

A RECONFIGURATION OF COMPANY AND/OR CORPORATE LAW THEORY

by

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Introduction

Reform of company and/or corporations law is particularly moribund. It is locked into a debate between bowdlerised sociological theory and hyper-individualism — between stakeholder theory and law and economics, apart from when it is informed by straightforward political opportunism. The purpose of this article is to cut through the consequent knot of meaningless dialectic with a little up-to-date thinking: late twentieth century if not new millennium, rather than nineteenth century and 1980s respectively. In its pages I explore how we got into our present state and posit one way out (of many, I suppose).

The article begins by identifying *The Case of Sutton's Hospital* as a key turning point in corporations law. In that case human beings were recognised to be the sole subjects of law. This, as any such decision must, leads to various issues in the accommodation of law to the position taken, issues which are generally solved by process and theory. This article describes the directions theorising took, following Lord Coke's vision of law and society, and ending in the present stand-off. My argument is that the consequence has been a threefold error. First, the subject of law is assumed to necessarily be the human being. Second, law and its nature is a singular given. Third, theorising takes place in a simplistic epistemology. The way out I posit is to recast the metatheory: to locate law within a larger description of government that does not presume that its means are the regulation of human beings. This is here done and the way it would reconfigure company and/or corporations law is set out. Finally, this reconfiguration is applied to the issue where the moribund status of reform in corporations and/or company law is most obvious: the issue, in pre-reconfiguration terms, of the social responsibility of corporate management.

The subject of law

*The Case of Sutton's Hospital*¹ was decided in 1612. It was argued 'openly' before 'all the Judges of England and Barons of the Exchequer'.² We are told that it was decided at this exalted level 'more for the weight of the value, than for the difficulty of the law'. Lord Coke reports it

1. For the confirmation of incorporation founded on works of piety and charity in times past. 2. For the better instruction how they which shall be founded hereafter shall be so established that no exception may be

¹ 10 Co Rep 23a.

² Except the Chief Justice of the King's Bench who we are told at 24b was sick and at 34b of which illness he died.

taken to them. 3. For the resolving of certain opinions and questions which were moved at the Bar, and which might have disturbed the peace of the law.

All in all, *the Case of Sutton's Hospital* was thought by Lord Coke to be a Very Important Case. And so also it has come to us down the centuries.

Nowadays we mainly cite *The Case of Sutton's Hospital* because Lord Coke says, at 32b, 'the corporation itself is only *in abstracto*, and rests only in the intendment and consideration of the law; for a corporation aggregate of many is invisible, immortal, and rests only in intendment and consideration of the law'. This is seen to be important because it is an explicit statement that there is such a thing as corporate personality apart from the human beings comprising it.³ Moreover it appears to accept the idea that a corporation is fictional, so falling on one side of a debate that raged 300 years later.

Yet it is still odd that the matter was considered important or undecided. After all, the report cites numerous cases about corporations which had already decided all the matters before the Court. Any generalisation or adoption of theory could hardly be the result of considered judgment for the 300 years before the matter was to be teased apart had yet to elapse. Thus the case stands solidly at the core of the common law as to corporations but what exactly it stands for is, like much of such historical material, hard to discern.

Lord Coke's educative purpose in reporting the case may be a clue as to what was going on. He clearly felt a need to set out the law clearly and comprehensively. The time was not yet right for Blackstonian commentaries, yet Lord Coke seems to find some deep confusions in a field where case-by-case development could be most injurious to the poor and sick, and to charitable work generally. How were charities to be set up and run? It was not that there had been no such charitable work until 1612, but that the common law seemed suddenly to be not dealing with the matter very well at all. Why was this?

The turn of the seventeenth century lies at the tail end of feudalism. The liberal era was to come. Lord Coke's towering legal intellect dominates this cusp. He formulates, in a series of other cases, a new constitutional structure at the centre of which is the common law. This requires him, in turn, to formulate how the common law governs. Lord Coke clearly sees law as governing the subject of the Crown: this is enunciated in *Calvin's Case*,⁴ which leaves institutions as non-subjects. They are defined away. However, they are obviously very important to the smooth running of the state. Hence the issue of the status of charitable institutions is seized upon. Lord Coke allows corporations a place but only as a figment of legal imagination.

The Case of Sutton's Hospital, on this reading, is more about establishing human beings as the subject of law than about deciding anything about corporations. There

3 Then, as now in the United Kingdom, the 'company' is considered to be plural – together the governors in the Case of Sutton's Hospital were the corporation. In other places the company is incorporated and it has incorporators (or governors or whatever). The varying terminology reflects the dual aspects of a corporations as both a thing and as a group deciding things. I am advised the same linguistic differences exist for sporting teams: in some places the team **is** and others the team **are**.

⁴ (1608) 7 Co Rep 1a; 77 ER 377; 2 St Trials 559.

was no necessity for human beings to be the sole subject of law. It may now be hard to conceive otherwise, but Gierke showed us how, at least in Maitland's translation:⁵ we could have looked for the capacity to will and recognised it elsewhere. Or we could have developed the path to which we are called by the contumacious cockerel or the Hindu idol;⁶ as Stoljar recognises, the separate pool of assets as the subject of law fits many situations comfortably.⁷

Despite all this, that the human being is the sole real legal person is generally now assumed; at very least, considered inevitable. This leaves the corporation as something that has to be explained. Accordingly, Lord Coke takes the obvious step of saying that although it doesn't exist, law will treat it as if it did. Since then, many have likewise attempted to theorise the corporation.

The Fictional Person's Consequences

Four hundred years after the *Case of Sutton's Hospital*, theories of the corporation come at us from all directions. They come from inside⁸ the law in the form of theories of the person, contract and shareholder primacy, and perhaps stakeholder theory. From outside, economics has most recently staked a claim for explanatory power, with less apparent success in its recommendations. If we deem institutional economics to be sociological⁹ and hence not really economics, the most recent incarnation of corporations law material from an economic perspective originates in 1976 in the *Journal of Financial Economics*¹⁰ in the form of agency theory of the firm and proceeds to various finely drawn descriptions of phenomena in corporate law.¹¹ Given that agency theory originated in a school of management,¹² it is not surprising management studies have resulted in a series of ways of thinking about companies. Team production and asset partitioning¹³ is the latest such effort but there are many others.

Political theory helped in building the foundation of incorporation by registration and limited liability and Berle and Means famously later forced a rethinking of the site of

⁵ See S. J. Stoljar, *Groups and Entities*, ANU Press, Canberra, 1973, 184-5.

⁶ G.W. Keeton, *The Elementary Principles of Jurisprudence* Pitman & Sons London, 1949, at 149 and see Exodus xxi 28. As to the latter, see *Pramatha Nath Mullick v Pradyumna Kumar Mullick* (1925) LR 52 Ind App 245. This is not to mention the beetles of St Julien-de-Maurienne tried and executed in 1545.

⁷ Stoljar, n 5 above.

⁸ See M. Davies, *asking the law question*, Law Book Company, Sydney, 1994, v. Gunther Teubner's autopoiesis makes a virtue of hermeneutics by characterising the development of law as reflecting in on itself: *Law as an Autopoietic System* (tr A Bankowska and R Adler) Blackwell, Oxford, UK, 1993.

⁹ A brief glance at Toennies work at the turn of the nineteenth century makes this fair.

¹⁰ M C Jensen and H W Meckling, 'Theory of the Firm: Managerial Behavior, Agency Costs and Ownership Structure', (1976) 3 *Journal of Financial Economics* 305. Of course, this has its progenitors; in this case most particularly R H Coase, 'The Nature of the Firm' (1937) *Economica* 4 386-405 (but also variously reprinted).

¹¹ M J Whincop M J *An Economic and Jurisprudential Genealogy of Corporations Law*, Ashgate Sydney, 2001

¹² The William E. Simon Graduate School of Business Management, University of Rochester , Rochester, New York

¹³ M. Blair and L Stout, 'A Team Production Theory of Corporate Law' (1999) 85 *Virginia Law Review* 247

power in firms. James Willard Hurst pushed this into a framework of legitimacy, the upshot being the corporate governance movement presently influential. Modern empirical sociology has taken Berle and Means' cue and investigated the corporation/firm and the actors involved in them with studies of interlocking directorships in almost every jurisdiction imaginable, of directors' attitudes and behaviours, of their independence, and studies in a multiplicity of other matters. Accounting firms and management consultancies have most recently taken up this activity. Theoretical sociology draws heavily on Toennies and Weber to describe contracting and bureaucratic procedures respectively. The upshot of the former is the institutional economics of Macneil and Williamson, although this is more often viewed as a variant of economics — the institutional economics adverted to earlier. Whincop, as we shall see later, attempts reconciliation, although ultimately his analysis leaves the question begging. Weber leads to Frug, but by then postmodernity has set in. Post modern sociology has had small say about companies as yet, although one can feel the impending cool change of Foucauldian governmentality in conferences. Meanwhile there are still a few Marxists out there looking at corporations — Paddy Ireland springs to mind. Anthropology has resisted the call to apply its tools to the corporate world, despite the desperate need for ethnographic studies of meetings of both shareholders and directors¹⁴ along the lines of Sally Wheeler's incisive study of creditors' meetings. Descriptions of business activity remain depressingly 'thin'.

It is easy in all this to lose sight of the fundamental question for the common law system as formulated by Lord Coke. It is, *pace* H L A Hart, just what is a corporation? Given that corporations exist within law, as recognised in *the Case of Sutton's Hospital*, how is the rest of law to be accommodated to them and how are their interior structures to be explained in terms of human beings? After all, the human being is accepted to be a unity, his or her interior structure does not have to be explained, and hence the human being can be a citizen or subject, a party to a transaction, a victim or perpetrator, and so forth. Decisions are accepted to have been made by observable evidence and there is no need to enquire or explain further. Within the structure of thinking after the *Case of Sutton's Hospital*, this is not true of corporations. Corporations have had to be reduced in some way to component human beings. And this is exactly what the theories do.

The human being is indeed central to most approaches — Gierke being the exception, but Wolff's mocking tone brought that back to a liberal reality. While much of the economics and management literature is more about the firm, rather than the corporation or company, as an economic actor thus harking back to 'black box' theory,¹⁵ agency theory's triumph is the rendering of the black box into terms amenable to analysis as contracting by evaluating, maximizing, rational human beings. Even the institutionalists deploy a softening of the rational actor, human beings' propensity to limited rationality and opportunism, to explain the transaction

¹⁴ Exemplified by Clifford Geertz, in his famous and engaging study of the Balinese Cockfight: 'Deep Play: Notes on the Balinese Cockfight' One might also turn to Sally Falk Moore's 'semi autonomous social field': Sally Falk Moore, 'Introduction' in *Law as Process* (1978). This is entirely apposite as it is founded in an understanding of corporations as separate fields of social activity. Or even Hunt's governance approach, as set out in Alan Hunt, *Explorations in Law and Society: Towards a Constitutive Theory of Law* (1993) ch 13.

¹⁵ Despite Coase's reference to the firm coalescing like a 'clot in a pail of buttermilk'

costs associated with the choice of institution, let alone legal form. Weberian methodological individualism underlies much of the rest. Lowe's 'little republics' did not survive the exigencies of limited liability, although the constitutionalism of *Automatic Self Cleansing Filter Syndicate v Cunninghame* is a pointer to an inarticulate sense of the political.

There are many summaries of these approaches and theories, none of which capture all of them and while there is considerable description of each approach there is little debate. Most discussions are conducted in a space cordoned off somewhere from general legal theory and there is a corresponding ignorance of origin and context. This is perhaps less true of economic theories — the origins of which, for all their limitations, are paraded — but is certainly true of stakeholder theory where Pound's sociological jurisprudence is bowdlerised in the extreme.

No theory is wrong in its explanations of corporations; at very least the wrong ones do not survive long. Most theories simply describe matters a little, or even a lot, differently from the next one. This would not matter in the slightest except that theorists are not content to be 'positive', in economists' language: they feel that they should recommend. And different explanations lead to differing and perhaps conflicting recommendations. For example, should directors' duties be owed just to the company, or to the association as such, or beyond, to stakeholders? How should employees be dealt with? Should there be a third organ within the corporation? How should oppression be formulated and who should be able to sue in respect of it?

What to do about it

We can deal with differences and inconsistencies in theories in a number of ways. We can treat the theories as glittering things, to collect them as a magpie does and parade them as a sign of some sort of prowess. This is the way textbooks generally approach the matter, although some adopt one or other approach as a structuring, even explanatory device. Most simply ignore the whole thing. Alternatively we can track the theories as Cheffins does and relate them in a more or less complete genealogy of knowledge now existing. This is usually a model of progress, although Cheffins is a little more sophisticated and also considers the Kuhnian paradigm and simple fads and fashions as the core of the genealogy.

Another way of dealing with theoretical differences and inconsistencies is to try for a reconciliation. Mostly this is done by reading all the other theories through the framework of the primary one. Alternatively an attempt to align the theories can be made. Whincop attempts both at the same time. Neoclassical economics can incorporate institutional insights in his analysis of legal personality. And to the extent it does not, the two are just spaces on a diagram about the deployment of the idea. Mind you, ultimately Whincop concludes the simple incommensurability of contractarian and communitarian analyses.

Yet another way of dealing with theoretical differences and inconsistencies is to attempt a metanarrative. This is what is attempted here — it is an investigation of the way in which we can understand the multiplicity of theories so that their recommendations can be assessed against each other as more than incommensurable

alternatives. In other words, the purpose of this essay is to provide a background against which the theories of and dealing with corporations can be read.

As will be obvious later, this essay is heavily influenced by the postmodern destruction of metanarratives. The irony identified by Eagleton amongst others is that that does itself involve a metanarrative. This essay happily embraces the latter point, being quite comfortable in its perception of the intellectual world as multilayered, with no discernable centre — an onion, as it were.

Before proceeding to set out this background, it behoves me to qualify my intentions. What follows is not meant to be a universal theory of the meaning of everything, or even everything legal. This, in turn, is not meant to say that it cannot throw light on many matters, it simply is that it seems to be useful in the context of corporate theory. Moreover, it is not intended to displace the theories adverted to before. It clearly does not have the substance. It is proposed as a means to facilitating discussions between adherents to theories, and of comparing and contrasting theories.¹⁶

A Metatheory

Encapsulating all the theories mentioned above requires a scheme, into which law can fit, that does not assume the existence in any particular substance or form of either the legal person or the law.¹⁷ The former should not be implied because it is the assumed centrality of the human being as the subject of law in *Sutton's Hospital* that set theorising off on its course to present confusion. The latter, law, is too contingent of definition to be a useful idea; as we shall see, it varies in meaning within the theories, its limits have been subject the subject of jurisprudence for hundreds of years, and it is in many ways an artefact of the particular culture in which it happens to be located.¹⁸

Abandoning, as William of Ockham advises, law and the legal subject as intellectual constructs is possible if a notion of 'technique of governance' is adopted. Governing, in this perspective, is simply the exercise of power within society; moreover, no institution as vague as 'the state' is implied. Exercises of power are made possible by ways of knowing, the language and patterns of thought within the community. These make ways and techniques of governing possible, particularly, but not exclusively, those when we govern ourselves. Thus if there is expertise in probability we accept ideas of risk and govern ourselves to reduce it. If we conceive of property and money value, we may accept prices as determined by markets as the means by which resources are allocated to us and rationing by price as governing us. In similar ways rule-making is accepted — not only are rules internalised in the community but also acceptance of rules and institutions of rule-making. In this way, individuals and groups are both empowered and constrained. Power is constrained and limited by the

¹⁶ Habermas' lifeworlds

¹⁷ This is not to say that human beings are not at the centre of reason. We are well down the chain of philosophy from those Cartesian and Kantian questions. The challenge here is to a particular relationship between law and human beings and the argument is that we can examine this fruitfully from a Foucauldian perspective.

¹⁸ After all, the notion that law can be set down as such separately from the institutions that make it is but a construct.

forms of acceptable rule-making. Those forms are the ‘techniques of governance’. Making law is just one such technology.

Law as a technology of governance removes the human being (and even property) from the central position in law and refocuses on power. While this could render some important issues invisible, for present purposes it does not appear to do so. Law itself becomes what the previous discussion implied — a description of constraint useful for some purposes but not a necessary entity in the argument. The things which are done, the actions that are taken, are the object of our attention. Thus Parliament makes laws through a series of actions summarized as ‘legislation’. Courts resolve disputes, leaving judgments which is systematised by subsequent judges, academics and practitioners, so constructing case law. Law, in this perspective, is not something that can be directly studied or known, it is only the evidence of its making or the trace of its passing that can be seen. This is, of course and ironically, HLA Hart’s point that we shouldn’t ask ‘What is?’ questions.

Purpose and Effect

Theories about corporations law, as those about most fields of law, deal with more than just the law. They cover the best law to do certain things, the effects of laws, how law can fit within other disciplines, or even what a theory from elsewhere says about law or its ideas. Law as a technology of governance is about the latter two, as we shall see, but the first two demand an expansion of its calculated coverage. The governmentality literature expressly repudiates purpose and effect, the first because it is unknowable and the latter because it is unascertainable. To ask ‘Why?’ is to be irrelevant. To ask, ‘What happened as a result?’ is to unduly limit causality to pre-existing and current discourses. Cause and effect are so interrelated with each other and with the technology of governance that they can only be observed as a unity. Yet to confine ourselves in that way is to deny the observability of many aspects of that which this essay purports to document: theories of corporations law. It renders too much invisible. Hence the concepts of ‘purpose’ and ‘effect’ fall to be explored and incorporated.

‘Purpose’

‘Purpose’ is the reason for doing something. It can be personal or public, of a group or institution, attributed or inherent. It can be of the action comprising the deployed technique of governance or of a theory describing it, or of the process framing a discourse which the techniques inhabit. This might seem so wide as to deprive ‘purpose’ of meaning but is implied by the idea that doing is an expression of power and therefore has reasons. Those reasons themselves inhabit a world of intellect which define and constrain what is done and, indeed, construct us as individuals. Thus purposes motivate or are seen to motivate the exercise of power but are also, in either case, the result of exercises of power. A judge deciding a case, in the process of which he or she makes a statement as to what the law is, has a variety of purposes as a subjective matter. These may be personal or private and never to be confessed — the plaintiff is attractive, the judge wants to go home ...; self aggrandising — the judge thinks he or she is a very clever fellow ...; or more professionally acceptable — this

area of law needs clarification or repair.... It may be that there is an agenda of moving the law to a stance more in tune with theory — competition law is prone to this, or with authority. These and a variety of other purposes can be attributed to the judge, indeed that is all we can do, and the judge may declare some of them, as Lord Coke did. Constraining the judge is their perception of their role as adjudicator, their ideas of precedent and what it means they can do, their appreciation of the law, ideas of justice and so forth. These constraints are not necessarily imposed, whether they are or not is beside the point, rather they operate as self-government by the judge. They are self-imposed because physical restraint is only very rarely exercised. The knowledge of possible consequences and feelings of rightness operate to constrain in almost all circumstances.

In this vein, statutes are both Acts of Parliament and acts of Parliament. The evidence of the deployment of the governmental technique is the formal statute. The purpose is, however more speculative. We can see the interplay between various descriptions. Of course, a true purpose is a mere construct, given that purpose is a matter of the intellect of individual human beings and Parliament is a group of human beings acting in a certain way in a certain environment (all of which helps to define the acts that have taken place as a governmental technique known as an Act of Parliament). Parliament's purpose can be nominated by Parliament or it can be later attributed by institutions or actors. No doubt each member of Parliament has a different set of purposes for participating in the decision and some may be common to all Parliamentarians.

'Effect'

Determination of effects of action inevitably invokes the incommensurability issue. In Kuhnian terms, results are dependent on the paradigm under which the measurement takes place. Evidence is theory contingent. In terms of techniques of government, the theory upon which evidence is contingent includes the conceptualisation of that on which power is exercised, including society, individuals and institutions. The statement of an effect depends on our way of knowing all these things. Nevertheless, that there are effects of action is implied by acceptance of time and consequence, and these can hardly be ignored as they are part of many of the theories examined here. Moreover, that hypothesis testing is theory contingent does not mean that effects do not result, it merely means that that contingency is open to analysis.

More to the point, if theorising is to have a justification it is that it is to lead to action in some endeavour, it is to have effects. This is important in two ways. First it implies the complex relation between effect and purpose. Purpose frequently decides what measurement of effect is to take place. Unintended effects are acknowledged and identified. In this legitimacy is often found. The legitimate action is one where the effects are the ones intended. The reverse is often also the case: the purpose is confined by the measurability of the effects. The expertise which identifies effects allows the imagination of the purpose. For example, the development of probability allowed the imagination of risk mitigation.

The second implication is that theorising, even metatheorising, has purposes and effects. Avoiding plunging into the waters of the critique of representation by

confining myself to the expression of theorising, the theorist acts by publishing thoughts. This act has purposes and effects which permeate the evidence of its existence. This applies to this essay and also to others. Again, we cannot say with certitude what any purpose is, nor the effects of any particular action, but this does not mean that those purposes and effects do not exist. Moreover, if we are talk of what is right to do, the critique of effects is vitally important.

To sum up then: the version of governmentality set out here for the purpose of reimagining corporations law places the evidence of the exercise of a technique of government — judgements, acts of Parliament — as the central perceivable element of theory. These are not law, merely the raw material from which we construct a vision of law. Around this element is a rich language and set of concepts which can locate theory and law (as a technology of government) against and in relation to each other.

Deploying the Metatheory

Corporations/company law and concepts deployed within it

Corporations law is a complex of cases and legislation, the legislation mostly riding on the cases rather than establishing the core language of the field of law. There are three main interrelated areas: How the corporation is to exist and act as a legal person within the legal system, how decisions are to be made within the corporation as an institution, and the construction of markets for property made possible by the corporate form. In each area there are prevailing and less influential ways of thinking, metaphors and techniques, with more or less effect on legislators, judges and practitioners, and, of course, academics, in their work.

An example of this is the section in most companies legislation deriving from the United Kingdom original that the constitution of the company is to be enforceable as if it were a contract. ‘Contract’ operates here in ambiguous ways. If the constitution of a company were a contract it would be a strange one indeed, as most of the most strongly held tenets in contract law do not apply: not all the terms are enforceable and not by parties in capacities other than shareholder or director; indeed, directors can enforce it in many jurisdictions when they are not party to it. Termination is mandated when unwritten expectations are belied by the contract itself — a rare example of the unwritten superseding the written. Oddly, the section itself is taken to establish the contractual nature of the relationship between the parties to the constitution of the company and to extend those who can rely upon it, but that relationship pre-existed the section and the purpose of the section has only been established by subsequent judicial fiat. By contrast, a concept of the relationship between stockholders and directors is lacking in US corporations law, rather participants in corporations have statute-given statuses with rights, the mediating concept being the business judgment rule. There is, then, in US law a poverty of exploration of decision making relations and perhaps for that reason there was a ready acceptance of the formulation proffered by economics: the agency contract. In yet another oddity, or perhaps idiocy, this ready acceptance has led to its proselytisation in the United Kingdom and Anglo-derived jurisdictions where the prevailing thinking was that the company is founded on contract anyway.

The agency contract theory of corporations resonates with the contract as a simile or metaphor in the determination of disputes arising between member and company, director and company, and between the members. They are frequently confused yet, although they are related, they are quite different things. The first is a theory or abstraction of relations in firms, which are themselves a descriptive abstraction of commercial institutions, while the second is a device employed by judges, and taken up by legislators, in resolving disputes. The first provides evaluative criteria and recommendations for governance, the second is a concept used to decide matters in disputes. There could be different concepts for this latter function and, arguably, there are. For example, it is quite conceivable that the underlying idea for the conceptualisation of relations within companies is that of association; hence there are members and decision-making apparatuses. 'Contract' is but a term which can usefully found a base of bindingness, the exceptions are founded on the way groups of people associated together behave. Alternatively political notions can underlie the concepts upon which dispute resolution can take place. Admittedly, this was tried by Arthur Lowe, and not pursued after a time, yet still might have some life.

There are many other examples of ways of thinking, metaphors and concepts inhabiting the governmental techniques represented by company/corporations law. The directing mind and will of a company is one which is perhaps a little out of control and stakeholder is in the process of being received.

The impact of retreating away from law to governmental technique as metatheory is that these ways of thinking, metaphors and techniques cease to be interrogated for their place as authority within a legal system. Rather they are acknowledged to be deployed at times within it. They are both disenfranchised as law yet also recognised as participating within that mental structure. To put it another way, whether or not they count as law is relevant only to the operation of the system, to its effects, and not to the things themselves. They work within governing, as referents for terms in legislation or for ideas used to reason in judgments, and are developed and changed in the social processes of these and other activities. This means that there is no substantial difference for our purposes between a set of ideas arising within legal discourse such as the contractual base to company/corporations law, and one from an outside discipline, such as the agency theory of the firm, except in terms of how they arise within the legal discourse, what they do and are meant to do, and how they are thought. Agency theory, often called contract theory, is highly influential in corporations/company law as providing a justification for shareholder primacy and a firm set of recommendations based on efficiency. It is founded in economics.

Economics and agency theory of the firm

Economics has a history of explaining and recommending for law in a variety of ways associated with its epistemology and consequent presumptions about human behaviour, and assumptions as to the proper purposes of change. Its epistemology is founded on firm structuralist grounds, mostly Popperian although with Kuhnian overtones. Science is the model because the world is unbearably complex and epistemology provides a method through which it can be observed. As a description economics provides way of understanding the world which may be and is deployed

within law within academia, in judgments and government reports and perhaps even the general populace. Its great strength is that it does encapsulate many relationships and enable their extrapolation in ways not otherwise observable. Yet, unlike science which makes no claim to recommend for the physical universe, economics also claims there is a state called 'efficiency' and that that is one worth seeking. The recommendations of economics are built upon this notion of efficiency. Description elides to recommendation in quite unqualified ways, especially when efficiency is not interrogated as an ethic. To some extent one gets the impression that the world is reconstructed to make the theory work — Posner's undergraduate texts are particularly guilty of confusing 'is' with 'ought', and *vice versa*.

The simplifications economics makes to a more or less extent for its model-building project include those as to the nature of human interactions, human choices, property, time, the state, and law. For present purposes it is important to note the key assumption that society is comprised of human beings and that law as a system of commands governs them. While there is interrogation of the production of rules and the enforcement of criminal law, there is little about what Hart would call 'secondary rules'. What there is, is a matter of institutional economics and not deployed in the economics of the firm. Arguably that is that against which agency theory is directed.

Given that economics in many ways is defined by its epistemology, it is particularly susceptible to the problems of theory contingent evidence in the testing of its hypotheses. For example the issue of the Delaware preference in the United States was repeatedly tested by measuring the stock price, discounted for other price movements, of corporations before and after moves to Delaware. The idea was that stockholders value corporations and if the stock price went up the corporation was worth more merely because Delaware's legal structure is more amenable to corporate managements. Initial analyses concluded that the stock price did indeed go up. Much was made of this as confirming the hypothesis that freedom for management is good for the economy. Later analyses concluded there was no significant change. But the whole exercise was flawed. Maybe the stock price only went up because stock purchasers thought that such a move meant corporate management was better. They may have been right in a way, because prevailing orthodoxy had it that the move was good, so to do it indicated that management was doing something. Both of these arguments indicate that cause and effect are not as closely related as the epistemology of the economics assumed.

In terms of the tri-partite generalisation of the law dealing with companies and corporations, economics is usefully deployed to understand and recommend for securities markets. After all, these are markets roughly approximating the sorts of things economics employs as the description of an analytical framework. For internal relations, agency theory is less directly deployable because its key relationship between human beings, the discrete and presentiated transaction emptied of substantive content, fails to encapsulate much of the subject matter of both legislation and cases. Agency theory thus becomes a source of critique and recommendation, claiming to originate these in abstracted models. It has little to say with respect to the rules establishing the personality of the corporation and how it is to exist and act within the legal system: there is little it can say. It has too thin a concept of law and deals with the consequences of *Sutton's Hospital* with assumption, just as the old joke would suggest. Society must by definition be reduced to its component human beings

thus corporations can only act as human beings or to be the product of the accumulated interactions of human beings. The social is represented by a notion of ‘imperfect market’, as an exception to the analysis, the consequences alone of which fall to be explained and addressed.

Stakeholder theory

Stakeholder theory pervades recent discussions of corporate governance and corporate social responsibility — debates over decision-making and the control of decisions. It provides a counterpoint to agency theory’s insistence on property rights and hence the pre-eminence of the capital provider by justifying reference to the interests of others in decision-making. The justification lies in the ‘stake’ the other has. If someone, or some group, has a ‘stake’ in a decision, their interest ought to be considered by the decision-maker. This applies to corporations/company law through the realisation that directors and other officers make decisions which affect many people other than the capital providers. These include creditors, employees, consumers, the environment and society generally. A little regard for its genealogy reveals that the theory in this form begs the questions with which it pretends to deal.

Stakeholder theory was developed by the American Realists in the first part of the twentieth century. They located law within society and believed that law should reflect society. Judges should do what is right by reference to the persons affected by their decisions. It was about judging. It enabled the effecting of purposes defined by a judge’s oath by providing a definition of justice when formulaic ideas of precedent were breaking down. A good example of how it works for corporations/company law is the judgment of Richardson J in *Thomas v Thomas* in the New Zealand Court of Appeal, a case widely cited to illustrate how unfairness in the management is to be determined. The following is the text most frequently quoted:

That conduct of the company which is unjustly detrimental to any member whatever form it takes and whether it adversely affects all members alike or discriminates against some only ... fairness cannot be assessed in a vacuum or simply from one member’s point of view. It will often depend on weighing conflicting interests of different groups within the company. It is a matter of balancing all the interests involved in terms of the policies underlying the companies legislation and sec 209 (Aust sec 232) in particular.

The clear injunction is to ‘balance interests’. But how do we know what the interests are? Interestingly, excluded from most extracts of the case is the passage immediately following the above. In this, ‘interests’ are defined by the pre-existing principles of New Zealand company law, of which the contractual foundations to the company are but one:¹⁹

thus to have regard to the principles governing the duties of a director in the conduct of the affairs of a company and the rights and duties of a

¹⁹ Cf US, where there is little to explain that relation and hence stakeholder theory has greater resonance.

majority shareholder in relation to the minority; but to recognize that sec. 209 is a remedial provision designed to allow the court to intervene where there is a visible departure from the standards of fair dealing; and in the light of the history and structure of the particular company and the reasonable expectations of the members to determine whether the detriment occasioned to the complaining member's interests arising from the acts or conduct in that way is justifiable.

Three points are illustrated here. One is that stakeholder theory does not tell what the relationships between the interests are beyond nominating them as things which have to be 'balanced'. Second, it does not in itself tell us what the interests are. Third, there is very little appreciation of its limits — limits which were thoroughly explored in the 1930s and ultimately lead to its rejection as a viable normative postulate. These were identified at the time as: the identity of the stakeholders, the homogeneity and solidarity of their interests, and the processes, beyond begging its own question by nominating them as 'balancing', by which competing interests are to be resolved. In terms of corporations/company law these translate to a lack of indication of which sets of interests are to be taken into account, how conflicts of interest within stakeholder groups are to be reconciled and how the discretionary power conferred on decision-makers to deal with these issues is to be controlled.

There is, however, utility to stakeholder theory. By focussing on law creation it displaces law into society generally and interrogates social structures to determine the effects of changes in the law. This process relies on disciplines of knowledge outside the law to determine those effects and hence is less afflicted with theory contingent evidence. Yet as it is formulated in corporations law it has taken a liberal materialist turn. This is partly as a result of the absence of guidance as to the process of 'balancing' and hence the failure to specify the moral considerations involved in 'justice'. The person is not necessary to the theory, although in the simplistic sociology attached to it within corporation/company law effects are seldom otherwise indicated.

Their Provinces

These three theories are each directed at describing certain aspects of the substance of law and the legal system taken together, and at recommending for choices as to what the law should be where it is unknown or mutable in particular ways. They thus can be said to have 'provinces', to use the Austinian terminology, although the location and extent of these provinces is vague and arguable.²⁰

A metatheoretical approach allows for the dimensions of the provinces of the various theories to be mapped. Remembering that 'law' has a very narrow meaning here (and 'theory' has a correspondingly broad one), theories have three dimensions: purpose/law/effect, systemic focus, and calculable purpose. They are not fixed in these dimensions; being mere ideas their communication is an exercise for which, in Stanley Fish's terms, there is, at best, one or more interpretive communities. The

²⁰ At this point I am moving away from straight post-structuralist Derridean thinking and moving towards Fish — what are the interpretive principles universally deployed and which ones are contingent and debated.

ideas thus change and mutate as interpretations are placed in them, and they may extend beyond or even shrink within the boundaries of their heretofore provinces. Their extensions are subject to analysis and critique, always from other theoretical standpoints.

Purpose/Law/Effect

The contractual theory of the corporation describes certain concepts deployed by judges and referred to in legislation. These concepts provide means to resolving disputes. In this guise they have a life of their own, being applied and disapplied in later disputes and rules, yet they are not seen as having an effect outside the law. They do, of course, as the resolutions to disputes ripple out financially and personally into society, but these effects are not reflected back to considerations of the effectiveness or justice of law. Indeed, the concepts are taken to define justice in the particular context. Similarly in the always-already-there world of doctrinal conceptual thinking, they are not taken to determine purpose for law. They are simply the way certain relations are to be thought.

Contrast this with the agency theory of the firm. In its narrowest sense, agency theory of the firm provides a way of thinking about firm structure, founded on rational actor theory of human conduct. Within its various versions the position and substance of the legal discourse of corporation/company remains ambiguous; it is abstracted, frequently into a set of property rights and at other times into a set of conditions, default or mandatory, arrived at in transacting. The found purposes of various laws are matched against the ideal of efficiency, which also provides the touchstone of the measurement of effect. Purpose/law/effect are elided into sets of recommendations for law, although this sits uneasily with claims about the legal process itself.

Stakeholder theory sits differently yet again, dealing primarily with the effect of law on groups within society. With an inarticulate sense of justice, at best a cost/benefit calculation bringing the approach perilously close to economics and Kaldor-Hicks efficiency, it recommends the law be changed to mediate these effects.

Systemic focus

Whereas ‘purpose/law/effect’ holds judgements and Acts of Parliament steady in its exploration of the various ways theories represent law acting in society, ‘systemic focus’ holds steady the elements of the process of law: process rather than substance. Law is produced within society by various processes occurring within and between institutions and humans. The various theories being discussed here concentrate to varying extents on parts of that process and this can be mapped as another of their dimensions.

The contractual theory of the corporation/company is about the thinking of judges as illustrated by their judgments. It is referred to in legislation and provides a framework for change. This should be contrasted with the economic theory of the firm which, being a description in abstracted terms, provides a framework for thinking about policy — what should be done in the field, whether it be by legislatures or courts. In the process of formulation of law, it indicates goals and provides evidence of effects within the terms of and for the purpose of formulation of those goals. Stakeholder theory is also about policy in this sense, but more narrowly focussed on decisions and on effects rendered invisible by the economics of the firm. It also sets out certain

concepts, the definitions of the interest groups, for use within judgments and legislation.

Calculable purpose

While postmodernity sternly advises that there is no firm connection between a communication and its referents, one of Fish' principles of interpretation could well be that readers calculate what the purpose of the communication is and that readings are mediated by this purpose. These calculations are for the most part agreed upon, although few would deny that they are only provisional. The factors involved in the calculations are what the writer or speaker says their purpose is and the way in which the theory configures and reconfigures subject matter. This is not to deny that writers and speakers have many other purposes in mind nor that for readers knowledge of any purpose is impossible, it merely asserts that we do formulate and attribute to communications intended purposes. This purpose, calculated and provisional though it might be, varies between theories, but tends to be common between readers of any particular theory at a given time. This is not to say that the theory cannot be deployed otherwise, merely that readers are mostly constrained in their appreciation of the theory by their perception of its purpose.

For contract theory this purpose is that it explains the relationship between stock or shareholders and the board of directors. It is also deployed to assert the primacy of residual cash flow claimants. Economic theory of the firm in its positive modality is there to enable analysis of the interior 'black box' of the firm and to explain behaviour within the discourse of economics. In its normative guise, economics of the firm recommends change against the touchstone of efficiency. Stakeholder theory is deployed quite specifically to argue against the primacy of residual cash flow claimants and more generally to be a measure of effect of decision-making. It also has variants, little referred to now, which explain the structure of the relationships comprising the company/corporation as being arrangements between a narrow range of stakeholders.

An Application of the metatheoretical approach

Many countries and jurisdictions in the world are struggling with demands for the social responsibility of corporations and companies. Indeed it is the debate surrounding these struggles that prompts this essay. In these debates corporate social responsibility²¹ and shareholder primacy²² are conceived of as theoretical opposites with little to reconcile them. Doctrinal positions between, such as enlightened shareholder value, schemes of disclosure or specific mandatory rights²³ are recommended, often building on long-established principles, mainly out of a reluctance to move away from established principles.

My contention here is that this situation has arisen because in both of those positions the primacy of the human being is assumed and other ways of conceiving the

²¹ Justified by stakeholder or 'communitarian' theory

²² Indicated by both contract and contractual theories

²³ Creditor protection provisions, eg transactions as to sharecapital, 588G; some employee protection; preferences in winding up.

dynamics of corporate life are thereby rendered invisible. *Suttons Hospital* excludes from law any conception of corporate life other than that which can be constructed out of the activities of individual human beings. Theory is deployed simply to explain the interior of the corporation. In this task the doctrinal theory of the contract has become confused with the quite separate agency theory of the firm despite difference in what I have here called the dimensions of their provinces. Their intersection is at the point of their utility, the calculable purpose — both seek to maintain stochastic residual cash flow claimant primacy, although one is out of conservatism and the other out of a belief in the overriding importance of efficiency. But in their other dimensions they differ and are inconsistent. Stakeholder theory is deployed to highlight the effect of shareholder primacy on other constituencies but does not have the breadth in terms of purpose/law/effect to reconfigure shareholder primacy's justifications within a context of human beings as the sole subject of law. Stakeholder theory becomes simply a justification for external constraints, to the extent that the matter is not shifted to being within the discretion of the decision-makers.

If we move away from the sole focus of law being human beings, a company/corporation can be conceived of as a community. There is no need to so radically alter the substance of law as to encompass creditors, employees and management into that community, a company/corporation can be a community of the members in some common enterprise ('enterprise' here is used in a broad sense). Given this, the problem of corporate social responsibility is the same as for human beings — how to instill a moral sense in that community and how that moral sense is to be maintained in the face of the pressure of self-interest. Society does not have twenty-odd years of pre-adulthood and dependency to school companies/corporations, although that is to anthropomorphise. Yet we can understand that community moral restraints are a matter of common understandings and restraints: Foucault's self-governance, if you like.

What, then, are the restraints that ought to be imposed? Of course, this is a moral question and is none the worse for it. After all, it is the thin morality of economics and the inarticulate morality of legal realism that the question seeks to depose. Yet the answer cannot be direct as the determination of which moral standards are relevant is context dependent, even if morality is not relative. However, given that the company/corporation is a community, we can attribute to it the capacity to determine for itself moral questions. The answer, then, is to allow the community to be a moral community and to be able to express for itself the restraints on decision-making.

The corporation/company as a moral community is quite consistent with existing law. After all, the contractual theory of the corporation/company is only a way of deploying an existing concept about people associating together, contract, to try and explain the association represented by the corporation/company. It does not do that job very well, as we have seen. An explicit acknowledgement of an associative impulse might work far better as it explains internal management, membership and a number of doctrines and statutory provisions. It also does not leave moral questions to boards of directors, which is surely a sensible result as they are hardly the sort of people to whom the resolution of such issues comes easily.

Implementation of this idea would be quite easy. It relies on established principles and law. After all, the constitution of a company/corporation divides power between

the organs of the company and this could be easily taken to imply that the moral framework is a matter for the members. The moral framework is part of the purpose of the institution and this could be inarticulate or expressed through a code of conduct set out in the constitution.

But why should the community bother? After all, Oliver Wendell Holmes' 'bad man' was a useful constraint on idealism in American law and the same thought would apply to companies/corporations. Moreover, competitive pressures are designed to ensure continuous cost reduction and moral restraints are one of the easiest costly items to remove. Even were the idea of the association as a moral community to be adopted, a race to the bottom is almost a certainty. To argue this, however, is to concede that moral responsibility cannot survive organisation. Agency, in this view, precludes morality. There are answers to this argument.

Responses to the race to the bottom must apply to all communities. They must be society-wide. Law, of course, has a part to play in this yet law has its limits. It is marginal and far too heavy handed. By far the best technique is for restraints to be internalised and for the community to express itself in social pressure. Anecdotally, directors are more often pressured by their peer group than forced by bargaining power. Certainly the City of London form of securities and takeovers legislation ultimately failed, but that it might work implies that we should recognise the possibility of and encourage social pressure to moral action. However, given that the City of London approach did fail, other techniques should be deployed.

Within the limits of law the code of conduct in a company's/corporation's constitution needs to be compulsory and effective. This could well be implemented by deploying the concept of corporate culture, as articulated by Fisse and Braithwaite and enacted in many places but notably in the Australian Corporate Criminal Code Act 1995 (Cth.). It is recognition of the need to define the interior workings of company/corporations in terms other than the acts of human beings. Hence it allows requires a 'culture of compliance' to exist if a company/corporation is to avoid the imposition of *mens rea* when it is required by law as the mental element in crimes and torts. A code of moral conduct would work within the concept of corporate culture to express the workings of the moral community. The absence of a code of moral conduct would imply a willingness on the part of the company/corporation to act in inappropriate ways and would make the mental element of crimes and torts extremely difficult to deny.

Compliance with law and social pressure on management is well and good, but it could be argued that this still would not be sufficient to impel compliance. This is to ignore the substantial internal pressure generated by a code of conduct incorporated in a company's/corporation's constitution. In existing law it would be enforceable by members, all the more so were this to be expressly provided. Compliance would be incorporated in director's contracts, perhaps compulsorily. And it would be an aspect of 'proper' for the purposes of directors' duties.

Conclusion

This essay has been about introducing a governmentality approach and deploying it to break out of the sterile debate over corporate social responsibility. The governmentality approach reveals the *Case of Sutton's Hospital* as having settled on the human being as the sole subject of law within the Coke paradigm of the constitutional state. This confines the issue for debate as to what should be done in law to the recognition of relations between human beings and leads to the present situation that corporate social responsibility is a matter of restraints imposed on the actions of corporate management.

The paradigm of the constitutional state confines theorising about law because to be accepted theories have to be consistent with that law. To be sure, they can recommend changes for law, but they are repudiated or mocked if they say the law is otherwise than as revealed in legislation or judgments. Thus, in theorising, the human being is required to be the subject of law. This deprives theorising at the very least of the rich vein of metaphor in and about law. The organic theory of corporate liability is the simplest example, acceptable only because it makes a human of the company. But there are many others, amongst which is the associative idea of the company/corporation. If these ideas are rendered acceptable and no more flawed than the presently held contractual and stakeholder theories, then many more strategies are made available to deal with the problems of irresponsible action by decision-makers empowered by accumulated capital.