U.S. 462 (1977)) – though the reality, according to a minority of commentators, is consistent with "optimal legal arrangements" (Winter, 1978: 7), a race perhaps only to the bottom line. These arguments, however, at least purport to seek a socio-legal policy; whereas appearances suggest that, even on insider dealing, the British legislature still has to make up its mind finally whether it is really on the side of Professor Loss or Professor Manne. At the root of that indecision is a failure to relate this area of responsibility to *public* interests.

Only in one area has the legislature intervened clearly with a definite pointer to social responsibility. After the decision in *Parke* v. *Daily News* ([1962] Ch. 927, 963) it became fashionable to decry the legal definition of the "interests of the company" as limited to those of shareholders over the long term. Judges suggested that creditors could not be excluded (Lord Diplock, *Lonrho Ltd.* v. *Shell* [1980] 1 W.L.R. 627, 634). Other judges have now shown their disquiet by heretically suggesting that the company's interests might be seen as the benefit to it as a "trading" or "corporate entity" (*Re Halt Garage* [1982] 3 All E.R. 1035, *per* Oliver J.) or by trying to give to "independent" shareholders control over certain issues (see Wedderburn, 1981: 207–211 on *Prudential Assurance Co.* v. *Newman Industries* (No. 2) [1980] 2 All E.R. 841; reversed [1982] Ch. 204 C.A.). Any such attempts for British courts to mould a new multi-dimensional concept of the "interests of the company" are likely to be still-born, especially when there is little realisation that they will involve a new balance of private interests within a frame of *public* interests which are largely lacking from the debate – unless the public interest be confined to the profitability of companies.

C. Proposals for Reform and the Companies Act 1980

As for directors, wishing to appear good citizens of their time, whatever the law said, it became

> "common form for them to declare that industry owes duties to employees, consumers and the nation as well as to the shareholders" (Gower, 1979: 578).

Even those who had insisted that directors are "there as the representatives of the shareholders' interests" began in the 1960's to accept that they owed obligations also to "employees, customers and creditors as well as . . . in some degree to the state," (Institute of Directors, 1973: 13); and surveys of management practice discovered that company resources were in fact used – or were thought by management to be used – for "social" purposes, chosen on the basis largely of

> "convention, lack of shareholder objection and presumed social value" . . . [or] "a general responsiveness to the changing social climate." (Shenfield, 1971: 165–169).

Companies did place non-legal duties upon themselves in ways that were said to be "world-wide"; great importance was placed upon American experience (Fogarty, 1966; 1967). Back in 1960, the Editor of that bastion of shareholders' interests, the *Investor's Chronicle*, told the "Jenkins" Committee that he too saw a company as having three "co-equal interests to serve" (shareholders, employees and customers) and to "rank" any one above the other would be "sterile" (H. Wincott in Company Law Committee, 1960: 49). In 1957 the Labour Party – in a document enchanted with a Berle and Means analysis – toyed with a plan to "work out in discussion" with unions and employers a code of social conduct for industry (Labour Party, 1957). The air of the 1960's was thick with schemes, many similar to American proposals already discussed, to reorganise corporate government. Some proposed that a "Companies Act should contain powers" for the government to declare any enterprise to be an "Enterprise of National Interest"; these would be obliged to negotiate their business arrangements (including investment) with government, which would have a right to remove directors; whilst employees would have power to "appoint representatives to the board" (Chorley and Wolff, 1963: 195). But many schemes preferred to reorganise the private company along the lines of various "constituencies":

To build on "co-partnership" or share owning to make the company "responsible" to shareholders, workers, consumers and the community (Goyder, 1961; 1975); to turn the shareholder into a fixed interest investor (Derrick, 1964; Derrick and Phipps, 1969); or at least equate him to a secured creditor unless he could fulfil a role as controller of management (Wedderburn, 1965); to "socialise" the company with a workers' "equity" fund (Allan, 1974); to divide the governmental powers between the constituencies (in a constitution of bewildering complexity, (Ross, 1964); or the issuing of "community shares" (Boswell, 1968).

Others sought an answer in "efficiency" or "social" *audits* (Foster, 1964). But, as an official committee set up to consider research on "social responsibilities of business" found, what was envisaged was a "flow of information" rather than an "audit" properly so-called in the absence of agreed[31] criteria (Social Science Research Council, 1976: 8). More interest was shown in these matters than in a reform and extension of "disclosure" – the traditional base of British company law – or even in the establishment of a Companies Commission to take over, or at least co-ordinate, the work of various "self-regulatory" bodies, though both were vigorously proposed (Labour Party Working Group, 1974: 18–31). A more modest version of the latter, to rationalise regulation of the markets, was rejected yet again by the City in 1982 (Gower, 1982; rejected by Council for the Securities Industry, 15 June 1982).

One feature distinguished this developing debate from that on corporate responsibility in the United States – the central place of the *employees* in many different types of plan as a "constituency" in the company. This was true not only of the socialist contributions. Liberals too had introduced that perspective from an early date (Liberal Party, 1928; 1968). One of its adherents took the lead in making the "European connection" to which we come later (Fogarty, 1965; and especially 1975); whilst others drew their inspiration from experimental companies based on co-ownership "commonwealth" principles (Blum, 1968).

True, there were and are others who do not share any such views. Some, like the Conservative M.P. Sir Brandon Rhys Williams, have tried for decades to solve the social and managerial problems by compulsory "audit committees" of shareholders to contain management.[32] Others have pursued the solution of 'non-executive' directors, who now play a larger role in British boards.[33] Although the presence of such outside members on the board is officially supported by the City institutions – including pressure from the Bank of England (*Financial Times*, 29 June, 1981) – their objectives and role are often obscure (see Pro-Ned, 1982). Their job is often seen by business as much to assist management as to modify its responsibilities (Corporate Consulting Group, 1980). And although comparative study has demonstrated that Britain had much to learn from the American experience (Schwarz in Rowe *et al.*, 1980: 108–117), reports of the "Golden Parachutes" permitted by American board committees to threatened insiders

[31] Once again you find here the absence of agreed criteria.

[32] See Williams (1969), drawing on American experience, but finding no little difficulty in equating the British with the very different American board of directors.

[33] "Non-executive" directors now number about one-third of all directors in large companies, and now reaching a majority position on the "audit committees" that exist in 25 per cent of companies. See Korn/Ferry International (1982).

and the large fees received by some "outside-directors" (*Financial Times*, 27 April, 1982: 19) have not further commended the "non-executive" solution to many British observers.[34]

The strongest support in business circles has been given to "voluntary" measures, backed by pressure from City opinion and institutions such as the Council for the Securities Industry. The only major document on the matter was produced by the Confederation of British Industry in 1973, a Report of its Company Affairs Committee. The Report was a valiant attempt. The first obligation of a company is, within its "main objects", profit "over the long term"; but the board should give attention to "relationships with employees, customers, suppliers, Government, local authorities and the general public." A minority of non-executive directors is recommended. But, though relations with employees are emphasised, no criterion (other than profit) is advanced where choice has to be exercised:

> "A company should behave like *a good citizen in business*. The law does not (and cannot) contain or prescribe the whole duty of the citizen". (Confederation of British Industry, 1973: 23).[35]

The remarkable thing about this debate was the chasm which yawned – and still yawns – in Britain between it and "company law" proper. On the one hand lay the micro-level debates – the "Jenkins" Committee in 1962 puzzling over fiduciary duties, shareholder rights, corporate opportunities, and the like, where discussion was bounded largely by traditional private categories. On the other were the "macro-issues" of the company "in society", where in the broad-brush work inadequate attention was perhaps paid to technical details of what in the end must emerge as private law. The continued existence of the first limitation was proven again in 1982 when Professor Gower's modest attempt to propose that the self-regulatory agencies be rationalised and backed by statutory arrangements (Gower, 1982) – much less than a Companies Commission – was rejected with shock by most of the City institutions (Council for the Securities Industry, 1982: paras. 7, 10).

This was the historical setting in which the legislature made a major innovation in the law about corporate structure, a clause that was proposed

[34] The results seem not so different from the estimated £ 1,450,000 "handshake" for one British chairman in 1983 (*The Observer*, 16 January, 1983).

[35] Emphasis supplied. This phrase was reproduced in many company "codes". See e. g. Turner & Newall Ltd. "Code of Business Practice" (1974: 9): "The company should behave like a *good citizen in business* and it should recognise in its decision-making the interests of the general public." Others are more concerned with "maintaining the good public image" of the company: (Taylor Woodrow Code, 1974: 9). Did these companies know of Professor Mundheim's comment that "The Corporation as a Good Citizen" was the most popular topic for after dinner speeches in the 1970's in America (1975: 1260)? Only one in four large companies seems to have such codes (International Management, 1983).

in 1973, but which, by reason of various Parliamentary mishaps, reached the statute book only seven years later. It requires directors

"to have regard, in the performance of their functions [to] the interests of the company's employees in general, as well as the interests of its members" (Sec. 46 (1) of the Companies Act 1980).

This duty, the Act hastens to add, is owed only to the company and is enforceable in the "same way as any other fiduciary duty owed to a company by its directors".[36] No criterion is given to the board as to the way in which employees' interests should be balanced against "members'" interests. The board must, it seems, strike the balance, just as it does between short and long term, equity and preference shareholders' interests. Yet Parliament implies that the shareholders are still the superior group. For in order that boards need have no fear of even vestigial obstruction by the principles in *Parke* v. *Daily News* ([1962] Ch. 927, 963) the Act of 1980 also empowers the company to make provision for the benefit of *employees* in redundancy situations – where all or part of the undertaking is being transferred – adding, significantly, that *this* power

"may be exercised notwithstanding that its exercise is *not* in the best interests of the company" (Sec. 74 (2) of the Companies Act 1980; emphasis supplied).

Those "interests" would appear to be primarily those of shareholders. This express incorporation of "employees' interests" into the company law definition of the "company's interests" was a relatively non-controversial idea from 1973 onwards, when it was proposed by a Conservative Government. It did not logically have much to do with a wider debate about "industrial democracy" to which we turn below and by which it was overtaken. But it is noteworthy that to the interests of shareholders, the legislature added only those of employees. Statute does not deal similarly with interests of creditors, let alone of consumers or of "the public". This has tended to reinforce the centrality in the debate of *employees* as the counterpart group to shareholders and management in regard to responsibilities and rights within the company.

V. The British Debate on "Industrial Democracy"

A. Threads of the Early Development

The reasons why the British debate about corporate social responsibility became in the 1970's a debate *mainly* about "industrial democracy" are, however, very complex and still unclear. It is tentatively suggested that the

[36] Whether that includes a derivative suit brought by a shareholder remains to be tested (Gower, 1980: 579).

following may be perceived as the main strands woven into this development:

(1) There had been a much earlier debate about the democratic government of enterprises. That stemmed partly from the work on "industrial democracy" in 1897 of Sidney and Beatrice Webb – but the enterprises under discussion here were "public". i. e. nationalised or municipalised (Webb and Webb, 1897). So from the beginning, the debate about "representation" on boards to run industries or enterprises had this century centred upon "public" (nationalised or municipalised) enterprises, another reason for the "political" character of the debate. The critical point in our context is that in the period between 1910 and 1932, the battle between those who, like G. D. H. Cole and the "Guild Socialists", wished to see workers' elected representatives administer such enterprises and those who, like H. Morrison, wished to see public authorities appoint neutral managers to do so ("The workers must not be the victims of incompetence") was won by the latter (Hanson, 1961: Ch. II). That victory gave birth to the "public corporations" of 1945–48 and ended debate on the matter in the labour movement for thirty years (see Sciarra, 1978; Kelf-Cohen, 1973).

In the 1960's, with the publication especially of a report on "Industrial Democracy" (Labour Party, 1967) and a Trades Union Congress report (1966: para. 260–290; see also evidence to the "Donovan" Royal Commission, 1968) the earlier tradition, gushed forth again, though acquiring in its renewal the unhappy label of "workers directors" (Elliott, 1978: 205–211). The reemergence of the old tradition, as if it had meanwhile gone underground, was critical. Whereas the Morrisonian model of the public corporation stressed "efficiency"[37] the school of "worker-representation" emphasised democracy, service and accountability. The latter more and more represented "social responsibility" which brought the debate into range of company law, in the "private" sector.

(2) Another strand drew upon more diffuse traditions of "service" and radicalism in Britain and society. Many of the writings already cited (Liberal Party, 1928; 1968; Fogarty, 1965; 1970; 1975; Goyder, 1951; 1961) touch upon those elements; whilst such writers as Tawney (1966) represented the more radical flavour, speaking the very language of "social responsibility" and of the need to use publicly owned industry as a "laboratory" for "different methods of making industrial democracy a reality" (1952; 1966: 185). In truth, recent inquiry has shown that a debate on "workers' control" had begun again at the birth of the "Morrisonian" nationalised industries early after the war (Coates, 1982: Ch. 8).

That should not surprise us. As early as 1923 (before the Morrison victory) we find Robertson – writing, Keynes said in his introduction, as an

[37] Note however, that the concept later came to be approximated more and more to "profitability".

"orthodox member of the Cambridge School of Economics" – devoting two of his eleven chapters on "The Control of Industry" to "Workers' Control" and "Joint Control"; noting the "noble" aspiration of worker-representatives to benefit the "trade as a whole"; detecting signs of a "rapprochement" with the capitalist enterprise and profit-seeking:

> "It does not seem too fanciful to hope that the "Guild spirit" may progressively permeate private enterprise [and] . . . to hope, and to insist, that Private Enterprise should become less chaotic, less secretive, less tyrannical than in the past – more determined . . . to use in the service of industry the self-governing instincts of the millions who carry out its commands" (Robertson, 1928: 160, 167).

Ex Anglia semper aliquid usitati.

It is significant that it has been this school of thought in Europe – and especially the trade unions, the least "ideological" in Germany alongside the more conventionally "political" in Britain and Sweden or the more Marxist in Italy or France – which this century has been in large measure the bearer of that cultural tradition which puts the employment relationship in the corporate enterprise into a unique category. As eminent jurists have insisted, the "contract" of employment is not just another commodity contract:

> "It is a command under the guise of an agreement. The employer by exercising his power fills in the blank [of the content] and that power vests in him by virtue of his *dominium*, his ownership of the means of production" (Kahn-Freund, 1949: 28).

It was no accident that the author was steeped in the traditions of Weber and of early Marx, tempered by a love of the liberal British tradition to which he became a devotee (Wedderburn *et al.*, 1983: Ch. 3). Collective organisation for the worker was therefore a necessity and a right, to a degree of deep social significance. Further:

> "Collective bargaining in Europe is ultimately a mediator of social change or it is nothing." (Wedderburn, 1983b).

In Italy, the era of political constitutionalism was overtaken for the unions in the 1960's by the practice of collective bargaining which became "Anglo-Saxon" in its vigour; but the "European" element remained, that element in workers' representation through a union which adds a social function to its role in the enterprise:

> "Workers' representation in the plant must operate within the context of a class vision which is global, something which is possible only if it partakes in the creation of wider areas of consensus" (Giugni and Cafagna, 1976: 68).

By the mid-1960's, the British stream had joined with the broader European river of this tradition. Chamberlain has remarked that "ideology" reappeared in Europe after 1968. Power still lay with business and the network of large corporations; but the legitimacy of the system was now ever more extensively challenged (Chamberlain, 1980: Chs. 4, 8):

"La question de la legitimité du pouvoir économique est posée dans vos entreprises." (Rocard, 1976: 193).

European trade unions differ *inter se* greatly. Indeed, it is true that on such issues as "worker directors" there exists a "fundamental identity of view between Marxist doctrine" (as held by the French C. G. T.) "and American trade unions" (Kahn-Freund, 1976: 27). But they have all – even the German unions – differed from labour unions in America – and do still, despite the current developments in industrial policy of the AFL-CIO – in bearing within them a challenge to that legitimacy and a demand for qualitatively new dimensions of responsibility.

(3) The final strand was, for Britain, full of paradoxes. Throughout their existence, the chosen method of advance for British trade unions has been collective bargaining. Elsewhere in Europe, other methods of "participation" in the negotiation and administration of the enterprise emerged, alongside frequently less developed bargaining machinery. After 1951 German trade unions were drawn into representation of the workforce on "top-tier" Supervisory Boards[38] of German companies[39]. Furthermore, Works Councils were established by law, "the central institution of German labour relations" (Wedderburn, 1978b: 453). The pattern of these institutions appears to deny industrial conflict, to be "unitary" in approach. Did not the German law state: "The employer and the works council shall work together in a spirit of mutual trust" (Sec. 2 (1) of the Works Constitution Act 1972) – hardly the language of collective bargaining? Indeed Dahrendorf (in some ways a Berle of post-war Europe) castigated such "co-determination" as based upon the fallacy that it could abolish the conflict which in the long run it was more likely to provoke (Dahrendorf, 1959: 248–272). But if "collective bargaining" could not reach the level of strategic corporate decisions, what was to be done?

Meanwhile, the European Economic Community had promoted a draft law – the "Draft Fifth Directive" – whereby European company law was to be "harmonised" after the German or Dutch patterns, with minority worker representatives on Supervisory Boards.[40] For those in Britain who saw "co-determination" as built *either* "in the land of collective bargaining on the pluralistic pattern" *or* "in the land of company law on the unitary pattern", the choice was clear; the latter was "alien to the trade union movement" and to the realities of life (Kahn-Freund, 1977b: 71,

[38] Ironically this happened on the iniative in part of British advisers (Spiro, 1958).

[39] In the "Montan" industries of coal and steel in genuine parity; in other large companies to the extent of one-third workers' representatives, to be extended in 1976 to nearly – but not quite – 50 per cent representation an extension challenged unsuccessfully in the courts, but otherwise resisted in practice by German employers (Kübler *et al.*, 1978).

[40] Commission of the European Communities (1972). Greatly revised after the Commissions's "Green Paper" (1975) and again 1983, O. J. of the E. C., No. 240/2.

75–76). Some British unions have held to that view. Yet paradoxically in an interim report of 1973, and in a final decision a year later, the unions of the Trades Union Congress by a great majority chose to demand participation on the directing boards of large companies in Britain (Trades Union Congress 1973; 1974). A century of tradition appeared to be smashed.

This was a moment of great importance for the British perspective of "corporate responsibility". The TUC response to the crisis of social legitimacy needs to be evaluated at a theoretical and at a practical level. Theoretically it did *not* imply acceptance of a "unitary" model of industrial relations. On the contrary, the first task, as the TUC saw it, was to extend the range of collective bargaining and of disclosure of information by the big corporations. But workers' membership on the board, where desired, could extend "joint control", or joint regulation" in Allan Flanders' phrase; *supplementing* the techniques of collective bargaining; reaching issues which it could not easily reach, e. g. corporate investment plans. And in order *not* to "integrate" and make workers' representatives into the "Quislings" that Crosland foresaw they would be[41], at a practical level the TUC made certain essential demands:

(1) representation must be on the board that has power to take effective decisions; (2) through the "single-channel" of established trade union machinery, not separate Works Councils; (3) on all effective boards in "groups" of companies; and (4) to the extent of 50 per cent of the Board's membership – no less (Trades Union Congress, 1974: Ch. 4, 1977 Supp.).

These demands illustrated that

> "both extended strategic bargaining and participation in the institutions of the enterprise" [may show that the] "old maps of 'unitary' and 'pluralist' models are inadequate" (Davies and Wedderburn, 1977).

In truth, the literature discloses that such simplistic categories cannot do full justice to the modern problems of "participation" or "industrial democracy".[42] The German and British debates about "industrial democracy", like the American debate about board restructuring, involved a competition between "constituencies". But only two – those of shareholders and workers – were prominent; and the social stakes were higher.

B. The Bullock Debate

The job of relating these themes to company law and structures in Britain was given to a Committee on "Industrial Democracy" chaired by Lord Bullock which reported in 1977 ("Bullock" Committee, 1977). Despite

[41] This being the case despite their "moral" right to be there on the board (Crosland, 1956: 359, 361).

[42] Simitis (1975); Davies (1975); Batstone and Davies (1976); Brannen *et. al.* (1976); Sciarra (1978); see Däubler (1981: 35); Wedderburn (1981 c: 73); Labour Party (1974).