Reconceptualising the Corporate Group

A study examining the legitimacy of Corporate Power

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I certify that all material in this thesis which is not my own work has been identified and that no material has previously been submitted and approved for the award of a degree by this or any other University.

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Signature: ……………………………………………………………..

Abstract

Since its inception in 1855, limited liability has been described as one of the greatest inventions of modern times. It has since become central to the functioning of the modern economy. Over recent decades, the use of corporate groups and their respective liability has become the subject of significant debate. This thesis examines English law, construction and subsequent challenges with corporate groups and their respective power. It investigates the mechanisms which have historically been used to control and monitor corporate power and its suitability for the corporate group. Through a corporate social responsibility framework, the thesis seeks to ascertain if these control mechanisms function in the group context, and if not, what is the impact on the legitimacy of power in these corporate groups. In doing so, the current study enriches the understanding of how legitimacy is understood in the context of the corporate group.

The precise focus of the thesis is the legitimacy of corporate power wielded by corporate groups. It demonstrates that groups wield power on an illegitimate basis despite a broad governance landscape. This legitimacy deficiency arises from a lack of historical debate, diluted control mechanisms and inflated growth utilising unique features of the corporate group. The thesis explores how power is magnified in the group context and the legitimacy challenges arising from this magnified power.

This thesis utilises empirical data to map the current corporate group to identify architectural patterns. It seeks to address the deficiencies by establishing an alternative framework. In so doing, it offers a framework of reconceptualisation toward a pluralist model of the corporation which is supported from the data analysed. Furthermore, it advocates for the use of technology and the capability of said technology to support the implementation of a pluralist conception.

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List of Abbreviations, Acronyms and Initialisms

AI	Artificial Intelligence
BEIS	Business, Energy and Industrial Strategy Committee
CCT	Corporate Citizenship Theory
CSP	Corporate Social Performance
CSR	Corporate Social Responsibility
DAP	Discretionary Administrative Power
ESG	Environmental Social Governance
FRC	Financial Reporting Council
NED	Non-Executive Director
NZ	New Zealand
ONS	Office for National Statistics
RPA	Robotic Process Automation
SC	Stewardship Code
SV	Stakeholder Theory
SVT	Shareholder Value Theory
UK	United Kingdom
USA	United States of America
USS	Universities Superannuation Scheme

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Chapter 1: Introduction

'Corporate governance is concerned with holding the balance between economic and social goals and between individual and communal goals. The corporate governance framework is there to encourage the efficient use of resources and equally to require accountability for the stewardship of those resources. The aim is to align as nearly as possible the interests of individuals, corporations and society.'[1]

Large corporations operate with capital and power analogous to that of the state. Recent failures and collapses of these large companies have caused many to question governance mechanisms and the holding of such power.[2] Collapses from companies such as Carillion, Debenhams and Arcadia have revigorated the debates as to appropriate governance and the purpose of business.[3] These failures demonstrate that progress has been slow since the high-profile bankruptcy in the 2000s of the US utilities giant Enron. Moreover, despite widespread criticism and economic loss, failures in large organisations remain prevalent. These corporate failures share common features which support the argument that these instances are not isolated but are current features of the corporate system.

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[1] Sir Adrian Cadbury, *Corporate Governance A Framework for Implementation Overview: Foreword by Sir Adrian Cadbury* (The World Bank Group, 1999) vi.
[2] Scholars are too numerous to list. See for example: Margaret M Blair, *Ownership and Control: Rethinking Corporate Governance for the 21st Century* (Brookings Institution 1995); Nina Boeger and Charlotte Villiers, *Shaping the Corporate Landscape: Towards Corporate Reform and Enterprise Diversity* (Hart Publishing 2018); Michael C Jensen, *A Theory of the Firm: Governance, Residual Claims, and Organizational Forms* (Harvard University Press 2003); Marc Moore, *Corporate Governance in the Shadow of the State* (Bloomsbury Publishing 2013); Mark J Roe, 'Corporate Short-Termism: In the Boardroom and in the Courtroom' in Jeffrey N Gordon and Wolf-Georg Ringe (eds), *The Oxford Handbook of Corporate Law and Governance* (Oxford University Press 2018); Iris H-Y Chiu and Ernest WK Lim, 'Technology vs Ideology: How Far will Artificial Intelligence and Distributed Ledger Technology Transform Corporate Governance and Business?' [2020] 18 Berkeley Bus LJ 1; Paul Davies, 'The UK Stewardship Code 2010–2020 From Saving the Company to Saving the Planet?' (2020) European Corporate Governance Institute-Law Working Paper; Grant M Hayden and Matthew T Bodie, 'The Corporation Reborn: From Shareholder Primacy to Shared Governance' (2020) 61 BCL Rev 2419; Peter Bailey, 'It Looks Like Corporate Governance Is Starting to Toughen Up (at Last)' (2018) Company Law Newsletter 1.
[3] The British Academy, *Policy and Practice for Purposeful Business: The Final Report of the Future of the Corporation Programme* (2021).

This thesis will critically evaluate the role of corporate power in the group context and its impact on corporate governance mechanisms. It will examine this corporate power through the ideology of legitimacy and how this is understood in the context of corporate groups wielding corporate power. The thesis will examine this from a corporate social responsibility (CSR) theoretical perspective, as this theory provides for a broader consideration of stakeholders, which will provide clarity in addressing the research questions. Furthermore, it will explore how these mechanisms could be reformed to reduce the challenges which stem from the advantageous position offered to groups. This thesis, therefore, advances the argument that English law has failed to develop a coherent set of rules for the operation of group companies outside of tax law.[4] Moreover, it investigates how the bedrock principles of company law function to underpin the operation of group companies which results in the wielding of corporate power.

These bedrock and fundamental concepts of limited liability and separate legal personality extend to each individual company within a group. The result is that each company within a corporate group is legally separate. This thesis will explore how these concepts function within a group and if the expansion results in the illegitimate holding of corporate power. The very nature of juridical person status within a group poses additional challenges when compared with traditional, non-group, structured companies. The ability to further shield assets and introduce jurisdictional divides is a unique benefit afforded to groups. It is unique benefits such as these that contribute to the growth of corporate groups and the correlative power which develops from this.

Companies can provide great benefits to the economy, yet somewhat paradoxically, they can cause economic and social harm.[5] Permitting and facilitating the extension of traditional corporate law principles to corporate groups magnifies already contentious issues within company law and society. These bedrock principles are premised on a 19th-century notion of the corporation, which is largely inadequate to govern the complexities of corporate groups.[6] This thesis presents the argument that the development of corporate

[4] See the Companies Act 2006 ss 399–408.
[5] For a detailed discussion on this see Boeger and Villiers (n 2).
[6] Phillip I Blumberg and others, *Blumberg on Corporate Groups* (Wolters Kluwer 2005) 1.

groups is not one of institutional design but one of gradual evolution.[7] The result is substantial devolution from the initial concept of the corporation and illegitimate holding of corporate power. The modern corporation is a political construct that requires further critical analysis in respect of its application within corporate groups and their related power.

This research challenges the legitimacy of the extension of limited liability to corporate groups in respect of its impact on corporate power. It then considers if these groups have an advantage to not only those they contract with directly but also parties affected by their corporate activity. The thesis seeks greater correlative liability analogous to the social conceptualisation of the company.

This chapter will set out the argument for the thesis, along with the aims and goals of the research. It will then proceed to introduce the theoretical framework, which outlines the adopted framework for the thesis. Following this, a definition of legitimacy will be provided to establish the term upon which the research questions will pose. The research questions will then be introduced, outlining the questions that the thesis seeks to answer. The methodology detailing how these questions will be addressed and then *explored*. An outline of the thesis will then be offered by way of a plan for the whole research product before highlighting some of the findings of the research.

1.1 Argument of the research

This section sets out the argument of the research. This research argues that corporate groups wield illegitimate corporate power. Furthermore, to address the legitimacy failure, a reconceptualisation of the corporation is required.

This thesis enlightens the understanding of the legitimacy of corporate power within the group context, ultimately concluding that legitimacy is misplaced, resulting in a legitimacy deficiency. This failure arises from corporate group power, which is predicated on its historical development. This research advances the argument that this legitimacy can not only be challenged but an alternative

[7] See section 2.2 below.

framework introduced to attain legitimacy. The very foundation upon which corporate groups are built is premised on control mechanisms, which are significantly diluted in the group context. This dilution results in reduced control mechanisms which diminish the legitimacy of the corporate power wielded. This power is achieved through corporate law bedrock principles such as limited liability and separate legal personality.

Reconceptualisation challenges the notion that shareholder primacy is the only model from which the corporation can be viewed. In presenting a more pluralist model of the corporation, to include wider stakeholders, the legitimacy failure can be resolved, and legitimacy restored to the corporate group. This reconceptualisation can be rationalised by the wide dispersion of shareholders within the modern corporation. This thesis presents empirical data to support the construct that identifying 'for the benefit of the shareholders' is inherently problematic, and a wider consideration can be justified based upon the widespread shareholding.

This enlightened understanding of corporate group power is explored in two principal ways. The first investigates the argument of legitimacy deficiency within the corporate group and presents the argument as to why corporate groups hold illegitimate power. The second approach is an exploration of alternative methods of conceptualisation, and how, if at all, these affect the position and effect of corporate group power. These methods of exploration will be further detailed in the proceeding subsections.

Legitimacy deficiency is the basis upon which this argument is constructed. It arises from the historical foundation upon which corporate groups have evolved. Davies opines in his historical analysis of company law that 'it is clear without the legislative intervention limited liability could never have been attained satisfactorily'.[8] The legislative basis upon which company law is built is, therefore, of significant importance in the evolution of the modern corporation. Moreover, corporate groups stem from this position of evolution. This research presents the

[8] Paul Davies and Sarah Worthington, *Gower's Principles of Modern Company Law* (6th edn, Sweet & Maxwell 1997) 46.

argument that the extension of these legislative provisions was 'accidental'[9] , and as such, the control mechanisms are not aligned with corporate power. This thesis maintains that the deficiency problem arises due to the concentrated levels of power that corporations maintain. Likewise, questions of adequate safeguards for the continuing use of limited liability and wielding power can be posed. One such example of this is the evolution of the corporate form, which has all but removed many of the protections introduced under the initial Limited Liability Act 1855.[10] These protections formed the basis for the legitimate holding of power, through incorporation in that, through a CSR perspective, responsibility and power are consciously coupled. The erosion and decoupling of power from responsibility in the group context result in a legitimacy failure.

The provisions within the Companies Act[11] apply to companies of all sizes; this can be represented by the seminal case of *Salomon*.[12] Here, the court expressly stated that if a company is validly incorporated, it is entitled to the benefits afforded by the legislation. This position remains the authority, despite any inherent divergence between the spirit and the letter of the law. The challenge in utilising this in support of the group context is that the economic and social landscape of the time differs vastly from that of today. In the period in which *Salomon*[13] was decided, the consideration and use of group companies were not as pronounced as in the present-day modern corporation. This, combined with the diminishing control mechanisms, contribute to this deficiency. One such example can be seen in the historical prerequisites for a company to be formed. During the period in which *Salomon*[14] was decided, safeguards such as capital maintenance and more involved registration requirement existed. Before 1844, a company could only be formed by a royal charter or parliamentary statute.[15] It was only in 1844 that the Joint Stock Companies Act 1844 introduced the ability to register a company without the need for a royal or parliamentary charter. This introduction of limited liability was not without intense debate. The requirements

[9] See: Blumberg and others, 'Limited Liability and Corporate Groups' (1986) 11 Journal of Corporation Law 573; Phillip I Blumberg, 'The Transformation of Modern Corporation Law' 37 Connecticut Law Review 611.
[10] See further analysis in section 2.1.
[11] Companies Act 2006.
[12] *Salomon v Salomon & Co Ltd* [1897] AC 22 (HL).
[13] ibid.
[14] ibid.
[15] Royal Exchange and London Assurance Corporation Act 1719.

for registration under the 1844 Act were onerous, with scholars claiming the exacting use of requirements was to rein in and control the use of companies.

The use of onerous restrictions to rein in the remit of corporations can be supported by empirical data. In 1844, the year in which companies were permitted to be freely incorporated, 119 companies were provisionally registered, with the 119 applications eventually abandoned.[16] The subsequent year, the number of companies registered rose to 1,520, which suggests an increase in businesses wanting to utilise the features afforded in the 1844 Act. This number is, however, distorted due to 1,463 applications being abandoned, resulting in just 4% of applications successfully achieving legal status.[17] Over the next 10 years, a similar picture emerges, with an average of just 24% of companies achieving successful legal status.[18] Following the introduction of the Joint Stock Act of 1856 and the Companies Act of 1862, there was a dramatic increase in successful registrations, an average of 82% achieving their legal status. Over a 12-year period, we can see the number of abandoned applications decrease, from initially 26% in 1856 to 0.04% in 1868.[19] This data directly supports the argument that there is a correlation between facilitative legislation and the growth of incorporations. This thesis presents the argument that the dilution of control mechanisms has further facilitated this growth within the corporate group and the result is the illegitimate holding of corporate power. Moreover, data demonstrates that there is a direct correlation between the reduction in registration requirements and the increase in the use of the corporate form. This is of significance because it supports the concept of the corporation as a political construct. As corporations continued to play a larger part in economic growth, the law became more facilitative rather than restrictive. The result is that the initial concept concerning such a contentious issue of limited liability has been diluted to such an extent that the protections in place to ensure that limited liability was used within the scope of its initial design have all but disappeared. This is supported by Watson, who claims that there is a substantial difference between

[16] Rob McQueen, *A Social History of Company Law: Great Britain and the Australian Colonies 1854–1920* (Routledge 2016) 50.
[17] ibid.
[18] ibid.
[19] ibid.

old and modern corporations.[20] Companies incorporated under the 1844 Act comprised members who held joint stock, whilst in the modern company, the entity contains a joint-stock fund. This evolution is from individual ownership and control to the separation of these two key facets. It is, therefore, argued that this more facilitative approach to company formation has contributed to the popularity of corporate groups and has done so in a great departure from its initial construct of much stricter control mechanisms. This departure has further grown concentrated power in the context of a corporate group, which holds this power without correlative accountability, resulting in the legitimacy deficiency.

The historical evolution has, therefore, resulted in greater use of the corporate form by the dilution of formality requirements, resulting in a separation of responsibility from power. These have in turn made the corporate group ubiquitous amongst the largest corporations. The historical framework presented in chapter two argues that legitimacy can be challenged based on this evolution due to the illegitimacy which stems from this dilution and the inadequate reasoning upon which groups have developed.

1.1.1 Readdressing legitimacy deficiency

In readdressing the legitimacy deficiency identified in the preceding subsection, this thesis argues a greater emphasis can be placed on the social institution and presents a more pluralist model. Such a model can align responsibility with power. Moreover, it argues that new technologies provide the platform for a previously considered theoretical adoption to become more feasible. This conception of the company to produce greater and more correlative accountability results in greater legitimacy. In addition, this social conception can be justified in larger corporations due to the share structures which are in place. This thesis argues that in utilising alternative methods of conceptualisation, greater legitimacy can be derived for groups with concentrated power. Moreover, empirical data collected and analysed by this research supports this realignment from the dominant shareholder primacy model.

[20] Susan Watson, 'How the Company Became an Entity: A New Understanding of Corporate Law' (2015) 120 Journal of Business Law 124.

Corporations maintain power which rivals the state, with financial power and status surpassing many countries.[21] When contrasted with the state, the state requires social justification to legitimate this power.[22] The legitimacy of power, regardless of categorisation, is accountability. To maintain and have continued use of this power, accountability must be in place. In the context of the state, this power is often kept in check by methods such as democratic elections with the ability to remove those in political power periodically.[23] The same, therefore, could be true of corporate managers; if corporations rival the state in terms of the power they possess, it is a natural corollary that there should be some form of accountability through control mechanisms. Control mechanisms such as share capital, and a specified number of directors, have previously been in place to ensure accountability is present. Moreover, annual general meetings provide a platform for shareholders to hold corporate managers to account. Such control mechanisms are problematic for several reasons in the context of a corporate group, and these challenges result in a legitimacy deficiency. These layers of complexity add to the difficulty in establishing accountability, as shareholders may be ill-informed as to the wider activity of the parent company. This holding of power without control mechanisms forms the basis upon which an alternative conception can be presented. Corporations have often gone unchallenged in their ability to partition assets within a group or have undercapitalised companies. This thesis, consequently, argues that this externalisation of risk contributes to the increased wielding of corporate power without its correlative control mechanisms. The group phenomenon presents its unique features which do not present themselves in other types of traditional ownership structures. In a traditional model, the shareholders are 'once removed' from the company itself through incorporation and limited liability: this has been dubbed 'the corporate veil'. This is considered the very foundation of the modern corporation. In the corporate group, the structure is significantly different, departing from this traditionalist view and providing unique benefits. There exist multiple veils, and the shareholders could be several layers down the structure, transitioning to 'twice removed', for

[21] See for example: ABC Finance, 'The Countries More Profitable Than Countries' (*ABC Finance*) <https://abcfinance.co.uk/blog/companies-more-profitable-than-countries/> accessed 11th January 2022; Business Insider, '25 giant companies that are bigger than entire countries' (*Business Insider*, 25 July 2018) <https://www.businessinsider.com/25-giant-companies-that-earn-more-than-entire-countries-2018-7?r=US&IR=T> accessed 11 January 2022.

[22] Mary Stokes, 'Company Law and Legal Theory' [1986] Legal Theory and Common Law 155, 180.

[23] See for example: Fixed-term Parliaments Act 2011, s 1.

example. The concept of limited liability, this research argues, was introduced to promote investment and had the concept of accountability annexed through safeguards that have now become significantly reduced.

The wide dispersion of shareholders[24] results in great use of 'exit over voice'[25] and shareholders who are reluctant to engage in activism. Shareholding of listed companies is now largely made up of insurance companies, trust and pension funds, investments and charities (institutional investors). This leaves a trivial proportion[26] of shares that are individually owned, and the majority of shareholders will be a minority with a reduced ability to individually hold corporate managers to account. Shareholding is, therefore, now very dispersed;[27] , the traditional theory of ownership can be detached from companies and their shareholders, leaving the company free to take a more balanced view of all stakeholders. This thesis argues this more balanced perspective can be achieved through the combination of a reconceptualisation of the company and utilising new technologies to enhance this decision-making. The argument is that changing how the corporation is conceptualised can mitigate the unique benefits afforded to corporate groups. In implanting the shift in conception, the thesis contends that social and societal inclusion could be implemented through new technologies. These new technologies provide the framework for the implementation of a pluralist model of the company, allowing wider stakeholders to be considered in corporate decision-making. This will, in turn result in greater coherency and correlative accountability through attaching legitimacy to corporate groups which have, to date, been absent. This reconceptualisation can be justified not only in its need to address the legitimacy deficiency but also in those traditional conceptions of ownership which are misplaced.

This thesis, therefore, advances the argument that English law has failed to develop a coherent set of rules for the operation of group companies, outside of

[24] As identified with empirical data in chapter five.
[25] Andrea Bowdren, 'Contextualising Short-Termism: Does the Corporate Legal Landscape Facilitate Managerial Myopia?' [2016] UCL Journal of Law and Jurisprudence 285; Mark Roe 'Corporate Short-Termism—in the Boardroom and in the Courtroom' [2013] The Business Lawyer 977.
[26] Office for National Statistics, 'Ownership of UK Quoted Shares: 2016' <https://www.ons.gov.uk/economy/investmentspensionsandtrusts/bulletins/ownershipofukquotedshares/2016> accessed 25 January 2022.
[27] See data presented in chapter 5.

tax law. The result is a substantial wielding of corporate power without a correlative control mechanism that aligns with the historical origins of company law. This failure has resulted in a legitimacy deficiency that requires greater consideration of how corporate law manages corporate groups. This research further presents the proposal that legitimacy can be regained, and this can be achieved through a reconceptualising of the corporation. Furthermore, the advances in technology allow for this theoretical position to be translated into the boardroom to address wider stakeholders.

1.2 Research aims and objectives

This research will demonstrate that the current literature concerning the legitimacy of corporate power, specifically in the group context, is largely inadequate. The focus of existing literature appears to stem from two distinct categories: corporate power and corporate groups, and not necessarily the relationship between the two. This research will consider these key concepts together through a CSR framework to explore the legitimacy from which corporate power is derived. This thesis will contribute to the existing literature in the field of company law and corporate governance concerning correlative accountability within corporate groups through the lens of legitimacy for power wielded within large enterprises.

This research, therefore, has two principal aims, outlined below:

1) *To explore how we evaluate and understand legitimacy in relation to corporate power.*

This research aims to explore legitimacy in the context of corporate groups and seeks to discover the historical basis upon which this legitimacy was built. There is significance in the historical development of company law principles which have resulted in the current construction of the corporate group. This research further aims to critically evaluate the historical development to ascertain the reasoning and justification for the extension of principles to corporate groups to determine if it is legitimate.

This thesis aims to ascertain the importance of the legitimacy of corporate power in the development of the corporation. Power has been described as a 'ubiquitous phenomenon'[28] that is highly opaque and contested. In the context of a corporation, power can have two operations. Power in terms of the internal effect refers to the decisions it makes on the running of the company. In this respect, it may well be the directors, officers and managers who operate the internal workings of the company. There is also the external element of power, whereby corporations utilise their market positions to gain an advantage.

This thesis aims to consider the impact of both internal and external effects of corporate power and the legitimacy of the exercising of this power. A starting point is the internal power dynamics within a company. Berle and Means[29] , writing in 1932, considered the balance of power within the context of a company. They explored the separation of ownership and control and how there may be competing interests operating within a corporation. Historically, partnerships were the main structure of business where the partners were both the managers of the business as well as the 'owners'. This differs significantly within limited companies; whilst it is possible shareholders could also be the managers and directors in large companies with significant social power, this is unlikely. What this results in is two parties with potentially different interests: there are the shareholders who maintain rights with the company and the directors who manage the company. It is this separation Berle and Means[30] identified, which is becoming more pronounced in the modern corporation and more so in the corporate group. This separation places additional challenges on the exercising of control within the ownership rights of shareholders. This is relevant in the context of corporate power because where shareholdings are so widely dispersed, shareholders become disinterested in exercising their rights. Therefore, if shareholders are not exercising these rights, the legitimacy of the power these corporations hold is diminished due to further separation between power and responsibility.

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[28] Marc T Moore and Martin Petrin, *Corporate Governance: Law, Regulation and Theory* (Palgrave 2017) 5.
[29] Adolf Berle and Gardiner Means, *Modern Corporation and Private Property* (Macmillan 1932).
[30] ibid.

In 1993, Parkinson, a leading scholar on corporate power, argued that 'Since the public interest is the foundation of the legitimacy of companies, it follows that society is entitled to ensure that corporate power is exercised in a way that is consistent with that interest'.[31] This statement maintains that the very legitimacy of corporate power is the public interest. Given the developments within company law in its historical development, this thesis will explore how legitimacy can be understood specifically in the corporate group. Moreover, it will evaluate the relationship between public interest and responsibility.

2) *To explore if alternative frameworks for the legitimacy of corporate power within the context of corporate groups is required.*

Scholars have argued that 19th-century notions are simply inadequate to govern the complexities of corporate groups, and the challenges remain unresolved.[32] This thesis seeks to utilise a historic analysis and CSR framework to evaluate why these challenges remain unresolved and if in reconceptualising the company's greater legitimacy can be derived.

It is the historical development of the principles of limited liability and separate legal entity which has allowed the legal group to develop unimpeded. This, in turn presents its unique characteristics that are not evident in individual ownership, which this thesis aims to elucidate and challenge. There is evidence to support the theory that before legislative interference, liability may have been already limited through contractual arrangements.[33] This supports the argument that limited liability as a statutory implement was not required.[34] It may therefore have been the case that the arguments in favour of the requirement for limited liability are misguided and need a greater legitimacy or reconceptualisation irrespective of structure. An objective of this research is therefore to establish the key role history and its political agenda have played throughout the development of the modern corporation to provide a lens through which this thesis can analyse the corporate group.

[31] John E Parkinson, *Corporate Power and Responsibility: Issues in the Theory of Company Law* (Oxford University Press 1993) 23.
[32] Blumberg and others (n 9) 1–5.
[33] See empirical data from Blumberg and others (n 9) 3–12.
[34] Academics have argued that one key element for legislation is the need to reduce contracting costs: see Reinier H Kraakman and others, *The Anatomy of Corporate Law: A Comparative and Functional Approach* (Oxford University Press 2017).

One of the largest challenges which faces company law at present is correlative accountability for the actions of companies. The importance of accountability links to corporate power and its legitimacy, which has been delineated above. Corporations are powerful, and this power is not in itself deleterious; however, it requires control checks. To continue the possession and use of this corporate power, there must be this legitimacy and control, which can be found through social accountability,[35] , which in turn results in the responsible use of power. Legitimacy is required to justify the exercising of corporate power and prevent 'abuse'. The concept of corporate abuse has been argued as a potential method for attaching liability and ensuring relevant accountability to companies. The difficulty with corporate abuse lies in its definition, and it has been claimed that identifying and pinpointing abuse can be challenging due to the lack of precise definition.[36] Gelter and Vicente offer one definition, explaining that 'abuse of the law is sometimes understood to refer to a situation where someone employs a legal entitlement to gain an advantage'.[37]

Abuse can be said to occur when the letter of the law is followed but not the spirit.[38] This has been expressly discussed by members of parliament who claim that companies are often breaching the very spirit of the Companies Act.[39] There are several problems with definitions, such as those offered in respect of breaching the spirit of the law. The most pertinent of these problems lies with defining the spirit of the law, as establishing what this presents challenges. This is inherently complex because what constitutes the spirit of the law is subjective. History demonstrates[40] that where there are elements of subjectivity, this is at the cost of certainty, which is highly valued within the commercial sector. These issues are magnified within a corporate group context, partially due to political and economic considerations in addition to purely legal ones. The threshold of

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[35] Moore and Petrin (n 28) 14.
[36] Hanne Birkmose, Mette Neville and Karsten Engsig Sørensen (eds), *Abuse of Companies* (Wolters Kluwer 2019) 4.
[37] Martin Gelter and Lécia Vicente, 'Abuse of Companies Through Choice of Incorporation?' in Hanne Birkmose, Mette Neville and Karsten Engsig Sørensen (eds), *Abuse of Companies* (Wolters Kluwer 2019) 13.
[38] ibid.
[39] See MP Ian Swales Publications.parliament.uk., 'House of Commons - Uncorrected Evidence - HC 870-I' (2017) <https://publications.parliament.uk/pa/cm201213/cmselect/cmpubacc/uc870-i/uc87001.htm> accessed 11 November 2017.
[40] See section 2.1 below.

abuse appears to be a high one which will be difficult to attain, resulting in little change to corporate correlative accountability. This has already been demonstrated in numerous tax cases demonstrating that corporations had strayed from efficiency to avoidance. One example is the case of Google, in which MP Dame Margaret Hodge branded Google 'completely obscene',[41] , with their actions going against common sense. In this case, they operated out of the United Kingdom (UK) but had their headquarters in Ireland. The sales staff, management and many customers were all within the UK; however, all transactions were not carried out by the UK company but by the Irish subsidiary. The reason for this was corporate planning and structuring. This is one example of what may constitute obeying the letter of the law but not the spirit. To follow the letter but not the spirit, this research argues, results in exercising of power without legitimacy, and as such, this power ought to be revoked. Furthermore, this thesis aims to investigate frameworks for effective correlative accountability within corporate groups and explore alternative frameworks to achieve legitimacy. The objective of the thesis is to critically analyse competing tensions to ascertain if a suitable framework could be developed and implemented to derive greater legitimacy where there may currently be a deficiency.

1.3 Theoretical framework

This section evaluates and justifies the theoretical framework which will be used throughout the thesis. It analyses the literature on corporate law theories and their importance within the framework. This section justifies the use of the CSR theoretical framework for the study. Millon argues that theorising about corporate law has played an important role in the arguments surrounding concrete questions of corporate law.[42] Moreover, Millon contends that corporate theory can also be used to legitimate or criticise corporate doctrine. This thesis evaluates the legitimacy of corporate power in the group context, and the use of CSR as a theoretical framework provides the platform to evaluate this legitimacy and critique the current model. The section will proceed to evaluate the theoretical

[41] Michael Bow, 'Margaret Hodge Condemns Google for "Obscene" Tax Avoidance' (*Independent*, London, 3 February 2016) <https://www.independent.co.uk/news/business/news/margaret-hodge-condemns-google-for-obscene-tax-avoidance-a6850296.html> accessed 4 March 2020.
[42] David Millon, 'Theories of the Corporation' [1990] Duke LJ 201.

framework that the thesis adopts. It will consider Carroll's pyramid of CSR as the basis for the study and further explore the relevance of CSR in the context of the thesis.

1.3.1 CSR as a theoretical framework

The concept of CSR is not unanimous, and Carroll[43] has identified that there are many ways in which CSR can be defined. Melé, in the Oxford handbook on CSR, derives four mainstream theories.[44] The theories are outlined as the following: corporate social performance (CSP), shareholder value, stakeholder and corporate citizenship theory (CCT). These four distinct categories have been collated through numerous scholars writing on CSR to identify key themes.

Klonoski[45] , writing in 1991, distinguished three kinds of theories. The first theory discussed was that of 'fundamentalism', which he argued was at one end of the CSR spectrum. The fundamentalism theory is based upon the premise of profit maximisation and is analogous to that of Milton Friedman.[46] This correlates to Friedman's 'rules of the game' concept, which posited that social responsibility is to be derived from the economic environment or the context in which the business operates. The only social responsibility from this theory is that of increasing the profits of the business. Klonoski argues that integral to this position is that of individuality and rights whereby the corporation is privately owned, and as such, activity needs to be conducted in a manner conducive to the rights held by those 'owners'. Klonoski's second theory defends the moral personhood of the corporation. The arguments evaluating moral personhood are based upon the structural ontological nature of the corporation itself. Encompassed within this evaluation are two interlinked considerations: that corporations are either moral

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[43] Archie B Carroll, 'The Pyramid of Corporate Social Responsibility: Toward the Moral Management of Organizational Stakeholders' (1991) 34 Business Horizons 39; Mark S. Schwartz and Archie B. Carroll, 'Corporate Social Responsibility: A Three-Domain Approach' (2013) 13 Business Ethics Quarterly 503.

[44] Domènec Melé, 'Corporate Social Responsibility Theories' in Andrew Crane and others (eds), *The Oxford Handbook of Corporate Social Responsibility* (Oxford University Press 2008).

[45] Richard J Klonoski, 'Foundational Considerations in the Corporate Social Responsibility Debate' (1991) 34 Business Horizons 9.

[46] Milton Friedman, 'A Friedman Doctrine: The Social Responsibility of Business Is to Increase Its Profits. A Friedman Business Doctrine' (*New York Times*, 1923 – Current file, New York, N.Y., 13 September 1970) <https://www.proquest.com/docview/117933451?accountid=10792&parentSessionId=DI71KmQxaqB%2FL4JGBScmExL6MyN6CHiqUHTV225mVeo%3D> accessed 18 February 2022.

persons or moral agents acting on behalf of their principals. From this perspective, Klonoski argues that personhood has a significant bearing on CSR. If the corporation itself is a moral person or agent, it can be held morally accountable for its actions in the same way as natural persons can. If they are not persons, they are unable to be held to account by society, and corporations will need to utilise another ground of moral agency to justify themselves. Comparisons to corporations as machines with no personhood can be made when evaluating how they could be held to account.

Klonoski's third theory encompasses elements of the social dimension of the corporation. This theory considers that by treating corporations as persons, their activity operates within a social context. As such, this approach considers the corporation to be a social institution with social responsibilities. Klonoski does highlight that the 'exact sense' in which the corporation is considered social differs amongst adherents to this approach. One context in which social construction can be sought is from the philosophical tradition. Anshen[47] argues that there is an 'evolving document' as a social contract for business. Klonoski, however, contends that this is not so much a formal document but a highly implicit social agreement. The criticism of such an approach is premised on the basis that the social contract is a fiction and, as such, its broad nature would be unenforceable. The proponents of the enforceability challenge present the practical argument that enforcing notions of abstract philosophical debate to commercial reality is inherently difficult. Another social dimension, in addition to that of the philosophical sphere, is the stakeholder or constituency approach. Buono and Nichols suggest that corporations are servants of a larger society and that as a result, there are diverse groups who have a stake in the corporation.[48] CSR arises due to the corporation's relation to and potential to affect the groups in society. In addition to stakeholder theory (ST) exists the legal creator view. De George argues that this viewpoint sees the corporation as a creature of law existing as a reflection of the law.[49] The corollary of this is the corporation is also

[47] Melvin Anshen, 'Changing the Social Contract: A Role for Business' in Tom Beauchamp and Bowie Norman (eds), *Ethical Theory and Business* (Englewood Cliffs 1979) <https://www.econbiz.de/Record/changing-the-social-contract-a-role-for-business-anshen-melvin/10001834772> accessed 3 April 2022.
[48] Anthony F Buono and Lawrence T Nichols, 'Stockholder and Stakeholder Interpretations of Business' Social Role' [1990] Business Ethics.
[49] Richard T De George, *Business Ethics* (Macmillian 1990) 101–102.

a creature of society and, as such, should act for the common good of society. Klonoski identifies that these social theories of CSR fall within the utilitarian angle seeking to derive the greatest benefit. The debate on CSR, as Klonoski classifies, is of three kinds: amoral, personal and social. Within each of these kinds lie further debates and classifications, but they can be classified into these three broad categories. Amoral considers the fundamentalism and the traditional stockholder argument. Personal evaluates both moral personhood and moral agency in the corporate context. Social encompasses a broader spectrum, including social contract, ST corporate citizenship and the philosophical underpinning.

Windsor approaches CSR theories from a differing perspective; they identify three key approaches.[50] Windsor depicts this from two perspectives, private wealth at one end and general welfare at the other. Within this spectrum, three classifications emerge economic conception, ethical conception and corporate citizenship. The economic conception is not dissimilar to Klonoski's with the focus on fiduciary duties and minimalist public policy. The focus on fiduciary duties is in response to the rejection of discretionary CSR with the responsibility to the general welfare and economic wealth creation. Linked to this is the minimalist public policy: Windsor argues that this dates back to Smith,[51] where the distribution of wealth through competitive markets results in greater efficiencies. The ethical approach to CSR presents the argument that there are defects in morally indifferent businesses, and there can be social advantages of morally sensitive stakeholder management practices. The moral framework in this CSR context is drawn from the composites of various moral frameworks. Frameworks such as Kant, Rawls and stakeholder rights are identified as theories that can be drawn upon. The paper makes the argument that these are preferential over utilitarianism because CSR uses a basic shared principle of impartial moral reflection and practising altruism. Given that altruism is voluntary and may involve costly contributions, this is a moral choice that should be made by those who are affected. Corporate citizenship, as the final category, sits in between the ethical and economic categories. Within this category, Windsor identifies that corporate

[50] Duane Windsor, 'Corporate Social Responsibility: Three Key Approaches' (2006) 43 Journal of Management Studies 93.
[51] Adam Smith, *The Wealth of Nations* (1776) vol 11937, 1937.

reputation, strategic philanthropy and political influence are key elements. Instrumental in corporate citizenship is the managerial discretion based upon voluntarism. Therefore, 'being a good corporate citizen' is more than consideration and inclusion of stakeholders; it requires a greater level of philanthropy extending past normal corporate behaviour. Windsor considers these categories as non-hierarchical but have conceptual relationships between them. Corporate citizenship can overlap with both private wealth and ethical conceptions separately. However, ethical and economic viewpoints are mutually exclusive within this spectrum and cannot overlap conceptually.

Garriga and Melé observe that there is a landscape of theories that are often controversial and unclear.[52] They identify four groups of classification: instrumental theories, political theories, integrative theories and ethical theories. The first of these theories is analogous to both Windsor and Klonoski in that the objective of the instrumental theory is that of wealth maximisation. This conception of wealth maximisation is representative of the well-known Friedman view that the only responsibility is to increase profits. Garriga and Melé contend that this has long been the dominant theory and has enjoyed widespread acceptance. The second group of CSR theories identified is that of political theories, which focus on the interaction between business and society and on the power and position of the business and their correlative responsibility. In the political analysis of CSR, two major theories within the political categorisation can be identified and distinguished: corporate constitutionalism and corporate citizenship. The term corporate citizenship may have different meanings dependant on the viewpoint. However, this corporate citizenship centres around philanthropy, akin to Windsor above. Corporate constitutionalism can, however, be distinguished, as its focus is on businesses being a social institution, and as such, they must use their power accordingly. This concept was first explored by Davis in 1960, where the role of business power in society was investigated.[53] Davis argued that the ability to grow social power is not the sole result of internal management and decision making. Moreover, with significant power, the ability to influence the equilibrium of the market increases. Davis subsequently created

[52] Elisabet Garriga and Domènec Melé, 'Corporate Social Responsibility Theories: Mapping the Territory' (2004) 53 Journal of Business Ethics 51.
[53] Keith Davis, 'Can Business Afford to Ignore Social Responsibilities?' (1960) 2 California Management Review 70.

two principles to express how social power should be managed: ‘the social power equation’ and ‘the iron law of responsibility’. The social power equation states that the social responsibilities arise from the social power corporations have. In other words, if the corporate managers have an increased social power or influence, their responsibilities raise or increase at the same rate. The iron law of responsibility refers to negative consequences: those who fail to use the power responsibly will lose the power they wield. Therefore, the power must be linked to accountability and responsible practice. Garriga and Melé’s third group of theories is dubbed integrative theories, and this group explores how the business integrates social demands. They argue that how businesses interact with these social demands gives the corporation a certain legitimacy. The theories contained within this group are based on detection and response to social demands to achieve social legitimacy, acceptance and prestige. Within-group lies CSP, which seeks social legitimacy with a process for giving appropriate responses. This model of performance was introduced by Carroll[54] within his pyramid of CSR, which has since become one of the most cited theories of CSR. The fourth group of CSR covers ethical theories, which cement the relationship between business and society. These are based upon ‘the right thing to do’ to achieve a good society. The range of these ethical considerations is broad, covering ST, human rights, sustainable developments and more. This ethical group extends past the social dimension of Klonoski but is similar to the classifications identified by Windsor.

The three studies by Klonoski, Windsor, Garriga and Melé have identified and highlighted some key classifications and theories within the remit of CSR. Whilst the three studies do not provide for a unanimous agreement with each other (or within some of their internal groupings), some common themes and theories which are present amongst all the studies can be extracted. Melé labels these as mainstream theories and identifies four common themes[55] arising from the literature. The first is CSP, a theory grounded in sociology, and this is in some relation to the second category of Klonoski. The second is shareholder value theory (SVT) or fiduciary capitalism; linking to the above, this is perhaps what

[54] Archie B Carroll, ‘A Three-Dimensional Conceptual Model of Corporate Performance’ (1979) 4 Academy of Management Review 497.
[55] Melé (n 44).

Klonoski describes as fundamentalism and Windsor identifies as economic responsibility theory. The third is ST, in its normative version based on ethical perspectives. The fourth is CCT, which has roots in political studies. Within these four mainstream theories, SVT is the dominant theory whereby the Friedman doctrine[56] is followed. This research will utilise the theories comprising the SVT, ST and CSP to support its argument for a pluralist approach toward corporate governance.

CSP, for the purposes of this research, can be utilised as a framework to evaluate and define legitimacy.[57] Melé recognises that CSP has evolved from several previous notions and approaches.[58] The theory asserts that there are social problems for which businesses have responsibilities due to their contributions to these problems. This concept of businesses contributing to problems as opposed to solving them has been the focus of a recent British Academy research project,[59] , highlighting the continuing relevance of this theory. The purpose of CSP is to improve social performance, which is achieved through the altering of corporate behaviour. This corporate behaviour is adjusted to account for more beneficial outcomes for society. This departs and differs from the SVT due to profits being sacrificed for social benefits, which contradicts the Friedman doctrine where profit maximisation must be considered above all else. Wood presents a CSP that identifies three levels: first, institutional, organisational and individual; second, the processes of corporate social responsiveness; and third, the outcome of corporate behaviour.[60] The institutional principle has also been called the principle of legitimacy and has its origin in Davis, who presents interesting arguments based on ethics and social legitimacy.[61] The work of Davis in 1973 emphasises the responsibility of corporations where they hold power which has a social impact. The argument presented is that, in this instance, businesses must assume the corresponding responsibility. The power and

[56] Friedman (n 46).
[57] A definition of legitimacy is available in section 1.7 below.
[58] Melé (n 44).
[59] The British Academy, *Policy and Practice for Purposeful Business. The Final Report of the Future of the Corporation Programme* (2021).
[60] Donna J Wood, 'Corporate Social Performance Revisited' (1991) 16 Academy of Management Review 691.
[61] Keith Davis, 'The Case for and Against Business Assumption of Social Responsibilities' (1973) 16 Academy Of Management Journal 312.

responsibility are premised on the iron law of responsibility, where those who do not act responsibly shall lose their power.[62]

ST opposes the notion of shareholder value maximisation, arguing that other interests should be considered. Interests such as employees as providers of human capital could be included, as could customers, creditors and broader interests such as the environment. Garriga and Melé observe that there are several approaches to ST, and scholars differ in approaches as to the extent of how external individuals should be taken into account. Clarkson defines the approach:

> The firm as a system of stakeholders operating within the larger system of the host society that provides the necessary legal and market infrastructure firm activities. The purpose of the firm is to create wealth or value for stakeholders by converting their stakes into goods and services.[63]

The difference in this approach to that of SVT is that ST considers that the very purpose of the firm is to create value for stakeholders. The justification for this argument is that this value can then be converted into stakes in goods and services. This approach is much broader than SVT and provides wider benefits from the corporation to more than just its shareholders. Irrespective of the shareholder and stakeholder debate, the need for a legal infrastructure occurs in both theories of CSR. In addition to CSP and ST, there is the theory of corporate citizenship. The concept of corporate citizenship is premised on corporations engaging in acts to promote goodwill based upon the notion of philanthropy. The notion of corporate citizenship is best viewed through Carroll, and his CSR pyramid,[64] , which Visser argues is the most well-known model.[65] This section will now proceed to evaluate Carroll's model in further depth.

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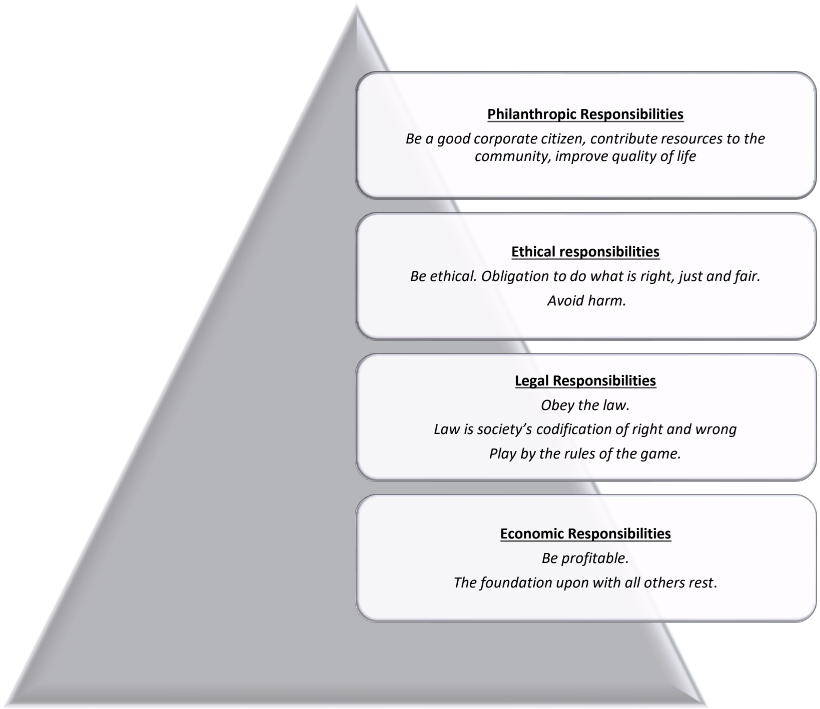
[62] Davis, 'Can Business Afford to Ignore Social Responsibilities?' (n 53).
[63] Max BE Clarkson, 'A Stakeholder Framework for Analysing and Evaluating Corporate Social Performance' in Clarkson Max (ed), *The Corporation and Its Stakeholders: Classic and Contemporary Readings* (University of Toronto Press 2016) <https://doi.org/10.3138/9781442673496-013> accessed 3 April 2022, 243.
[64] Onyeka K Osuji, 'Corporate Social Responsibility, Stakeholder Needs and Sustainable Development-Overcoming Contextual and Regulatory Challenges through the Values Paradigm' (2020) 8 Kilaw Journal.
[65] Wayne Visser, 'Revisiting Carroll's CSR Pyramid' [2006] Corporate Citizenship in Developing Countries 29.

Carroll's CSR model encompasses four parts, which he has designed in a pyramid, depicted in Figure 1 below, analogous to Maslow's famous rendition.[66] The four parts are broken down into the following categories: economic, legal, ethical and discretionary/philanthropic CSR.



[67] *Figure 1 Carroll's Pyamid of Corporate Social Responsibility*

The model which Carroll has depicted is a result of 30 years of businesses and firms struggling to comprehend the challenges of their responsibility to society. The result is a balancing of commitments between the corporations' owners[68] with their obligations to an ever-broadening group of stakeholders who can claim both legal and ethical rights. This challenge requires the transition from amoral and immoral directors into moral directors. This transition, Carroll argues, will result in CSR becoming a reality. For CSR to be accepted by conscientious businesspeople, it should be framed in such a way that the entire range of business responsibilities are embraced from this perspective. Carroll introduces

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[66] Abraham Harold Maslow, 'A Theory of Human Motivation' (1943) 50 Psychological Review 370. See also: William Kremer and Claudia Hammond, 'Abraham Maslow and the Pyramid that Beguiled Business' (*BBC News Magazine*, 2013) <https://www.bbc.co.uk/news/magazine-23902918> accessed 3 April 2022.

[67] Archie B Carroll, 'The Pyramid of Corporate Social Responsibility: Toward the Moral Management of Organizational Stakeholders' (1991) 34 Business Horizons 39, 42.

[68] Owners in this context defined as the shareholders.

his pyramid of CSR comprising four key themes, each of which builds upon the others, commencing with the economic and building upwards.

The first position which Carroll identifies relates to the economic responsibilities that corporations hold. The basis for this is that these responsibilities are the foundation upon which all of the others rest. Therefore, it is the first step of CSR and economic stability, and this responsibility needs to be in place to build upon the other elements of CSR. This economic principle is uncontentious: Klonoski considers this as his fundamentalism theory, Windsor as the economic responsibility theory, and Melé as the economics of wealth creation. Therefore, Carroll's positioning of economic responsibilities and the need to 'be profitable' is well justifiable as the first stage in good CSR. Without economic support, more philanthropic considerations will simply not be possible, and there will be no resources to carry these out. Carroll, in revisiting his theory, identified that profits are necessary to reward investors for growth.[69] Whilst it may appear contradictory, and indeed some of the scholars discussed earlier have identified them as distinct theories, economic considerations are social, and the contribution to their profitability provides benefits society more generally. The next category Carroll defines is that of legal responsibilities, obeying the law. This is premised on the ideology that law is society's codification of right and wrong, and as such, companies should comply with the rules of the game. This is the next logical element of CSR: if the first is to be profitable, then corporations should only be able to be profitable insofar as they obey the law. Polluting a local water supply may render significant profits,[70] , but this activity may operate outside of the rules of the game and, as such, should not be permitted. At its narrowest, businesses should comply with the laws and regulations as a condition of operating.

The next two elements which Carroll identifies are ethical responsibilities and philanthropic opportunities. These elements are more contentious than the preceding two, as they operate in a sharp departure from the shareholder maximisation theory or the Friedman doctrine. The ethical responsibilities provide

[69] Archie B Carroll, 'Carroll's Pyramid Of CSR: Taking Another Look' (2016) 1 International Journal Of Corporate Social Responsibility 1.
[70] *Okpabi and others (Appellants) v Royal Dutch Shell plc and another (Respondents)* [2021] UKSC 3.

that there is an obligation to do what is right, just and fair, and ultimately avoid harm. This 'be ethical' element follows from the construct that normative expectations of most societies hold that laws are essential but not sufficient. In this regard, the second category of legal measures provides the essential basis for the bare minimum of what is deemed acceptable and sets these out. The ethical element views this from a broader angle, looking at normative expectations, for example, what corporations should be doing in their decision-making. This differs from what they have to do by the relevant legal provisions. The inclusion of ethical considerations elevates a business's CSR from doing what is required as the legal minimum to doing what is right morally. This links to the transition from amoral or immoral managers Carroll identifies from the outset. As part of these ethical expectations, businesses will be responsive to the spirit of the law and not just the letter of the law. This also links to recent parliamentary debates, especially in light of the tax avoidance whereby the letter of the law is followed but not the spirit.[71] The last stage of the pyramid is philanthropic or discretionary responsibilities. Corporate philanthropy embraces businesses' voluntary or discretionary activities. Discretionary extends past both the legal requirement and moral normative assumptions of business. Carroll describes this element as being a good corporate citizen, which can be achieved by contributing to the community and improving the community members' quality of life. Within this community, five stakeholder groups are identified: owners (shareholders), employees, customers, the local community and society at large. The argument presented is that the primary difference between the ethical and philanthropic categories in this model is that business giving is not necessarily expected in a moral or ethical sense, and this voluntary nature is philanthropic. This is a consideration of being a good corporate citizen, where companies should seek to solve problems rather than create them. This study investigated corporate purpose and supports the current relevance of such categorisation by Carroll.

The aim of Carroll's pyramid is a unified whole. Stated in the form of an equation it would read as follows: economic responsibilities + legal responsibilities + ethical responsibilities + philanthropic responsibilities = total CSR. The attractiveness of

[71] See: House of Commons Committee of Public Accounts, *Tax Avoidance: Tackling Marketed Avoidance Schemes* (2013); Publications.parliament.uk, 'House of Commons - Uncorrected Evidence' (2017) <https://publications.parliament.uk/pa/cm201213/cmselect/cmpubacc/uc870-i/uc87001.htm > accessed 11 November 2017.

such a model for CSR is that each of the four components addresses various stakeholders with varying priorities. Working up the pyramid, shareholders will benefit through considerations of economic matters. Progressing through the remaining three categories, stakeholders in a broader context are considered. Moreover, the paper argues that the pyramid should be seen as sustainable and that these responsibilities represent long-term obligations. These long-term obligations do not detract from shareholders' interests, and they provide a platform and justification for broader considerations than a shareholder-centric position. This research will therefore adopt a CSR theoretical framework based on Carroll's pyramid of CSR.

1.3.2 Strengths of CSR

The preceding subsection has evaluated CSR as a framework, analysing the theory and how it has been defined by scholars. This section and the proceeding section will consider the strengths of CSR to justify its choice as the theoretical framework whilst also considering its weaknesses. Several strengths can be identified: first, the theory seems ethically superior to maximising shareholder value because it takes into consideration stakeholder rights and legitimate interests. The alternative to these stakeholder considerations is shareholder primacy. Ethical superiority arises out of consideration for more than a return on investment. Consideration of shareholders is a narrow approach that benefits the minority; for example, the decision to utilise fossil fuels may render greater profits, but renewable energy may be deemed more ethical. The shareholder-dominant approach will always result in the weighing up of profit-sacrificing against what the shareholders can expect in return for this sacrifice. An example of this could be that a corporation decides to close down a polluting factory, with the sacrifice in this scenario being the closure of a profitable factory. The possible benefit to these shareholders could be increased public perception, which may increase sales performance. The closure of such a factory, under the SVT, requires justification to the shareholders in exchange for an economically definable benefit. The strengths of CSR and this focus on ethical decision-making result in this economically definable benefit not being required. It removes the onus on management to value profits over stakeholders.

Through its focus on long-term self-interest, CSR also provides support for the notion of separate legal personhood. Where managers are focussed on short-term returns and delivering profits for each quarter, this focus can affect the longevity of the business. This focus on deliverable profits is premised on shareholder wealth maximisation and the shareholders being the owners of the corporation. CSR provides a longer-term approach in terms of both sustainability for the company and its wider stakeholders. This affirms the very concept of the corporation and does not detract from it being its legal person, and a greater focus on resilience and longevity provides a stronger outlook. Davis also highlights that one of the strengths of CSR is the ability to prevent some of the problems which can arise out of focus on short-term profits.[72] The argument presented is that prevention is better than cure, which is an argument in favour of a proactive as opposed to a reactive system. Preventing business failures and contributions to problems is desirable over 'curing' them after the damage has been done. This links to the claim that businesses often have the resources to aid this prevention and, as such, are well placed to consider greater CSR inclusions.

The key strengths of CSR are the tools it holds to tackle difficult sociocultural norms and provide solutions to some of the problems which arise out of business activity. Considering sustainable decision-making for stakeholders, in addition to stockholders, will increase the resilience of businesses and strengthen their longevity. Moreover, for this research, a CSR theoretical framework provides a foundation to evaluate the legitimacy and how this can be defined and evaluated against the research questions. In summary, the greatest strength of the CSR theoretical framework is in providing a broader approach to governance and the ability to consider more than the law and economics framework.

1.3.3 Weaknesses of CSR

Whilst CSR as a theoretical framework can boast many strengths in dealing with more contextual and broader issues; it is not without its weaknesses. Its largest challenge is the vagueness of the concept of CSR. Carroll's pyramid has depicted four elements that provide clarity to mitigate the vagueness; however, being a

[72] Davis, 'The Case for and against Business Assumption of Social Responsibilities' (n 61).

good corporate citizen can be interpreted in many ways. The general criticism of corporate citizenship is that it is a diffuse concept that includes many different topics as to the public-private relationship and contributions. It can be argued that this vagueness affords flexibility which allows businesses to be a good corporate citizen in a way which they consider. There is also flexibility in how businesses consider and evaluate stakeholder interests within the CSR model. Conversely, this level of flexibility can result in businesses not engaging with CSR as intended, rendering its framework redundant: this is a linked weakness. The ability to consider wider stakeholders has been accused of being an excuse for managerial opportunism and providing a basis for self-serving behaviour.[73] In this regard, corporate managers may be able to carry out actions that do not directly derive profit and justify this based on CSR. The absence of a rigid framework outlining obligations for managers to consider provides an additional risk to opportunism.

A further prevalent argument opposing CSR as a theory is that it goes against the business assumption of the classic economic doctrine of profit maximisation. Friedman is one of the leading proponents of this position, claiming that the responsibility should be fixed on the delivery of profits for shareholders. This is analogous to the 'shareholders' money argument' whereby it is the shareholders' capital that is being expended to achieve CSR objectives. From this perspective, it is indefensible that capital should be expended contrary to the shareholders' interests to benefit stakeholders. This can be further connected to the division of public and private affairs. The corporation, by its very nature, is a private organisation, and as such, it should operate within the confines of the private market. Public considerations should be left to those who are responsible for public decision making, and this should be left to those qualified to do. Freeman and Liedtka observe the efficiencies of such public interference, which is discussed below.

Freeman and Liedtka present the argument that CSR promotes incompetence within business decision-making.[74] This argument is based upon the skillset and qualifications of the corporate managers, for which Freeman and Liedtka argue

[73] ibid.
[74] Edward Freeman and Jeanne Liedtka, 'Corporate Social Responsibility: A Critical Approach' (1991) 34 Business Horizons 92.

CSR leads to managers making decisions beyond their expertise. Expanding on this, they claim that philanthropy represents charity taken on by choice; ethical conduct, on the other hand, is obligatory, and making these decisions is inherently complex. This complexity requires the evaluation of humans as social and economic beings, which corporate managers are simply unable to evaluate. The result is corporate managers making decisions that are not fully informed and which they are ill-equipped to deal with. Consideration of these complexities with welfare and socio-economic norms are not akin to corporate strategies, and treating them as such results in incompetence. In essence, it is inefficient to expect managers who hold business expertise to deal with social ills. Whilst this is a reasonable weakness identified, it is not an insurmountable challenge for large corporations. This could be mitigated with specialist directors, much like non-executive directors (NEDs), who have a role to play. Associated with the efficiency argument is the Adam Smith[75] theory which holds that greater efficiency can be derived from dividing up labour tasks. Despite this economical background, Smith contends that when working in this efficiency model, greater social interests can be brought about. The invisible hand is the concept which dictates that where individuals act in their self-interests, a greater social benefit can be obtained.[76] In the corporate scenario, providing an opt-out option exists, the company produces and sells a product for which the purchaser is better off for owning, as is the company following the sale. This process is carried out over time through many transactions, with each party concerned with their own self-interest acting as an invisible hand producing unintended social benefits. Interrupting this with social considerations may alter this premise and affect the market as a regulator.

CSR also considers that with ownership rights come responsibilities, not only for directors but for shareholders. Freeman and Liedtka[77] argue that rights and responsibilities are only part of the issue and not the whole story. An analogy is drawn to a pie whereby knowledge and responsibility are cut into discrete slices. Some responsibilities, the slices of pie, are placed onto the plates of producers, government consumers etc. Whilst this depiction appears attractive in ensuring

[75] Adam Smith, *The Theory of Moral Sentiments* (Penguin Books 2010).
[76] ibid.
[77] Freeman and Liedtka (n 74).

that each stakeholder gets their respective slice of the CSR pie, Freeman and Liedtka argue this cannot invoke the differing levels of complexities the slices of pie represent. There is an abstract level of shareholder v stakeholders, and even if the slices could be easily identified, the qualification and quantification are too complex to provide a satisfactory solution. In essence, the argument presented is that assuming each element Carroll depicts in his pyramid can be qualified or quantified is misplaced. This section has considered and evaluated some of the weaknesses presented in opposition to CSR as a theoretical model.

1.3.4 Alternative frameworks

Another suitable option for the theoretical framework of the research is that of law and economics. The law and economics theory is dominant in corporate law and offers the reason for justified legal practice. Butler contends that law and economics offers a framework where legal objectives can be modelled and common objectives to unify areas of legal activity.[78] The law and economics theory is predicated on the notion that human beings are rational maximisers for individual benefit. This links to the invisible hand notion proposed by Smith, whereby the result of this individual maximisation will eventually result in overall social benefit. The exchanges in an economic context have variable outcomes, which are definable due to the benefit arising from those exchanges. When this is compared against CSR, the law and economics framework is overwhelmingly more certain than the notion of wider stakeholder consideration that CSR advocates for. The concept of law and economics is not absent philosophical underpinning. It works with utilitarianism through this notion of increased maximisation. Each individual maximises their interests and own economic endeavour, which, results in greater collective maximisation, which increases utility. Where those disadvantaged by this position may be considered the 'losers', they can be compensated, and overall increased utility will be achieved. The basis of the law and economics theory is that of efficiency, and each individual seeks to be efficient with their time and resources, which will benefit society more generally. This, in turn, reduces the role of law required to govern

[78] Brian Edgar Butler, 'Law and Economics' (*Internet Encyclopedia of Philosophy and its Authors. A Peer-Reviewed Academic Resource*, 23 November 2021) <https://iep.utm.edu/law-econ/> accessed 23 November 2021.

exchanges, and legal provisions need only be utilised to redress unequal bargaining powers or positions. One argument favouring the economic analysis of law is that it can adjust theories as developments emerge. Evidence of this can be seen in the case of behavioural economics, game theory and public choice theory, which operate as variants to the traditional economic efficiency position.

1.3.5 Choice of framework

CSR and law and economics both provide frameworks grounded in established legal theory that could be utilised for this study. The benefit of the CSR framework over the law and economics approach is that it provides a broader consideration of social inclusion beyond economic efficiencies. This is not to suggest that the two are diametrically opposed, but that CSR affords greater parameters to explore the research questions. For this reason and the analysis in the preceding sections, law and economics can be discounted and CSR favoured. As identified, the concept of the legitimacy of corporate power can be investigated through the CSR framework considering each of the elements in Carroll's pyramid. This discussion of CSR elements provides for a broader consideration of stakeholders, which will provide clarity in addressing the research questions. Given the focus of the research on legitimacy and the existing body of literature in CSP about legitimacy, CSR will be adopted as the theoretical framework from which the research questions will be assessed.

1.4 Defining legitimacy

This thesis explores how legitimacy can be understood and evaluated in relation to corporate group power. The hypothesis is that corporate groups lack the legitimacy to hold the power which they wield. The research questions seek to address how the current legitimacy deficit can be challenged and if alternative frameworks can be used to derive greater legitimacy. The theoretical framework has provided the lens through which legitimacy will be analysed. Given the focus of this research on 'legitimacy', this subsection seeks to outline the definition of legitimacy which will be used throughout this thesis.

Legitimacy in the context of this research is considered a prerequisite to corporate power. Davis and Blomstrom contend that 'the idea that responsibility and power go hand in hand appears to be as old as civilisation itself'.[79] They argue that stated in the form of a general relationship, the social responsibilities of the business person need to reflect the amount of social power they have. Corporations wield significant power, which has social outcomes despite the private sphere in which those decisions are made. The research seeks to establish if this power is magnified in the group context and if so, how the legitimacy of this power is affected. Companies are granted their legitimacy and subsequent power through society and are expected to exercise it in a manner which society considers responsible.[80] There are objective minimum requirements that incorporated companies must comply with by way of checks and balances to retain their incorporated status and their correlative power. The iron law of responsibility indicates that those who do not exercise power within the social confines with which it was granted will lose such power. Power must, therefore, be controlled, and it is this control that is at the centre of legitimacy. This can be done through control mechanisms, such as fiduciary duties, shareholder voting and activism. The legitimacy of this power is derived from these control mechanisms and checks being in place.

This research seeks to determine what legitimacy of power is present in the group context. It will evaluate this through a historical analysis. This historical study provides the basis for corporate legitimacy and the control checks deemed to be a requirement to grant limited liability. Having established the basis upon which limited liability derived its legitimacy, this can be contrasted with how corporate power is utilised in the group context. Moreover, the thesis will discuss if these control mechanisms are analogous to those which initially provided legitimacy for the limited company. This research contends that if the control mechanisms are not analogous to the company's initial inception, and different from standalone corporations, then they are held to a different standard.[81] This different standard can challenge the notion of legitimacy from which corporate power is granted, resulting in a legitimacy deficiency.

[79] Keith Davis and Robert L Blomstrom, '(1968) 11 Academy of Management Journal 2, 172.
[80] ibid.
[81] See Jean-Philippe Robé, 'The Legal Structure of the Firm' (2011) 1 Accounting, Economics, and Law 1.

Legitimacy is, therefore, a prerequisite to corporate power, which arises through incorporation and is argued to be magnified in the group context. Those who exercise corporate power must have it legitimised through control mechanisms. Determining what constitutes a legitimate action or actions can be evaluated against the CSR theoretical framework explicitly looking at the CSP model on social performance.

1.5 Questions

The overarching aim of this thesis is to examine and elucidate how legitimacy can be understood in relation to corporate group power. To achieve this aim, the thesis seeks to answer four research questions to combine theoretical knowledge with practical considerations for evaluating legitimacy. First, it seeks to ascertain the following: have the two bedrock principles of company law – limited liability and separate legal entity – been accidentally extended to corporate groups? Blumberg contends that arguments in favour of limited liability are not applicable in groups and that the extension of this principle was a historical accident.[82] This first question posed by the research seeks to evaluate this extension in the context of corporate power to ascertain if the power wielded as a result of these bedrock principles is illegitimately held. Second, this research poses the question, to what extent is power magnified in the corporate group? The notion of corporate power is problematic within the company law sphere, and this research seeks to establish if, in slipping out of this already problematic area, the group power dynamic is magnified. It will evaluate this based on scrutinising whether the division of ownership and control is at a greater disparity in the context of a corporate group.

The third question addressed is that of addressing any identified legitimacy deficiency. Can greater legitimacy be derived from an alternative framework or conceptualisation of the company? It, therefore, asks, if there is a challenge with the legitimacy of corporate groups, is there an alternative framework? Fourthly, in implementing any alternative framework, the thesis asks the final question: if

[82] Blumberg, 'Limited Liability and Corporate Groups' (n 9) 626.

greater legitimacy can be derived from an alternative framework, how could this be realised? The research will explore how new technologies could provide a platform for any implantation of possible change. New technologies, with their range of tools, can bring benefits previously deemed unfeasible. In evaluating alternative conceptions to regain legitimacy, this thesis will explore how this could be assisted by new technologies, if at all.

The four substantive questions, therefore, are:

1) Have the benefits of incorporation been 'accidentally' extended to corporate groups, resulting in the illegitimate holding of corporate power?
2) To what extent is corporate power magnified in the corporate group?
3) Can greater legitimacy be derived from an alternative framework or conceptualisation of the company?
4) If greater legitimacy can be derived from an alternative framework, how could this be realised?

1.6 Methodology

This research will adopt an interdisciplinary research methodology that is largely doctrinal. In addition to utilising traditional 'black letter' primary sources, including case law, legislation and scholarly journals, the thesis will explore methods from other disciplines to answer the research questions.

Approached through a CSR lens, the thesis challenges the notion of legitimacy of corporate power within the corporate group. This is evaluated based on both historical and statistical analysis. To fully evaluate the evolution and legitimacy, an evolutionary account is required. Teubner[83] identified the systems theory which holds that law is influenced by, and influences, external systems. The thesis utilises empirical data and conducts statistical analysis to analyse the corporate group and support its recommendations.

[83] Gunther Teubner, 'Evolution of Autopoietic Law' in Gunther Teubner (ed), *Autopoietic law – A New Approach to Law and Society* (de Gruyter 2011).

The methodological approach in combining these different fields is patterned on the development by Roberts.[84] The research also draws upon empirical data showing patterns within the field of company law, allowing the research to produce graphs and reports from data available from Companies House and other sources. This section explains the features of the interdisciplinary approach adopted for this thesis, offers a justification for the selected disciplines, and considers how scholars apply this methodology in company law.

Given that legal research aims to contribute to the knowledge in a given field, any legal research must stand up to scrutiny. For the research to stand up to this scrutiny, established and accepted research methods must be used. The methods outlined in the succeeding section justify the methodology encompassed, establishing their accepted use within company law. Since this thesis will utilise various methods, it is important to establish what a method means. Whilst the terms method and methodology are used interchangeably, they mean different things.[85] A method can be defined as something done to enhance knowledge.[86] This is an action, for example collecting data and analysing through a framework to answer a research question. The methodology is often used to refer to these methods collectively. This thesis will utilise a broad range of methods to encapsulate an interdisciplinary methodology, and the justification for this is further explored in the following paragraphs.

Doctrinal research is considered the purest form of legal research,[87] where critical analysis of the literature of what is known and what is unknown is carried out.[88] The doctrinal method is, therefore, the black-letter approach to the law, looking at the literary works to reach conclusions. Hutchinson believes doctrinal research is a two-stage process, first locating the law in the literature and secondly analysing it. This argument is persuasive: all elements of legal research require an element of doctrinal research to establish what is currently known about the field being researched. The analysis can benefit more from a range of methods.

[84] Paul Roberts, 'Interdisciplinarity in Legal Research' in Michael McConville and Wing Hong Chui (eds), *Research Methods for the Arts and Humanities* (2nd edn, Edinburgh University Press 2017).
[85] Dawn Watkins and Mandy Burton, *Research Methods in Law* (Routledge 2013) 2.
[86] ibid.
[87] Roberts (n 84) 100.
[88] Terry Hutchinson, 'Doctrinal Research' in Dawn Watkins and Mandy Burton (eds), *Research Methods in Law*, vol 1 (Routledge 2013).

As already delineated, this research will utilise different methods of analysis from different fields to address the questions posed. The starting point must, however, be doctrinal to provide the historical framework this research intends to utilise. Doctrinal research has been defined as seeking to 'provide a detailed and highly technical commentary upon, and systematic exposition of, the content of legal doctrine'.[89]

It is from this technical analysis that the research seeks to analyse the fundamental principles of corporate law and their relationship with the corporate group, specifically in relation to group power. The doctrine has developed and evolved over the last two centuries, and this research seeks to use this historical analysis to challenge the legitimacy currently found in the corporate group. Following the doctrinal underpinning, the research will then utilise interdisciplinary methods to evaluate corporate groups' power and potential effects on society. Given the rich history and evolution within company law, a doctrinal element is essential in establishing a solid foundation to analyse the current construction of the law. It will also provide a comparator of how the current law differs from its predecessor through a black-letter approach.

The justification for selecting methods from business and economics studies and business studies is the importance of these fields in understanding company law. Moreover, statistical analysis provides data to link the theory with the practice. Given that company law governs the business, the two are intrinsically linked. Deakin argues that the understanding of economic methods is important in establishing how corporate governance functions. Moreover, Deakin presents the argument that systems arise between agency and structure. In this sense, they are also adaptive, and they co-evolve with the environment and each other.[90] Given that these systems co-evolve, an analysis of the environment in which the law operates is beneficial. This is a persuasive argument given the role economics plays in the governance of a company. This links to practical elements which need to be considered and which may not present themselves in black-

[89] Michael Salter and Julie Mason, *Writing Law Dissertations: An Introduction and Guide to the Conduct of Legal Research* (Pearson/Longman 2007) 49.
[90] Simon Deakin, 'Legal Evolution: Integrating Economic and Systemic Approaches' (2011), 7 Review of Law & Economics, 3.

letter research alone.[91] If law co-evolves with external systems, these external systems need to be analysed in conjunction with their doctrinal origins.

Legal concepts and terminology are the results of judicial ontology. Terminology and legal concepts cannot be studied on their own without context because this will restrict the level of analysis which can be carried out. Deakin explains this by utilising the example of the 'employee', which requires unpacking.[92] The reason for this is that certain rights attach themselves to employees, and all of these rights are embedded within the definition of an employee. Additionally, without context, what is an employee? This example applies to this research because in the absence of a strict definition for corporate groups, we need to establish what is meant by this in its social and economic environment. The historical lens through which this research aims to analyse the corporate group requires an economic and business setting to place juridical concepts in the economic reality from which they derive. A business is not a company it is a process that can be encompassed within a company or, indeed, in many other structures. A detailed understanding of what a business is, and perhaps more pertinently, what a business is not, will benefit this research more than if doctrinal research alone was used. One simplistic definition of business is offered by Heitor De Avila Santos:

> Business can be classified as an organization that is involved in commercial, industrial, or professional activities. A company may manufacture a product, render a service, or act as a third party on retailing manufactured goods.[93]

A business's aim, therefore, is to generate profit, which is usually done by offering a product or a service. Understanding the role of business and how this has shaped or been shaped by legislation will assist in answering the research questions. This research aims to utilise the study of business to enrich the analysis of the thesis. Moreover, this analysis deals with the concepts such as supply and demand and why certain decisions are made or could be made to produce a defensible outcome. The branch of economics this research seeks to

[91] Simon Deakin and Alan Hughes, 'Comparative Corporate Governance: An Interdisciplinary Agenda' (1997) 24 Journal of Law and Society 1.
[92] Simon Deakin, 'Juridical Ontology: The Evolution of Legal Form' (2015) 40 Historical Social Research/Historische Sozialforschung 170, 171.
[93] Joao Heitor De Avila Santos, *Business and Society* (Society Publishing 2019) 5.

utilise is behavioural economics. This is concerned with developing theories to better understand the world in which we live.[94] The concept of behavioural economics is that it supplements the traditional branches of economics and seeks a more realistic foundation for how decisions are made. This thesis questions the role of power in the historical development of corporate groups to challenge the legitimacy which they are built upon.

Empirical data analysis can reveal counter-intuitive patterns, which in turn can test basic assumptions about the world.[95] The empirical data this thesis will be analysing will be data provided by government sources such as Companies House, the Insolvency Service and the Office of National Statistics. The thesis will also seek data from business-orientated databases such as Fame and Orbis to highlight corporate structures and the links amongst corporate groups. This research will also utilise data from annual returns for case study analysis. This data will provide the base for analysis through the framework set out by the thesis. Analysis of empirical data can contribute to several sectors, including academics and practitioners.[96] Moreover, given the co-evolutionary importance of corporate law, using such data provides a broader understanding of the corporate group.

Deakin opines that the social realm is a subset of the natural one and that analysing legal concepts in their social reality is when these concepts are best understood.[97] The law may seek social change, or societal values may seek to change the law. Change to the law may also be driven by factors external to society and may be impacted by political values, which might encompass corporate power. The legitimacy of corporate power is control, which requires legislative input to avoid a laissez-faire market. Corporate power should have a cost, and one way to enforce this cost is to ensure companies carry out their business within the expectation of society.[98]

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[94] Nick Wilkinson and Matthias Klaes, *An Introduction to Behavioral Economics* (Red Globe Press 2017) 4.
[95] Alan Dignam and Peter B Oh, 'Disregarding the Salomon Principle: An Empirical Analysis, 1885–2014' (2011) 39 Oxford Journal of Legal Studies, 4
[96] ibid 33.
[97] Deakin, 'Juridical Ontology: The Evolution of Legal Form' (n 92) 174.
[98] Janet Dine, 'The Abuse of Company Groups' in Hanne Birkmose, Mette Neville and Karsten Engsig Sørensen (eds), *Abuse of Companies* (Wolters Kluwer 2019) 36.

When analysing how power affects society, there need to be parameters set for how we measure these effects. This thesis utilises a CSR framework to critically evaluate the effects of power on society. The research seeks to ascertain if looking at the company differently changes how the company as a facilitator of contracts is perceived. It will allow the research to investigate a broader interpretation of the law.

The justification for utilising an interdisciplinary approach can be based upon the social context in which corporations exist. They operate with significant corporate power, which permeates society, and to ascertain the legitimacy of corporate power; these external systems must be included. This research will, therefore, utilise research methods encompassing statistical data analysis and doctrinal research to provide the thesis with rich interdisciplinarity. Company law governs how businesses operate; therefore, interdisciplinary methods to understand why groups are structured and how this affects their corporate power will provide a more coherent response to the research questions than if doctrinal analysis alone was used.

It has been argued that we are now seeing more litigated cases that are generally outside of the traditional company sphere;[99] however, companies are being used as a vehicle, driving the causes for litigation. One reason mooted for such contentious activity is tax planning, as we have seen with Google, Amazon and Starbucks, but other reasons such as family financial planning could be another, as we saw in the case of *Prest*.[100] This provides evidence of company law expanding into different disciplines,[101] strengthening the argument for interdisciplinary research.

There have been numerous critiques directed towards pure doctrinal research as to how the law on paper cannot simulate the reality of what happens in practice. This thesis will be investigating corporate power within corporate groups; therefore, a pure doctrinal research methodology may not yield the results required to answer the questions posed by this research. Cheffins argues that

[99] Dignam and Oh (n 95).
[100] *Prest v Petrodel Resources Ltd* [2013] UKSC 34.
[101] Such as tax, politics, economics.

doctrinal research does not qualify as a theory, as he considers theory to be external to the law.[102] He considers that theoretical scholarship is the study of law from the outside, utilising other intellectual disciplines. This concept of studying the law from the outside is a convincing argument. The law works in action affecting those that it governs. This strengthens the argument that the law should therefore be studied from this viewpoint. Interdisciplinarity has the potential to impact rules on behaviour and increase overall comprehension of law as a field.[103]

Cheffins contends that company law evolved from an uninspiring field to gain prominence, utilising an economic approach when discussing company law methods.[104] The change in method for researching company law has deepened the analysis and improved scholarship. This is due to the change in methods to include a wider array of literature than was previously utilised and is a persuasive argument in favour of using more flexible research methods. Cheffins not only maintains that utilising alternative approaches in the field of company law is accepted but further claims that as a result, it has made the field gain more prominence. The prominence evolving into company law could be due to the practical application and increasing relevance of company law when combing the research methods to evidence the role it plays in society. For example, the large-scale collapses of Carillion, BHS and Flybe have had significant impacts on society and the economy. It has been highlighted that interdisciplinary research in company law is becoming more common.[105] The change in direction from a pure doctrinal methodology, therefore, appears to be gaining ground in the field of company law. Cheffins states that as 'the rules governing corporate activity tend to be a state of flux, knowledge of the law as it is now should be accompanied by an understanding of the forces which determine its current form and its ongoing development'.[106]

This argument is in favour of interdisciplinary research because the study of factors external to law – such as behaviour, economics and history – can provide

[102] Brian R Cheffins, 'Using Theory to Study Law: A Company Law Perspective' (1999) 58 The Cambridge Law Journal 197.
[103] ibid 201.
[104] ibid 209.
[105] ibid 215.
[106] ibid.

insight where doctrinal research or legal theory alone cannot. This links to the reasoning from Deakin, who argues in favour of legal principles being understood in their social reality.[107] Deakin highlights the importance of understanding the economic effects of corporate governance systems.[108] Consequently, in governance, a balance is to be struck between accountability and competitiveness.[109] In ascertaining what is meant by this accountability and competitiveness, interdisciplinary methods yield the most comprehensive results due to the co-evolutionary relationship which exists. This argument for interdisciplinary research is on the basis that there has been longstanding collaborative working therein.[110] Claiming that there are several illustrations of interdisciplinarity and giving examples such as law and philosophy, law and economics and law and politics,[111] Roberts argues this has developed into specialist hybrid courses being offered by institutions, such as law with business studies. Due to this development and common cross-over with certain topics, Roberts poses the question, what is truly legal research anymore? Roberts claims that even topics such as justice are no longer exclusively legal.[112] The argument here is that regardless of how methods are categorised, it is unlikely, given the development of research, that legal methods are now exclusively legal, and the exclusively legal method is becoming less common. True legal research is defined as an insider perspective on law and its institutions, a purely internalised research method.[113] This feeds into the traditional doctrinal analysis which has become so entrenched within legal scholarship. On this, it has been emphasised that doctrinal analysis cannot determine if the law is effective in practice.[114] Roberts advocates that interdisciplinary is an asset and is essential for many kinds of research problems.[115] A caveat has been provided that the research questions posed must suit interdisciplinary research and that mediocre research does not simply become improved because interdisciplinary methods are 'injected'.[116] An interdisciplinary approach is indispensable when research questions cannot be answered without data. Comparing this with the views of

[107] Deakin, 'Juridical Ontology: The Evolution of Legal Form' (n 92) 171.
[108] Deakin and Hughes (n 91) 3.
[109] ibid 3.
[110] Roberts (n 84) 93.
[111] ibid.
[112] ibid 94.
[113] ibid.
[114] ibid 105.
[115] ibid 100.
[116] ibid.

Cheffins and Deakin, the data which is required to answer questions of corporate governance and company law measures the impact decisions have on society and how companies operate. This type of data cannot be derived from a doctrinal method alone. Therefore, the interdisciplinary is a method that is not only developing as legal scholarship progresses: depending on the questions posed by a researcher, interdisciplinarity provides a framework for which truly legal research alone may not be able to provide answers. This conclusion on doctrinal research and the analysis of interdisciplinary from Roberts is analogous to the arguments of Deakin and Cheffins.

Not only are interdisciplinary research methods in legal scholarship becoming more accepted, but following support from Cheffins, Deakin and Roberts there is an application in the field of company law more specifically.[117] Whilst the doctrinal method is considered the most historically dominant research method, there is now growing acceptance for interdisciplinary methods about legal scholarship. Despite this, Hutchinson argues that in most elements of interdisciplinary research, there will be some doctrinal aspects that remain.[118] The arguments presented by scholars highlighted in this section demonstrate the persuasive arguments in favour of interdisciplinary research. Moreover, even in adopting interdisciplinarity, the long-established methods within the doctrinal realm will still be utilised but simply enhanced by the inclusion of additional fields. The direct applicability to the methodology applied to this research will permit the research to address the questions posed to provide a new contribution to the field.

This section has identified the importance of establishing a coherent methodology that will enable the proposed research questions to be answered. It has also been evidenced that whilst a doctrinal research methodology has historically been dominant, there is a growing acceptance for interdisciplinary research, especially in the field of company law specifically. Additionally, it has been argued that in most interdisciplinary methodologies, academics agree that there will be some form of the doctrinal method due to the nature of legal scholarship. This research

[117] See Adaeze Okoye, ‘Reflexive Law and Section 172 Reporting: Evolution of Social Responsibility Within Company Law Limits?’ (2021) 32 European Business Law Review 501.
[118] Terry Hutchinson, ‘The Doctrinal Method: Incorporating Interdisciplinary Methods in Reforming the Law’ (2015) 3 Erasmus Law Review 130.

will, therefore, utilise a methodology categorised as interdisciplinary, composed mainly of doctrinal methods to identify and evaluate the law, with methods from wider literature to answer the questions posed.

1.7 Outline of the thesis

This chapter has identified the aims and arguments of the thesis along with the research questions setting out what the research intends to address. This chapter has also provided the methodology outlining the methods which will be used to address the questions posed by the research. It has also provided the theoretical framework, CSR, which the thesis will utilise to answer the research questions. The concept of legitimacy is central to this research; as such, a definition of legitimacy and its significance for the research has been offered.

Chapter two will move on to address the first task and question of the research in exploring the basis upon which the corporate group evolved. It critically analyses both the emergence of the bedrock principles of company law and explores the benefits of incorporation, which result in corporate power. This analysis of the historical position will provide a framework to compare the historical legitimacy of these principles against the evolved modern corporate group. It surveys the historic and meteoric rise of the modern group. It will evaluate the historical evolutionary development of the modern corporation and the importance of this evolution in the group context. In analysing this legal evolution, this chapter also considers the judicial interpretation over time to draw parallels with the evolution of modern business. This interpretation provides a touchstone of the reception of corporate groups throughout their historical development. Chapter two will then proceed to discuss the evolution of the modern corporation to map the changes over time.

Chapter three will evaluate the role of corporate power, analysing what is meant by corporate power and its significance. It considers if the separation of ownership and control[119] has increased and to what extent this plays a role in the modern corporation. Chapter three will also evaluate restrictions and proposals

[119] This separation is the central argument of Berle and Means, and this thesis will analyse its relevance nearing a century after its initial conception.

for restrictions on corporate power. This analysis of the role of corporate power provides the platform to address the question of the magnification of corporate power in the group context, which is explored in chapter four. Chapter four will identify what makes corporate groups unique and what this result is on corporate power. It will ascertain the role of corporate power in its magnified state of the corporate group. Furthermore, it will evaluate how this corporate power manifests itself and consider methods of legitimising the power which it wields to ensure correlative accountability.

Chapter five will encompass the interdisciplinary methods, exploring empirical data on corporate groups. The chapter will proceed to evaluate the scale of the corporate group and establish if the problem hypothesised is, in fact, of practical significance. This chapter will consider the abstract position against the position with a defined data set of companies. Secondly, the chapter will explore the beneficial owners of corporate groups to draw parallels between conceptions of company law theory. This will provide a platform to explore the applicability of the Friedman doctrine in the capacity of the corporate group. The analysis will seek to provide an understanding as to the economic underpinning and reasons for corporate groups. Case studies of corporate groups will also be included within chapter five to provide a practical element to structures of companies. This chapter contributes to addressing how power is magnified support for alternative frameworks and conceptions of the company. This dovetails into chapter six, which will explore how legitimacy can be derived both from a theoretical perspective and from a practical implementation perspective. It will evaluate alternative methods of conceptualisation of the company to derive greater legitimacy. These alternative methods will be evaluated against the need to legitimise corporate power and against the historical backdrop which underpins the modern corporation. Exploring these alternative conceptions, chapter six will seek to address what benefit can be derived and if alternative models would address the purported legitimacy deficiency of corporate power within the corporate group. Having critically evaluated differing conceptions, the chapter will explore how any change could be introduced. New technologies as methods of implantation will be further explored. With alternative conceptions and methods of implantation considered, the chapter will move on to proposals to facilitate this. Company law is technical, and with fiduciary duties binding managers, there would need to be legislative facilitation for any change to be accepted. Proposals will be put forward to facilitate any changes presented by the research. Chapter seven of the thesis will move to provide a conclusion and summarise the findings and apply these to the research questions.

1.8 Findings

This thesis has explored the inherently complex nature of corporate groups to enhance the understanding of how corporate power manifests itself within the group structure. The principal finding of this thesis is the omnipresence of the corporate group within large corporations and its wielding of power without a legitimate basis. The data study identified the use of the corporate group in all large corporations. There is a direct causal link between the use of the corporate group and the growth of corporate power. This transcending of the corporate group was based upon the evolution of the modern corporation extending the bedrock principles to the group. Whilst it is expected that corporations will change over a significant period, how this evolution occurred is peculiar. There was a lack of debate in the expansion of these principles to the corporate group; furthermore, the common law position shows a demonstrable shift over the years in which the group became dominant. The iron grip of *Salomon* remains, the corporate group is a product of evolution, and this thesis affirms the position in the UK aligning with the historical accident Blumberg discovers within the United States of America (USA).

The result of such growth without debate and control mechanisms gives rise to a legitimacy failure of corporate power within the group. Legitimacy is at the centre of wielding corporate power, and those who exercise power must have it legitimised through control mechanisms. This is the paradigm of responsibility and power. The historical evolution has failed to develop control mechanisms as the group grew in prominence, resulting in the finding that group power is illegitimate. The empirical data shows the use of groups is synonymous with large organisations facilitating further growth with unfettered power. The finding of this thesis is that there is a legitimacy failure of power within the modern corporate group, which requires addressing. This research proposes a pluralist social conception of the corporation and further finds that implementing this through new technologies is both plausible and defensible.

1.9 Summary

This chapter has introduced the argument of the research along with the aims and objectives. It has set out the research questions and the theoretical framework from which these will be approached. It has also detailed the methodology outlining how the research questions will be answered. It has also provided an outline for the thesis, including what will be discussed in each chapter, how this relates to the overall thesis, and the questions it seeks to answer. This chapter has also provided a summary of the findings of the thesis. Chapter two will provide critical analysis of the historical foundations of company law to enable an established framework to address the research questions posed.

Chapter 2: The Rise of the Modern Corporate Group

'[Limited liability] is a privilege healthy as tending to the expansion of opportunities and commerce, but it is open to abuse. Irresponsible structural engineering – involving the creating, dissolving and transforming of incorporated companies to the prejudice of creditors.'[1]

The preceding chapter, chapter one, outlined the goals, argument, research questions and theoretical framework of this research along with the methodology. It also defined the concept of legitimacy and how this would be evaluated throughout the research. Chapter two seeks to advance the thesis by exploring the historical evolution of the corporation. This will enable the proceeding chapters to critically analyse the effect this evolution has had on corporate power and, subsequently, its legitimacy. Moreover, this chapter will provide the historical framework for challenging legitimacy. It will present the argument that limited liability was not initially intended to extend to the corporate group and as such groups are not held to the same standard. The aim of this chapter is to investigate and analyse the history of the modern company and its requirement for law to govern these corporate principles and their subsequent applicability to the corporate group. This analysis will provide a framework for the thesis to both challenge the legitimacy of the corporate group and present methods of attaining greater legitimacy. The next chapter, chapter three, will consider the role of corporate power and the result of the evolution that this chapter analyses.

The historical origins of the business organisation and its evolution into the modern corporation warrant a critical evaluation due to its intrinsic link with the corporate group. Both the historic and modern treatment of the corporation is individualistic in nature, and each corporation is legally separate. This stems from the parallels drawn to natural persons who are all individually unique. This research posits that this individualised treatment is misplaced, as corporate groups are not akin to individuals who are not aligned to enterprise operation. The contextual position should be reflected and not sperate from the legal position. In analysing the effect of the current legal position on corporate groups,

[1] *Nicholson & Ors v Permakraft (N.Z.) Ltd (in liq.)* (1985) 3 ACLC 453 [460].

it is fundamentally important to analyse historical developments and attempts to resolve the tension between the contextual and legal positions. This chapter will, therefore, explore how both parliamentarians and the judiciary have treated corporations in the evolution cumulating in the widespread use of the corporate group and examine the tensions between legal and economic separateness.

Part one of this chapter will look at the historical evolutionary development of company law and its fundamental importance for the concept of limited liability in the group context. Analyzing the historical nature and ascertaining how the current law came into existence will provide a framework for understanding the need for company law and how it has developed over time. This research argues that the development of company law has not developed at the same rate as the modern corporation, requiring further historical analysis to fundamentally understand how the concept of limited liability came into existence. The development of the Anglo-American corporation into corporate groups has been described by some scholars as a historical accident.[2] Therefore, the context of history is required to demonstrate that principles of modern company law are of great significance in establishing if corporate groups lack legitimacy.

Part two of this chapter will consider the historical evolution and the judicial interpretation of the legal principles of corporate groups. This analysis will provide a platform to understand how these principles have been conceived in the judicial context and how this has shaped the modern corporate group. Part three will investigate the legal theory behind the need for corporate law. The theoretical background will be the foundation for the investigation of differing methods of conceptualisation of the company, analysed in chapter six. Legal theory must be seen in the context of the relevant historical period; therefore, this chapter will contribute to the thesis by providing the basis for company law and establishing its importance within the UK legal framework. Having evaluated the literature and basis upon which corporate legal principles are premised, the research will proceed to investigate the effect this has had on corporate power and how this manifests itself in the group context.

[2] Phillip I Blumberg, 'Limited Liability and Corporate Groups' (1986) 11 Journal of Corporation Law 573.

This chapter will, therefore, proceed as follows; first, it evaluates the historical evolution of the statutory company law provisions. Within this analysis, the argument is presented that the legislative formation requirements have increasingly become diluted. The result of this dilution is that the 'standard' the modern corporate group is held to is vastly different from the one which was in the contemplation of government when company rights were introduced. This chapter then proceeds to assess to what extent this disparity between modern and historical corporations has been considered within the courts. This analysis of the judicial interpretation demonstrates a conflicted approach throughout the last century with attempts to disregard the corporate form at various points over this period. Irrespective of the economic climate being different between modern and traditional companies, the principles established in seminal case law remain the touchstone of corporate law. The chapter then appraises the theoretical underpinning of company law. Having demonstrated that the evolution without debate is problematic, the chapter considers alternative approaches. In consideration of alternative approaches, the chapter moves to consider the very basis for limited liability and separate legal personality.

2.1 The historical evolution of statutory company law

This section will first evaluate the historical evolution of corporate law and its significance of this evolution. The finding is that key features of company law, such as limited liability, were never intended to extend to corporate groups. The result of this is that power wielded by these groups lacks correlative control mechanisms, which undermines their legitimacy. The importance of this historical analysis is therefore of significance. This section will further consider and evaluate the evolution of the Companies Act. Since its inception, there have been several iterations which have eroded some of the control mechanisms, further challenging the legitimacy of the corporate group. The argument is submitted that the dilution of some control mechanisms has further facilitated the use of the corporate group, resulting in growth. Chapter five identifies that corporate groups in larger corporations is ubiquitous: this historical evolution has made a considerable contribution toward this growth. The latest Companies Act[3] and its

[3] The Companies Act 2006.

current iteration will be considered, both in its definition of the corporate group and how judicial interpretation of the groups has developed over time. This evolution over time maps out how legislative reform has been adopted and the impact of changes on the use of the limited company.

2.1.1 The significance of historical evolution

The importance of the historical evolution of principles of the company cannot be overstated. This subsection presents the argument that the evolution of company law has resulted in the growth of the corporate form and its extended use in the group context. Blumberg contends that the doctrine of limited liability in the context of the corporate group is one of a 'historical accident'.[4] This subsection will investigate how historical evolution has become significant in the creation of the modern corporate group. This is supported by scholars such as Blankenburg, Plesch and Wilkinson, who argue that the modern corporation is a result of gradual evolution shaped by corporate power.[5] This direct correlation between corporate power and evolution has led to the mass adoption of the corporate group. This development has resulted in irreversible corporate responsibility.[6] This chapter argues that the historical justification for bedrock principles – such as limited liability – was initially subject to strict constraints on power. The expansion to groups does not correlate with the initial norms of the corporation. This historical erosion of these constraints has resulted in the power balance being shifted and misplaced.[7] The use of corporate groups, as further explored in chapter five, has facilitated and enhanced the growth of the corporation, resulting in this power-balance shift. The dilution of these constraints has resulted over a period of corporate laws evolution ceding to corporate power and the conflicting aims of those running organisations and those governing them. The greater the power, the greater the risk of misuse of the bedrock principles,

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[4] Blumberg, 'Limited Liability and Corporate Groups' (n 2).
[5] Stephanie Blankenburg, Dan Plesch and Frank Wilkinson, 'Limited Liability and the Modern Corporation in Theory and in Practice' (2010) 34 Cambridge Journal of Economics 821.
[6] Paddy Ireland, 'Corporate Schizophrenia: The Institutional Origins of Corporate Social Irresponsibility' in Nina Boeger and Charlotte Villiers (eds), *Shaping the Corporate Landscape Towards Corporate Reform and Enterprise Diversity* (1 edn, Hart Publishing 2018).
[7] Dalia T Mitchell, 'Legitimating Power: A Brief History of Modern US Corporate Law' in *Research Handbook on the History of Corporate and Company Law* (Edward Elgar Publishing 2018).

increasing risks such as managerial opportunism.[8] This development of the law relating to corporate groups is of fundamental importance, as without limited liability and its expansion, corporate groups would not have grown into their current pervasive form. The extension of these corporate principles to artificial persons from natural persons is a result of historical evolution and one which has been extended to corporate groups with a lack of substantive debate.[9] This lack of debate results in a legitimacy failure for corporate groups as they wield power without the control mechanisms initially envisaged. As the corporations grew, procedural scrutiny did not allow the adaptation of principles. Tsuk Mitchell contends that this historical development has increased corporate power, not mitigated it.[10] This can also be seen in legislation which adopts a hands-off approach to business operations.[11] This increased corporate power continues to influence the evolution of corporate law and has continued to do so for the last century, permitting principles to be extended to fit different models of business.

Many contend that limited liability, the most significant feature of corporate law, commenced around the time of the South Sea bubble.[12] However, a recent paper has argued the importance of historic company law occurs much earlier.[13] The claim is that this importance of corporate law can be dated back to the 1550s, further supporting the importance of historical data. Three important periods are presented; period 1, before the conceptualisation of limited liability 1600–1800; period 2, in which the emergence of limited liability 1780–1855 as previously identified; and period 3, where the convergence to a single uniform liability regime was happening. The widely accepted view is that corporate history began in period 2 with the emergence of the limited liability doctrine. Harris, however, argues that periods 2 and 3 are a corollary from what he dubbed period 1. This predates the mention of limited liability and appears to correlate to larger

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[8] ibid.
[9] Janet Dine, *The Governance of Corporate Groups SE - Cambridge Studies in Corporate Law No. 1* (Cambridge University Press 2000) xix.
[10] Dalie Tsuk Mitchell, 'The End of Corporate Law' (2009) 44 Wake Forest L Rev 703.
[11] See s 172 of the Companies Act 2006 for example, and the discussion from Elaine Lynch, 'Section 172: A Ground-Breaking Reform of Director's Duties, or the Emperor's New Clothes?' (2012) 33 Company Law 196.
[12] 1700–1725, see Paddy Ireland, 'Finance and the Origins of Modern Company Law' in Grietje Baars and André Spicer (eds), *The Corporation: A Critical, Multi-Disciplinary Handbook* (Cambridge University Press 2017); Blumberg (n 2); Mitchell (n 7).
[13] Ron Harris, 'A New Understanding of the History of Limited Liability: An Invitation for Theoretical Reframing' (*SSRN*, 2019) <https://ssrn.com/abstract=3441083> accessed 29th August 2019.

enterprises created by royal charter, such as the East India Trading Company. Data is provided to support this theory claiming the term 'limited liability' was not used in books until the 1800s.[14] The relevance of this data is the argument that companies prior to limited liability were still enjoying prosperity. This appears to contradict the longstanding justification for limited liability and separate legal personality, the promotion of the economy by reducing risks for investors. One of the drivers for limited liability was that without limited liability, economic growth would be slow due to the lack of investors. This presents a differing argument claiming that had limited liability not been introduced, this would have had a nominal effect. This is of significance for the corporate group, as the group has become powerful due to its ability to partition and divide its operations. Moreover, without limited liability, the requirement of legitimacy becomes less significant because the power wielded is analogous to power wielded by other business forms. This argument contradicts a widely accepted viewpoint that limited liability is one of the great inventions of modern times.[15] This challenge to the accepted view is defended by examples, one of which is the widely debated[16] pro-rata liability that existed in California up until the 1950s. Harris submits that this use of proportional liability in California did not stunt any growth of California when compared to other US states in the same period. Scholars have argued in favour of bringing back proportional liability for certain types of companies.[17] This is controversial and whilst it remains superior in its argument compared to unlimited liability, jointly and severally, it increases the exposure to risk with no limit, which will disturb the capital market.

Limited liability can also be seen across the USA,[18] and evaluation of the Anglo-American corporation provides a greater context in which to investigate the history of the corporation. Additionally, consideration of the American company provides insights which cannot be found within the laws of England and Wales. The USA, for example, can have different legislation governing their companies

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[14] ibid 15.
[15] Nicholas Murray Butler, *Why Should We Change Our Form of Government?: Studies in Practical Politics* (Palala Press 1912) 82.
[16] For example, see Gordon G Sollars, 'An Appraisal of Shareholder Proportional Liability' (2001) 32 Journal of Business Ethics 329 and Jonathan M Landers, 'A Unified Approach to Parent, Subsidiary, and Affiliate Questions in Bankruptcy' (1975) 42 The University of Chicago Law Review 589.
[17] Sollars, 'An appraisal of shareholder proportional liability' (n 16).
[18] An analysis of historical US legislation is beyond the scope of this research.

despite operating within the same country and economy. This provides a unique opportunity to analyse two regimes operating within the same country at the same time. This makes for a rich comparison due to the commonality of cultures and economic outlooks. One such example is the state of Massachusetts, which provides a real-time comparator to the state of New York with its forward-thinking principles. Massachusetts, unlike New York, remained at the unlimited liability end of the spectrum. New York is regarded as the birthplace of the modern corporate group permitting companies to own shares in one another; it is, therefore, a progressive state in relation to companies. Harris presents the argument that despite Massachusetts following the unlimited liability regime, it remained the most advanced corporate economy in the USA. This argument is based upon empirical evidence showing the number of charters being issued around 1820. The comparison is that despite New York offering progressive limited liability, it grew no faster than the economy of Massachusetts. This provides support for the argument that shareholder liability was not a major factor in growing economies. This argument challenges the conventionalist argument that limited liability fundamentally improves the economy. Despite this persuasive argument, the data sampled is a small data set. The data from the 1800s is based upon around 100 companies. This is vastly different from the significant increase in the modern corporation. This data set is smaller than the average number of subsidiaries operating under one parent currently. Additionally, the Massachusetts Act of 1830 revised the legislation, introducing a form of limited liability. This piece of legislation followed from several business failures, which suggests that there was pressure to introduce limited liability. This introduction of limited liability was forthcoming despite the success due to the pressure following business failures. This supports the argument that corporate law has aimed to be facilitative in its approach to governance.

The examples in the preceding paragraphs demonstrate that historically there has been disagreement with the implementation and application of doctrines such as limited liability. Additionally, these doctrines need not have been implemented at all due to the prosperity which was happening in their absence. Irrespective of this, limited liability and its use has continued to grow. However, the argument that limited liability is one of the greatest modern inventions is far stronger. The imposition of limited liability allows for more capital to be traded freely and in the modern age of technology far more easily. In the 1600–1900s, there were very few companies,[19] which meant trading stocks would have been a much smaller undertaking than it currently is today. If there was the imposition of proportional liability (as it was historically in California) or no limited liability (as was the case in the 1700s), tracking and tracing shareholders would be difficult. In the modern shareholder market, shares are held for seconds or minutes, and the imposition of liability to these shareholders is currently limited. The use of these historical principles could result in liquidation of tracking each shareholder down to apportion their liability, a difficult task.

This section has outlined the importance of history in the context of corporate law and how the development of limited liability was introduced. The evolution into limited liability has been claimed to be part of a three-stage process whereby it was initially never discussed or required before being used partially and then consuming all modern companies. This evolution will be considered further in the next section, investigating the progress approaches to legislation to demonstrate how this has transformed over time. The chapter will then proceed to consider how the legislation has been interpreted.

2.1.2 Development of company law legislation

The aim of this section is to critically evaluate the historical development which has resulted in the current construction of the Companies Act 2006. This research argues that this development, and its subsequent dilution of control mechanisms, has resulted in the increase of the corporate form. This increase is especially prevalent within large corporations, with a significant number operating as part of a group.[20] This lack of debate and underdevelopment of the law relating to corporate groups has resulted in a legitimacy failure. This subsection serves the purpose of identifying how this failure has arisen to enable further chapters to propose methods of correcting this legitimacy failure.

[19] Compared to the volume which is seen in today's economy.
[20] See chapter five for empirical data.

The modern company as a form of business had a slow take off within the UK.[21] Micklethwait and Wollridge argued that Britain failed to produce the larger industrial firms which were the key to economic success. This identifies an early example of the very problem the modern company sought to address, attracting investment. Britain was, historically, a world leader and therefore did not feel the need to adapt to change. The consequence of this was that in the early 20th century, American counterparts dwarfed the size of Britain's businesses. Change was required to gain a larger pool of investors, and this was facilitated through concepts such as limited liability and separate legal personality. This argument presented by Micklethwait and Wollridge can be supported by the data presented by Harris and supports the theory of the second period being the most significant for the development of company law.

The current legislation for the governance of companies is found within the Companies Act of 2006. This statute provides for limited liability[22] and separate legal personality.[23] As identified earlier, provisions can be traced back to 1600 when companies could be created by royal charter.[24] However, despite this earlier discussion, the basis of the current iteration of the Companies Act can be traced back to 1844 with the Stock Companies Act ('the 1844 Act'). Davies contends that legislation in the form of the 1844 Act introduced three main principles which constituted the basis of our company law from that time.[25] These were: a clear distinction between private partnerships and joint stock companies, incorporation by registration opposed to charter, and publicity and transparency as a safeguard mechanism. These three main principles have remained in place over the evolution of the legislative development between 1844 and 2006. The incorporation by registration has become one of the most facilitative features of modern company law, with significant amendments over the last century. Prior to the 1844 Act, there was a requirement for corporations to have a parliamentary or royal charter to become incorporated. The result of this was a small number of companies operating in the periods between 1720 and 1844. Bakan argues that

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[21] John Micklethwait and Adrian Wollridge, *The Company, A Short History of a Revolutionary Idea* (1st edn, Orion Publishing Group Ltd 2003).
[22] Companies Act 2006 s 3.
[23] ibid s 16.
[24] See the Bubble Act of 1720 (Royal Exchange and London Assurance Corporation Act 1719 s XVII) and Bubble Schemes Colony 1740; South Sea Company Act 1720.
[25] Paul Davies and Sarah Worthington, *Gower's Principles of Modern Company Law* (6th edn, Sweet & Maxwell 1997) 38.

the reasoning behind charter registrations was due to the South Sea company promising mountains of gold and silver which led to a dramatic rise in company stock.[26] The directors of the company appeared before parliament charged with fraud and breach of trust.[27] Therefore, companies in the early stages of development were being utilised to obtain capital which was deemed dishonest by parliament. The Bubble Act of 1720, therefore, prevented incorporation except for chartered companies. The transition to registration in 1844 marked an important departure from charters and the commencement of the move into the modern corporation. The 1844 Act provided separate legal status and the ability for members to buy shares; however, there was no introduction of limited liability. The 1844 Act set out requirements[28] for formation which included registered details, which were not present and a contribution to the cause of the problem prior to 1720. There were half-yearly submissions which appear to have served the purpose of maintaining checks on the company.

The largest development came in the form of the Limited Liability Act of 1855. Limited liability has been termed the greatest invention of modern times.[29] The main benefit of limited liability is that the personal assets of the shareholder are protected, should a company enter insolvency. This asset shielding functions is two sided. The shareholders' personal assets are limited to their investment, and conversely, the property of the company is limited for use by the company and not its members. Limited liability has been argued to be the driver of the modern economy: by allowing limited risk investment, there is a greater incentive for rentier investors. The introduction of limited liability was not without much contention and debate. Its introduction divided the opinion of both commentators and parliamentarians. Whilst being debated in Parliament, Earl Grey opined the following:

> [I]t is to introduce an entirely new principle into our commercial legislation, and one which the highest authorities, both in law and in commerce, view with distrust and apprehension. It proposes to depart from the old-

[26] Joel Bakan, *The Corporation: The Pathological Pursuit of Profit and Power* (Hachette UK 2012) 7.
[27] ibid.
[28] For a list of requirements see Joint Stock Companies Act 1844 s IV.
[29] Butler, Why Should We Change Our Form of Government, (n 15) 82.

> established maxim that all the partners are individually liable for the whole of the debts of the concern.[30]

Earl Grey opposed the notion of limited liability due to the historic use of businesses whereby those who ran the business were liable for the debts of the whole concern. This viewpoint was in line with the traditionalist viewpoint at the time of its introduction. Businesses had historically been run as partnerships where each partner was both owner and controller of the firm. It was this traditionist viewpoint which was holding Britain back in its economic development. Earl Granville suggested that the introduction of limited liability would be for the public good and the interests of the trading community, and businesses.[31] This argument was based on the premise that commerce should be freed from restrictions and create a more attractive marketplace. This directly opposed Earl Grey, suggesting that any objections would simply be delaying the bill. This context of 'delaying the bill' as discussed in the parliamentary debates, suggests an element of inevitability. The limited liability corporation was taking off in other jurisdictions, and as such, Britain needed to implement this to remain competitive. Proponents of the bill claimed that experienced investors, managers and directors could be brought in to run and manage companies on behalf of the members. Furthermore, the introduction of bi-annual reports along with the additional incorporation requirements would act as a balancing check on the businesses. *The Times* suggested that the alterations would prevent 'unscrupulous persons' promoting for their own aggrandisement.[32] After the bill was implemented into statute, it was criticised by mainstream press, claiming that it 'limits the liability of the higher classes to be punished like the common peopled for the offences they have committed'.[33] This argument draws parallels to the concerns of Earl Grey, who conceived that it would allow business owners and managers to escape their own liability for their own mismanagement or decisions. *The Times* considered the change to be one of the greatest commercial changes

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[30] Limited Liability Bill, HL Deb 07 August 1855, vol 139 cols 1895–918 <https://api.parliament.uk/historic-hansard/lords/1855/aug/07/limited-liability-bill#S3V0139P0_18550807_HOL_4d> accessed 19th July 2019.
[31] ibid.
[32] 'The Limited Liability Acts' (*The Times*, 29 January 1887) 6 <http://link.galegroup.com/apps/doc/CS100977725/GDCS?u=exeter&sid=GDCS&xid=6c292358> accessed 19 June 2019
[33] Gilbert a'Beckett 'Limited Liability for Noblemen' (*Punch*, London, 27 October 1855) <http://link.galegroup.com/apps/doc/ES700214279/GDCS?u=exeter&sid=GDCS&xid=90e582e> accessed 25 January 2022

within a generation. This was achieved by its departure from dishonesty in selling shares for a worthless company and protecting investment and boosting capital growth. This historical account demonstrates that the introduction of limited liability was not without its opposition and debate. The challenge of balancing political and social agendas to best serve society was evident in the introduction of limited liability. More evident was the notion of control mechanisms to offset the potential challenges critics of the change identified. The introduction of limited liability was advanced on the notion of adequate control checks.

The result of the introduction was a positive one for business and the economy, and within a short period after introduction, there were reports of a rush of new companies being registered.[34] The Limited Liability Act[35] was replaced in 1856 by the Joint Stock Companies Act 1856, which combined the previous Joint Stock Companies Act of 1844 and the Limited Liability Act. The Joint Stock Companies Act of 1856 was replaced by the first Companies Act of 1862, which is the first descendant of the Companies Act 2006, the current leading statutory authority. Since the 1862 Act, there have been approximately 13 legislative amendments and four full new versions of the Acts implemented, taking us to the most recent 2006 Act. Each of these full versions and revisions has attempted to streamline corporate governance, and it is argued that in doing so control mechanisms have been disturbed.[36] The 1856 Act had the requirement of seven directors,[37] , whereas under the current iteration, only one is required.[38] The bi-annual returns have turned to annual returns, model articles of association are provided and the doctrine of ultra vires all but removed, along with minimal share capital being significantly reduced. It is now easier than ever to benefit from incorporation in the running of any business of any size. Companies since the introduction of the 2006 Act have, much like following the introduction of the Limited Liability Act, made a rush of incorporations, see Figure 2 below.

[34] The Financial Times, 'The Rush of New Companies.' (*Financial Times*, Financial Times Historical Archive, 16 April 1888) <http://tinyurl.galegroup.com/tinyurl/AGpBd7> accessed 19 June 2019.
[35] The Limited Liability Act 1855.
[36] For example, section 24 Companies Act 1985 which imposed personal liability was repealed in The Companies Act of 2006.
[37] Joint Stock Companies Act 1856, s 6.
[38] Companies Act 2006, s 12.

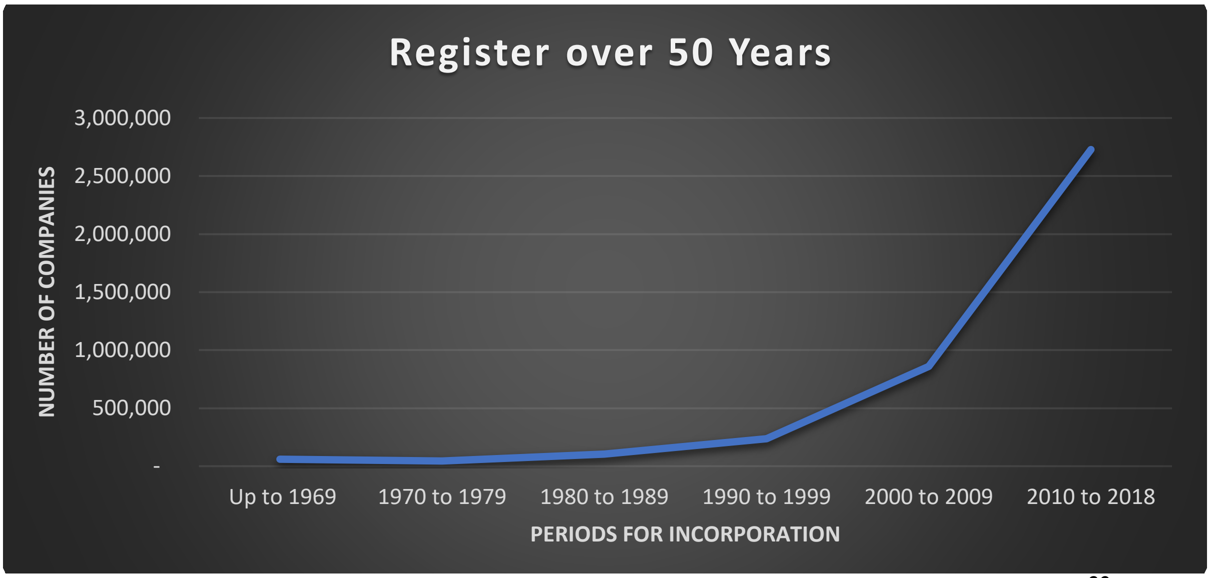

Figure 2 Register over 50 Years - Graph produced for this research utilising data supplied by Companies House [39]

Figure 2 evidences the dramatic shift over a period of 50 years in the use of registered companies. Several interesting observations can be drawn from these statistics. From the period 1990/2000 to 2000/2009, there was an increase of over 260%, and from 2000/2009 to 2018 another growth of around 200%. There is a direct correlation between the introduction of the 2006 Act and the growth of incorporations and companies. The statistics show a spike in registrations post the introduction of the Companies Act 2006. It is argued that the reduced formation requirements and ease of registration has contributed to this growth, much like the spike in 1855. The statistics show the increasing agenda of parliamentarians to continue to push ease of contracting and the form of a company. It is the argument of this thesis, however, that this further dilution creates additional problems, particularly in the context of corporate groups. Registration and the formation requirements are now much easier and economical to fulfil than those of the current Act's predecessors. Theoretically, a parent company could set up a company not only for each division but for location, office, employee etc. This thesis seeks to challenge the underlying reasons for this and determine if the accountability first envisaged on the passing of the Limited Liability Act still hold true today.

[39] Gov.uk, 'Statistical Release Incorporated Companies in the United Kingdom' <https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/502927/Incorporated_Companies_in_the_UK_January_2016-ver0.1-9.pdf> accessed 10 March 2016.

This subsection has evaluated the basis upon which limited liability and separate legal entity were introduced. Moreover, it has contrasted the formation requirements from its initial inception against the current position, highlighting the removal of some protections to third parties. This section has also demonstrated that the change in requirements has resulted in increased use of the corporate form. This thesis will proceed to argue that many of these corporations operate as part of a corporate group which has fulfilled this growth. This growth of the corporate group has further resulted in increased corporate power, for which the correlative monitoring requirements have become absent. The next section will proceed to consider the judicial interpretation of corporate law as it has evolved.

2.2 Historical judicial interpretation of corporate law

The preceding section considered the introduction of principles such as limited liability and separate legal personality and their evolution through statute and parliamentary intervention. The argument was made that the initial control mechanisms which legitimised corporate power had become diluted and removed. This section will proceed to evaluate the role judicial interpretation had on legislative developments and the creation of the modern corporation. The evolution of modern corporate law has been one with significant debate, as this section will demonstrate, in determining the role of corporate law and the tension between the letter and the spirit of the law. Moreover, elements such as directors' duties have become codified in the latest iteration of the Companies Act, supporting the courts' importance in their interpretation.

This chapter has already elucidated the importance of history in the legislative facilitation of corporate groups. This section will proceed to critically evaluate how attempts have been made to rationalise the corporate group and its correlative liability. As this section will demonstrate, deviations from the separate legal nature have been considered throughout this history; however, the principles from 1844 remain governing the 2022 corporation. Following *Prest*,[40] considerations as to alternative legal principles have been considered to attach liability notwithstanding the separate legal status. These traditional legal principles

[40] *Prest v Petrodel Resources Ltd* [2013] UKSC 34.

operate outside of company law, and the individuality of each company remains the current valid position. The result is that where groups are governed differently, this is carried on through mechanisms external to company law.[41] Considerations of justice have been contemplated by the courts as possible permissible reasoning for disregarding the corporate veil. Irrespective of positions evaluated by the courts, the reluctance to consider the contextual and economic realities of the group remains the current approach. This section will, therefore, consider these justifications to ascertain on what basis attempts to resolve these tensions were considered. This analysis provides a historical framework to demonstrate the evolutionary and accidental growth of the corporate group.

The landmark case of *Salomon v Salomon & Co*[42] (*Salomon*) has become the most cited and entrenched case setting the foundations for the modern corporation.[43] A detailed analysis of the facts is not pertinent, but a plotting of some of the key issues will provide a platform to evaluate the underlying issues and the subsequent judicial decision. Whilst Salomon is described as a landmark case and has received extensive scholarly debate, and it is a literal interpretation of the Act. Lord MacNaghten asserted this in the judgment, stating that provided the formalities of the Act have been complied with, the company is properly incorporated, and the promotors are entitled to the protection. This perspective appears to align with the letter of the law approach as opposed to the spirit of the law. *Salomon* is contentious due to the way in which the requirements of the Act were complied with. A brief overview of the facts will assist with the analysis. Mr Salomon was a sole trader who incorporated his business into a limited company. Shares and directorships were divided amongst the Salomon family to meet the minimum formation requirements. The business fell into insolvency with Mr Salomon in possession of a large debenture over the limited company. The challenge for the court was to establish if the company had been validly incorporated and if the liability of Mr Salomon was indeed limited. The frustration from the creditors was that Mr Salomon, in this instance, was a one-man company and not the persona ficta being presented as Salomon & Co, an early case of spirit v letter of the law.

[41] See *Adams v Cape Industries plc* [1990] Ch 433.
[42] *Salomon v Salomon & Co Ltd* [1897] AC 22 (HL).
[43] Over 300 cases have directly cited *Salomon* with the majority of these in the 1980s.

The case comprises of three conceptions of judicial interpretation. The first two courts agreed that Mr Salomon's liability was not limited, and he should be liable; however, they concluded this for different reasons. In the court of first instance, the agency argument was accepted by Vaughn Williams J, who accepted that the company was an agent for the shareholders, and as a result, Mr Salomon would be required to indemnify creditors. The case was taken to the court of appeal, where the justices drew a distinction between traditional companies and one-man companies. The conceptual interpretation in this appellate court aligned with the spirit of the Act, seeking to attach a purposive approach. The Act was intended for larger companies and to operate to perform more public-based services. This suggests that at the time of the decision, the court believed *Salomon v A Salomon & Co Ltd* was a company in name only, and not two distinct legal persons. Contrasting this with the development of the legislation, this does not appear a misplaced ruling. The Bubble Act 1720 was introduced to prevent dishonesty, and the introduction of the Limited Liability Act in 1855 was to promote entrepreneurial investment. The case of Salomon appeared to fall outside of what was intended, and the concept of one-man companies was not perceived to be intentional or legitimate. This correlates to corporate groups, as often[44] the parent is the single owner and controller of their subsidiaries. In the immediate case of Salomon, there was limited investment offered in this case and just a change of formalised business structure. Lindley LJ supported this view by claiming that the legislature never contemplated an extension of limited liability to sole traders.[45] This conception provides a dialogue for the use of the corporation at the time this case was brought before the court. Accordingly, the Court of Appeal accepted the argument that Mr Salomon was a trustee of the company. In forwarding this argument, the court decided that Mr Salomon was to indemnify the creditors under the principles of trusteeship. The Court of Appeal claimed that Mr Salomon had used the company's name to screen himself from liability. This is a rather obtuse conclusion from the Court of Appeal, given that the very introduction of the Limited Liability Act was for this very purpose to provide a level of protection. However, in this instance, the Court of Appeal had concluded that using the statute in this way, for an extension of sole traders, was not permissible. A clear

[44] See chapter 5.
[45] *Broderip v Salomon* [1895] 2 Ch 323, 337.

distinction between incorporated sole traders and incorporated companies was made, with the judicial interpretation being that this was beyond the intention of the Act.

The House of Lords, on appeal, rendered a decision based on an altogether different interpretation than the courts preceding it. Having considered the case, they concluded that Mr Salomon was neither an alias, agent, nor trustee of the company, but they were distinctly separate. Lord MacNaghten directly addressed the comment in the previous judgment in relation to owners using the legislation to screen themselves. He claimed that taking full advantage of the protection offered by the Act is perfectly acceptable and despite the size, provided the formation requirements had been adhered to, Mr Salomon was entitled to the full protection of the Act. It has since been claimed that 'dummy' shareholders were being utilised to fulfil these requirements.[46] However, the requirements were met, and the House of Lords believed that full protection was afforded. The House of Lords, therefore, ultimately decided in favour of Mr Salomon, overturning the judgments of the previous two courts. The case of *Salomon* is interesting and important for the evolution of the company because it had two lower courts agreeing that Mr Salomon should be liable for the debts of the company but disagreeing on how to attribute this liability. As this chapter has demonstrated, limited liability was already a contentious element, and based on moral and equitable grounds, the justices thought it not desirable for Mr Salomon to escape liability. However, as a matter of legal construction the House of Lords decision was that, regardless of the size or structure, the use of the corporate form is not an abuse or misuse of the legislation to form a company to shield liability. This is the very foundation of the modern group; the UK adopts a general corporate law regime over a specific group law regime.[47] Therefore, companies of all forms will be governed by these generalised principles of corporate law and applied to the group context. The judicial interpretation is therefore of significant importance to the early evolution of the modern corporation and more substantially, the modern group. Whilst the Court of Appeal was overruled in *Salomon* by the House of

[46] Ireland, 'Corporate Schizophrenia: The Institutional Origins of Corporate Social Irresponsibility' (n 6) 241.
[47] Klaus J Hopt, *Groups of Companies. A Comparative Study on the Economics, Law and Regulation of Corporate Groups* (European Corporate Governance Institute, ECGI, Law Working Paper 286/2015, 2015).

Lords, it is noteworthy that prior to a ruling on a fact of law the consensus was that the protection should not apply.

The succeeding parts of this chapter will evaluate and demonstrate that the extension of the corporate form has been tested further in differing ways throughout its historical development and evolution. This research seeks to establish how this evolved and if this development has undergone the same scrutiny and critique which was given at the inception of limited liability.[48] The argument presented by this research is that these extensions and dilutions of control mechanisms have not had the same level of scrutiny and debate as the introduction of these bedrock principles. The development of these principles has been extended and applied further than first anticipated, which requires further analysis as to how this evolution developed.

The distinct separation between the company and its shareholders had been contested before the case of *Salomon*. Moreover, such separation was considered prior to the introduction of the introduction of limited liability. In 1843, 40 years before *Salomon* and 10 years before the introduction of the Limited Liability Act, *Foss v Harbottle*[49] considered this separation. Here, the behaviour and activity by the directors of an incorporated company involving the sale of development land of substantial value was brought into question.[50] The shareholders proceeded to bring a claim against the directors, claiming that the directors were trustees of the shareholders and as a result, owed duties to the shareholders. The court held that the harm was not exclusive to the shareholders and that the company itself had also suffered loss.[51] This statement from the court, just like *Salomon*, was asserting the separate nature of the company from its shareholder regardless of the circumstances. This decision affirmed that the members of a company are distinct from the corporation itself.[52] This clear distinction was supported through *Salomon* and can be evidence of the evolution of cases. This further supports the argument that separate legal entity predates the Limited Liability Act and indeed the 1844 Act.

[48] By way of example, see the comments from Earl Gray in the preceding subsection.
[49] *Foss v Harbottle* (1843) 2 Hare 461.
[50] With inflation the capital value was in the region of £9,000,000 today.
[51] *Foss v Harbottle* (1843) 2 Hare 461 [459].
[52] ibid.

The doctrine of limited liability in application to groups is one which has been arrived at without any deep consideration and merely as a consequence of limited liability.[53] This chapter now moves to evaluate cases which have facilitated the creation of the modern corporate group. *Gilford Motor Co v Horne*[54] (*Gilford*) is an example of where a company has been utilised for the effect of avoiding liability for a pre-existing obligation. Despite sharing similarities to *Salomon*, the courts found and imposed this liability despite the limited liability. The case can be distinguished from *Salomon* due to the creditor liability, which was being avoided; this was established in the course of ordinary business, whereas in *Gilford* this was not the case. The defendant in *Gilford* was employed as an officer of the claimant company and was under a restrictive covenant not to solicit any customers. The defendant set up a limited company and claimed it was the company not the defendant who was soliciting the company. This is a captivating claim, as under the strict principle in *Salomon* the claimant themselves was not soliciting the customers: it was in fact the separate company. The court, however, felt free to disregard the separate entity and impose an injunction to prevent the solicitation of further customers. This case demonstrates the willingness of the courts to disregard the principle which was entrenched within *Salomon* to attach liability. *Gilford* was one of the first cases to fall under the sham or façade principle by which the court felt able to disregard the separate legal entity. This case is of fundamental importance in the evolution of company law not only because it provided authority to disregard the veil but because it set the foundations for what Lord Sumption, in obiter, dubbed the evasion principleWhich has provided extension discussion and further scholarly debate. [55]

In *Smith Stone & Knight Ltd v Birmingham Corp* (*SSK*),[56] there was a parent company seeking to have separate legal personality disregarded. This removal of liability is the reverse of the asset shielding seen in many other case examples. The benefits attributed with incorporation, as described by Lord MacNaghten in *Salomon*, were being asked to be removed at the request of the parent company.

[53] Paul Davies and Sarah Worthington, *Gower's Principles of Modern Company Law* (11th edn, Sweet & Maxwell 2021) 193.
[54] *Gilford Motor Co Ltd v Horne [1933] Ch 935.*
[55] Discussed in detail later in the chapter.
[56] *Smith, Stone & Knight Ltd v Birmingham Corp* [1939] 4 All ER 116.

This would be a voluntary piercing of the veil. The treatment of *Salomon* meant the division between parent and subsidiary, shareholder and company, appeared entrenched and absolute. In this case, there was a compulsory purchase of the land for which the subsidiary was paid compensation, but the parent was not. The parent was therefore prevented from claiming the compensation offered. Fletcher Moulton LJ claimed it was to be a question of fact in each case and of whether the subsidiary was carrying on the business as the company's business or as its own.[57] The court produced six points to assist in addressing this question. These points revolved around control and where the capital came from, and where the profits flowed. In this case, it was held that possession by a separate legal entity was not conclusive on the right to claim, and because the subsidiary was not operating on its own behalf but on behalf of the parent, the parent could be compensated under the scheme. This case is of substance in the development of our modern company law due to the fact it disregarded the veil on seemingly arbitrary factors at the request of the parent company. The language by the judge in the case often referred to the parent as 'the company', suggesting that the subsidiary was merely a division of the parent despite its separate legal status. This case does not align with *Salomon*; however, the case could be distinguished because it was at the request of the shareholders not the creditors. This is paradoxical in nature when contrasted with *Salomon*. The creditors in *Salomon* claimed the controller behind the company was to be liable, but the court disagreed on the basis of separate legal personality. However, here in this present case, the parent[58] was requesting the personality to be lifted, which has been dubbed 'reverse piercing'. This aligns with the shareholder primacy theory, whereby key features of company law can be disregarded at the request of the 'owners' but not creditors or third parties.

In 1962, in the case of *Jones v Lipman*,[59] land was transferred to a company in which the director was a related party. The claim, in this case, was that the company was not in breach of the land contract and could not be obligated to transfer the land by way of an order for specific enforcement. This case is important in the development of the modern company because it outlined and

[57] ibid 121.
[58] The controller.
[59] *Jones v Lipman* [1962] 1 WLR 832.

expanded on *Gilford* on what constitutes an abuse of the corporate form. The intention from the connected director was to avoid the sale of the land. Lindley LJ used terminology which would be used for similar cases over the next half a century, what he dubbed a mere cloak or sham.[60] In this present case, the court held that due to the company being used for a purpose not intended, specific performance was granted in this case. This was a pre-existing obligation, the contract to sell the land, which the company was being utilised to avoid.

In *Littlewoods Mail Order Stores Ltd v IRC*,[61] , Lord Denning declined to treat the wholly owned subsidiary as a separate and independent entity. Denning claimed that 'courts can and often do draw aside the veil … They look to see what really lies behind. The legislature has shown the way with group accounts and the rest. And the courts should follow suit'.[62]

This perspective from Lord Denning provides some context as to the development of company law. The court here decided, like in *SSK*, that the corporate personality could be disregarded in the right circumstances. The cases analysed thus far demonstrate a willingness for the courts to attribute liability despite the decision in *Salomon.* Lord Denning's statement affirmed that courts have the power to 'pull off the mask to see what lies behind', which could be argued as the basis for the principlesdiscussed by the justices in *Prest*. The justification offered by Lord Denning appears to be one of equitable origin, attaching liability where it ought to be attached despite the House of Lords clearly ruling that this was not within the court's powers. Denning claims that as the legislature has identified groups by implementing group tax legislation, there is justification for treating companies within groups as one entity. The tax treatment, Denning argued, provided the platform for courts to consider groups a single entity.

The 'enterprise concept' is one which Lord Denning continued to favour as can be seen in the case of *DHN Distributors v Tower Hamlets LBC*[63] (*DHN*). *DHN* is often cited as the case which introduced the concept of single economic unit for

[60] ibid 836.
[61] *Littlewoods mail order stores ltd V. Inland revenue commissioners* [1969] 1 WLR 1241.
[62] ibid 1254.
[63] *DHN Food Distributors v Tower Hamlets LBC* [1976] 1 WLR 852.

corporate groups. The significance of *DHN* is in the evolution of company law as it builds upon the previous decision of Littlewoods by the same judge. The case involved a compulsory purchase of land, land that was owned by the wholly owned subsidiary; however, the parent operated from the land. The compensation set out by rule (2) of s 5 of the Land Compensation Act 1961 was paid the legal owner, the subsidiary, not the parent. The group fell into insolvency due to not being able to find alternative premises, and the parent company sought to have compensation for losses which exceeded just the land cost. Lord Denning called the case 'three in one' and proceeded to call the group 'the firm',[64] suggesting that their operation was one and the same. This is analogous to the argument presented by Robé,[65] , who contends that the firm and the company are two different business forms. Lord Denning argued that the group is virtually the same as a partnership in which all three companies are partners. In this sense, each company within the group operated as part of the wider 'firm' in a way which is identical to partners. Denning further claimed that they should not be treated separately so as to be defeated on a technical point and furthermore, that they should not be deprived of compensation. This was justified on the grounds that the parent should justly be paid for the disturbance. This argument aligns with the equitable concepts in disregarding legal personhood. Denning argued that 'The three companies should … be treated as one'.[66] This assertion builds on from *SSK*. Denning supports an argument for a single economic unit and a claim which would otherwise be defeated on a technical point. This is a departure from the principle in *Salomon* where the court concluded that if the requirements of the Act were complied with, the protections afforded would be applied. This technical point which Denning alludes to is the very foundation of the modern corporate group. Groups are technically legally separate legal entities; however, the economic reality is different.[67] *DHN*, *Littlewoods* and *SSK* all represent a sharp departure from *Salomon* and could have formed the basis for further group law had it been developed further.[68] However, this conception

[64] ibid 857.
[65] Jean Philippe Robé 'The Legal Structure of the Firm' (2011) 1 Accounting, Economics, and Law 1, 21.
[66] *DHN Food Distributors v Tower Hamlets LBC* [1976] 1 WLR 852 [859].
[67] See data study in chapter 5.
[68] See *Woolfson v Strathclyde RC* [1978] SC (HL) 90 where it was distinguished, and *Prest v Petrodel Resources Ltd* where it was all but confirmed it could not apply.

of economic reality has since not been favoured or followed by the courts, as will be demonstrated.

The applicability of *DHN* has, however, been subsequently questioned by courts in further judgments. In *Woolfson v Strathclyde regional council*[69] (*Woolfson*), there was a distinction drawn between *DHN* and *Woolfson*. In *DHN,* the companies were wholly owned subsidiaries, whereas in *Woolfson,* there was no such straightforward ownership structure. The House of Lords rejected the concept of a single economic unit and reaffirmed the strong principle in *Salomon* being the strength of separate legal entity. The case of *Woolfson* also discussed the concept of 'mere façade' and developed the argument which was presented within *Gilford* and *Jones* respectively. This discussion of a pre-existing obligation would eventually form the basis for the concealment and evasion principles introduced[70] in *Prest* some three decades later. The evolutionary result is that within two years of the single economic unit argument being accepted by the court, the House of Lords reduced its applicability. This highlights a change in direction within a short period to reduce the scope by distinguishing *DHN* and reaffirming the *Salomon* principle. This introduction and subsequent abolition of the single economic entity principle demonstrates two possibilities: the first is an erroneous decision by three senior judges. The second is that there was a development of the modern corporation, which necessitated the shift from this single entity. Irrespective of the accepted viewpoint, the contention and disagreement further demonstrate a clear lack of debate or cohesion regarding how groups were to be treated.

The case of *Re Southard*[71] affirmed the *Salomon* principle in the context of corporate groups. The court expressly stated that subsidiaries and other members of the groups are not responsible for the liabilities of other members of the group. This aligns with the decision in *Salomon* and the concept of the 'single-man company' which was at the forefront of the debate. Each subsidiary may be conceived as a single-man company with this entity being the parent. This extension of single-man companies to single entity companies is an extension

[69] *Woolfson v Strathclyde RC* [1978] SC (HL) 90.
[70] In extensive obiter comments by the justices.
[71] *Re Southard & Co Ltd* [1979] 1 WLR 1198.

which permits and normalises the use of wholly owned subsidiaries owned and operated under the control of a parent. This case of *Re Southard* is where Templeman LJ in this case famously opined the following:

> English company law possesses some curious features, which may generate curious results. A parent company may spawn a number of subsidiary companies, all controlled directly or indirectly by the shareholders of the parent company. If one of the subsidiary companies, to change the metaphor, turns out to be the runt of the litter and declines into insolvency to the dismay of its creditors, the parent company and the other subsidiary companies may prosper to the joy of the shareholders without any liability for the debts of the insolvent subsidiary. [72]

Lord Templeman here acknowledges the incoherencies within the law relating to corporate groups and identifies that whilst these exist, the principles in *Salomon* depict the current position. This is paradoxical in the sense that Lord Templeman appears to be objecting to how corporate groups are able to be constructed; however, notwithstanding, this continues to apply *Salomon* due to the doctrine of precedent. This is due in part to the historical evolution, which has presented inconsistency throughout the last century and has cumulated in the law having 'curious features'. The language from Templeman LJ suggests some contention against groups of companies in the way the court describes their function. Irrespective of the contention and incoherent nature, there can be no presumed liability within a corporate group, which affirms the principles identified in *Salomon.* A further example of this is *The Albazero*,[73] *,* where the court of appeal confirmed the rights of one company in a group could not be exercised on another.

Nicholas v Nicholas[74] (*Nicolas*) saw a family case, much like *Prest*, where a matrimonial home was owned by a company controlled by the husband. Dillon LJ, obiter, claimed that if the company had been a one-man company and thus the 'alter ego', there should be a transfer of the property. Cunning-Bruce LJ claimed the court could pierce the veil and make an order. The relevance of this case for the purpose of historical plotting is the obiter comments from two of the judges. They both were in favour of the argument that the veil, in theory, could be

[72] ibid 1208.
[73] *Owners of Cargo Laden on Board the Albacruz v Owners of the Albazero (The Albazero)* [1977] AC 774.
[74] *Nicholas v Nicholas* [1984] 1 WLUK 458.

pierced to ensure relevant property was attributed in accordance with accompanying legislation. This concept is an early framework of the concealment principle of what has been established in *Prest*, and the basis of the primary claim arises from the nature of the relationship between the husband and wife. This is closely linked to the principle of the pre-existing obligation which can be imposed. The case of *Nicolas* can therefore be understood as the early formation of what has developed to become governing principles, despite this case receiving generally negative judicial treatment.

In *Re A Company*,[75] the court further considered the concept of using its powers to achieve justice where necessary. In considering this case, Cummings-Bruce LJ argued that due to the activities of the corporation, the court could permit the disregarding of legal personality in order to achieve justice. This introduction of a legal precedent to achieve justice further added to the incoherency of the legal debate. Establishing what is 'just' is inherently difficult as an objective construct. In *Trustor AB v Smallbone*[76] (*Trustor*), the court refused to pierce the corporate veil merely on the grounds that it was necessary to do so in the interests of justice. Moreover, the court identified the conflicting nature and tension between the previous cases in relation to the applicability of piercing the veil.[77] Andrew Morritt V-C reaffirmed that for the veil to be pierced, there must be some form of impropriety, utilising the façade principle from *Gilford.* Without this impropriety, even if the result would be 'curious', justice is not a sufficient reason alone to disregard legal personality.

In the seminal case of *Adams v Cape Industries plc*[78] (*Adams*), parent company liability in respect of tortious claims was considered. The case involved an international group of companies for which a separate limited company in each jurisdiction was created, not only creating a corporate veil but also a jurisdictional veil. The subsidiaries operated in high-risk activities involving asbestos, and a claim in tort against the wealthier parent company was presented. Slade LJ opined that 'Our law, for better or worse, recognises the creation of subsidiary

[75] *Re a Company* [1985] BCLC 333.
[76] *Trustor AB v Smallbone (No 2)* [2001] 1 WLR 1177.
[77] ibid 535.
[78] *Adams v Cape Industries plc* [1990] Ch 433.

companies'.[79] Despite refusing to attribute direct liability, Slade LJ stated that general law would apply notwithstanding the corporate law position. Slade LJ, therefore, concluded in a similar manner to the previous cases and claimed there are curious features of company law with parent companies and groups of companies as such examples. This builds on the argument in *Nicholas* that despite the wish to attribute liability, the legal position must be followed, even if the economic position represents an alternate reality. The court in *Adams* rejected that the court was entitled to disregard the veil simply because the structure was used to ensure the legal liabilities of the group had been protected. The court concluded that irrespective of whether this type of structuring is desirable, this is not a question for the court because the right to use a corporate structure in this manner remains inherent in our corporate law.[80]

The case analysis coupled with further examples[81] render the departure from *Salomon* in the group context questionable when based on a meritocratic argument. It is unlikely that the principle outlined in *Salomon* will be ignored in the group context. This evolution without significant debate results in one of the 'curious features' within modern company law. The contribution *Adams* provides to the evolution of company common law is twofold: firstly, in respect of tortious claims and secondly, in respect of corporate groups. The court held that the claim could not proceed, that the mere fact that there were group connections or relationships was largely irrelevant and that each company remains separate. Cases such as Adams have contributed to the legal development, utilising principles initially considered for private companies and applying them into the corporate group context. The judges in *Adams* confirmed that despite corporate group relationships, the group is to be governed by the general law such as the principles outlined and confirmed in *Salomon*. *Adams*, therefore, can be seen as a case which promotes corporate groups and validates their structure according to the principles of *Salomon*. It builds on the existing general law that it considered and provides a further platform for future cases to build on to facilitate further evolution strengthening corporate groups' legal rights. Moreover, in considering *Re A Company*, the court held that it was not possible to pierce the corporate veil

[79] ibid 536.
[80] ibid 543.
[81] See *Yukong Lines Ltd of Korea v Rendsbury Investments Corp of Liberia* [1998] 1 WLR 294 & *Re Polly Peck International* [1996] 2 All ER 433.

to achieve justice because this is not consistent with *Adams.* In *Ord and another v Belhaven Pubs Ltd*[82] (*Ord*), the claimants were seeking to attribute liability to a company within a group which had restructured. There was an argument of asset stripping, as in *Creasy*,[83] but the judges overturned it as no longer authoritative. The judges considered that there was no evidence other than a genuine restructuring for which the claim would have to be taken against the subsidiary, not the parent. This case builds on *Adams* and further strengthens it. Despite cases where there has been questionable restructuring within a group, the court will assert the *Salomon* principle as group members are to be considered separate.

In *Coles v Samuel Smith Old Brewery (Tadcaster)*,[84] , the court distinguished between impropriety and sham when looking to attach liability. The threshold for establishing a sham has historically been difficult, Lord Sumption in *Prest*[85] commenting that the question of sham has historically 'begged too many questions to answer'. This was evidenced in *Tadcaster*, where the court could see no sham or façade. The court of first instance deemed if there was an absence of these elements, no further orders could be made. On appeal, the facts of *Lipman* were compared, and the judges concluded that veil piercing was unnecessary and found, irrespective of the veil, specific performance was available as a remedy. This principle is the early foundation of what has become the concealment principle. This is a significant development because it exemplifies the use of alternative legal provisions to attribute liability where it would have otherwise been evaded on a technical point of company law. Moreover, it demonstrates the intention of the courts to utilise alternative remedies so as to not disrupt the longstanding principles of corporate law. This is further emphasised in *Gencor ACP v Dalby*,[86] where the impropriety was introduced.

The concept of the alter ego was further debated in the case of *Ben Hashem v Al Shayif & Anor.*[87] This is a similar discussion to that of *Salomon*, which was

[82] *Ord and another v Belhaven Pubs Ltd* [1998] 2 WLUK 260.
[83] *Creasey v Breachwood Motors Ltd* [1992] BCC 638.
[84] *Coles v Samuel Smith Old Brewery (Tadcaster)* [2007] EWCA Civ 1461.
[85] *Prest v Petrodel Resources Ltd* [2013] UKSC 34.
[86] *Gencor ACP Ltd and others v Dalby and others* [2000] 2 BCLC 734.
[87] *Ben Hashem v Ali Shayif & Anor* [2008] EWHC 2380 (Fam).

debated over a century before. The court refused to recognise the company as the alter ego of the defendant, which aligns with the early principles of company law. The court considered the concepts of impropriety and the concept of degree of control before concluding there was not enough evidence to support either. Justice Munby claimed that ownership and control of a company are not in themselves sufficient to justify disregarding corporate personality and he claimed that this was the very essence of the *Salomon* principle.[88] The significance here is that control of the company is more likely to exist in the group context.[89] The exercising of control has the capacity to produce legitimacy failures due to the structural construction of the modern corporate group. Munby further argued that there must be some impropriety in accordance with *Adams* and *Ord*, and that piercing in the interests of justice cannot be done. It also provides further authority and affirmation that ownership and control alone is not enough of a reason for the court to pierce the veil. This concept has been expanded past the natural person that was seen in *Salomon* to the juridical person which is now ubiquitous in the modern corporation. Therefore, this case provides express authority[90] that just because a parent exerts control there will be no grounds for piercing the veil. What can be seen from the comments is a discussion and summary of previous decisions affirmed in this case that ownership and control are irrelevant for attributing liability.

The concept of control can, however, be considered with relationships between parent companies and wider creditors within the remit of tortious claims. In the case of *Chandler v Cape plc*[91] (*Chandler*), the court used traditional principles of negligence to hold a parent company owing a duty of care to the employee who was contracted to a subsidiary company. The finding of a duty of care is fundamentally different from a departure from corporate personality, and the court expressly asserted this remained unaffected. The court imposed appropriate circumstances where the law may impose tortious liability.[92] These circumstances were that the parent and the subsidiary operate as part of the same field, and the parent has or ought to have knowledge of the health and

[88] ibid 159.
[89] Supported by data study in chapter five.
[90] In a more specific application than *Salomon.*
[91] *Chandler v Cape plc* [2012] EWCA Civ 525.
[92] ibid 80.

safety of a particular industry. Additionally, the subsidiaries' system of work is unsafe, as the parent knew or ought to have known. The parent must have also known that the subsidiaries' employees would rely on that superior knowledge for their safety. If these circumstances were met, the parent would assume responsibility toward employees of the subsidiary and potentially have liability imposed on them. The court expressed that the duty of care to employees of its subsidiaries was subject to the three-stage test in *Caparo v Industries plc v Dickman*.[93] The remit of this liability, remains within tort, and *Chandler* provides authority that mere use of the corporate form cannot be utilised to defeat a claim where otherwise it would have been successful. The application of *Caparo* and the fact the court expressly stressed that this was not an instance of veil piercing suggests that the court were distancing itself from the veil argument. In utilising tortious principles, liability can now be attached to parent companies providing the test in *Caparo* can be satisfied and the requirements in *Chandler* are satisfied. Whilst *Chandler* appears to offer a liberal approach to liability, the reality is the C*aparo* test will rarely be satisfied and will still leave a significant number of tortious claimants with claims unsettled,[94] mitigating its potential impact. This case contributes significantly towards the current construction of the modern company because it appears to offer some reprieve to a much-debated issue of tortious liability within companies. It establishes liability but not based on any company or commercial principles. The case of *Chandler* therefore establishes that, irrespective of its narrow applicability, liability can be attached to companies without affecting the veil of incorporation.

This theme of narrow applicability continued in *VTB Capital plc v Nutritek International Corp*[95] (*VTB*), where Lord Neuberger questioned whether the courts had any general power at common law to pierce the corporate veil.[96] Lord Neuberger in this case introduced an undesirable level of uncertainty within the common law.[97] The evolutionary significance of *VTB* is the introduction of the concept that the veil cannot be utilised to impose contractual liability where there

[93] *Caparo Industries plc v Dickman* [1990] 2 WLR 358.
[94] See Christian A Witting, *Liability of Corporate Groups and Networks* (1 edn, Cambridge University Press 2018) 7.
[95] *VTB Capital plc v Nutritek International Corp* [2013] UKSC 5.
[96] ibid 130.
[97] Christopher Hare, 'From Salomon to Spiliada: Orthodoxy and Uncertainty in the Supreme Court' [2013] 72 The Cambridge Law Journal 280.

was none before. Unfortunately, within this case, Lord Neuberger's comments cast significant doubt over the principle of piercing the corporate veil. Writing at the time the judgment was handed down, Hare opined that this decision would do nothing to help the lower courts resolve their confusion.[98] The contribution of *VTB* was therefore largely negative due to its role of further uncertainty. This questioning of the doctrine resulted in further confusion, which was discussed further in the subsequent case of *Prest*.

The landmark case of *Prest* sought to reconceptualise the challenges and uncertainty which arose from cases preceding it and to introduce some clarity on liability through its discussion in obiter which provided some rich commentary from the justices. Some scholars have since argued that following the judicial commentary in Prest that this has clarified the position due to the direction in which the judges appeared to favour.[99] Lord Sumption, on discussing the corporate veil, opined that the question has been heavily burdened by authority and characterised by incaution dicta and inadequate reasoning.[100] This inadequate reasoning can be evidenced through the historical evolution in the preceding paragraphs. Lord Sumption also claimed there has been confusion, as the previous case analysis highlights, as to the terminology and its application.[101] The court identified that existing legal obligations and traditional matrimonial law could be utilised to attribute liability. Methods such as these have been dubbed 'skirting the veil'[102] to attach liability without affecting bedrock company law principles. However, whilst the judges agreed in respect of the beneficial ownership and the court was not required to pierce the veil, the court did proceed to offer some clarification on the doctrine. Lord Clarke opined that despite the veil not being pierced, it would be a lost opportunity to add further general comments on the vexed principle on the question of the veil.[103] The Supreme Court continued to offer some detailed obiter to clarify this confused and vexed concept. The significance of this case requires a more detailed analysis. Two main questions were to be considered: is there a doctrine of piercing the corporate veil,

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[98] ibid.
[99] Witting [n 88], William Day, 'Skirting around the Issue: The Corporate Veil after Prest v Petrodel' (2014) 2 LMCLQ 269
[100] *Prest v Petrodel Resources Ltd* [2013] UKSC 34 [19].
[101] ibid [28]
[102]. Day, [n100].
[103] *Prest v Petrodel Resources Ltd* [2013] UKSC 34 [106].

and if there is, when does it apply? Lord Sumption leading the judgment, offered two new concepts, presented in obiter, attempting to simplify the law and propose categories into which cases may fall. Lord Sumption argued that the principle of piercing the corporate veil did exist as a power for the courts. This was, however only the case if a company was being abused for the purpose of some relevant wrongdoing: this is well established in the authorities.[104] Lord Sumption claims that the previous categories of sham or façade 'beg too many questions to provide a satisfactory answer'[105] and that in many of the previous cases they could have been decided on other grounds.

Lord Sumption puts forward two principles which he claims are behind the protean terms which have been used previously. These are the concealment and evasion principles: the concealment principle is legally banal and does not involve piercing the corporate veil at all. The court, in these cases, is not disregarding the façade but only looking behind to discover the facts which the corporate structure is concealing. The evasion principle is different. It permits the court to disregard the corporate veil if there is a legal right against the person in control of it, which the imposition of the separate legal personality of the company will defeat the right or frustrate its enforcement.[106] The focus, therefore on the evasion principle lies in evading a pre-existing obligation. This appears to be drawn from the cases of *Gilford* and *Jones*, where a company was introduced to circumvent an existing obligation. The concealment principle is just utilising conventional principles and involves no veil piercing or interference with traditional corporate law. Lord Sumption claims that many cases will, however, fall into both categories, though the reasoning behind the evasion principle is to avoid the abuse of separate legal entities which frustrates enforcement. The critique to this approach is that the term 'abuse' has a very narrow definition and is limited in cases where there are already pre-existing obligations. This narrow approach was likely intended to be as such to avoid further expansion of *Prest* and dilution of *Salomon*. The important interpretation of these comments from Lord Sumption is that there is indeed a limited principle of attaching liability to those who control companies.[107] It further expressly agrees that there is a principle of piercing the corporate veil:

[104] ibid 27.
[105] ibid.
[106] ibid 28.
[107] ibid 36.

it is just narrow and required to fit into the circumstances Lord Sumption described. Writing prior to *Prest*, Witting had argued that ordinary civil law should be utilised to establish liability and doing so would not affect the *Salomon* principle.[108] The concealment concept appears therefore one to have been favoured prior to its introduction in *Prest*.

The case of *Prest* canbe argued to have brought much clarity in what by the courts own description was a confused area of the law. Whilst the case was primarily decided upon a trust law basis , and as such the decision is not binding it provides a clearer direction on the viewpoint of the court and likely future direction. and I The Judges , however, did not all agree on the principles proposed by Lord Sumption. Lord Neuberger also commented that the case history and the academic commentary pertaining to the doctrine of piercing the corporate veil had been confused and as a result are unsatisfactory.[109] Lord Neuberger claimed that whilst *Gilford* and *Jones* provide support for doctrine, it has never been invoked properly. Lord Neuberger nonetheless concluded that the doctrine does exist, and it would be wrong to disregard it because it has generally been assumed to exist in all common law jurisdictions.[110] Lord Neuberger argues however that the doctrine should only be invoked where a person is under an existing obligation which is frustrated by the imposition of the company. He, therefore, appears to consider, after diligent deliberation, that the doctrine exists but only in the narrow formulation as proposed by Lord Sumption. Lord Neuberger does however go on to add that in accordance with Lord Denning in *Lazarus Estates Ltd v Beasley*,[111] cases of fraud would be treated differently by virtue of fraud unravelling everything. Baroness Hale[112] claimed the decision in *Salomon* was the day the modern business was born and that this must be born in mind when considering whether to disregard the veil. Baroness Hale, however, concluded that the principle of piercing the veil existed but disagreed that all cases could be categorised neatly into two principles.[113] She opined there may be examples where individuals who operate companies should not be able

[108] Christian Witting, 'Intra-Corporate Conspiracy: An Intriguing Prospect' (2013) 72 The Cambridge Law Journal 178, 3.
[109] *Prest v Petrodel Resources Ltd* [2013] UKSC 34 [64].
[110] ibid 80.
[111] *Lazarus Estates Ltd v Beasley* [1956] 1 QB 702 [712].
[112] With whom Lord Wilson agreed.
[113] *Prest v Petrodel Resources Ltd* [2013] UKSC 34 [92].

to take unconscionable advantage of the people they do business with.[114] This viewpoint from Baroness Hale is broader than the approach proposed by Lord Sumption and implies further scope for unconscionable bargains. Lord Mance, in the same vein as Baroness Hale, concurred that it is not possible to foreclose all situations and to do so would be 'dangerous'.[115] Lord Mance, however, considers that the doctrine should be a 'final fall back' and only used in very rare cases. Lord Clarke agreed that such a doctrine exists, but its limits are unclear.[116] Lord Clarke, in a similar disposition to Lord Mance, limits the scope, agreeing that it should only be deployed in a very rare case and only after all other conventional methods have been of no assistance. Therefore, Lord Clarke considers it a doctrine of last resort. Lord Walker opines that piercing the corporate veil is not a doctrine at all,[117] it is a label which has been used indiscriminately. Lord Walker concludes by stating that no clear example has yet been identified if there is a small residual category in which it operates.

The case of *Prest* is therefore significant because the judges' consensus, albeit in a persuasive non-binding way, is that the doctrine applies. The result of this from a corporate group context is the solidifying of the principle of separation between group companies. This supports the creation and use of corporate groups to structure business operations. There remains, however, a lack of coherency. Whilst Lord Sumption has proposed some principles, these have been criticised as being too narrow to have any real effect.[118] Lee, for example, argues that these principles render further development of the law difficult because of their narrow nature. Tan claims that not all abuses will be captured under the concealment or evasion principles.[119] This draws parallels with the discussion amongst all the judges, who are at variance regarding how the doctrine applies, or if it does so. Baroness Hale expressly highlights that unconscionable advantage could be taken of individuals which would fall outside of the evasion and concealment principles. Their lordships, whilst agreeing on the outcome of this case, could not agree on how the doctrine of piercing the

[114] ibid 92.
[115] ibid 100.
[116] ibid 103.
[117] ibid 106.
[118] Pey Woan Lee, 'Case Comment: The Enigma of Veil-Piercing' [2015] International Company and Commercial Law Review 1.
[119] Cheng-Han Tan, 'Veil piercing - A Fresh Start' [2015] Journal of Business Law 20.

corporate veil should operate. The court should not have a *carte blanche* to pierce when they see fit. However, a balance should also be to ensure litigation is not always required. Whilst *Prest* does much to clarify a much-confused area of corporate law, with its narrative, the fact that the judges of the Supreme Court could not agree on the application or limits highlights how uncertain the law has been or could potentially become. This is a shareholder's paradise in the context of corporate groups, and permits the ability to create economic units with legal separation between the entity, irrespective of the economic reality. Prest, therefore, provides a gloss of clarity with the consensus that a principle does exist in English law. It is, however, unlikely to be utilised with conventional English law principles to be the primary route of attaching liability.

In *Pennyfeathers Ltd v Pennyfeathers Property Co Ltd*[120] (*Pennyfeathers*), the High Court considered the application of *Prest* in a case where the directors were purportedly in breach of their fiduciary duties for personally pursing a business opportunity. The court considered both the evasion and concealment principles as laid out by Lord Sumption in *Prest.* The case of *Pennyfeathers* can be seen to further confuse the doctrine of piercing the veil because Justice Rose appeared to apply both the concealment and evasion principles to the case where they were not applicable due to the lack of intention to avoid a pre-existing obligation. In addition, it would not have been appropriate[121] to utilise *Prest* because of the availability of the more conventional remedies outlined by Lord Sumption. Whilst this case evidences the use of the principles in *Prest*, it does, however, add to the confusion. This draws parallels to the comments of Baroness Hale regarding categorising into two distinct concepts. It highlights the concern that the doctrine is not able to be applied consistently and coherently and casts doubt. In *R v Boyle Transport (Northern Ireland) Ltd and others*[122] (*Boyle*), the court considered the application more broadly to clarify if the corporate principles of separate legal personality applied similarly in civil and criminal jurisdictions. The Court of Appeal held that despite these differing jurisdictions, the established principles applied equally in both civil and criminal contexts. In considering previous civil decisions, the court argued that a broad approach to disregarding the veil would not be

[120] *Pennyfeathers Ltd v Pennyfeathers Property Co Ltd* [2013] EWHC 3530.
[121] Nupur Upadhyay, 'Piercing the Corporate Veil: An Analysis of Lord Sumption's Attempt to Avail a Troubled Doctrine' (2015) 21 Auckland UL Rev 114.
[122] *R v Boyle Transport (Northern Ireland) Ltd and others* [2016] EWCA Crim 19.

appropriate. The test is not one of justice, and Davis LJ opined that 'so vague an approach would be unprincipled and would give rise to great uncertainty and inconsistency in decision making'.[123] The Criminal Court attempted in the first instance to apply this broad-brush approach to achieve justice, a concept which has already been discounted in the civil courts. The Court of Appeal concluded, however, despite this being heard in criminal proceedings, that it was not a licence to depart from established principles of company law. This judgment affirms *Prest* due to the court's resistance, even in criminal proceedings, to disregard the principles of separate legal personality. It is therefore arguable following decisions in both matrimonial and criminal cases that the principles laid out in *Salomon* and further considered in *Prest* have been strengthened, narrowing the application of veil piercing in all but the most limited cases. The Court of Appeal did consider the concept of a sham, which does suggest further difficulties in the application of *Prest* given Lord Sumption's comments on the use of such terminology. Whilst *Boyle* has provided further confirmation in the facet of veil piercing as a doctrine, it has not done so with the coherence in which *Prest* implicated.

AAA & Others v Unilever plc[124] (*Unilever*) considered tortious claims following on from *Chandler* and as discussed *Vedanta Resources plc v Lungrove*.[125] *Unilever* comprised a case where employees of a subsidiary in Kenya were seeking to establish sufficient proximity to establish a duty of care. The appeal in this case involved the appellants claiming that the parent company had breached their duty of care in failing to take effective steps to protect them from politically driven violence. The court concluded the appeal should be dismissed due to the proximity. Sales LJ opined that none of the decisions as to how to handle such a crisis required the input of the parent, and on this basis a duty of care could not be established. Despite dismissing the appeal, the court proceeded to give some general guidance as to when a duty of care may be established. Sales LJ stated the following:

> There is no special doctrine in the law of tort of legal responsibility on the part of a parent company in relation to the activities of its subsidiary, vis-à-vis persons affected by those activities. Parent and subsidiary are

[123] ibid 88.
[124] *AAA v Unilever plc* [2018] EWCA Civ 1532.
[125] *Vedanta Resources plc v Lungrove* [2019] UKSC 20.

> separate legal persons, each with responsibility for their own separate activities.[126]

This stance by Sales LJ firmly reasserts the principles in *Salomon* clarifying that only if the imposition of a duty of care is established via traditional tortious law, will it apply. There is no doctrine which arises from a parent and subsidiary relationship. Sales LJ claims that whilst consideration was given in *Chandler* there was no separate test established from the general principle for the imposition of a duty of care in relation to a parent company. Whilst the legal principles are the same, Sales LJ claims they will often fall into two basic types: where the parent has in substance taken over the management of the relevant activity in place of the subsidiary (as in *Vedanta)* or the parent has given relevant advice to the subsidiary about how to manage a risk.[127] These two summarised categories provide greater clarity for establishing a duty of care. If, for example, a parent company replaces the management of a subsidiary a duty of care could be established. In accordance with *Chandler* the relevant tortious requirements will still need to be met, as outlined in *Caparo*. *Unilever,* therefore, provides authority for establishing tortious liability building on from *Chandler*; it also confirms that there is no special provision and that traditional tortious requirements must be satisfied. This strengthens the position of the separate legal entity going further to ensure the corporate veil is not affected in tortious cases, which is analogous to what Lord Sumption described as the concealment principle in utilising conventional principles to establish liability.

In *Hurstwood Properties (A) Ltd v Rossendale BC and another*,[128] the court considered *Prest* and the implications on continuing obligations. The case involved business rates owed to the council by a company following restructuring and creation of special purpose vehicles. The argument presented by the council that in line with *Prest* this was an evasion case due to companies being imposed to prevent an existing obligation. The obligation to pay the business rates was argued to be pre-existing and as such falls within the evasion principle introduced in *Prest*. This argument was rejected by the Supreme Court on the basis that the evasion principle cannot extend to future obligations, as this is beyond the scope

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[126] *AAA v Unilever plc* [36].
[127] ibid 37.
[128] *Hurstwood Properties (A) Ltd v Rossendale BC* [2021] UKSC 16.

of the principles outlined *Prest.* The court argued that this argument is wholly misplaced and that imposed liability on the controller's fresh liability was not in alignment with the evasion principle. The basis for this judgment is predicated on the way in which business rates accrue. The liability arises day by day, therefore the liability owed by company ceases where the restricting and special purpose vehicle was introduced. There was no ongoing or continuing liability attached to the original business rates payer. This consideration of the evasion principle further affirms the restrictive nature of the evasion principle introduced in *Prest.* It limits the existing obligation to one which is quantified at the outset of the imposition of the company, irrespective of possible future obligations. This refusal to attach liability within the context of connected companies further strengthens the position of the corporate group and facilitates the growth of their power.[129]

The historical judicial interpretation as demonstrated by the preceding analysis, identifies an inconsistent and incoherent evolution, ultimately cumulating with *Prest.* Initially, in *Salomon,* the court grappled with the context of a single-man company when it appeared this was not the intention behind the formality requirements. The courts have since dealt with the challenges of incorporated companies with close connections. In *DHN* and *Littlewoods*, the courts appeared sympathetic to the idea of an economic entity-based approach; however, this has since lost favour with the judiciary. The iron grip of *Salomon* and the literal interpretation has remained the touchstone for company law since its inception, and cases as recent as 2021 continue to cite the decision in *Salomon.* The ruling in *Salomon* was predicated on the 1856 Act, which, as the preceding section identified, had more control mechanisms. The evolution of Companies Acts cumulating into the 2006 Act has seen dilution on control mechanisms; however, the allegiance to *Salomon* has remained. This is irrespective of a changing modern corporation and the legislation which facilitates it. This friction between the evolving market and legislation can be seen in the conflict within the cases evaluated. Notwithstanding the interpretation and the seeming desire for the judiciary to adjust the provisions, the modern corporation is wedded to *Salomon*.[130] This combination of judicial reluctance to adjust the principle coupled

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[129] See chapters 3 and 4 for a more detailed analysis.
[130] Brenda Hannigan, 'Wedded to Salomon: Evasion, Concealment and Confusion on Piercing the Veil of the One-Man Company [2013] Irish Jurist (1966-) 11.

with legislative dilution has facilitated the modern group. This section has identified judicial interpretation and the reluctance to depart from *Salomon* despite creative interpretation from the judiciary. The next section will proceed to consider the cumulation of the evolution, evaluating wider literature. It will then move to consider legal theory and the need for corporate law.

2.3 Theoretical underpinning of modern company law

The preceding subsections have presented the argument that the evolution of company law has been haphazard in its development over the last century. These bedrock principles of company law have evolved over time; however, this evolution has been fraught with judicial debate. The first subsection analysed the legislative evolution over time, and the second the judicial interpretation. The analysis of these two strands identifies a reluctance to depart from the position in which we started. Lipton[131] dubs this the iron grip of *Salomon*, which despite some reasoned counter-arguments, remains in place. This section seeks to build on the legislative and common law evolution by evaluating the theoretical arguments surrounding this evolution. Moreover, it will appraise the need for specific corporate legislation and how the approach which has resulted in the current construction could be amended to keep the legal and economic interests aligned.

A challenge which the evolution of company law presents is this iron grip of *Salomon*. In the seminal case of *Prest* and cases after, *Salomon* has been cited and applied. Corporate groups as a form of business were little known at the end of the 19th century,[132] , and therefore, they could not have been in the contemplation when *Salomon* was decided. The analysis of the evolution demonstrates that the courts attempted to consider[133] the group application when they grew to prominence. Subsequent decisions returned to the bedrock principle of *Salomon* solidifying its significance in the context of corporate law. The

131 Phillip Lipton, 'The Mythology of Salomon's Case and the Law Dealing with the Tort Liabilities of Corporate Groups: An Historical Perspective' (2014) 40 Monash University Law Review 452.
132 See: Ron Harris, *Going the Distance: Eurasian Trade and the Rise of the Business Corporation, 14001700* (Princeton University Press 2020); Micklethwait and Wollridge (n 21); Lipton (n 129).
133 *DHN Food Distributors v Tower Hamlets LBC* [1976] 1 WLR 852.

principle of *Salomon* has wide-ranging implications, as the development of business enterprise resulted in a greater use of the corporate form. These were seemingly governed on a principle of the 19th century despite operating in a 21st-century economy. Lipton contends that the result of the evolution has enabled the controllers of groups to limit torts.[134] This has been considered in depth with the *Cape* cases where control has been a significant factor. Despite being able to attach liability, this is still limited in its scope due to the requirements needed to succeed in a claim. There remain these challenges and difficulties to claimants which were not initially conceived when 19th-century cases were considered.

Additionally, the preceding sections have highlighted that early corporations were subject to greater control mechanisms. These control mechanisms and checks and balances, which were in place at the time of the *Salomon* ruling have decreased. The number of executive directors has decreased to a single director, the share capital has all but been removed, and the requirement of more regular returns has also been removed. Therefore, the result is that not only are corporate groups incomparable of being held to the same standard, but the standard is also substantially different and operating in a different landscape to the precedent set. Corporate groups retain the benefit identified in *Salomon* of separate legal personality irrespective of the substantial change in legislative footing which underpinned *Salomon*. The extension of limited liability to the corporate group becomes less defensible when compared against this historical evolution.

The basis for claim in the cases brought against companies within the evolution of corporate law principles arises out of the idiosyncratic nature of the corporation. Each corporation is unique in their business operation and as such there are social elements which attach themselves when challenging bedrock principles of company law. These social elements can influence norms which have appeared throughout this evolution. Hardman argues that moral hazards can occur and limited liability can harm third parties.[135] Norms have become embedded within our modern corporation. Since the inception of limited liability, it has become the 'norm' for businesses to convert their method of business structure to limited

[134] Lipton, (n 129).
[135] Johnathan Hardman, 'Descriptive Determinants of Ostensibly Normative Corporate Law Arguments' (Society of Legal Scholars, Durham University 2020).

companies or limited liability partnerships from the origins of sole traders and traditional partnerships. This is evidenced by cases as early as *Salomon* where a merchant incorporated their small sole trader or single-man company. Donovan argues that social norms can influence policy, and as such understanding, the architecture becomes increasingly important.[136] Moreover, given norms can be a form of social construction, and they are capable of deconstruction.[137] Hardman argues that these normative elements of law are based on descriptive determinants.[138] The elements of normative law, the social norms which have helped shape and evolve company law, can be challenged on their own legitimacy. Following *Salomon*, the use of corporations expanded and became normalised, and this has subsequently been expanded to group companies, with formation requirements reduced to entice small companies. Hardman presents the argument that these normative elements are often predicated on elements which are no longer relevant, and these should be foregrounded to bring clarity to the debate. This supports the argument of lack of debate in the development of corporate groups, which is analogous to the argument presented by Dine.[139] Hardman contends that elements such as limited liability and separate legal personality are based on descriptive elements which can be rebutted and no longer relate to the concept with which they were initially proposed.[140] The iron grip of *Salomon* can, therefore, be challenged due to its descriptive elements in the first instance and subsequently could have had further debate. This is not to argue that *Salomon* has been decided incorrectly: the argument is that greater consideration as to descriptive and specific elements could have directly contrasted against the elements of the modern corporation. This appears to be the consideration of *DHN*, where the economic reality was considered at length.

Norms, therefore, have played a pivotal role in the initial foregrounding of the bedrock principles of company law. Some scholars have argued that limited liability can be significant reformed or removed in some cases. Griffin, for example, highlights that in 1855 the very purpose was to generate economic

[136] Anna Donovan, *Reconceptualising Corporate Compliance: Responsibility, Freedom and the Law* (Bloomsbury Publishing 2021).
[137] ibid.
[138] Hardman (n 133).
[139] Dine (n 9).
[140] Hardman (n 133).

growth.[141] Moreover, the argument is presented that the practical benefits have become too readily available, which in turn invites the 'probability of exploitation'.[142] As a result of the dilution of control mechanisms and reduction in reporting requirements, Griffin proposes that strict adherence to an absolute form of limited liability should be abandoned. Whilst this strict adherence has resulted in some 'curious' outcomes, the prospect of a functioning replacement seems unattainable. The entrenchment and iron grip which has resided over company law for the last century renders structural change difficult. Moreover, specialised legislation and regulations are required for the functioning of a modern company. A removal or departure from limited liability presents challenges of certainty and enforcement of contractual bargains. Kraakman argues that corporations have unique anatomy which needs to be considered from a legislative perspective to reduce agency costs.[143]

The anatomy of corporate law maintains that it has unique characteristics which the law must 'of necessity'[144] provide for. Kraakman identifies five key characteristics: legal personality, limited liability, transferable shares, delegated management and investor ownership. Without mandatory laws, these key characteristics become difficult or expensive to enforce. Without limited liability introduced by the state, there would be an increase in costs of contracting due to monitoring and negotiating terms. If companies wished to include limited liability without the provisions of the Companies Act, this would need to be negotiated and contracted. This is inherently difficult, and as such, the imposition of legislation reduces the cost of contracting with standardised terms. The consideration of legal personality is likewise problematic without systematic provisions in place. Declaring a company as a separate person without registration and incorporation is simply not possible. A juridical person is required to be established by the state, as this is where rights are established. This is impossible to achieve without statutory provisions. Transferable shares and investor ownership are also more streamlined in the context of a registered company. An open market for shares which are transferable provides for a more

[141] Stephen Griffin, 'Limited Liability: A Necessary Revolution' (2004) 25 The Company Lawyer 99.
[142] ibid 100.
[143] Reinier H Kraakman and others, *The Anatomy of Corporate Law: A Comparative and Functional Approach* (Oxford University Press 2017).
[144] ibid.

buoyant market. Moreover, the ability to establish investor ownership in the market also reduces the cost of monitoring. Shareholders can buy and sell their shares without the concern of other shareholders and liability being attached through their ownership. Without transferable shares, the cost of monitoring and transacting would be increased. Delegated management provides for an experienced board; this permits shareholders to invest and have their investment overseen by an experienced board. Without company law governing this relationship, the costs of negotiating terms between shareholders and managers would be disproportionate. Therefore, company law provides for standardised and agreed terms, which reduces the costs of contracting. The idiosyncratic nature of corporations suits systematic regulation which would be difficult to replicate without specific corporate law. Therefore, arguments in favour of significant departures from limited liability or other key characteristics are not persuasive given the entrenchment which has arisen since the inception of limited liability and separate legal personality.

This section has evaluated the theoretical underpinning of company law and argued that despite the confused application, specific corporate law is required for the functioning of the modern corporation. Furthermore, it has presented the argument that the evolution to its current construction is one without significant debate as to the applicability of legal rules. The evolution has resulted in a dilution of formality requirements, and these requirements are based upon economic and social norms which fail to account for the descriptive elements. The result of this is evolution towards a more 'hands-off' approach to governance which can increase opportunism and which facilitates the use of corporate groups and hierarchal structuring. Irrespective of this approach, specific legislation is required for the functioning of the modern corporation, and arguments for removal of features such as limited liability are unpersuasive.

2.4 Summary

This chapter has provided an analysis as to the evolution of the corporate form, demonstrating that the historical evolution has failed to adequality debate the applicability, and consequences, to the corporate group. This lack of debate has resulted in a legitimacy failure of corporate groups, who, can wield significant

power without the correlative liability or accountability initially conceived. The evolution which has developed to become a facilitator of corporate groups is a result of legislative amendments with reducing formality requirements. Additionally, the courts have tended to follow a literal approach to applying the legislation. Moreover, despite tensions and frictions between economic and legal realities, the judicial interpretation presents a confused and complex history of this evolution. This chapter has presented the argument that the combination of facilitative legislation and judicial interpretation has cumulated in a lack of legitimacy for corporate groups. This is predicated on bedrock principles requiring strict control mechanisms which have been eroded over time. *Salomon* remains the touchstone for corporate law; however, this is a 19th-century principle which was decided when different control mechanisms were in place.
Additionally, the concept of a group company was not in contemplation when the legislative provisions were introduced, nor when *Salomon* was decided. This failure in legitimacy therefore is twofold, firstly, with corporate groups not being considered from the outset of company law principles, a lack of debate. Secondly, the corporate landscape in the 21st century is vastly different from when these provisions were introduced. This failure has presented itself where judicial interpretation has attempted, and failed, to attach liability to redress this legitimacy failure. The use of the limited company within the modern corporation has become ubiquitous; therefore, despite the legitimacy failure, its removal or reversal of the historical evolution is not persuasive. Companies have unique features which require specific legislation and provisions such as separate legal personality and limited liability. The subsequent chapters will critically analyse the effect of this legitimacy failure on corporate governance before proceeding to propose methods of reconceptualisation.

Chapter 3: Corporate Power

'As a growing proportion of the population becomes socially excluded, the private commercial corporation is an ever-increasing locus of power and an ever-growing cause of that exclusion.'[1]

The role of power in a corporate context is one which is cloaked in allegory, with the result that constructing a singular defensible definition is inherently difficult. The previous chapter evaluated how the evolution of limited liability to corporate groups emerged by virtue of accidental extension. This chapter will evaluate the role of power in the corporate context (corporate power), with the subsequent chapter analysing how corporate power differs, if at all, in a group context. This analysis engages with the hypothesis that corporate groups lack the legitimacy to wield the substantive power which they possess. Therefore, this chapter contributes to the thesis by providing a framework of corporate power which can be used to address the research questions. This thesis seeks to ascertain if corporate power is magnified in the group context.
Additionally, does this power that groups wield have the correlative legitimacy to enable the continued use and exercising of this power? This chapter will proceed to provide a theoretical analysis of how corporate power has historically been legitimised. This will provide the platform for the subsequent chapter to ascertain if legitimacy is present in the group context.

In order to determine how power arises in the corporate context, it is beneficial to evaluate the wider concept of power. John Galbraith identified three types of power: condign, compensatory and conditioned.[2] Condign power, Galbraith asserts, 'wins' by the ability to impose alternative preference by the threat of adverse consequences. This is analogous to the 'mobster' example posed by Berle, who claims that power can be exerted by brute force.[3] Compensatory power is simply exercised by payments in kind. Conditioned power, Galbraith argues, is central to the functioning of the modern economy.[4] This is carried out

[1] Alastair Hudson, *Understanding Company Law* (Routledge 2017) 280.
[2] John Kenneth Galbraith, *The Anatomy of Power* (Corgi Books 1985).
[3] Adolf A Berle, *Power without Property: A New Development in American Political Economy*, vol 56 (Harcourt, Brace & World Inc 1959) 82.
[4] Galbraith (n 2) 23.

by changing belief by means of persuasion, education or social commitment to what seems proper. This draws parallels to the broader scope argument made by Berle, whereby a central position which commands allegiance and cooperation by many is adopted. Power can therefore be surmised into words of ordinary English as follows: power is the cause of the individuals to submit to the will of others, either by force, financial means or persuasion.

Given that power is social in nature, it follows that there are relational elements. In its simplest terms, there will be a relationship between those who exercise power and those who are subject to it. In the corporate context, there are many relationships such as those with both shareholders and stakeholders. These types of power could be referred to as internal power and external power within a company. The internal power dictates the governance of a company between all the stakeholders, and the external power relates to the power the company wields at the expense of society, more generally. It is submitted that whilst these types of power are distinct, the latter arises due to the former. It is this far-reaching remit of the corporation in its ability to exercise its power to a wider audience which presents unique challenges. Moore claims that whilst individuals in one degree or another may have the power to exert their will on others, in the business corporation there is extraordinary capacity and will on others in this Galbrathian sense.[5]

Berle identified two distinct categories of relationships.[6] The first refers to a relationship between a person[7] capable of exercising power towards other individuals and groups over which the power can be made use of. Secondly is societal power, where particular power is organised and exercised within the social and political structure. These two categories are important characteristics of the modern corporation. The relationship between parties can be between the company and its shareholders, and stakeholders such as employees and creditors. This category is likely to be the more prominent category of relationship on which power is exerted in a smaller company. The second type of relationship with respect to society power is likely to be prominent in larger organisations due

[5] Marc T Moore, 'Understanding the Modern Company through the Lens of Quasi-Public Power' [2015] University of Cambridge Faculty of Law Research Paper, 8.
[6] Berle, (n 3) 79.
[7] Juridical or natural.

to their position in capital markets. This occurs due to the important role corporations play in the distribution of global wealth, as the capacity in which they operate affords them greater societal power. Mikler carried out empirical research into the political power of corporations and established that Fortune Global 500 companies amount to half of the global economy, with the top 20 global companies having greater sales than the expenditure of the bottom 166 states.[8] The result is significant due to the influence corporations can have on the states in which they operate. Mikler presents the concept that corporations are in charge from a political perspective. He supports this with the example of the global financial crises, whereby some states governed in the interests of these entities over those of their citizens.[9] This argument is particularly persuasive and timely given the recent COVID-19 pandemic,[10] where many countries across the world aimed to balance the economy, the corporations' interest with a public health crisis. This can be further demonstrated by the comparison of approaches between New Zealand (NZ) and the UK. The UK appeared to place a greater emphasis on the economy, and the protection of these organisations resulted in a significant difference in public health outcomes from that of its NZ counterpart. This is analogous to both the globalist and sceptical conception of corporations' political power, where corporations are able to influence state policy.

Corporate power is therefore wider than power in its traditionalist sense. Whilst many of the features of traditional power are identical, corporations' financial and structural construction allows for this power to transcend the limits of power exercised by individuals. Moreover, limited liability separates those who may benefit from the use of the power, the shareholders, with those who exercise it, the management. Corporate power can therefore be defined as the ability held by corporations to wield their will on both those whom they share direct relationships with and wider societal stakeholders. Its ability to surpass those direct relationships is premised on its financial and organisational structure within the marketplace.

[8] John Mikler, *The Political Power of Global Corporations* (John Wiley & Sons 2018).
[9] ibid 1.
[10] A discussion as to the economic effects of COVID-19 is beyond the scope of this thesis.

The chapter proceeds as follows: it first looks to ascertain how corporate power is exercised and the justifications for wielding this power, its legitimacy. The chapter then moves on to evaluate the division of ownership and control and how corporate power is affected as a result of this. This is significant due to the capacity in which corporations exercise their power. As established in the preceding section, power can be derived from its financial position, and given the separate legal status this position may be generated by many individuals whose rights should be protected. The chapter then moves on to establish who wields the power in a modern corporation and provides an argument for the significance of this. Having provided a working definition of corporate power and who holds this power, the chapter moves on to analyse the effects of this. The control mechanisms of this power are then analysed to ascertain if sufficient controls and checks in terms of monitoring for legitimisation are in place. Finally, the chapter considers alternative methods of controlling corporate power and legitimising the holding of this power.

This chapter contributes to the thesis as it provides a framework for corporate power, which allows the subsequent chapter to critically evaluate how corporate power is manifested in a group structure. Moreover, it identifies how power in the corporate context is legitimised, which affords the subsequent chapter a basis for analysis in the context of a corporate group. In establishing this already fragile legitimacy, the thesis will then be able to ascertain if governance within the context of corporate groups further exacerbates or alleviates corporate power. This will address the research questions in respect of the role of corporate power within a corporate group.

3.1 Theoretical origins of corporate power and its legitimacy

Berle claims that power is next to love as one of the oldest social phenomena in human history.[11] Moreover, it has been argued that power within the corporation is ubiquitous.[12] Given this omnipresence of power, methods of qualification have been developed over time to qualify the wielding of power. This section will

[11] Berle (n 3) 77.
[12] See Marc T Moore and Martin Petrin, *Corporate Governance: Law, Regulation and Theory* (Palgrave 2017) 5; Moore (n 5) 6.

proceed to analyse the theoretical origins and legitimisation mechanisms attached to corporations that wield power.

Berle contends that given the social nature of the phenomenon of power, it cannot be quantified. He compares this to property which can have a value attributed, even in the case of intangible property such as goodwill: this is not the case with power. This lack of quantification contributes to the inability to attach restrictions on power as it grows or is transferred. As this chapter will go on to analyse, the separation of ownership and control has resulted in rentier shareholding and a significant separation between ownership and management, which in turn provides isolated power for those in managerial roles. Moore has dubbed this discretionary administrative power (DAP),[13] for which accountability is required to establish legitimacy. The concept is that the ability to hold those who wield power to account provides a form of legitimacy.

The way in which power is exercised within the corporation supports the requirement of control mechanisms to legitimise this power. Berle claims that an organisation's external power is exercised principally in six ways.[14] The first is the application of their capital in determining when and how operations are carried out. In this instance, the external power is exercised by the use of their position[15] to decide how operations are performed. This is self-perpetuating in the sense that the more capital an individual or holder of power has, the more they are able to determine further use. This is analogous to the argument from Mikler that corporations are in charge. The second way of exercising power is through the use of raw materials and a company's capacity with which to buy them. The impact is that the producers are reliant on selling their supplies or raw materials. An example of this can be found in the supermarket milk price war between farmers and supermarkets.[16] In this instance, the suppliers, the farmers, were being forced to supply their milk at a price lower than the cost of production. Thirdly, Berle argues that scientific knowledge and the capacity to bring new products to market is also a way to exercise corporate power. This can be linked

[13] Moore (n 5) 21.
[14] Berle (n 3) 82.
[15] Their financial position.
[16] BBC News, 'Farmers in Fresh Protests over Supermarket Milk Prices' (*BBC News*, 2015) <https://www.bbc.co.uk/news/uk-33777075> accessed 8 July 2020.

to the first point in relation to capital: individuals with capital to develop products will be able to derive further profit from new products. Fourthly is the ability to administer and fix their prices, and fifthly companies' ability to determine their own funds for philanthropy, which is much akin to CSR. Lastly, and more substantially, the ability to withhold or declare dividends within a corporation demonstrates power. The ability of a corporation to retain its wealth can be argued to facilitate the exercising of power in the preceding ways. Corporations are given the freedom to be run in their own best interests,[17] , which affords managers the ability to withhold dividends to those who provide capital to the company. Whilst it could be argued that exercising power in any of these ways is detrimental to those who are subject to it, there remain justifications.

Economic power is justified chiefly by the fact that it is needed to produce, supply and distribute goods and services.[18] This links to the classic Smithian concept of division of labour: there are those required to manage and exercise power over others to ensure greater productivity. Power is therefore justified and required for the functioning of a modern economy; it does, however, require legitimising. This concept of legitimising corporate power is contested with opposing viewpoints on the method to legitimise. Berle defines legitimacy as the rightful possession of power.[19] Stokes claims that much of company law can be understood as a response to the problem of legitimacy of corporate power.[20] This assertion suggests that the concept of corporate power and the legitimacy of holding this power goes to the heart of the company. Parkinson argues that the public interest is the foundation of the legitimacy of companies, and society is entitled to ensure it is exercised in a way which is consistent with this interest.[21] This viewpoint is analogous to that of Berle, who argues public consensus is an important factor in legitimising corporate power.

The theoretical origins of corporate power are predicated on the concept of legitimisation. Corporations require power to function, society needs

[17] See Companies Act 2006, s 172 for example.
[18] Berle (n 3) 100.
[19] ibid 99.
[20] Mary Stokes, 'Company Law and Legal Theory' [1986] Legal Theory and Common Law 155, 156.
[21] John E Parkinson, *Corporate Power and Responsibility: Issues in the Theory of Company Law* (Oxford University Press 1993) 23.

corporations,[22] , and therefore the concept of legitimising the power required has developed. This section has provided and analysed the underlying theories of power and identified the need to legitimise this power. The next section will analyse the separation of ownership and control, utilising the framework outlined in the seminal works of Adolf Berle and Gardiner Means. It will consider the effects of the diverging roles of both ownership and control before evaluating methods of legitimation.

3.2 The Berle and Means corporation

This section will evaluate the separation between ownership and control, as recognised by Berle and Means.[23] It may be questioned why the famous work of 1932 is being examined in this thesis, and the reason for this is due to the significant change in the corporate landscape in the early 20th century. The introduction and growth of institutional investor have resulted in a sizeable shift in the way individuals invest their capital. The result is that many shares are held by institutional investors as opposed to individual shareholders. This rise of 'institutionalisation' has the capacity to further separate ownership and control between those who may be considered the beneficial owners,[24] and those who manage corporations and wield power. Moreover, the growth of complex structures such as groups further separates owners from control due to the nature of the separate legal entity. These changes in the corporate landscape provide justification for analysing the Berle and Means corporation. This section seeks to establish if this change in landscape further exacerbates the separation of ownership and control. Furthermore, given that control is heavily associated with legitimacy,[25] this section will provide a platform to evaluate current methods of legitimacy of corporate power.

Control can be argued to be at the centre of the legitimacy of corporate power: those who exercise power must have it legitimised, and this can be done through control mechanisms. This thesis identified in chapter two the importance of

[22] See John Micklethwait and Adrian Wollridge, *The Company, A Short History of a Revolutionary Idea* (1st edn, Orion Publishing Group Ltd 2003); Mikler (n 8).
[23] Adolf Berle and Gardiner Means, *Modern Corporation and Private Property* (Macmillan 1932).
[24] Beneficial owner in this sense being the end investor, the capital provider.
[25] In the sense that those who maintain control over property are deemed accountable for the use of such property.

control mechanisms being aligned with bedrock principles of company law. Those who hold property have the rights to exercise control over their property. Economist John Kay compares traditional ownership of property to that of share ownership.[26] Traditional property can be used, sold, rented and disposed of at the property owner's will. Moreover, the owner of the property will be responsible for its misuse and be able to admit the right for creditors to take a lien on it. This traditional concept of property ownership and package of rights is not the same in the context of companies and share ownership. A shareholder of a supermarket, for example, does not have the right to walk into their nearest store and use company property based on their share ownership. In this sense, the ownership of the modern corporation differs from traditional property ownership. In the corporate context, this traditional view is that shareholders hold residual claims over the company and, as such can be considered the owners of the company but not owners of its property.

Writing in 1932, Adolf Berle and Gardiner Means wrote one of the most influential and inspiring works of the 20th century. Their work concerned the growing use of more widely held[27] corporations where the company was financed by the public at large, as opposed to closely held corporations which were manager owned. In the widely held corporation, these managers had no, or negligible, interest in the company and were compensated by a fixed salary. They claimed that the Anglo-American corporation had ceased to be a private business and had become an institution.[28] This was a shift from the position seen in *Salomon*,[29] which makes possible great aggregations of property.[30] Supporting their argument with empirical data, Berle and Means highlighted that the result of this shift was the distinct functions between shareholders and managers. The shareholders were generally unable to exert control over management, and the board's day-to-day supervision was internalised. This resulted in the true separation of ownership and control whereby the role of most shareholders and members within a widely held corporation is that of a rubber stamp.

[26] John Kay, 'The Stakeholder Corporation' in Gavin Kelly, Dominic Kelly and Andrew Gamble (eds) *Stakeholder Capitalism* (Palgrave Macmillan 1997)128.
[27] Or public.
[28] Berle and Means (n 23).
[29] *Salomon v Salomon & Co Ltd* [1897] AC 22 (HL).
[30] Berle and Means, (n 23) 6.

Berle and Means observed that the separation of control produces a condition where the interests of the 'owner'[31] and the management diverge, and this divergence has caused the checks which were formally in place to disappear.[32] They argue that we have arrived at a situation whereby the shareholder in the modern corporation has surrendered a set of definite rights for indefinite expectations.[33] This is directly due to the separation of ownership and control, and the shareholders are subservient to the dominant managers. Shareholders now have little interest in a company's management, and their interest is centred around return on capital. This, Berle and Means claim, is dramatic given that the company was initially conceived as a quasi-partnership.[34] The position of a partner in a partnership is that they are jointly liable for the liabilities of firm and specifically in this context, the management of the firm. Shareholders have little interest in any management responsibilities, which Berle claims falls outside the traditional concept of property ownership, as they have surrendered control over their wealth.[35]

This divergence of interests is even further pronounced in the modern company given the share ownership structures. 13.5%[36] of shares are owned by individual shareholders with 85%[37] being owned by other shareholders, who include institutional investors, pension funds and financial intuitions. This is a departure

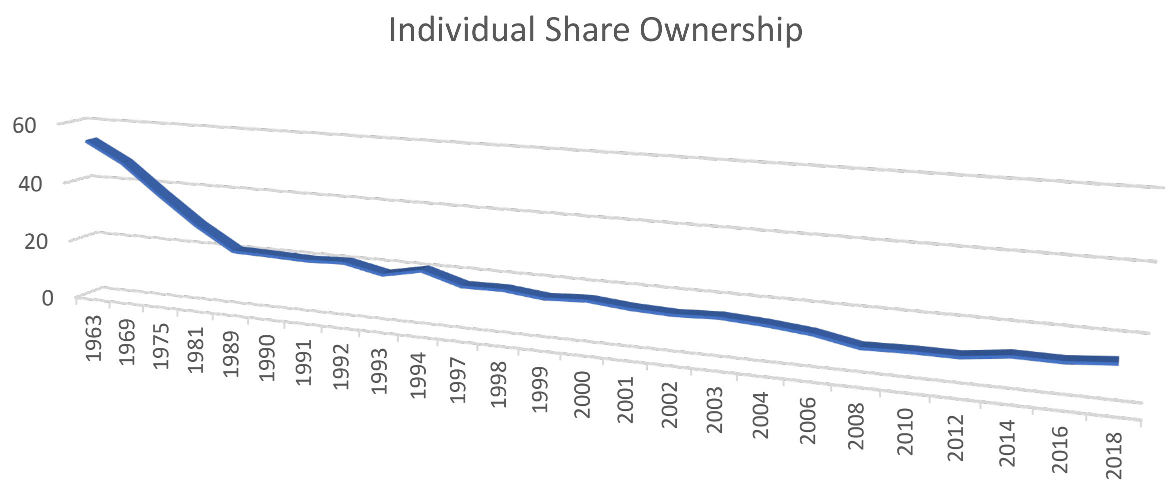

Figure 3 Individual Share Ownership

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[31] For this purpose, we can read this to be the shareholders.
[32] Berle and Means, (n 23) 7.
[33] ibid 244.
[34] ibid 217.
[35] ibid 297.
[36] Office for National Statistics, *Ownership of UK Quoted Shares: 2018* (Office for National Statistics 2018).
[37] The remaining ownership less the shares owned by the public sector.

from not only the owner-manager firm but also from the position in 1932 when Berle and Means wrote their monograph. The data suggest that individual ownership was historically in excess of 50% and has declined steadily over the last 50 years (see Figure 3).[38]

The result of this is that ownership and control have further diverged. The provider of capital is once, if not twice removed from the company in which their capital is ultimately invested. This increased separation results in the growth of managerial power, with boards which have increased ability to entrench their positions. This is due to the way in which capital is now invested; there has been a rise in institutional investors, with investors choosing to diversify their investment portfolios. This differs from investing in a single company: an investor may now decide to place their capital with a fund where a specialist investor will invest this comingled capital amount amongst a wider portfolio. The effect of this is that as opposed to investing the £100 in company X, the investor invests their capital into fund A, whose manager spreads this capital to companies B, C, D, E and F. In doing this, the capital investor has a decreased risk of losing all their capital as it is spread, and the fund is managed by a professional. The effect of this on separation of ownership and control is the reduction in the already dwindling bundle of rights that the capital investor can utilise. Their funds are now removed from direct voting rights and placed in the hands of the institutional investor.

Stapledon observes that the interests can be divided up to create parcels of shares with three main types,[39] the first being the registered holder of the share, which is the member named on the register. The second type is the beneficial owner whereby the registered holder may be holding the shares on trust for beneficiaries. The third main interest is the holder of the voting rights, which could be a fund manager employed by a trustee. The argument Stapledon presents is that there are multiple parties and organisations involved in the trading and holding of shares, with the introduction of the fund manager being the latest. With these three main rights, it may well be the case that the same person holds all

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[38] Chart produced using Office for National Statistics data from *Ownership of UK Quoted Shares: 2018* (Office for National Statistics 2018).

[39] Geofrey Stapledon, 'Institutional Investors: What Are Their Responsibilities as Shareholders?' in J Parkinson, G Kelly and A Gamble (eds), *The Political Economy of the Company* (Hart Publishing 2000), 202.

three rights: this is the traditional concept whereby ownership and control are exercised by one individual. The rise of institutional investors has resulted in these rights becoming more dispersed and held by different persons.[40] Therefore, the bundle of rights associated with corporate ownership is shared amongst multiple rights-holders, resulting in exercise of control being made more difficult. Braun, therefore, contends that ownership has radically changed since the popularisation discussed by Berle and Means.[41] This is due to the fact that the structures of portfolios are more diversified and the position of the dominant shareholders, the asset managers. The argument put forward is that the cumulative result of this division is that the corporate stock is divorced from its economic interest in it. This viewpoint is widely supported,[42] , with academics and legislators attempting to invigorate institutional investors to exercise the rights they hold. Palan argues that the firm is an intermediate institutional structure used by groups of people with controlling interests whose legal obligation and sense of social responsibility are less defined. [43] Such a lack of definition can be argued to result in diminishing exercise of control rights. This volatile nature of shareholding can result in 'short-termism' for which Blair claims regulation is required.[44] In response to this, Stapledon provides some regulatory options for reform. One proposal put forward is compulsory voting. In this instance, the holder of the share, the member named on the register, would be required to exercise their vote. This presents a number of challenges in its execution. Firstly, where shares and voting rights are held by trustees and not those beneficially entitled to the revenue, there are difficulties in casting their votes. For example, does the legal owner of the share exercise their rights as they see fit, or do they seek approval from their beneficial owners? Moreover, if the shares are held by a fund and beneficial assets are commingled, how do the rights holders determine whose beneficial interest is considered when there is a conflict? Providing these

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[40] Either natural or juridical.

[41] Benjamin Braun, 'The Great Re-Concentration and the Eclipse of Ownership [2019] Working Paper, 3.

[42] For example, see: Margaret M Blair, *Ownership and Control: Rethinking Corporate Governance for the 21st Century* (Brookings Institution 1995); Stapledon, 'Institutional Investors: What Are Their Responsibilities as Shareholders (n 39); Paddy Ireland, '2 The Corporation and the New Aristocracy Of Finance' in Jean-Philippe Robé, Antoine Lyon-Caen and Stéphane Vernac (eds), *Multinationals and the Constitutionalization of the World Power System* (Routledge 2016); Parkinson (n 21).

[43] Ronen Palan, 'Corporate Power in a Global Economy' [2016] Susan Strange and the Future of Global Political Economy: Power, Control and Transformation 152, 100.

[44] Blair (n 42) 54.

concerns are surmountable, a further problem of enforceability and monitoring arises. If companies are required to have 100% of the shares vote for a quorum, little may be achieved. Additionally, enforcing voting through fines challenges the core concept of limited liability. Liability would not be limited if fines could be imposed upon members for non-compliance with constitutional voting. Whilst there are benefits which can be attributed to compulsory voting, such as greater control through engagement, the costs outweigh these benefits. Two further proposals for regulatory reform were also put forward by Stapledon: a requirement for fund managers to disclose voting actions and a requirement for trustees to adopt a voting policy. The concept of disclosure of voting actions is persuasive because it affords beneficial investors to review voting actions history and has the potential to influence managers indirectly. For example, investors may be more inclined to invest with a fund which is closely aligned to their interests, such as green energy. In this example, investors would not invest in funds which were at a substantial cost to the environment. This principle functions in the same way as consumers being unwilling to buy products of poor quality. The difficulty with the transference of this principle into the capital investment market is that it is inherently complex. If investors were confident of their own investments, they would not require asset managers, and therefore making voting decisions history available could result in investors being unable to scrutinise them or disinterested in such scrutiny. This disinterest is another argument against disclosure: shareholders are fixated on short-term returns. Therefore, provided they see a return on their investment, shareholders may be disinterested in reviewing voting history, resulting in its introduction being made redundant.

The requirement for a voting policy is the most persuasive amongst Stapledon's proposals for regulation. The requirement could function much like a shareholder's agreement between beneficial interest holders and the asset manager or other interest holders. In this instance, the legal member would be free to cast votes without concern for conflicting interests of beneficial interest holders. The voting policy requirement could also provide a framework so that investors are confident that their collective interests will be exercised. This has the potential of bridging the ownership and control due to legal ownership being collectively owned. Bringing ownership and control closer together mitigates some of the concerns highlighted by Berle and Means. It has been argued that this is a great re-conception and provides increased strength to dominant shareholders.[45] This, in turn has seemingly perfected the reunification of ownership and control.[46] The difficulty with this conclusion is that in this scenario, the power is held by the legal owner as a trustee of the beneficial owner.[47] If we can accept that this has reunified the division of ownership and control, there remains a division of control rights between those who hold the beneficial interests and those who hold the legal interest on trust. Moreover, when coupled with the disinterested investor, this merely shifts the power from one organisation to another whilst introducing monitoring costs,[48] which renders the proposal unpersuasive. This is analogous to the conclusion drawn by Stapledon, who concedes that institutional investors are not obliged to be engaged within governance legislating, and forcing them to do so is unlikely to have the desired outcome.

The importance of the position of institutional investors has been brought to the forefront of the corporate agenda with reports such as the Walker review; the role of institutional investors remains one of the most debated issues in corporate law.[49] Following on from this, the Financial Reporting Council (FRC) introduced a Stewardship Code (SC) in 2010. A number of the initial principles draw parallels to proposals put forward by Stapledon. Principles on disclosure of policies, voting activities and conflicts of interest appear to be favourable to what Stapledon was advocating. This policy on voting aims to have institutional investors play a more active role. This lack of active engagement Blair claimed caused myopia, and in taking a more active part this would be reduced.[50] From January 2020, a new SC came into force which aims to extend this engagement not only for asset managers and owners but also the service providers who support them. The new code provides a definition of what is meant by stewardship which was absent in its predecessors. It states, ‘Stewardship is the responsible allocation, management and oversight of capital to create long term value for clients and beneficiaries leading to sustainable benefits for the economy and society’.[51]

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[45] Braun (n 41) 21.
[46] ibid 21.
[47] Braun dubs this the factual owner.
[48] Blair (n 42) 187.
[49] Paul Davies, ‘The UK Stewardship Code 2010-2020. From Saving the Company to Saving the Planet?’ [2020] European Corporate Governance Institute-Law Working Paper, 10, 10.
[50] Blair (n 42) 140.
[51] Financial Reporting Council, *The UK Stewardship Code 2020* (2020) 4.

The SC coming into force in 2020 is the third iteration to be introduced, eight years after its first conception. This third code has twelve principles for asset owners and managers and a further six principles for service providers. This can be seen as a significant expansion to the first code which had seven principles aimed towards broader engagement. Davies contends that the fact the SC went unamended whilst its companion code[52] over the same period underwent three amendments only supports the argument that the first SC was unsuccessful.[53] One area of significant difference between the first and most recent version is that in the latter, not only does the SC apply to asset managers, but it also applies to service providers. Moreover, the third SC goes beyond engagement, and whilst this remains an aim of the code, it is now only one of a number of recommendations. Following the 2020 code coming into force, Davies analysed the failure of the first. He identifies two distinct incentives for asset managers:[54] financial and reputational. The difference between the versions lies in incentives, where the structure is different. Reputational incentives operate more strongly in relation to the second version of the SC. Reputational damage can be defined as maintaining a good name with parties who have the capacity to harm you.[55] The code has a focus on a more social outlook with factors such as climate change and environmental social governance (ESG) integration. This arguably has pivoted the focus away from the performance of individual companies and more towards the effects on society.[56] This shifted focus towards a more societally driven company only further extends the concept of ownership and control if the benefit of the company is to be aimed toward society more generally. This inclusion within the revised code is in line with the amendments of s 172 of the Companies Act 2006, permitting corporate directors to consider wider stakeholders. The addition of ESG now permits investors to include stakeholders in their consideration. Given the condemnation of the code in the Kingman review, Davies claims that the code can be said to have had a remarkable escape.

[52] Financial Reporting Council, *The UK Stewardship Code 2020* (2020).
[53] Davies (n 49) 4.
[54] ibid 15.
[55] Definition provided by Davis, ibid 27.
[56] ibid 31.

Ireland advocates that argument of distribution of wealth through institutional investment is misplaced.[57] The proposition that wealth ends up back with society through this distribution is misunderstood, and the very concentration of this wealth supports the theory that share ownership is not democratised.[58] This assertion from Ireland supports the argument for further separation of ownership and control due to the fact that democratisation is not functioning in practice as intended. Given the rise of institutional investment from faulty foundations, the dispersion of ownership and control can be argued to be further progressed than initially envisaged by Berle and Means. The importance and sustained growth of the institutional investor has only further divided ownership and control and in turn has widened the gap between those who provide capital and those who manage the capital.

The preceding discussion confirms the continuing relevance of the Berle and Means corporation and the ongoing role this separation plays. Moreover, the prior analysis highlights the increased importance due to more dispersed shareholding and increasing institutional investors. This provides a lens from which to view the firm between the management on the one hand and the shareholders and beneficial interest holders on the other to establish the potential discretional power that managers wield. The next section will evaluate the role of corporate power and analyse the effect this separation of ownership and control has before ascertaining if control results in wielding of power.

3.3 The role and possession of corporate power in the modern corporation

The preceding section has elucidated the growing division between ownership and control. This section will evaluate the role of corporate power in the modern corporation and establish which individuals wield this power. Berle and Means famously highlighted that the interests of the owner and the manager were divided, and where there was division, these managers should be controlled to ensure this power was not left unmonitored. In a widely held corporation, the managers are those who make the decisions. Padfield defines the role of

[57] Ireland, '2 The Corporation and the New Aristocracy Of Finance' (n 42) 57.
[58] ibid.

corporate governance and the required rules and theories. These determine how scarce resources will be allocated and what the goal of corporate decision-making should be.[59] Moore considers the application of corporate power in terms of relational architecture.[60] It is this relational architecture which is of great importance within corporate governance, as the corporation is a 'thing' and not a person, and it, therefore, requires natural persons to manage it.[61] These natural persons and officers of a corporation will be subject to a hierarchical structure. It is this structure where power is held and shared amongst those running the corporation, which must be analysed to ascertain if the power wielded is legitimate.

The issue of who controls a corporation is of fundamental importance. Corporations hold almost the same rights as individuals but often enjoy benefits that individuals cannot.[62] Robé highlights that corporations can be eternal, whereas with natural persons upon death, assets are redistributed. More importantly, companies can buy shares in other companies to isolate risks, creating groups. This isolation of risks allows the company the ability to gain power advantages.[63] The fact that legal entities are treated the same as individuals but enjoy additional benefits is a source of perversion in the world power system.[64] These rights are an enabler of corporate, economic and political power. The corporation, by its very nature, is made up of many actors within it who exercise the rights of the corporation. The company is simply unable to manage itself due to its artificial nature; it therefore requires natural persons to run the company and undertake corporate decisions. The question therefore arises as to who wields significant power amongst these actors. Shareholders can be identified as persons with significant control, with powers to appoint and terminate the board. This control could be argued to be the wielding of substantial power due to the fact that actions may be taken in shareholders' interest to avoid termination. However, as the preceding section analysed, there is a divergence

[59] Stefan J Padfield, 'The Role of Corporate Personality Theory in Opting Out of Shareholder Wealth Maximization' (2016) 19 Transactions: Tenn J Bus L 415, 416.
[60] Moore (n 5) 4.
[61] Whilst corporate directors exist, the principle is the same, and the corporate director will need a natural person to act upon its behalf.
[62] Jean-Philippe Robé, Antoine Lyon-Caen and Stéphane Vernac, *Multinationals and the Constitutionalization of the World Power System* (Routledge 2016) 22.
[63] This is further explored in chapter 4.
[64] Robé, Lyon-Caen and Vernac (n 62) 25.

of ownership and control, with individual shareholdings less prominent. Power is therefore often exercised by managers without recourse due to shareholders' lack of monitoring and engagement. It is this managerial power which this section will critically evaluate.

The term ‘manager’ can depict a wide range of roles within a corporation, and it will often refer to the board of directors or executive board. However, depending on the size of the organisation, a manager could be someone absent from the title of a director but responsible for key managerial decisions. The wider term manager will therefore be utilised to encompass all those who may wield power on behalf of or through a company.

The preceding sections have analysed the separate roles of ownership and management. The prevailing conception of the corporate theory is that of the shareholder model, whereby the role of corporate law is to ensure that the company serves the best interests of the shareholders.[65] To achieve this goal, stakeholders and actors must undertake roles within the company to this end. The separate legal entity principle dictates that shareholders, despite often being considered ‘owners’ of the company, do not automatically assume a managerial position within the company. Moreover, given the large companies and diverse shareholding, this would be impractical if not impossible. Managerial positions, therefore, need to be filled formally by appointment or by a delegation of an officer of the company. A company must have directors, with a minimum number of two for a public company and one for a private company.[66] These directors occupy a position with substantial power, and they can exercise this power as they wish and have the power to bind the company.[67] Following formal appointment, directors[68] are free to delegate to discharge their duties.[69] Therefore, management functions can either be carried out by those in office as a director or those who have been delegated such authority. Therefore, we can surmise that the roles of the actors within a company are the directors, or those delegated

[65] Reinier Kraakman and others, *The Anatomy of Corporate Law: A Comparative and Functional Approach* (Oxford University Press 2017).
[66] Companies Act 2006 s 154.
[67] ibid s 40.
[68] Subject to their individual model articles, see model art 5.
[69] For example see: *City Equitable Fire Insurance Co Ltd, Re* [1925] Ch 407, *Dovey v Corey [1901] AC 477*, *Norman v Theodore Goddard [1991] BCLC 1028*, *Re Barings plc (No 5) [2000] 1 BCLC 523*.

to carry out the running of the company, and the shareholders to appoint the directors and ensure they discharge their duties.

It is of particular note that given these two distinct roles, there is an element of similarity with public law. Moore advocates for a 'quasi-public' understanding of the company, arguing that the concept of power cannot be understood by the private orthodox position of the company.[70] This argument is premised based on DAP whereby power is allocated to a manager assuming a position within an organisation. DAP is distinct to the corporate form and as such, has the potential to utilise power in differing ways due to how capital is raised. DAP, Moore argues, entails the sacrifice by an individual investor of their freedom of action in the expectation that a net gain on material welfare will be brought.[71] Essentially, the investor[72] waives their traditional property rights in the hope of a return on their investment. In doing this, they hand over their property rights to be managed by another person, and the position grows with the size of an organisation because the size of the capital being managed increases. The holder of this DAP has the cumulative property rights of all investors, and as investment grows, so too does this DAP. Moore submits that DAP is tantamount to quasi-public power, and just like public power, it must be 'checked' by its citizens; so too must this power of the company be checked to legitimise it.[73] This correlates to the legitimisation of power in a more generalist context. Those who wield power must have it legitimised in order to have continued possession of such power. In the public context, such as Moore highlights, this is done by the electorate voting every five years[74] and removing those in power who may have exercised in contradiction with the wishes of those who bestowed the power upon them. The corporate context should operate in a similar way; however, given the dispersion of shareholding and the general disinterest of shareholders, this legitimisation is not analogous to the public position. The fundamental point is that there is a collectivised process of resource accumulation and then subsequent administration which is legitimised through voting. However, despite their similar

[70] Moore (n 5) 5.
[71] ibid 9.
[72] Either individual or institutional.
[73] Moore (n 5) 5.
[74] Fixed-term Parliaments Act 2011

processes, this method of checking corporate power remains subservient to that of public power.

The existence of DAP in a corporate setting has been argued to present additional challenges. Private officeholders are able to wield substantial discretion in allocation of economic resources.[75] Moore contends that there are two interlocking concepts in DAP, namely: allocative power which provides a range of uses for investment, and appropriative power which gives legal capacity to determine a rate of return without consent of the capital provider.[76] The appropriative power gives corporations latitude to establish capital accumulation. The process of capital accumulation in itself is not nefarious, as there are good commercial reasons for doing so. The issues lie in the fact that the decisions in this respect are left to the managers within the corporation on what level of capital is retained. By its very nature, corporate autonomy is paradoxically predicated on the collective loss of individual autonomy.[77] The corporate power and level of board autonomy is based on the surrender by the collective individuals of their autonomy. One method of explanation is that the autonomy and collective power of those capital providers is being transferred to the corporation for the managers to discharge this power. The foundation of internal corporate power and its imbalance, therefore, lies within the structured decision-making board.

This structured board derives its position from two distinct but interlocking principles: board supremacy and board control over corporate dividends.[78] Board supremacy, Moore argues, is a constitutional right which is often defended by the board.[79] The concept of board supremacy further entrenches the power of the management board. The board requires supremacy to undertake their functions and discharge their duties, but in being supreme they retain their power. This level of supremacy leads Moore to assert that in some corporations, residual legal ownership can be said to sit squarely with the board.[80] This argument suggests that the power which sits with the board is akin to traditional property ownership whereby ownership rights are exercised. Delegation can therefore be said to be

[75] Moore (n 5) 10.
[76] ibid.
[77] ibid 11.
[78] ibid 15.
[79] ibid 15.
[80] ibid 17.

a prerequisite of corporate efficiency, and given that shareholders are practically unable to replace managers,[81] there is a practical requirement to maintain a board of managers to run the company. Parkinson claims that delegation of management comes with a risk.[82] Indeed, Stokes concludes that efforts to subject corporate managers to controls from power being exercised arbitrarily have not been successful.[83] Stokes's viewpoint is analogous to that of Parkinson, who determines that despite the manager's role being fiduciary, the majority of companies have escaped shareholder control.[84]

The position of managers as actors within a corporation can therefore be concluded as those wielding the power. This follows as a result from the shareholders individually wielding little power unless they are a majority shareholder, which as the empirical data shows is infrequent. Moreover, their collective power through their economic contributions is passed to the company. The company assumes the power of those collective contributors through their economic contributions, and this power due to the artificial nature of the company needs to be delegated. This delegation is toward directors and those who have power sub-delegated.

The delegation shares a solid theoretical underpinning from the division of specialist roles within the Smithian economic theory. In this sense, the specialist function of management is carried out by one party whilst the providers of capital are different. Each actor has their role, and their division into these roles is efficient. The power wielded by corporations is therefore exercised by the managers who are often removed from the shareholders. This section has identified the different roles within a corporation in respect of the corporate and economic power dimension. It concludes that power is most likely held by the managers and that the further removed from shareholders, the greater risk of this power being utilised arbitrarily. The next section will explore the effects of managers holding this power and if this is of importance within the concept of corporate governance.

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[81] Parkinson (n 21) 63.
[82] ibid 51.
[83] Mary Stokes, 'Company Law and Legal Theory' [1986] Legal Theory and Common Law 155 173.
[84] Parkinson (n 21) 55.

3.4 The effects of corporate power

The preceding sections analysed the divergence of ownership and control; moreover, it established that the ultimate controllers of power within a corporation are the internal managers. This section will analyse if this wielding is legitimate and establish the importance of who holds this power. In doing so, this chapter seeks to address the following question: why does it matter that power vests with managers? Moore presents the argument that corporate power can be viewed as quasi-public, given the current corporate governance structure. He further claims this is structurally unstable due to the absence of a framework underpinning effective accountability.[85] This section will analyse the current framework to ascertain the importance of managers holding substantial power within the corporation.

One significant factor underlying this importance is corporate power's influence on society. The chapter has already delineated the meaning of power and its ability to impose its will on others. This 'will' extends further than individuals directly connected with a company. Parkinson argues that corporations will have greater bargaining power over governments, which makes them a special case when attempting to influence legislation.[86] This viewpoint is analogous to Stokes, who claims that corporate power is concerning because it threatens the political-economic organisation which is associated with liberal democracy.[87] Moreover, this view is shared by Mikler, who presents empirical data to support the vast political power corporations wield. This links to the rule of law and the need to impose controls and checks on power. Establishing who wields power and ascertaining how this is utilised allows an analysis of the current forms of checks and controls.

It has been established and is indeed widely accepted that shareholders cannot replace managers, and their role within corporate governance is to legitimise the power held by managers by exercising their voting rights. In this sense, it is

[85] Moore, Understanding the Modern Company through the Lens of Quasi-Public Power' (n 5).
[86] Parkinson (n 21) 20.
[87] Stokes (n 20) 156.

argued that the corporation operates much like public law, with managers in the position of power and the shareholders as those who effectively put the managers in power. Whilst theoretically possible that any nefarious conduct by these managers could result in the shareholders removing them from office,[88] the passivity of the modern shareholder renders this outcome unlikely. However, there remain further issues which should be explored in relation to the conflicting wishes of the shareholders and the managers. Jensen highlights that often the objectives of the managers and the shareholders may conflict.[89] The competing interests of shareholders and managers need not give rise to an immediate concern. First and foremost, despite the popularist theory of the shareholder model,[90] the directors owe their duties to the company and not to shareholders directly. This may appear somewhat circular in that the directors owe duties to the company, and the company is collectively considered to be owned by shareholders, but the subtle difference is significant. The very interests of widely dispersed shareholders could themselves be conflicting, which without the duty applying to the company may generate difficulty in managers reaching decisions. An example of competing interests has been codified in the Companies Act 2006 s 172,[91] which provides a broader scope of requirements that directors may consider in discharge of their duties, or in their exercise of power. Section 172 provides a broader scope for directors to make decisions, and also evidences that whilst the interests of shareholders and managers may conflict there may be commercial and substantive, and therefore legitimate, grounds for this.

Jensen highlights additional sources of conflict between managers and shareholders.[92] Firstly is choice of effort, the claim is that effort is good for the firm but bad for the managers. This is premised on the basis of managers putting in the minimum amount required to discharge their duties. Naturally, the shareholders and the company will want the manager who is deriving payment to produce the greatest amount of effort to promote the company. Conversely, the manager may wish to carry out as little effort as is required to remain in the post or avoid a hostile takeover. This viewpoint is akin to the self-entrenchment

[88] By virtue of the rights in Companies Act 2006 s 168.
[89] Michael Jensen, *A Theory of the Firm: Governance, Residual Claims, and Organizational Forms* (Harvard University Press 2003) 9.
[90] Shareholders as owners.
[91] Companies Act 2006.
[92] Jensen (n 89) 9.

argument made by Parkinson, who claims that senior executives may become lethargic where they become effectively unremovable.[93] Where managers consider themselves unremovable, the effort they produce may be significantly lower than that required for the company's efficient running. The second source of conflict Jensen highlights is the differential risk exposure; managers have trivial human capital invested and as such may be less concerned about the long-term success of the company. Managers may, therefore, be more concerned with their position and make short-term decisions to remain in office which could have detrimental effects for the value of the company in the long term. This links with the third conflict of interest Jensen highlights, that of limited tenure within the corporation. The corporation has an indefinite life and is 'eternal' in the sense it can exist in perpetuity, whereas the managers running the company have a limited time in which they derive an income and benefits. This again links to the short-termism argument in that shareholders and the company may be looking for long-term successes or that long-term success is the best economic decision for the company, but the manager may be fixated on the short-term nature of their appointment. Given that shareholders are to exercise checks and controls on managers, the conflicting interests between both parties may mean that they are not best placed to do so.

A further issue with the isolation of power to managers is the potential lack of control or monitoring, that is carried out to legitimise the power wielded. Stokes presents the argument that no matter how much the law strives to give shareholders the power to challenge the company, this is a fruitless endeavour due the size of the average shareholding.[94] This is a highly persuasive argument, even more so given the development since Stokes's writing in 1986. This thesis has indicated that the increase of institutional investment has only further diluted the shares within corporations. This reduction in share size results in many, if not all, shareholdings being minority shareholders with little to no voting power. Moreover, Parkinson submits that; furthermore, this very real separation of ownership and control could result in management seeking deviant goals.[95] This links to the preceding argument that incompetent and self-serving directors have

[93] Parkinson (n 21) 99.
[94] Stokes (n 20) 168.
[95] Parkinson (n 21) 207.

escaped effective shareholder control and, as such, have entrenched their position, enabling them to not only become lethargic but to potentially act in their own interests. Parkinson provides an example: monitoring the disposal of assets at market price is difficult.[96] Whilst transactions at an undervalue the potential to be returned under s 238 of the Insolvency Act 1986, this requires a company to become insolvent. The Companies Act does provide some constitutional protection,[97] but the problem of enforceability and detection occurs. This low probability of detection not only prevents managers from being caught but it also has the added problem of encouragement. This further links to the managers' interests being separate from the shareholders. One example of this is in boards acting collectively, whereby board members are less likely to condemn the behaviour of a fellow member, the groupthink paradox. This is because there is the potential for the collective interests of the board to benefit the board members as opposed to the company. A further example of this is regarding their own remuneration: it is in the board members' interest to set their own salary as high as affordable, whereas this may not be in the interests of the shareholders, as their investment return will be reduced. This directly relates to an issue Jensen highlighted, that of adjustment following identification.[98] It could be concluded that the issues of management are easily identifiable in contrast with the position Parkinson takes. A further issue arises in relation to the timing of the identification. The way in which the management operates results in problems becoming severe before being identified.[99] In collectively organising themselves, and absent active shareholders, managers occupy a freer rein which has the potential to entrench their positions. Moreover, when mismanagement is identified, the problems are severe, and adjustment is difficult, given the culture within the management structure. The problem is, therefore twofold, in that the managers lack significant control, which can result in unmotivated or self-serving managers, which is further exacerbated by problems of identification and holding to account. This can be summarised as a result of lack of control or insufficient control by shareholders. The need for control is an important aspect of the legitimisation of corporate power.

[96] ibid.
[97] For example, s 41.
[98] Jensen (n 89) 31.
[99] ibid 31.

The engagement of the shareholders is of significant importance, as control is often vested with managers, who require monitoring. This has been brought to the forefront of the corporate governance agenda following the introduction of provisions such as s 172 of the Companies Act,[100] which requires greater consideration of wider stakeholders. Moreover, the UK Corporate Governance Code requires regular engagement with major shareholders to understand their views on governance and performance.[101] Research carried out by Grant Thornton over the last 18 years has ascertained the engagement of majority shareholders with FTSE 100, 250 and 350 companies. It is noteworthy that amongst the majority shareholders until 2019, engagement had been on a downward trajectory.[102] 2019 saw the first increase in four years with engagement reaching 44%, increasing 31% in the preceding year.[103] Despite this first increase in engagement for several years, the data is still troublesome in terms of engagement. Firstly, engagement is defined in the research by asking the question, 'to what degree does the board demonstrate the steps taken to understand the views of major shareholders?'[104]

This question considers the matter of degree as to the demonstration of understanding the views of shareholders. The vagueness of this question posed to gain the data is concerning because it simply seeks to ascertain if the board understands the views of the shareholders, not that they exercise them. It is, however, not unsurprising that in ascertaining the views of shareholders, the board members will seek to exercise these views to avoid termination of their position on the board. There are further difficulties this data presents, the first of which is that the level of engagement is still low even on this vague question posed. The level of engagement within the FTSE 100 appears to be most notable, with engagement passing 50% of shareholders, with 62% of shareholders engaged. This is a significant increase on their previous year of 44%, which could suggest engagement is increasing within the FTSE 100. Within the FTSE 250 and FTSE 350, the data shows a bleaker picture with engagement levels over the last four years averaging 27% and 35%, respectively. These levels of

[100] Companies Act 2006
[101] Financial Reporting Council, *The UK Corporate Governance Code 2018* (Financial Reporting Council, 2018) Provision 3.
[102] Grant Thornton, *Corporate Governance Review 2019* (Grant Thornton 2019).
[103] ibid 34.
[104] ibid 34.

engagement with shareholders therefore amount to around a third of shareholders within the majority of large companies. This figure can be argued to be further diluted by the fact that the data which these levels of engagement are predicated on are 'major shareholders' not all shareholders. This categorisation of major, not all, shareholders means that the real figure of engagement is indeed much lower than what is reported in this data when all, and not just major, shareholders are considered.

Given the low levels of engagement within the large corporations, this generates greater importance in power being exercised legitimately. For those who wield power to continue wielding it, it must be legitimised for the continued exercise of this power. The lack of engagement from shareholders presents an additional problem of legitimisation due the shareholders' interests being diminished. Problems of disinterest regarding monitoring could present themselves in several ways. Firstly, the lack of engagement could result in shareholders simply not exercising their voting rights, resulting in complacent and potentially self-serving managers, as discussed in the preceding paragraphs. Lack of engagement and monitoring in this regard can result in managers having unencumbered power with lack of relevant controls which ought to be in place. Following the empirical data from Grant Thornton, given shareholder engagement has been below the 50% threshold for several years, the threat of termination of appointment[105] from the shareholders is somewhat decreased.

The divergence of interests is another reason why disengagement might present a challenge regarding legitimisation of power. This issue is twofold: firstly, in that shareholders may have competing interests, and secondly, institutional investors may either avoid exercising their votes or cast them in a contradictory way. If shareholders' interests are competing, votes could also be conflicting, resulting in further freedom for managers of corporations. Secondly, managers could be exercising their power to benefit themselves indirectly to ensure their longevity on the board or seek career progression with another company. This is the issue of short-termism, which is widely debated[106] as a significant problem within

[105] By way of ordinary resolution.
[106] For example, see: Andrea Bowdren, 'Contextualising Short-Termism: Does the Corporate Legal Landscape Facilitate Managerial Myopia?' [2016] UCL Journal of Law and Jurisprudence

corporate law. The managers will be fixated on short-term results to either maintain their own position or gain a position elsewhere. This appears to have a practical underpinning: if a corporation is investing in wider stakeholder issues to the detriment of investor returns, then the position of those managing the corporation could be compromised. This is because many investors are institutional and seek a return on their investment. Likewise, if a corporation is not seen as profit-making, the managers will not be an attractive acquisition for alternative corporations to appoint. Therefore, it is in the interests of managers to undertake activities which result in short-term gain as this results in the return on investment which institutional investors so desperately seek. The disadvantage lies within the legitimisation of corporate power that these managers wield. If investors see a return on their investment, they will likely be disinterested as to how this return on capital is obtained. This paves a route for potential irresponsible managers who have large discretion to exercise the power they hold as they wish; Ireland argues this is part of the framework which makes corporations schizophrenic in nature.[107]

This section has evaluated the importance of managers as the holders of power within the corporation and the outcomes of wielding this power. It has also analysed pitfalls in the legitimisation of this power, the lack of monitoring and checks on management. Following on from the identification of these issues of legitimacy and control checks, the next section will provide an analysis as to how this power is controlled and legitimised. Following on from the dispersion of interests and power vesting with arbitrary managers, the next section will evaluate the existing controls which managers are subject too.

3.5 The current methods of monitoring and control of managers

285; Paddy Ireland, 'Company Law and the Myth of Shareholder Ownership' (1999) 62 Modern Law Review 32; Ireland, 'Corporate Schizophrenia: The Institutional Origins of Corporate Social Irresponsibility' in Nina Boeger and Charlotte Villiers (eds), *Shaping the Corporate Landscape Towards Corporate Reform and Enterprise Diversity* (1 edn, Hart Publishing 2018); Prem Sikka and others, *Regulatory Architecture to Enhance Democracy and Business Accountability* (2019) amongst others.

[107] Paddy Ireland, 'Corporate Schizophrenia: The Institutional Origins of Corporate Social Irresponsibility' (n 106).

This section will consider and analyse the existing provisions used to legitimise corporate power held by managers. It will first investigate the duties of the directors and to whom these are owed and in what capacity. Moreover, it will analyse if these provisions effect the use and control of power, and if they mitigate and monitor corporate power. Following the analysis of legislative provisions and protections to corporate power, this section will consider the applicability of the regulations on corporate power. It will evaluate the use of the UK Corporate Governance Code to establish if this supports the legitimacy of power. In analysing these two categories, which impose restrictions on managers, this section will conclude that current restrictions and monitoring are unsuccessful in their legitimisation of corporate power.

A primary source of legitimisation lies with the Companies Act[108] itself. Whilst there remains an argument that managers appear to have unfettered powers, they owe some fiduciary duties. Fiduciary duties are codified within the Companies Act and apply to directors of the company who owe certain duties to the company. Whilst this chapter has referred to managers in a broader concept to encompass those with managerial responsibility, and the duties may nonetheless still apply. Section 250[109] provides that directors need not be named or formally appointed as directors if they assume the role of the director. The standard has been set high by the courts, and general managers are unlikely to be found as directors.[110] The duties are therefore more likely to be relevant in terms of delegation and ensuring that the director who is delegating their power is responsible for monitoring the delegate by virtue of their duties owed to the company.

There are seven principal duties which directors must discharge whilst in office. These duties provide an additional means, other than the articles, to regulate directors. A director's control of property puts them into a fiduciary role. In this sense, these codified duties are to complement the existing common law fiduciary position. To fully evaluate these duties, it is necessary to first outline what they

[108] Companies Act 2006.
[109] The Companies Act 2006.
[110] For example, see *Re Hydrodan (Corby) Ltd [1994]*, *Re Richborough Furniture Ltd [1996]*, *Secretary of State for Industry v Tjolle [1998]* and *Secretary of State for Trade and Industry v Hollier [2007]*. The duties provide an additional means to regulate directors where corporate governance fails.

are and their parameters of application. The duties can be found with s 171 and s 177 of the Companies Act 2006 and outline the basic duties which a director is to discharge. It is important to note that despite the generally accepted shareholder ownership model, these duties are owed to the company itself and not to shareholders.[111] Section 171[112] requires that directors must act in accordance with the constitution[113] and only exercise powers for the purpose in which they were conferred. This provision is protecting the constitution of the corporation to ensure powers granted are not exceeded and that the object of the company[114] is adhered to.

Section 172[115] has shown to be one of the more controversial duties introduced by the 2006 Act. It provides that there is a duty to promote the success of the company, and prima facie the duty to promote success does not appear contentious. The contention arises with the factors in which directors are to give consideration in discharging this duty. The duty is to promote success for the members as a whole. In determining this, the statute provides some specific considerations: long-termism, employees, other constitutional purposes, creditors, the environment and the need to act fairly amongst its members. Section 172 can therefore be argued to be revolutionary, as it is manoeuvring away from the traditional shareholder ownership model and more towards the 'enlightened shareholder value concept. Section 172 provides a greater consideration of wider stakeholders, which is an evolution from its previous position. The inclusion of this wider stakeholder approach has engaged much debate as to its effectiveness.[116] Whilst this provision permits the inclusion of wider stakeholder interests in corporate decision making, the wording of the provision makes it clear that directors may only have regard to this if it benefits the members as a whole.[117] Therefore, if in making a corporate decision it

[111] Companies Act 2006 s 170 (1).
[112] ibid.
[113] As defined by in s 257 ibid.
[114] If an object is outlined.
[115] Companies Act 2006.
[116] For example, see: Georgina Tsagas, 'Section 172 of the Companies Act 2006: Desperate Times Call for Soft Law Measures' in Nina Boeger and Charlotte Villiers (eds), *Shaping the Corporate Landscape: Towards Corporate Reform and Enterprise Diversity* (1 edn, Hart Publishing 2018); Irit Mevorach, *Insolvency within Multinational Enterprise Groups* (OUP 2009); Irit Mevorach, 'A Fresh View on the Hard/Soft Law Divide: Implications for International Insolvency of Enterprise Groups' (2018) 40 Mich J Int'l L 505; Padfield (n 59).
[117] Shareholders.

benefits stakeholders but not members more generally, then this enlightened shareholder value is somewhat diminished. Palmer's[118] argues that it is defence more than a duty. It claims that the ambition of avoiding director accountability has not been achieved. The result is that directors will now be able to justify almost any bona fide approach, provided they can argue it is in the interests of delivering the success of the company. Section 172 has been counter-intuitive and created a defence by which to avoid some of the other duties, and only further increases the autonomy of the directors and their power.

Section 173 provides that directors must exercise independent judgement. This was traditionally expressed as the requirement not to fetter their discretion. This duty appears to suggest that directors must undertake all management decisions and are not able to delegate their decision-making power. Indeed, the duty does not grant or confer a power to delegate, but it does not prevent delegation provided is not inconsistent with the company's constitution. This duty does introduce elements of moderation to those to whom they delegate power: they remain responsible for discharging their duties, therefore, this provision can prevent delegation as avoidance of liability strategy.

Section 174[119] states that the directors must exercise reasonable care, skill and diligence. This test was traditionally subjective and only required a director's own knowledge and experience. The result of this was that it allowed poor directors to escape liability where a person of their office ought to have possessed the requisite skill.[120] This traditional subjective test has since been codified in the 2006 Act whereby an objective test requiring the general skill which may be reasonably expected of a person carrying out functions of a director is to be considered. Moreover, the general knowledge of a director's skill and experience specific to themselves, the subjective element, is also applicable. The subjective element has therefore been combined with an objective element which arguably presents a much more stringent test. This double level of the test is important in the control of corporate power. Under the subjective test alone, a poor director, or simply one unaware of delegated management decisions, may be able to

[118] Geoffrey Morse and Sarah Worthington, *Palmer's Company Law* (Sweet & Maxwell 2010) 8. 2616.
[119] Companies Act 2006.
[120] *City Equitable Fire Insurance Co Ltd, Re* [1930] 2 Ch 293.

escape liability. With the modern test of reasonable care, skill and diligence, the directors are required to be informed of the business that they are managing.[121] Moreover, directors are not able to evade liability for negligence by avoiding activities in their directorial role: they must remain engaged with the company they are managing.[122]

A substantive area for concern is that liability in regard to this duty is in relation to negligence, and directors will not be responsible for damages for misjudgement. Therefore, directors may justify their actions and decision-making on the grounds of commercial decision-making, which by its nature is risky.[123] The duty is owed to the company and remedies remain equitable, which presents problems of enforceability and practical rectification.

Sections 175–177[124] seek to prevent conflicts of personal interests and personal benefit to the managers when acting on behalf of the company. Section 175 provides that the director must avoid a situation in which they have direct or indirect interests which conflict. This applies to the exploitation of any property, information, or opportunity. This duty does not apply where the situation cannot reasonably be regarded as likely to give rise to a conflict of interest, such as intra-group trading, as this will be known at the time of the transaction. Moreover, the duty does not apply if the matter has been approved by the directors. Where the power is held by managers, this significantly dilutes the duty because other directors[125] have the ability to authorise the conflict. Section 176 prohibits benefits being derived from a director acting or not acting to gain a benefit. Section 176 has a similar defence to 175 whereby the duty is not infringed if the acceptance of the benefit cannot reasonably be regarded as likely to give rise to a conflict. The same example of group transactions applies here: a director may benefit from a related company and this is unlikely to be regarded to infringe this duty. The substantive difference between 176 and 175 is that there can be no ratification by the board. Therefore, this duty is stricter on imposing a liability, encompassing tangible and intangible benefits. The Bribery Act 2010 now affects

[121] *Equitable Life Assurance Society v Bowley* [2003] EWHC 2263.
[122] *Dorchester Finance Co v Stebbing* [1977] 7 WLUK 144.
[123] Profit can be defined as reward for risk.
[124] Companies Act 2006.
[125] Provided the votes meets a quorum and the articles do not prohibit the authorisation.

this area of the law, creating a criminal offence, which further prevents the whitewashing approval from board members for infringing directors' duties. Section 177 refers to the duty to declare an interest in a proposed transaction. The declaration is to be made to the other directors[126] and must be made before the transaction. There are a number of exceptions as with the preceding duties, if the directors are already aware, or if the transaction relates to a service contract. The duty is however only to declare an interest in a transaction, and the board are free to permit the transaction provided there are no restrictions in the articles, or if in allowing the transaction, they would be in breach of the other duties. Therefore, this duty can be subject to whitewashing, where directors collectively approve breaches of duties or interests in proposed transactions.

The duties outlined are owed to the company and not to members of the company or individual stakeholders. This presents a problem of self-perpetuating power whereby the checks and duties imposed on directors can, often, be approved by other members of the board. The directors are to consider wider stakeholders given the enlightened shareholder value introduced in s 172; however, this has widely been criticised, with parallels being drawn to the emperor's new clothes.[127] Moreover, duties such as s 172 provide a defence to act more broadly. The courts have shown some willingness to restrict power in a group context. Pennycuick J, obiter, said that a director must not be guided by the interests of the group as a whole.[128] This provides additional guidance that practical considerations such as commercial benefit to the whole group or individual members[129] are not a valid defence for not discharging duties.

The enforcement of the duties is governed by s 178, which outlines common law principles such as damages, an account of profits and compensation. These require action being taken by the company or by virtue of a derivative claim. Given that the power and control is often vested with the managers and there is frequently a lack of shareholder engagement, the risks of breaching the duties are not outweighed by potential benefits. This, coupled with the low probability of

[126] Providing the company is not single director company, s 186 Companies Act 2006.
[127] Elaine Lynch, 'Section 172: A Ground-Breaking Reform of Director's Duties, or the Emperor's New Clothes?' (2012) 33 Company Law 196.
[128] *Charterbridge Corporation Ltd v Lloyds Bank Ltd* [1970] Ch 62.
[129] For example, the parent or sister company.

being caught, results in the duties becoming redundant for the purpose they purport to serve. Greater enforcement can be found under the Company Directors Disqualification Act 1986, where a breach of the duties can provide evidence of a director being unfit for office.[130] Often, this provision will only assist in a reactive manner, preventing directors who have breached duties historically from being able to breach them in the future. The protection afforded here is problematic for two principal reasons: it is predicated on insolvency proceeds, and the burden of proof is high. Courts have proven unwilling to disqualify directors for poor decisions, and as such commercial decisions[131] will not be brought into question, which further dilutes the protection afforded by the Act. Moreover, directors in breach can seek relief from the court if they ought fairly to be excused. Therefore, what appears prima facie as substantial directors' duties remain duties encompassing multiple defences and routes of avoidance of their liability, only further enhancing rather than restricting the power the directors wield.

In addition to the duties which impose limitations on managers' powers, following a report by the Cadbury Committee in 1992, a UK Corporate Governance Code was introduced. The Code focusses on issues of corporate governance and concerns ensuring that the governance environment is in line with rapid development. The Code states that companies do not exist in isolation and that to be sustainable businesses they need to underpin society and the economy.[132] The aim of the Code is therefore broader than the duties and provisions in the Companies Act, aiming to align corporate governance with society more generally following rapid developments. The latest version of the Code was published in 2018, and all references subsequently to the Code will refer to the 2018 iteration.

The Code does not set out a strict set of rules; its aim is to be flexible and to introduce principles. These principles are introduced on a 'comply-or-explain' basis and put the emphasis on the corporate board to use this flexible approach responsibly. The new Code is separated into five sections, each of which has its own subset of detailed provisions. Section 1 considers the board leadership and

[130] Company Directors Disqualification Act 1986, s 6.
[131] For example, see: *Re Stanford Services* [1987] 3 WLUK 304.
[132] Financial Reporting Council, *The UK Corporate Governance Code 2018* (Financial Reporting Council, 2018) 1.

the purpose of the company. It maintains that the success of the company should seek to be long-term, which will contribute to wider society. This section also requires directors to act with integrity and promote engagement from wider stakeholders. The focus of s 1 is in relation to monitoring and ensuring the decision-making process is aligned with good commercial codes of practice. Section 2 provides for a division of responsibilities and the inclusion of NEDs. In dividing the responsibilities, the power one manager can hold is also divided. Introducing a broader board to include external NEDs also permits a level of monitoring to prevent the whitewashing approval discussed in the preceding paragraphs. Section 3 requires that the board has a committee who should oversee the process for appointments. Moreover, it states that all directors should be required to have an annual re-election of their position. This annual re-election permits the company to terminate directors who seem to underperform by virtue of stakeholder voting. This links to the argument of Moore, who provides an analysis of the company as quasi-public: the theory in this respect is that underperforming or self-serving directors will be removed on their re-election. Section 4 introduces the requirement of an audit committee to monitor the integrity of the financial records. Section 5 requires a remuneration committee which externalises the setting of remuneration of directors to prevent the setting of their own or fellow directors' remuneration.

It can therefore be surmised that the Code includes significant provisions on monitoring and ensuring that significant power is not held by a single manager or within a concentrated group. Dividing up resources amongst managers is not only efficient in the Smithian sense, but it also proportions risks. The introduction of NEDs imposes additional levels of checks and balances to the board of directors to ensure compliance with broader consideration of stakeholders. The Code by comparison is therefore far more ambitious in its remit than the Companies Act. One reason for this which has been put forward is that codes which are applicable across jurisdictions are more easily agreed and applied, and the flexibility affords greater compliance.[133] Compliance with the Code is, however, optional in the sense that it operates on a comply-or-explain basis. The listing rules require a statement in the reporting of a public company on how the principles have been applied, or if not, then why.

[133] Tsagas (n 116).

The comply-or-explain concept is attractive due to its flexibility, as a rigid set of rules may be counterproductive for corporations. The comply-or-explain concept also permits a broader scope of considerations than would be workable under statutory and codified rules. The concept is problematic for several reasons, firstly as it is optional in compliance, which presents challenges. The optional nature is predicated on market forces: for example, a company not complying with the Code may be viewed in a negative commercial light which may result in less transactions with that company and fewer interested investors. An example of consumer consideration affecting a corporation's value can be seen in the VW emissions scandal, where share prices dropped by 30%.[134] The focus on market enforcement is misplaced, as it assumes that investors will be aware of how the Code is to be interpreted and that non-compliance will deter investment. Moreover, non-compliance would also have to be a significant factor for end consumers or transacting parties to deter them from trading with the corporation. The introduction of NEDs could fill this gap in ensuring compliance with the Code is adhered to and properly recorded. Research shows, however, that NEDs are disengaged and often intermingled with the corporations, as they sit on the board from which they purport to be independent.[135]

This is analogous to empirical research carried out by Arcot, Bruno and Faure-Grimaud, who analysed the functionality of comply or explain.[136] In analysing compliance since the Code's introduction, the paper noticed a tendency toward compliance; however, this was followed with poor language being used within explanations. It identifies that the concept of compliance in and of itself is troublesome. There are few guidelines, and the result is that a company who believes it complies with the Code, but who does not in reality, will provide a statement of compliance incorrectly. Arcot, Bruno and Faure-Grimaud here identify the problems of not only reported compliance, but that the compliance

[134] Benjamin Snyder and Stacy Jones, 'Volkswagen's Tanking Stock Price' (*Fortune*, 23 September 2016) <https://fortune.com/2015/09/23/volkswagen-stock-drop/#:~:text=German%20automaker%20Volkswagen%20has%20seen,%24110%20as%20of%20Wednesday%20afternoon.> accessed 27 August 2020.

[135] Prem Sikka and others, *Regulatory Architecture to Enhance Democracy and Business Accountability* (n 106).

[136] Sridhar Arcot, Valentina Bruno and Antoine Faure-Grimaud, 'Corporate Governance in the UK: Is the Comply or Explain Approach Working?' (2010) 30 International Review of Law and Economics 193.

that is recorded may be misleading. They make the claim that enforcement and monitoring is left to market participants, which as alluded too is also problematic. Keay supports this position, adding to the argument that shareholder engagement is lacking, which undermines the effectiveness of the principle.[137] Keay argues that this lack of shareholder engagement is a significant concern.[138] This concern is due to the monitoring role the shareholders are purported to assume. The concept is aimed at shareholders ensuring that the board has complied and provided adequate explanations for not complying; however, this is not the case. Moreover, Keay highlights that the statements which companies' issue for compliance or non-compliance are brief and uninformative, which creates difficulties in monitoring; the argument is supportive to Arcot, Bruno and Faure-Grimaud's.

The position is, therefore, one of unintended consequence and design, as the intracule duties which have been drafted and the Code lack the enforcement required to mitigate the risks. The result is that corporate power is held by the managers and in the absence of significant fraud or illegal activity, the collective power of management remains inadequately monitored for the power wielded. This section has analysed the provisions aimed at controlling corporate managers' behaviours and presented the argument that despite substantive detail the enforceability is lacking. Corporate power is permitted on the basis that it is subject to adequate controls, which legitimises this power. This section has presented that several controls appear to provide this legitimisation, but in reality, lack enforcement. This lack of enforcement is even more troubling in the group context due to the further dilution of voting rights.[139] The next section will consider proposals put forward by scholars in attempt to resolve the issues this section has highlighted. It will evaluate the proposals on reform of directors' duties and the Corporate Governance Code and test their applicability to corporate power.

3.6 Existing proposals for reform

[137] Andrew Keay, 'Comply or Explain in Corporate Governance Codes: In Need of Greater Regulatory Oversight?' (2014) 34 Legal Studies 279.
[138] ibid.
[139] See chapter 4.

This section will evaluate existing proposals to mitigate the risks of corporate power held in concentrated groups as outlined in the preceding sections. It considers the application of proposed amendments to duties alongside the Code. It then applies this in relation to corporate power, where it is narrowly held to establish the likelihood of success of these reforms. The section will proceed as follows: it will first look at the enforcement by an existing regulatory body as proposed by the Business, Energy and Industrial Strategy Committee (BEIS). It will then consider the reforming of company boards to establish if the introduction of a two-tier management board would derive greater accountability and monitoring. Finally, it will evaluate the proposal of a company's commission to enforce the duties outlined by the legislation and regulation.

The BEIS reviewed corporate governance in 2017 following a commitment by the government to improve the behaviour of 'big business'. As this chapter has argued, the power and subsequent behaviour is exercised by individualised corporate managers. This report preceded the 2018 UK Corporate Governance Code and 2020 UK SCs and some amendments have been adopted such as the proposal for greater reporting and transparency on compliance. This compliance and transparency, as argued in the preceding paragraphs, can create somewhat of a 'false positive' where it appears that companies are complying because they believe that they are, when in actuality, they are not. The level of enforcement was something considered by the committee, and they subsequently proposed reform in this area. In preparing this report, there were submissions by scholars, accountancy firms and representatives of big businesses including the Institute Of Directors. Whilst this level of engagement with a broad group provides an overarching picture, there is the risk following the empirical results by Arcot, Bruno and Faure-Grimaud,[140] that they may agree where they may not fully comprehend what they are agreeing too. Moreover, the businesses may agree that the current level works for them where it does not work for the larger proportions of society which the report aimed to replicate. Submissions are made by scholars of significance due to their purported independence and specialisms within the area.

[140] Arcot, Bruno and Faure-Grimaud (n 136).

Professor Andrew Keay provided written evidence[141] from which an argument in respect of proposals from the committee for reform was put forward. Keay highlighted two principal concerns with the landscape of corporate governance. First was the lack of definition of what ‘have regard to’ means in the context of s 172 and how this could result in directors not complying in this respect. Secondly, Keay posited that the enforcement for breach of these duties was lacking, arguing that the only parties who could enforce these duties were the board, who may be unwilling to do so for several reasons. Therefore, the second argument from Keay is more substantive because even if there was a clear definition of ‘have regard to’, the lack of enforcement would render it all but redundant. The priority, therefore, must be in the enforcement of these duties. Keay argues that the lack of a UK regulator weakens the corporate governance system when compared with other jurisdictions. Keay presents a compelling argument for external enforcement, arguing that it will not only enable enforcement for breaches but that the fear of enforcement for breach would deter directors in the first instance. This draws parallels to this chapter’s earlier analysis that lack of enforcement can act as encouragement for breach. Moreover, Keay claims that this would promote confidence for all companies, as both large and small companies would be required to comply, and this in general, would be in the public interest. The argument put forward is that the UK’s provisions were amongst the most highly regarded in the world, but its enforcement left them almost redundant. Keay is therefore advocating for an external regulator to enforce these duties. This viewpoint is countered by Professor Vanessa Knapp,[142] , who claims that further regulation would hinder board decisions and come at a substantial cost to the government. She also claims that this is unlikely to render different outcomes due to the clear and enforceable duties. This argument is not persuasive, as derivative claims by minority shareholders are inherently costly and difficult, and therefore enforcement for breach – whilst theoretically clear – is practically difficult. Professor David Kershaw supports the difficulty of enforceability argument claiming that the subjective duty makes it hard to enforce.[143]

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[141] Publications.parliament.uk., ‘Corporate governance: Government Response to the Committee’s Third Report of Session 2016–17 - Business, Energy and Industrial Strategy Committee’ (15 September 2017) <https://publications.parliament.uk/pa/cm201719/cmselect/cmbeis/338/33802.htm> accessed 11 November 2017, CGV0010.
[142] ibid CGV0031.
[143] ibid CGV0120.

The submissions to the committee evidence a significant problem with enforceability, both in regard to identifying the duty with s 172 and then even once identified to apply and enforcing this duty. The committee, in their report, therefore, recommended that formal legislation be introduced to give the FRC the additional powers it needs to engage and hold to account company directors in respect of the full range of their duties.[144] This power is twofold in its application, the first recommendation being that the FRC would be able to investigate and report publicly to the shareholders, which would remove the barriers to comprehension of complex legal issues. Secondly, the committee recommended legal action could be a route taken if the duties are not complied with.

This recommendation from the committee is persuasive and follows the submissions of scholars who submitted evidence to the committee. It aligns the problems identified by Keay of misalignment of duties and enforceability ensuring that directors comply with the duties which are in place and act as legitimators of the wielding of the power they hold. The government's response to the recommendation was disappointing. It claimed that the FRC was one of a number of bodies which could regulate the enforcement, and opposed the introduction of the legislation referred back to these institutions to identify the gaps. The government appeared to show interest in external enforcement but has yet to advance this position.

The argument for external enforcement is attractive, and there remain beneficial characteristics for its application. The argument that the government has made following this report does, however, raise legitimate concerns. There are a number of bodies, and selecting a single external regulator remains difficult. A recent Labour policy-making report criticises the independence of these external bodies, arguing that the framework for investigation is inadequate. Whilst the proposal by the committee for the FRC to regulate is a persuasive one to externalise enforcement, this level of externalisation is being brought into question. By way of example, the Labour report utilises empirical data to collate the members of these independent bodies. With the FRC board, the report argues that the board and its operations team are dominated by those with links to the

[144] ibid Recommendation 3.

big accountancy firms.[145] This level of domination and integration with the FRC presents questions to real independence. If the body responsible for enforcing a breach of duties has direct business links with the corporation itself or through its auditors, there will be little difference to the current position. This is the very suggestion Knapp made in her submission to the BEIS in 2017. The proposal therefore of utilising an existing body such as the FRC to monitor the UK Corporate Governance Code merely shifts the enforceability from one board to another, which is not persuasive. The introduction of a new independent body or public organisation may therefore render more independent results, but there remain challenges of comprising such a body with sufficient experience without the business links Sikka and others claim are problematic.[146]

One proposal which is discussed within the report by the BEIS and has been partially adopted within the UK Corporate Governance Code is the concept of market forces. Transparency and reporting are purported to have the effect of adjusting investor choices which in turn affect the value of a corporation. Stokes argues that the growth of the corporate enterprise has shattered the presumption that power is able to be legitimised by a competitive market.[147] This is due to the fact that separation of ownership and control have generated problems of short-termism and that corporate structures changed the way in which business is carried out.[148] This is supported by Jensen, who claims that with the shutdown of effective capital markets mechanisms for motivating change, there remains a reliance on internal control, which as this chapter has highlighted, remains inherently problematic.[149]

An additional proposal which has been widely debated is the formation and constitution of the board. It is well known that the UK operates a unitary board system whereby there is a single board appointed by the members. This separation of ownership and control which Berle and Means highlighted in 1932 has been one of the most debated concepts in company law for the last century. Ireland suggests that there might be a benefit in recoupling these two constructs

[145] Sikka and others, *Regulatory Architecture to Enhance Democracy and Business Accountability* (n 106).
[146] ibid 23.
[147] Stokes (n 20) 158.
[148] ibid 158.
[149] Jensen (n 89) 37.

and altering the conceptualisation of the firm.[150] One method of recoupling would be to have members on the board who have human capital invested. With capital investors on the board, the short-term wealth maximisation resulting in rentier shareholders may render different and more socially responsible board decisions. The concept of NEDs as independent directors entrusted to ensure the UK Corporate Governance Code was complied with, along with duties discharged, has not been a great realisation. By way of example, the three NEDs employed at Carillion, which infamously fell into liquidation, were paid £60,000 a year for working one or two days a month;[151] this level of remuneration for the small role NEDs play is not in isolation.[152] This suggests that the role of NEDs especially within large corporations is financially driven, as opposed to a monitoring role.

The role of NEDs is therefore questionable, given their remuneration and close connection with the executive board members. An alternative would be the introduction of a two-tier board, whereby a supervisory board operates to perform the monitoring in place of the shareholders. This supervisory board would be made up of stakeholders such as employees who provide human capital to the company. The benefit of such a system is that the workers will be invested in the company and may have a desire for the long-term survival of the company given they derive their income from it. Moreover, the employees as internal actors within the corporation will be aware of structural and technical elements, enabling them to better monitor the board. This type of structure is common in other jurisdictions such as Germany and France. Within England and Wales, s 172 Companies Act 2006 and the Corporate Governance Code aim to serve a similar purpose but as discussed are largely inadequate. The argument in favour of a supervisory tier is persuasive; however, it is not without its challenges. Firstly, since the inception of the modern company, the UK company has worked on the basis of a single-tier board and this is embedded into the 'constitutionalisation' of the company. Altering this structure would come with significant cost and restructuring to many companies. This intricate task would consume finance and time, which in the current economic climate, neither business nor government have. The make-up

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[150] Paddy Ireland, 'Defending the Rentier: Corporate Theory and the Reprivatisation of the Public Company' [2000] The Political Economy of the Company, Hart <https://ssrn.com/abstract=2068379> 1 accessed 3 April 2022.
[151] Prem Sikka and others, *A Better Future for Corporate Governance: Democratising Corporations for their Long-Term Success* (2018) 31.
[152] ibid 40.

of the supervisory board also presents challenges: taking the enlightened shareholder value criteria, the supervisory board would require a breadth of constitutions. It is also of importance that transplanting the concept from one jurisdiction to another is not a simple process.[153] Simply because a concept works in one jurisdiction does not necessarily result with success in another. An important factor in the corporation concept is the type of business that dominates the jurisdiction in which the board system operates. For example, two-tier boards are frequently seen in jurisdictions in which there is heavy manufacturing and production. Therefore, whilst the theoretical benefits may be easy to see, the practical application and introduction of a two-tier board system may prove practically problematic. A more persuasive argument would be in favour of compulsory inclusion of an employee representation on the unitary board.

The difficulties of regulators have already been discussed at length within this paper. One proposal put forward by Sikka's technical paper was the introduction of a Companies Commission.[154] This draws parallels to the recommendation from the BEIS, but with the significant difference that the enforcement would be the commission's, whose sole function is as a company law enforcer. Sikka opines that the level of organisations that are responsible for enforcing company law are in fragmentation and disarray. The report lists twelve bodies which have responsibilities, and many of these fall into the financial sector as opposed to specific company law. Overhauling the enforcement into a singular commission would remove the fragmentation and overlapping functions. The detail of the framework for such a commission was absent from the report; however, the argument for the urgent need of a regulator to promote good governance was persuasive. Companies are of variant sizes and the UK Corporate Governance Code only applies to larger corporations, and therefore by splitting companies up into subsidiaries, the voluntary code could be avoided. The introduction of an enforcer would be able to identify technical structures and advocate for enforcement. This argument for the introduction of a Companies Commission is therefore the most persuasive proposal. However, given the reluctance of the

[153] See: Pierre Legrand, 'The Impossibility of "Legal Transplants"' (1997) 4 Maastricht Journal of European and Comparative Law 111; Alan Watson, *Legal transplants and European Private Law*, vol 4 (Metro Maastricht 2000).
[154] Sikka and others, *Regulatory Architecture to Enhance Democracy and Business Accountability* (n 106) 42.

government to implement enforcing changes following the recent committee report, it is unlikely that this will come to fruition. Moreover, given that there are already many bodies which regulate elements of company law, there may be a reluctance to introduce additional bodies.

This section has analysed proposals from scholars on ways to control and enforce the duties in place to curtail managerial power. It has considered enforcement recommendations by a government committee, the reconstruction of corporate boards and the introduction of an independent Companies Commission. Ultimately, whilst benefits could be derived from all proposals, there remain barriers to the introduction into the corporate governance structure. The result of this is corporate power remaining held and utilised by managers in an unmonitored fashion, which challenges the legitimacy of the holding of corporate power. Without adequate controls and monitoring, this power is illegitimate and in need of reform or adjustment.

3.7 Summary

This chapter has provided a critique of the existence of corporate power within the modern corporation. It has provided a working definition of corporate power, identified the holders of corporate power, and evaluated the legitimisation of power through restrictions and monitoring. It has ultimately argued that the role of corporate power within a modern corporation is significant but lacks the requisite legitimisation. The role of the Companies Act 2006 is inadequate in controlling and monitoring the holders of powers, and despite the wide remit of the UK Corporate Governance Code, the lack of enforcement entrenches this power. This chapter has further argued that the inclusion of the institutional investor creates an additional dimension to the separation of ownership and control Berle and Means identified. This additional dimension only further exacerbates the already troublesome monitoring and further extends the remit of corporate power.

This analysis has provided a framework and understanding for the role of corporate power in the modern corporation more generally. The next chapter will evaluate how this corporate power operates in the context of a corporate group to ascertain if additional challenges arise, or, indeed if the creation of a group reduces the broad scope of corporate power. The significance of corporate power is not to be understated, and the increase in the trajectory of structured groups has the potential to further challenge the legitimacy of corporate power. Chapter four will critically evaluate the role of corporate power discussed in this chapter in the context of corporate groups to further address the research questions.

Chapter 4: The Effect Corporate Groups Have on Corporate Power

'Activities of Groups of Companies provide continuing fascination for the commercial lawyer. This fascination is due to the fact that there exists an obvious gap between commercial reality and regulation and this gap discloses a serious shortcoming of the law.'[1]

The preceding chapter identified the role of corporate power and how it applied in the context of corporate management. This chapter seeks to build on this in the context of corporate groups. It seeks to ascertain if the role of corporate power changes within a group and if so, how? To facilitate this analysis, it must first establish what factors and characteristics are unique to a group and how this could change the dynamics of corporate power vested in corporate managers. This chapter will therefore look at the concept of corporate groups and critically analyse what makes them unique when compared to a standalone company. The chapter will then proceed to consider how these characteristics and factors affect the role of corporate power, if at all, and the likely consequences.

Over recent years, there has been a demonstrable shift towards corporate structures and corporate groups. Chapter two analysed the historical evolution which resulted in the accidental extension of limited liability to corporate groups. Chapter three analysed the role of corporate power in the modern corporation following the diverging interests of owners and managers. This chapter will look to build on these preceding chapters to ascertain the importance of this extension of key features of company law toward corporate groups, and the effects of corporate power on these fundamental provisions.

The chapter proceeds as follows: it seeks to define the corporate group and ascertain what a corporate group is. It will achieve this by evaluating legislative definitions of the elements which, when combined, amount to a group. It will also consider wider definitions provided by scholars. The chapter, having outlined the definition of the corporate group, will investigate why corporate groups may be

[1] Frank Wooldridge and Marco F.H. Schmidt, *Groups of Companies* (Sweet & Maxwell 1991) ix.

constructed. Ascertaining the reasons for the construction of corporate groups will provide for an in-depth analysis of the challenges of these group structures. Following on from the definitions and reasons for corporate groups, the chapter will critically evaluate the challenges these corporate groups present. Within this analysis, the chapter will consider both direct and indirect challenges which arise from group structure and power exercised.

4.1 Defining the corporate group

There has been much debate as to what constitutes a group of companies. For example, does a 1% share in another company result in that company becoming part of the other company? The Companies Act 2006 has several provisions which include the term 'group' but none of these provisions provides a clear, uniform definition. This lack of definition could be argued to allow for a more flexible application depending on the circumstances in which group activity is carried out. Section 192[2] provides an exception for transactions with members or other group companies which might otherwise be prohibited or require approval from the members.

Under s 192,[3] if a transaction is between a holding company and its wholly-owned subsidiary, or from two wholly owned subsidiaries of the same holding company, the transaction which is substantial does not need approval from its members. This appears to suggest that groups are made up of wholly owned subsidiaries in a hierarchical structure with a focus on ownership. In accordance with s 208,[4] there is an exception for intra-group transactions relating to loans by a company. The language used in the exceptions to loans for approval by members differs from substantial property transaction approval. Section 208 provides that where a loan or quasi-loan to an associated body corporate or a credit transaction is entered into as creditor for the benefit of an associated body corporate, then no member approval is required. A 'group' in the context of s 208 is therefore not predicated on ownership but more association with other corporations, a broader conception of the corporate group. Section 399[5] includes specialist reporting

[2] Companies Act 2006.
[3] ibid.
[4] ibid.
[5] ibid.

requirements for groups and states that at the end of a financial year a parent company must prepare group accounts for the year unless the company is exempt. The focus on this provision is on reporting in line with Directive 2013/34/EU[6] to produce these accounts. The language here changes from 'holding company' to 'parent company', and this provision lacks a further definition. The focus is on ownership requirements in terms of percentile shareholders; however, this is applicable for exemptions to the reporting rule. Section 611[7] refers to groups in the context of relief from requirements as to share premiums. Group reconstruction relief is available for wholly owned subsidiaries or two wholly owned subsidiaries of the same group. The definition here is premised on the concept of outright ownership between companies and the relevant holding company. The construction of what constitutes a group is therefore not clear from the interpretation of the provisions outlined above. Part 38[8] provides an interpretation section which outlines definitions which elsewhere might have been absent. Section 1159[9] outlines the meaning of subsidiary. A company is a 'subsidiary' of another company, its 'holding company', if that other company holds a majority of the voting rights in it, or is a member of it, and has the right to appoint or remove a majority of its board of directors. The importance of the definition here lies in control with voting rights in reference to the board of directors. Section 1159 provides clarification on a wholly owned subsidiary: this is a company which has no members except those of that other holding company and that other's wholly owned subsidiaries or persons acting on behalf of that other or its wholly owned subsidiaries.

Section 1162 defines parent and subsidiary undertakings. Subsection 2 provides that an undertaking is a parent undertaking in relation to another undertaking, a subsidiary undertaking if it holds a majority of the voting rights in the undertaking, or it is a member of the undertaking and has the right to appoint or remove a majority of its board of directors. The focus here on parent and subsidiary undertakings is predicated on control, either in voting rights, control contracts or

[6] Directive 2013/34/EU of the European Parliament and of the Council of 26 June 2013 on the annual financial statements, consolidated financial statements and related reports of certain types of undertakings, amending Directive 2006/43/EC of the European Parliament and of the Council and repealing Council Directives 78/660/EEC and 83/349/EEC Text with EEA relevance.
[7] Companies Act 2006.
[8] ibid.
[9] ibid.

the company construction. The Companies Act[10] , therefore, provides provisions for transactions and undertakings between parent companies, holding companies and subsidiaries which are either wholly owned or owned with significant control rights. The Companies Act,, therefore, lacks a substantive and coherent definition of how these relationships, terms and transactions combine to create a 'group'. Witting for example, argues that the definition of a corporate group should not be based on rudimentary concepts of traditional ownership, and parent and subsidiary relationships.[11] He argues that groups should also be legislated and governed with respect to their networks as well as their hierarchical ownership relationships.

A more encompassing definition of the corporate group is found in Directive 2013/34/EU of the European Parliament and of the Council in art 2 – definitions. The directive defines a group as a parent undertaking and all its subsidiary undertakings. Affiliated undertakings are any two or more undertakings within a group, the parent and its subsidiaries. An associated undertaking means an undertaking in which another undertaking has a participating interest. This definition appears broader than the traditional group definition, including other undertakings in which a group of companies may have an interest. An undertaking is presumed to exercise a significant influence over another undertaking where it has 20% or more of the shareholders' or members' voting rights in that other undertaking. This caveat requires this significant influence to be linked to voting rights, which typically come with share ownership. Therefore, the associated undertaking, by this definition, is merely an extension to the corporate group for companies within the group which fall below the wholly or majority owned classification. This definition does not provide a broader definition to include a wider group of networks, which Witting advocates.[12] The statutory provisions are therefore vague and appear to differ on their application as to what can reasonably be regarded as a group. The contentious nature of a group of companies has resulted in much scholarly debate, which this chapter will critically evaluate.

[10] Companies Act 2006.
[11] Christian A Witting, *Liability of Corporate Groups and Networks* (1 edn, Cambridge University Press 2018).
[12] ibid.

Professor Blumberg, the leading scholar on corporate groups, defines a corporate group as, 'a business made up of commonly controlled corporations, often numbered in scores or hundreds that collectively conduct an enterprise under the control of a parent corporation'.[13]

Blumberg, therefore, asserts that the main feature of what constitutes a group is control, often by a common parent. This is analogous to some of the provisions seen in the Companies Act and the EU directive; however, the element of control is not limited to wholly-owned, partially owned, or 20% or more. It could be argued that to have substantial control, 26% of shares is needed to prevent a special resolution. In the context of the modern corporation with non-voting shares and founders shares amongst several other classes of share, control determined by a percentage of stock is unlikely to capture all those who exert control within a group to provide a suitable definition. Robé goes so far as to make a distinction between a firm and the corporation.[14] The corporation is the company itself, and the firm is made up of many corporations. Robé argues that the complexity has resulted in widespread confusion over this terminology amongst lawyers. The firm or enterprise is a wider network of corporations which make up the firm. Robé's definition is wider than that of Blumberg and the statutory provisions and is analogous to that of Witting to include a wider network. The firm is made up of other corporations, members and other stakeholders. The fundamental feature is that all are managed by a singular management board or organisation.

The difficulty in providing a singular and absolute definition of what a group fundamentally is remains inherently difficult, and this is reflected in the preceding analysis. All definitions analysed above include an element of control, and the extent to how wide-ranging this control can extend differs amongst scholars and contexts. This research will adopt the broader position based on control, but not limited to control exclusively through share ownership. The argument for wider conceptions and business relationships is persuasive by Witting and Robé; however, including corporations with the definition of groups where joint ventures may be in place introduces additional complexities where there is shared control.

[13] Phillip I Blumberg and others, *Blumberg on Corporate Groups* (Wolters Kluwer 2005) xi.
[14] Jean-Philippe Robé, 'The Legal Structure of the Firm' (2011) 1 Accounting, Economics, and Law 1, 21.

Therefore, the definition of a group utilised by this research is the following: a group is made up of several corporations whereby there is an element of shared control by a common entity.

This section has analysed differing definitions of corporate groups and established a working definition which will be utilised by this research moving forward. It has considered different positions from scholars and legislation to evaluate what a corporate group is within the modern corporation. The next section will evaluate why corporations and businesses structure themselves into groups.

4.2 Understanding the reasons for the use of corporate groups

This section will analyse potential reasons for organising an enterprise into groups: commercial, legal and practical. There exist many reasons, as this section will outline, why enterprises organise themselves into complex structures. Corporate structures are not necessarily nefarious, but the enterprise, as opposed to the corporation, is typically not held to the same standard, which presents challenges.

Judgment proofing is one reason why an enterprise may structure its business into the corporate group as defined in the preceding paragraphs. Judgment proofing is where a group is structured so that the group's main assets remain with the holding or parent company whilst the risks are undertaken by the subsidiary company, which is often undercapitalised. It has been argued that the ability to create subsidiaries 'at will' has the potential to create a dark side to incorporation.[15] An example of judgment proofing is the following: Company A is the holding company that initially finances the company, Company B owns the assets, and Company C carries out the business which may or may not be a business risk. Company C would rent assets from either company A or B, with profits flowing upwards but losses remaining where they are. This activity can become complex when jurisdictional veils are introduced in addition to veils of incorporation. Both of these add an element of protection to Company A. This

[15] Witting (n 11) 80.

type of structure can deny creditors access to assets which have been utilised to trade. *Chandler v Cape*[16] reinforced that parent companies may have a duty of care to employees or third parties of their subsidiaries; however, the threshold for enforcement remains high. There must be control, and the tortious test of *Caparo v Dickman*[17] must be used to establish this relationship. Companies within a corporate group could therefore introduce a number of companies to dilute this control and subsequently 'proof' their assets. The main feature, as elucidated above, within a corporate group or enterprise is that decision-making can be made downwards whilst profits move up the structure. The increased risk, when compared to a single corporation, is that the structure can be manipulated to the ends of the ultimate parent company.[18] This feature is unique to corporate groups due to the economic power and financial structures which can be utilised to structure the group to protect the assets.

Witting presents four reasons for the formation of corporate groups.[19] Firstly, the formation of a corporate group means that the parent company can determine the level of shareholding amongst each business. This has several benefits; the parent company can share the risk with other companies or other individual or institutional shareholders whilst maintaining control. This allows for both a reduction in risk and the ability to raise capital whilst maintaining control. Secondly, separate incorporation permits a better understanding of different businesses by external parties. The argument here is premised on separation of businesses to enable external parties to assess each part individually. This is beneficial for the purposes of creditors granting credit due to the credit being advanced to the specific business seeking capital. Thirdly, local regulation may require incorporation in the jurisdiction the company operates in, for example, banking. This forms a mandatory reason for creating a group to ensure relevant regulations are adhered too. Fourthly, it is easier to sell a business that is operating as a separate shell because it is more tax efficient to transfer shares of a company as opposed to assets.

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[16] *Chandler v Cape plc* [2012] EWCA Civ 525.
[17] *Caparo Industries plc v Dickman* [1990] 2 WLR 358.
[18] See: Witting (n 11) 169.
[19] ibid 48.

Considering each of these in turn, it is important to ascertain how these features are unique to the corporate group or if these reasons can extend to a single corporation. The first reason presented for the use of a corporate group is that separation has the effect of risk sharing in each area of business. In this example, the parent company can determine the appropriate risk they are willing to expose themselves to and offer the remainder of the shareholding to the market. In this scenario, there is a balance for the parent company, maintaining control and mitigating risks. This permits the parent company to share its risks with investors or other companies. A practical example of this can be seen with the company MKM Building Supplies Ltd (MKMBS).[20] In this case, MKMBS is the parent company with 71 subsidiaries.[21] Each of the subsidiaries represents a local business where there is a physical presence. MKMBS, as the parent, maintains control in each of these companies with >75% shareholding, but in each case a small amount of the risk and shareholding is held by external parties. This is a simple example of the risk-sharing capabilities of a corporate group whereby each branch of the business is a separate company controlled by the ultimate parent. In the MKMBS example, at each location, irrespective of ownership, the MKM brand is being held out as the company to external third parties. Whilst this arrangement is theoretically possible with an individual as opposed to a corporate group as 'the controller' and multiple companies, it is not practical given the number of shareholders and interests in the average parent company. By way of example, the parent company has multiple shareholders, and the parent company then has a majority share in the subsidiaries. Without the parent company as a vehicle to manage and control these subsidiaries, the structure would be difficult to replicate without a significant cost of contracting. Moreover, the ability of a parent company to hold out a brand with subsidiaries trading is something which cannot be replicated without a group structure. Therefore, the ability to risk share and allocate risks to different business areas and sectors is a unique feature of a corporate group.

The second reason offered for the functioning of groups relates to the idea of better understanding from external parties. The main advantage cited for this is

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[20] See The Business Desk, '£70m stake sold in builders' merchants' <https://www.thebusinessdesk.com/yorkshire/news/746625-70m-stake-sold-in-builders-merchants> in reference to the business model. Accessed 21 October 2020.
[21] Data sourced from Fame, <https://fame.bvdinfo.com/>.

that better understanding can be advantageous when seeking capital finance. The basic premise is that a lender may be more willing to provide capital when it is secured against the activity for which the finance is being used. This separation of trading activities allows for a more comprehensive understanding of the nature of the business to allow for capital injection decision-making. For example, consider a conglomerate seeking finance for a successful division of their business: if the other divisions of their businesses are not trading as successfully, then the overall financial picture of the firm could be diminished. This, however, may have the capacity to work in the opposite way in seeking to attract finance for a division which is trading poorly but where the remainder of the conglomerate is successful. In this regard, the ability of the parent company to create subsidiary companies at will puts the parent company in a more favourable position. In the same regard as the previous reason identified for creating groups, whilst this operation of incorporating companies per sector can be carried out by an individual shareholder and controller, this is practically unlikely. This is due to the parent company maintaining control whilst being owned[22] by a widely dispersed shareholding group at the parent company level.

The reason of local regulatory law requiring the incorporation of a company in the jurisdiction it operates in is uncontentious and is an example whereby a parent company may be required to incorporate a subsidiary without a choice. Whilst this may not be unique to corporate groups, the ability to be able to create multiple subsidiaries internationally controlled by one parent is uniquely advantageous to groups.

The fourth reason for forming groups is the ability to sell corporations as opposed to private property. This concept relates to the disposal of a company as opposed to the corporation as per the other reasons proposed. In this context, the sale of shares in a company is more tax efficient than the sale of property owned by a company. In addition to this, disposal of company assets by virtue of the sale of a company will be quicker and will reduce contracting costs. The company, in this regard, is treated as property due to the shares being saleable on the open market. This allows a parent company to maintain control but retain the ability to dispose of an underperforming or, indeed well-performing company with ease.

[22] Utilising the shareholder ownership conception of the company.

The separate nature of trading activities may also be attractive for investment funds seeking a long-term investment. The ability to clearly see the trading activities distinguished from the enterprise in which it sits makes for an easier sale. This ability to sell corporate shells promotes the very concept of short-termism whereby more generally, companies can be quickly disposed of if their market price is high or is falling. The feature is unique to corporate groups due to the control which can be maintained from the board of the parent company whilst maintaining the ability to dispose of a company quickly.

In addition, there remain further potential reasons for corporate groups. One key feature of corporate groups is the concept of dedicated management. In a large conglomerate or multi-faceted business, the duties placed on directors to exercise the duty of care, skill and diligence[23] may provide additional challenges. By way of example, if a larger enterprise is responsible for managing all operations, the objective knowledge requirement[24] becomes more difficult to satisfy. Experts in financial accounting may have very little to offer the production division, for example. The introduction of an enterprise with multiple subsidiaries for each division provides a framework for more expert management to oversee the subsidiary whilst remaining under the control of the parent company. The benefit of group structures permits the ultimate parent to exercise this control whilst the parent's shareholding can be diversified.

The purchase of an existing business is an additional reason for corporate groups. The merger and takeover market have already been considered in this research in the context of the market for control. In this context, a company can purchase the shares of an existing business to take control of that corporation. The parent company may decide to retain the operations of the purchased company, resulting in the company becoming part of the group.

In the context of market saturation, the ability for corporate groups to present different brands whilst, in essence, being an enterprise further extends the market strength. The UK food and grocery sector provide good illustrations, with Unilever being a prime example. Within the food and grocery market, Unilever occupies a

[23] Companies Act 2006 s 174.
[24] ibid.

significant market share in excess of 50% globally,[25] , whilst many consumers may be unaware that this is the case. This can be demonstrated through a number of their brands; for example, consumers looking for tea may consider PG Tips or Lipton as options and consider that they have a choice in their selection. Both brands, however, are operated by Unilever. Moreover, Unilever has extended to more luxury markets, such as the T2 brand for loose tea. This ability to maintain significant economies of scale whilst having the persona of multiple different companies is unique to the corporate group and highly attractive for the purposes of structuring and judgment proofing. This is a common feature of the food and grocery sector, with brands such as the Coca-Cola company offering Fanta, Oasis, Sprite, Lilt, Appetizer and even Smart Water, saturating the market. The ability to provide diversified brands through companies to present the persona of certain brands whilst control is often exercised by a parent corporation is a further unique feature of the modern enterprise.

This section has evaluated potential reasons for the creation and use of corporate groups. It has ascertained the key features of why enterprises structure their business into a corporate group. Additionally, this section has assessed why certain features are unique to the corporate group as opposed to the single corporation. The next section will analyse the features unique to the corporate group and ascertain if there are additional challenges which are present in a group corporation but not present in single corporation enterprises.

4.3 Challenges of corporate groups

This section will build on the preceding section, investigating if the unique features presented by a corporate group pose additional challenges. Robé argues that the corporate group is not held to the same standard as the corporation.[26] This section will proceed to critically engage with this position to establish the effects of the unique characteristics of the corporate group. The preceding section highlighted the reasons for corporate groups, and often these

[25] Statistica, ‘Unilever's grocery Market Share Worldwide from 2012 to 2020’ (*Statista Inc*, 22 January 2021) <https://www-statista-com.uoelibrary.idm.oclc.org/statistics/254613/unilevers-grocery-market-share-worldwide/> accessed 22 January 2021.
[26] Jean-Philippe Robé, ‘The Legal Structure of the Firm’ (2011) 1 Accounting, Economics, and Law 1, 21.

reasons resulted in unique features. The reduced cost of contracting for corporate groups gives them an advantage which is difficult to replicate without group structuring, given that the legislative framework is based upon the standalone company, the advantages gained by a corporate group combined with the fact that they are not held to the same standard results in these unique challenges. The previous chapter evaluated the role of corporate power in the modern corporation and set out how this is exercised and by whom. This section will now proceed to consider if the balance of corporate power shifts within corporate groups due to their unique features.

One of the challenges with corporate power is with its legitimisation. The separation of ownership and control vests power in the hands of a small number of individuals. The structuring of an enterprise into a group presents specific problems by diluting the power of other stakeholders and increasing the power of the parent company. Empirical analysis carried out by Nicodano confirms that by structuring in a pyramid system, each layer act as a multiplier for power and a dilution for shareholders.[27] Control is the centre of the legitimacy of corporate power,[28] , and generally those who have property rights exercise control over their property. Given the separation of ownership and control, this is not the case within the modern corporation. Therefore, legitimacy of control resulting in corporate power remains of significant importance. Shareholders relinquish control over some of their proprietary rights to be managed by a professional manager. However, shareholders retain certain rights which can be enforced to ensure managers are carrying out their role in accordance with shareholders' wishes. These rights create the basis of the legitimisation of the wielding of power in the form of corporate control. The challenge therefore is the effect on these control mechanisms in the context of the corporate group. This section will proceed to consider how control mechanisms are challenged within the context

[27] Giovanna Nicodano, 'Corporate Groups, Dual-Class Shares and the Value of Voting Rights' (1998) 22 Journal of Banking & Finance 1117.
[28] See: John E Parkinson, *Corporate Power and Responsibility: Issues in the Theory of Company Law* (Oxford University Press 1993) 23. John E Parkinson, *The Political Economy of the Company* (Hart Publishing 2000); John E Parkinson and G Kelly, 'The Conceptual Foundations of the Company: A Pluralist Approach' (1998) 2 Company, Financial and Insolvency Law Review 174; John Kay, 'The Stakeholder Corporation' in Gavin Kelly, Dominic Kelly and Andrew Gamble (eds), *Stakeholder Capitalism* (Palgrave Macmillan 1997)128; Adolf Berle and Gardiner Means, *Modern Corporation and Private Property* (Macmillan 1932) xxxix.

of a corporate group. Control mechanisms are closely linked to the accountability of corporate management, holding them to account and removing if necessary. This is the theoretical basis for the legitimisation; however, as the previous chapter illustrated, diverse membership has resulted in these rights becoming diluted. The argument put forward by this chapter is that the challenges identified in the preceding chapter become magnified and further exacerbated in the context of the corporate group. These challenges are not confined to shareholders but also extend to wider stakeholders. By way of example, Parkinson argues that the significant bargaining power held can influence governmental decisions.[29] It is well established that there is also the risk of managerial opportunism within the group context.[30] In this sense, parties such as creditors could be disadvantaged by strategic decisions being made for the enterprise as a whole, as opposed to for individual companies.

One consideration which challenges control mechanisms is that of agency relationships within the context of the group. Hopt argues that whilst groups remain the modern reality of the corporation, this entails significant agency problems.[31] In this scenario, there are three distinct problems which can arise: firstly, the conflict between managers and shareholders; secondly, the conflict amongst shareholders, especially where there is a division of controlling and minority shareholders; and thirdly, the conflicts between the group shareholders and other stakeholders. Whilst a corporation which is not within a group may also have conflicts between shareholders and stakeholders, it is submitted that this is more prominent in a group scenario. The two most common methods of group structuring are horizontal and vertical. With the typical horizontal group, there will often be a parent and then branches off of this. With a vertical group, each company represents a layer between itself and the ultimate parent (see Figure 4).

[29] Parkinson (n 28).
[30] See: Klaus J Hopt, *Groups of Companies. A Comparative Study on the Economics, Law and Regulation of Corporate Groups* (European Corporate Governance Institute, ECGI, Law Working Paper 286/2015, 2015); Paul Davies and Sarah Worthington, *Gower's Principles of Modern Company Law* (11th edn, Sweet & Maxwell 2021) 299.
[31] Hopt (n 30).

Figure 4 Vertical and Horizontal Group Structure Example

Given the group structures, there are more stakeholders involved, which as a result, can render more conflicts between these stakeholders and the members. Within continental Europe, parents hold enough share capital to maintain control. This differs from the position in the USA, where wholly-owned companies are more common.[32] The result of parents not wholly owning their subsidiaries within Europe is a broader sphere of shareholders which could give greater rise to conflicts. This is the direct result of strategic planning by the parent or the result of corporate management opportunism through the parent's board. In the horizontal structure outlined above, there is the potential for conflict between shareholders of the group and shareholders of the subsidiary. If the subsidiary is controlled by the parent, it can be utilised to meet the needs of the parent company as opposed to the subsidiary, which generates an imbalance of shareholder considerations. This is of significance due to the power held by the parent company. This power can be extended by virtue of using the subsidiary to its own potential detriment. Legitimising corporate power in this context is increasingly difficult. The shareholders of the subsidiary may have different wishes to that of the parent; however, as the parent maintains control, actions can be ratified and the interests of the minority shareholders cast aside. Given corporate power vests with management, there is the additional challenge of holding corporate managers to account in the group context, which is substantial. Conflicts are likely to be resolved in favour of the parent company due to the control[33] they maintain within the subsidiary. The question therefore to be addressed is, can legitimacy of corporate power be gained from the shareholders of the parent company? Given shareholders of the parent company are likely to

[32] ibid.
[33] >51% shareholding in the subsidiary.

be interested in the performance of their immediate investment, the parent company, the argument is not persuasive. Corporate managers could be on both the boards of the parent and the boards of the subsidiary, permitting further exercising of the parents' strategic planning. Corporate directors are also currently permitted to be directors of companies, and the parent company could therefore be a director of its subsidiaries.[34] The potential for conflicting interests and lack of accountability has been addressed, and corporate directors will shortly be prohibited.[35] This control exercised by the parent over subsidiaries within the group presents significant challenges to the expectation that corporate managers should be held to account for the power they themselves wield.

When discussing parent company control, it is important to ascertain what is meant by control by the parent. Blumberg contends that control by the parent is a rationale for enterprise treatment of the corporate group.[36] Control by the parent can be exercised in several ways, which will be considered in turn. Blumberg claims that whilst control can be considered broad; there are four primary categories which can be considered.[37] The most prevalent is the control to elect the majority of the board which Blumberg argues will be apparent in every parent–subsidiary relationship. It has been established that the board of the company, be it standalone or part of a wider group, maintains the power to run the company as they see fit.[38] It therefore follows that the ability to elect the board members of a company affords greater control to the parent organisations. If the board members of a subsidiary are to make decisions, and their appointment was at the behest of the parent, the will of the parent is more likely to be exercised. This challenges the concept of legitimisation of corporate power, due to the board of the subsidiary not being held to the same standard as other standalone companies. Breaches of protective mechanisms, such as directors' duties, can be ratified either by the board or by the parent company in their capacity as shareholders. The result is that the independent capacity of boards is diminished due to the close relationship to the parent company. This is due to the power wielded by the parent, the power here to appoint the majority of the board.

[34] See *Charterbridge Corporation Ltd v Lloyds Bank Ltd* [1970] Ch 62, 74 for a discussion on separate consideration within a group context.
[35] Small Business, Enterprise and Employment Act 2015, s 87.
[36] Blumberg and others (n 13) 6–7.
[37] ibid 11–23.
[38] Subject to restrictions in the companies constitution or in acts of illegality.

Secondly, there is the category of interweaving, whereby there may not be a diverse board or policies which are group specific. Within the categories, the challenge is primarily with decision-making policies: specific group policies on board decisions could be interwoven into the fabric of board decision-making across all subsidiaries. This presents difficulties, as it has the potential to affect the subsidiaries to their own detriment whilst serving the goal of their ultimate parent. Linked to this interweaving of policies, there may also be a similar construction of corporate boards. Whilst the same construction of boards across many group companies is not inherently nefarious, it raises concerns over the independent nature of board decisions. Directors are under a duty to exercise reasonable skill and independent judgment,[39] and discharging this independent judgment across a number of corporations challenges this control mechanism. Moreover, Blumberg argues that the intrusion of decision-making going beyond normal levels absorbs significant control from the subsidiary. This level of control would be most evident in day-to-day decision-making where the parent is involved on a more regular basis. All these categories of control relate to parent companies impeding on the management of the subsidiaries, notwithstanding their separate legal status. The challenge here is that the subsidiary company, through its human agents, may be inclined to make decisions to benefit the parent and not the subsidiary. In doing so, they are not subject to the same control mechanisms as other standalone companies. The diluted control mechanisms correlate directly to the argument Robé presents of enterprise groups not being held to the same standard.

In addition to the challenges of control mechanisms within the corporate group, other issues also exist. The preceding section focussed on the direct relationship between the parent and its subsidiary and the potential to generate inequalities. This section will now proceed to consider the indirect challenges which may present themselves within group structures. The importance of considering indirect challenges is due to the difficulties of ascertaining intention. Whilst companies may set out to structure companies within a group as part of a larger strategy, this may not always be the case. Companies may have been incorporated for a specific purpose. However, indirect outcomes such as parent company opportunism may result in deleterious consequences, notwithstanding

[39] Companies Act 2006 s 174.

the initial lack of managerial intention. This part will now consider managerial opportunism and the seeking of deviant goals, increased risk-taking and the diluting of shareholder and stakeholder interests.

These concepts of parent company opportunism and seeking of deviant goals could result in managers making decisions to benefit parties other than those they owe their fiduciary duties to. Given that the basis for profit can be defined as reward for risk,[40] there are greater incentives to utilise corporate groups and increased risks of opportunism. The basic premise is that faced with several opportunities; corporate managers may be inclined to make corporate decisions which bear the most risk because they also may render the most reward. In the context of a corporate group, both the risk and reward are magnified but they may be displaced. The decision to expose the subsidiary to greater risk may be subject to a different analysis than a standalone company, due to the disposability of the subsidiary company. This risk analysis could be altered in the group context for several reasons. Parkinson presents the argument that due to the separation of ownership and control, there is greater potential for management to seek deviant goals.[41] Extending this concept of separation of ownership and control, the managerial dynamic within a corporate group is somewhat different to that of a standalone company. Shareholders of the parent company are further separated from managerial input in the subsidiary. This disparity of ultimate ownership, the investors, from managerial decision making is increased in the corporate group context due to the introduction of corporate layers between companies in the group. The result of this is subsidiary companies being overseen by parent companies that can manipulate subsidiary companies to meet the needs of the ultimate parent. They can do this due to the mechanisms to prevent deleterious corporate behaviour being significantly diluted. This relates back to the argument of Robé with groups not being held to the same account. In the context of directors' duties, these are unlikely to be enforced to the ability of the parent company to ratify behaviours. Moreover, in the shareholders context, the ability for shareholders of parent company to exercise complaints for actions of the subsidiary is unavailable due to the very nature of separate legal entity.

[40] Frederick B Hawley, 'Final Objections to the Risk Theory of Profit: A Reply' (1901) 15 The Quarterly Journal of Economics, 603.
[41] Parkinson (n 28) 71.

The use of corporate groups within large multinational organisations is increasingly common, and most large organisations will have been structured in this way.[42] Iannaccone submits that due to the nature of groups of companies, they cannot be considered to operate as wholly independent and, as such are open to abuse;[43] this argument is supported by Dine.[44] The use of shareholder opportunism, parent company opportunism in the group context, is therefore argued to increase the risk of this abuse. Milton extends the argument on what may constitute opportunism, arguing that the reason for companies' defaults to their creditors can be broken down into two categories.[45] Ordinary business failure is the first identified by Milton; this is irrespective of structure and banal. The second reason is that of opportunistic behaviour, where shareholders are able to extract value from the company, ether deliberately or recklessly utilising the shield of limited liability. The concept of limited liability has been extensively analysed in earlier chapters, and the evolution of this shield of limited liability extending to groups magnifies some of the problems identified by Milton. The premise is that limited liability has facilitated shareholder opportunism which would have not existed without limited liability. The argument is, therefore, that limited liability has resulted in a culture of opportunism which is now evident with modern corporations. In the corporate group context, this issue is magnified: with each subsidiary there is another layer of limited liability protection, and the risks of opportunism increase. This view is supported by Ikuta, who claims that corporate groups have gained significant power with the global economy through their abuse of separate legal entity.[46] The specific abuse Ikuta references is that of judgment proofing by creating multiple companies within a group. This links to the idea of limited liability providing a platform for opportunism. Ikuta contends

[42] See Mariangela Iannaccone and Anna Rosa Adiutori, 'The Liability of Directors and the Abuse of Companies' in Hanne Birkmose, Mette Neville and Karsten Engsig Sørensen (eds), *Abuse of Companies* (Wolters Kluwer 2019). Janet Dine, 'The Abuse of Company Groups' in Hanne Birkmose, Mette Neville and Karsten Engsig Sørensen (eds), *Abuse of Companies* (Wolters Kluwer 2019). H Hansmann and R Kraakman, 'The Essential Role of Organizational Law' (2000) 110 Yale LJ 387. Data study in chapter 5.
[43] Iannaccone and Adiutori (n 42).
[44] Janet Dine, 'The Abuse of Company Groups' in Hanne Birkmose, Mette Neville and Karsten Engsig Sørensen (eds), *Abuse of Companies* (Wolters Kluwer 2019).
[45] David Milton, 'Piercing the Corporate Veil, Financial Responsibility, and the Limits of Limited Liability' (2006) 56 Emory LJ, 1340.
[46] Daisuke Ikuta, 'The Legal Measures against the Abuse of Separate Corporate Personality and Limited Liability by Corporate Groups: The Scope of Chandler v. Cape Plc and Thompson v. Renwick Group Plc' (2017) 6 UCLJLJ 60.

that bargaining power contributes towards opportunism and that where parties are at a disparity of either negotiation strength or lack of knowledge, this can render greater opportunism. This can present itself in several ways. In the context of the corporate group, the lack of knowledge could result in parties entering into an agreement with a subsidiary, believing it is the parent that they are contracting with. The increasing ability to operate through opaque transactions has the potential to undermine creditor positions,[47] which can encourage greater opportunism.

Opportunistic behaviour from groups is not the only indirect challenge which presents as a magnified challenge. Risk-taking is inherent within corporate management and stems from the risk-for-reward definition provided in the preceding paragraphs. The particular challenge with risk-taking in corporate groups is the disposability of subsidiaries which may alter the decision-making process or formula. The concept is that with higher risk comes higher reward, and in exposing the subsidiary to higher risk, the parent maintains the ability to remain legally separate but remain able to derivate profit. This is analogous to the judgment-proofing argument, whereby a parent company, having identified an opportunity which comes with risk, is able to shield the assets of the parent. This practice is within the remit of the current legislative framework: every single company is legally separate, and the parent cannot be liable for the debts of its subsidiaries.[48] This has led to scholars claiming that corporations maintain the ability to be 'schizophrenic',[49] whereby on the one hand, they are considered separate but on the other, they can maintain control and derive profits. In the context of the corporate group, this is further magnified, as parent companies can maximise corporate prospects with a mitigated risk but isolate their risks to subsidiary companies. This challenge is of particular concern for corporate groups as opposed to standalone companies due to the control and resources available to the parent which may not be evident in a single corporation. This

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[47] Reinier H Kraakman and others, *The Anatomy of Corporate Law: A Comparative and Functional Approach* (Oxford University Press 2017) 115.
[48] There is an exception in the rare case that a parent company maintains a duty of care for the employees of a subsidiary where a significant degree of control is maintained, as in *Chandler v Cape plc*.
[49] See: William T Allen, 'Our Schizophrenic Conception of the Business Corporation' in Lawrence Mitchell (ed) *Corporate Governance* (Taylor and Francis 2017); Paddy Ireland, 'Corporate Schizophrenia: The Institutional Origins of Corporate Social Irresponsibility' in Nina Boeger and Charlotte Villiers (eds), *Shaping the Corporate Landscape Towards Corporate Reform and Enterprise Diversity* (1 edn, Hart Publishing 2018).

mitigated risk to the parent has the potential to increase risk-taking and engage in short-termism. The continued facilitating of groups in this context provides a unique challenge and, as identified in the preceding paragraphs, does so without holding them to the same account as standalone corporations.

An additional challenge with the use of groups is the further dilution of both shareholder and stakeholder interests. Sharfman describes fiduciary duties as extensive,[50] and these duties are one of the key mechanisms for governing the power wielded by corporate management. The challenge remains with the enforcement of these duties. Sharfman contends that these duties only apply insofar as those who have a controlling interest are willing to exercise this mechanism.[51] In the context of corporate groups this presents further challenges, as parent companies with control are able to exercise this control to the benefit of the ultimate parent, not the class as a whole. This is especially concerning following data from Hopt, who identifies that in Europe,[52] subsidiaries within a group are more likely to be a majority shareholding, as opposed to wholly owned. The result is that minority shareholders of subsidiary companies will often have their interests subservient to those of the parent who maintains control. This reinforces the challenges outlined in the preceding sections, where the argument is made in respect of legitimising corporate power through control mechanisms. The control mechanisms are unable to function in the same capacity as in a standalone group due to the interests of the parent company in its shareholding. The interests of the parent will likely be considered the primary aim of the group of companies, and the result of this is diminished interest for shareholders of subsidiaries.

In addition, there is the challenge of shareholders of the parent company being unable to engage in activism for the decision making of the parent company. For example, shareholders A, B and C may be shareholders of company X, who in turn has a majority shareholding in companies Y and Z. Company X, in its capacity as shareholder of companies Y and Z, is able to exert control over these two subsidiaries; however, shareholders A, B and C’s ability to engage in activism

[50] Bernard S Sharfman, ‘The Risks and Rewards of Shareholder Voting’ [2020] SMU Law Review, Forthcoming, 869.
[51] ibid.
[52] Hopt (n 30).

in relation to the shareholding decisions made by X is severely diminished. This is the case for several reasons. Firstly, there may be a lack of transparency on the actions of X and its expanded transactions with subsidiaries. A, B and C's ability to engage in activism in this regard is limited due to their awareness of the transaction executed/conducted by the company in which they are members. A, B and C may be able to engage in activism towards X in a general sense by voting on the removal of directors, or pursuing a derivative action. This presents its own challenges: the parent company, X in this example, may be transacting with many subsidiaries, and the ability for shareholders to express concern over the relationship with a single subsidiary is inherently difficult. Therefore, the shield of limited liability and the separate legal nature of the subsidiary and parent relationship has the capacity to further reduce the ability of shareholders to vote or engage in activism.

Stakeholder interests is a further feature in which different consideration is provided for in the group context. The shareholder-centred approach to corporate governance has historically been the favoured conception of the company. The climate towards greater stakeholder interests has grown in recent years, cumulating in the enlightened shareholder value concept. Within this concept, directors can consider wider considerations from wider stakeholders than simply the shareholders' interests.[53] The corporate group inserts additional challenges in the application of considering these wider interests. A corollary of more complex group structures is a wider and more complex set of stakeholders. With the introduction of companies within a group applying group policies to corporate management, the insignificant consideration of stakeholders is further reduced. Individual stakeholders become an interest of a much larger organisation with various stakeholder interests within the group. The result is that stakeholders who may have a good claim to consideration from the subsidiary, as a standalone company, find their voices unheard. This challenge is further heightened where subsidiaries carry out high-risk activities.[54] Given that activism through the stakeholder is already fairly limited due to the conception of the company, this further dilution in the group context is concerning.

[53] A full analysis on this enlightened shareholder value is beyond the scope of this chapter.
[54] Such as in *Adams v Cape Industries plc* & *Chandler v Cape plc*.

This chapter has defined the corporate group, ascertained the reasons for the construction of the corporate group and evaluated the challenges corporate groups pose given the power that corporations wield. It has been argued that not only are the challenges magnified in the corporate group, but that distinct challenges unique to the group also exist. The next chapter will proceed to provide some empirical data and practical analysis as to how corporate groups are structured. This will be achieved through the use of case studies and data on companies from the register from Companies House. Following this chapter, the question of greater legitimacy will be addressed. It will seek to pose the following question: if corporate corporations wield significant power, which is magnified in the group context, can greater legitimacy be derived from alternative conceptions and constructions of the company?

Chapter 5: Mapping the Corporate Group

'Legal concepts are continuously open to empirical data [and they] serve as a bridge between facts and norms.'[1]

The preceding chapter, chapter four, emphasised the unique problems and challenges with corporate power in the context of the corporate group. It discovered that the problem of separation of ownership and control are magnified in this specific context. Furthermore, it revealed that groups are not held to the same standard as standalone corporations and as such the holding of power is illegitimate. The previous chapter argued that the corporate groups are not legitimate for three reasons. Firstly, control is fundamental to corporate power and given the dilution of shareholders and their respective relinquishment of property rights, control mechanisms on corporate power lack substance. Secondly, the boards of subsidiary companies are not held to the same standards and as a result, breaches of fiduciary duties are inherently difficult to enforce. Thirdly, in the use of subsidiaries to serve the means of the ultimate parent the company defies the 'spirit' of the privilege of incorporation where the reality is a single economic unit. These findings built on the analysis in chapter three which highlighted that the separation of ownership and control resulted in shareholders being further diluted from their shareholding, and corporate power growing as a result of this. Therefore, in the group context, there is growth as a result of the further separation. Chapters three and four have therefore presented the argument that there remain inadequate controls on corporate managers by virtue of corporate ownership. This correlates closely to the historical analysis, chapter two, which demonstrated that the use of the corporate form into corporate groups was an evolutionary practice, which might be dubbed an 'accidental extension'. The cumulative effect of this is that corporate groups are a creature of this evolution without their own legislative framework or footing, thus undermining their legitimacy. Corporate groups present their own unique challenges with respect to corporate power which lacks legitimacy due to this accidental extension of corporate law to groups.

[1] Simon Deakin, Juridical Ontology: The Evolution of Legal Form' (2015) 40 Historical Social Research/Historische Sozialforschung 170, 174.

This chapter builds on the preceding analysis to demonstrate the result of this extension into the modern corporation, which is argued to be without legitimacy. It will proceed to establish that the problems following the divergence of ownership and control are not abstract ideals but exist on a practical level. This, in turn, will allow chapter six to provide recommendations and parameters for how greater legitimacy can be derived. This chapter seeks to progress the research in two principal ways. The first is that it will demonstrate that the theory of the extensive nature of corporate groups is a common theme throughout large companies and is present in all large enterprises. This chapter proceeds to evaluate data held on corporations to ascertain structures and how this presents itself in the largest companies. This consideration of the larger companies is fundamental given the argument presented that power is illegitimate following the further separation of ownership and control. The first part of this chapter, therefore, considers the types of structures which can be evidenced by empirical data. This analysis provides support for the argument that corporate groups operate on a wholesale level amongst the largest companies, resulting in vast power being utilised without the correlative accountability to legitimise it. The second way in which this chapter progresses the research is in respect of identifying the owners of larger corporations. The importance of accountability has already been discussed at length in this thesis, and accountability can be achieved through shareholders exercising their voting rights. This chapter identifies that in the largest companies, the shareholding is significantly 'diffused'. Therefore, what can be concluded is that the role of shareholders becomes less important, and even more so in the group context where the dilution permeates through each subsidiary. This dilution, coupled with group structures and the increasing use of institutional shareholders, has resulted in a significant departure from the original premise of capital providers to corporations. This finding undermines the traditional Friedman doctrine[2] whereby the shareholders are the sole beneficiaries to the firm's responsibilities. Identifying shareholders within these corporate structures is inherently difficult, and once they are identified the shareholding holds a trivial degree of influence. This further challenges the ability for the rights holders to be heard by management, resulting in disengagement

[2] Milton Friedman, 'The Social Responsibility of Business Is to Increase Its Profits' in *Corporate Ethics and Corporate Governance* (Springer 2007).

and the use of exit over voice. This in turn reduces the ability for members to hold corporate managers to account. For subsidiaries, holding corporate managers to account for their actions in respect of a specific subsidiary is likewise inherently difficult. This entrenches the power of the corporate managers within the subsidiaries and results in more opaque practices between group companies. Therefore, the amalgamation of large numbers of companies within a corporate group and difficulties in identifying shareholders to become more active exacerbate the existing problems of corporate power in the group context. Identifying the 'owners' or residual rights owners provides support for alternative considerations of the corporation.

This analysis will contribute to the thesis by addressing the question of company law providing an advantage to those operating within a group. This concept of facilitating an advantage is problematic for a number of reasons; firstly, the inability for adequate controls to be in place presents a challenge where corporate power is in the hands of a small number of corporate managers. The result of this is corporate groups not being held to the same standard and control mechanisms not functioning as intended. Secondly, where company law facilitates such a corporate advantage through the structuring of companies into a group, this problem self-perpetuates and becomes embedded into corporate culture.[3] Moreover, this chapter concludes that where challenges of corporate groups exist, they are disproportionately favoured towards larger companies and the use of corporate groups facilitates growth. In this sense, as the size of the corporation and enterprise grows, so too does the use of the corporate group, which further exacerbates the problems identified in the earlier chapters.

This chapter, therefore, first looks at the economic reality of the corporate group and then moves to how these groups are 'held' to enable the subsequent chapter to make recommendations for reform. The widely dispersed shareholding of large corporate groups provides a persuasive justification for a shift from the shareholder primacy model, which has been the dominant conception of the corporation for the past century. This chapter will, therefore, provide the framework for an alternative method of corporate groups attaining legitimacy. It

[3] Anna Donovan, *Reconceptualising Corporate Compliance: Responsibility, Freedom and the Law* (Bloomsbury Publishing 2021).

will achieve this by utilising publicly available data and analysing this through empirical methods and statistical analysis to gain an understanding of corporate structures and their ownership. This critical analysis will provide chapter six with a conceptual framework to put forward the parameters for a reconceptualisation of the corporate group and how the ownership of a large enterprise may be perceived.

Structure of the chapter

This chapter will proceed as follows: section 5.1 will outline and explain the methods and selection and collecting of data which have been utilised to generate charts. The patterns demonstrated in these charts highlight two principal paradigms. The first is that the use of the corporate group is more common in larger corporations, and the use of subsidiaries supports financial growth. Secondly, these charts demonstrate that the shareholding of the parent corporation is dispersed very widely and often is held by intermediaries.[4] The subsequent analysis of these charts supports the argument that groups lack legitimacy by virtue of both their widely held shareholding and the ability to control subsidiaries without correlative control mechanisms. Moreover, the data identifies that the use of groups further perpetuates financial strength, which increases corporate power; this research argues that this power requires legitimacy for its continued use. The selection of this sample data is significant because it frames the basis for the conclusions of the chapter. The data used is sourced from Companies House and Fame to produce the charts which support the arguments of the research. The data collected is primarily on the structural architecture of companies within the data sets and the respective owners of companies within the data sets. The conclusions of the chapter identify the commonality of extensive use of corporate groups the larger the corporation, coupled with increased dispersed ownership in the ultimate parent company.

Section 5.2 proceeds to evaluate the data on a more quantitative basis to establish broad patterns amongst some of the largest companies operating within England and Wales. The patterns which have been identified display a commonality of the use of the corporate group amongst large corporations, which

[4] Such as pension funds, hedge funds and institutional investors more generally.

appears to grow and draw parallels with the turnover of each group. Moreover, a clear pattern emerged demonstrating that the use of companies was significantly more prevalent in public companies. This suggests that private limited companies are more likely to form part of a corporate group that be parent controller of one. Additionally, the use of subsidiaries within large public groups is overwhelming, and this has a direct result on the growth of corporate power. Therefore, the main discernible pattern within this analysis is the link between group size, use and financial strength. This provides an overarching view of how organisations appear to structure themselves and the respective correlations which follow as a result. This is supported by the similarities identified across the 200 companies within the data set.

Section 5.3 proceeds to evaluate case studies to provide a more in-depth analysis. The pattern of similarities demonstrated from the initial qualitative analysis provides a level of confidence that any subsequent patterns identified across the 10 case studies will provide an accurate representation of corporate groups. The purpose of the studies of 10 companies is, therefore, to enable the research to ascertain patterns of structures and ownership through large corporations. This is achieved by providing further analysis of the 10 companies with the highest value[5] within the UK. This qualitative research provides deeper analysis and explanations for the patterns identified in the preceding analysis. The chapter does this by examining structures and patterns within specific companies and comparing these to ascertain further patterns within the larger context. This part then proceeds to consider the ownership of subsidiary companies to ascertain where control of the subsidiary exists. It was discovered that parent companies maintained control[6] of subsidiaries and in the majority of cases the subsidiaries were wholly owned. This demonstrates the level of control parent corporations have over their subsidiaries and the role of subsidiaries and their ownership structures. This advances the understanding of corporate groups and how subsidiary companies are controlled. The chapter then proceeds to consider the shareholding of the parent company to ascertain who maintains voting rights. The possession of voting rights is important because it allows for

[5] Statista, 'Brand Finance. Most Valuable Brands in the United Kingdom (UK) as of May 2020' (*Statista Inc*, 2020) <https://www-statista-com.uoelibrary.idm.oclc.org/statistics/292024/most-valuable-brands-in-the-united-kingdom/> accessed 22 February 2021.
[6] Over 50% of shareholding.

activism and allows shareholders to use their votes to engage in this. The use and exercising of votes act as a control mechanism on corporate power; therefore, activism has an important role to play in corporate governance. Widley dispersed or unengaged shareholders can further entrench the position of corporate managers and the power they wield. This chapter contributes to the overarching aim of the thesis as it supports the challenge to the legitimacy of corporate groups, through their ownership. This challenge presents itself with diluted control mechanisms as power is collated through the use of subsidiaries and utilised by the parent companies. This research argues that this collective use of networks of companies is illegitimate due to the inability to hold corporate managers to account for their action in board decisions of the subsidiary. The patterns identified in this chapter support this challenge due to both the correlation between use of subsidiaries and financial growth coupled with the widespread wholly or majority-owned subsidiaries.

Section 5.5 of this chapter sets the foundation for a wider conception of the corporation and provides justification for a move toward stakeholder theorisation due to the diffused shareholding of larger companies. It provides a framework for a departure from the shareholder-centred approach given the widely dispersed nature of the shareholders and the challenge of legitimising these large groups. This departure from the traditional approach allows the proceeding chapter to consider alternative frameworks which can be utilised to derive greater legitimacy. The concept of the legitimacy of the corporation is one shrouded in debate about its definition and relevance. The strand of legitimacy of interest for the purposes of this study is that of the legitimacy of corporate power. In order to maintain possession of this power, it must be legitimised. In chapter three, this research investigated the historical origins of corporate power and the traditional methods of legitimatisation. Legitimisation is the rightful possession of power; the rightful possession is achieved by accountability from those who wield this power. Accountability can be achieved via control mechanisms through shareholder engagement and legislative restrictions. Donovan maintains that legitimacy-based compliance is fundamentally based upon a psychological model of understanding compliance decisions.[7] In this sense, social norms appear where citizens believe the relevant party has the authority and that it is being exercised

[7] Donovan (n 3) 74.

fairly. Donovan argues this is self-perpetuating and dubs this the ‘compliance degeneration cycle’ where initial drivers of creative compliance undermine the legitimacy which once existed. Therefore, this concept of legitimacy is of fundamental importance due this being a requirement for wielding significant power. Legitimacy is derived from the ability to hold those with power to account and is required for the rightful possession of power.[8] Moreover, some scholars have argued that the public interest is to be the foundation of the legitimacy of companies.[9] This is required in the corporate context, as public interest is the justification: fair exercise of power is permitted because it is facilitated by the statute, which in turn has control mechanisms. These control mechanisms give society confidence that these companies are justified in wielding power.[10] Therefore, control can be argued to be the centre of the legitimacy of corporate power because it justifies the holding and exercising of such power. This chapter contributes to the research because it deconstructs the concept of legitimacy in a corporate group when coupled with widely dispersed shareholders. It provides empirical support that legitimacy within the large corporate group is currently absent and that corporate groups are operating without the requisite legitimacy. Chapter six will then proceed to make recommendations for how legitimacy can be achieved given the corporate group structure and the widely dispersed shareholding.

Purpose of the data study

This thesis has thus far evaluated the lack of legal footing for limited liability in the context of the corporate group. Indeed, Lipton argues that the extension of limited liability was not what was intended and that real issues of social and economic importance arise.[11] Chapter four also presented the argument that corporate power in the context of the corporate group is magnified due to its structure and the advantages which follow. The corporate group has been described as a ‘shape-shifter’, and its structural architecture makes the group an

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[8] Adolf A Berle, *Power without Property: A New Development in American Political Economy*, vol 56 (Harcourt, Brace & World Inc 1959) 99.
[9] John E Parkinson, *Corporate Power and Responsibility: Issues in the Theory of Company Law* (Oxford University Press 1993) 23.
[10] Donovan (n 3).
[11] Phillip Lipton, ‘The Mythology of Salomon's Case and the Law Dealing with the Tort Liabilities of Corporate Groups: An Historical Perspective’ (2014) 40 Monash University Law Review 452.

engine for injustice and fraud.[12] This chapter will seek to ascertain the economic reality, and the ubiquitous nature of corporate groups. It is from this that we can confirm what may be expected is the reality. In this respect, the expectation is that large corporations will form corporate groups; however, this data study seeks to ascertain if this is the reality of what the current market is displaying. This chapter will first seek to position the economic reality of the group and its position within the market. It will then proceed to consider the ultimate beneficial ownership of the parent companies.

This positioning of the market is significant due to its association with the theory of the firm. Jensen and Meckling argue that the theory of the firm and the theory of markets are closely aligned.[13] In discussing this, they claim that there are actors who have important roles to play within this theory. In the group context, the relationships between these actors present additional challenges. Directors of a parent company may have differing interests than the subsidiary, and this tension could increase agency costs. Jensen and Meckling contend that the firm is a 'black box' where outputs are calculated with requisite inputs. The argument is that most organisations are simply legal fictions that serve as a nexus for a complex set of contacts amongst individuals. In the group context, these contracts and relationships become more intertwined with individuals having interests across a number of companies within a given group. The data this chapter presents is that this complexity within the group context is more the 'norm' as opposed to the exception to the rule it historically may have been. Clark expands upon this, affirming that corporate management is often prone to conflict with shareholders. Due to this conflict, the increased need for monitoring becomes more important.[14] This requirement for increased monitoring where interests differ becomes increasingly problematic in the group context. The shareholders who wish to actively monitor their investment within a group must attempt to navigate the structure of the organisation, which is likely to increase the cost of monitoring.

[12] Jay Lawrence Westbrook, 'Transparency in Corporate Groups' (2018) 13 Brook J Corp Fin & Com L 33.
[13] Michael C Jensen and William H Meckling, 'Theory of the Firm: Managerial Behavior, Agency Costs and Ownership Structure' (1976) 3 Journal of Financial Economics 305.
[14] Gordon Clark and Michael Viehs, 'Corporate Social Responsibility: The Case for Active Ownership by Institutional Investors' in Dominic Barton, Dezsö Horváth and Matthias Kipping (eds), *Re-imagining Capitalism* (Oxford University Press 2016).

There is increasing relevance as to the size of the organisation and its structure. Data collected in 2002 from Blumberg[15] identifies that the average number of subsidiaries was 187.[16] The data collected in this research suggests this has doubled and the use of the corporate group is becoming more dispersed than before. Therefore, whilst there might be an expectation as to the formation of groups, the use of these groups and the sheer number of subsidiaries is increasing. With this increase comes increased corporate power. Blumberg extended the argument in 2002 that this increase has made corporation law vulnerable due to the different society in which the initial rules were formed in.[17] Hansmann and Kraakman argue that organisational law plays a crucial role in permitting the formation of a separate pool of assets and the subsequent importance of the ability to partition assets.[18] The importance here is that creditors can have confidence in a pool of assets for debt. For example, a finance company loaning business funds to start a car rental company will have the confidence that the assets will be held and used by the subsidiary. In the event of insolvency, the values of the cars will be protected from other creditors. Whilst this provides a level of justification for organisational structuring, this could be achieved through divisions within a company and contract law for securing a charge. The law is therefore providing a facilitative framework for organisations to partition and structure assets to reduce costs of contracting.

Therefore, this chapter and its data study serve two principal purposes. First, it establishes that the reality of corporate groups is ubiquitous in large enterprises. Moreover, the use of these corporate groups results in a significant, not trivial, number of subsidiaries. This develops the argument presented in chapter four. Secondly, this chapter seeks to identify the ultimate beneficial owners of these large corporate groups. In ascertaining ownership, will provide a framework to consider further conceptions of the corporation in chapter six. The current chapter seeks to determine if groups are minority, majority or wholly owned by the subsidiary to establish levels of control. It also seeks to establish if the parent

[15] On 200 largest corporations in the United States.
[16] Phillip I Blumberg and others, *Blumberg on Corporate Groups* (Wolters Kluwer 2005) 1–14.
[17] ibid.
[18] Henry Hansmann and Reinier Kraakman, ‘Organizational Law as Asset Partitioning’ (2000) 44 European Economic Review 807.

company has controlling shareholders and who the ultimate controllers of the parent company are.

Aligning the Data Study

This chapter explores statistics of the modern corporate groups and makes use of empirical date to support the argument of the thesis. The central argument is that the growth and development of the corporate group has led to a dilution of controls available to constrain corporate power. This in turn reduces the legitimacy of such power. The data study in this regard provides the foundation to consider how else legitimacy might be achieved and potential patterns and reasons for group structuring.

The use of data allows the thesis to plot the landscape of the modern corporate group and compare this against theories of the corporation. In this regard, the data study allows the thesis to deconstruct what the corporation is, so that it may be reconstructed in the form of proposals advanced by the thesis. The deconstruction comes in the form of challenging the notion of shareholder primacy. One of the fundamental tenants on which shareholder primacy is the 'shareholders money' argument and this justifies the conception of them being deemed 'owners' of the corporation. The empirical study demonstrates that in the modern corporate group, identifying shareholders money is inherently difficult. Moreover, scholars such as Watson and Ireland contend that corporations have evolved from partnerships and historical features are predicated on shareholders wishing to play a role within the corporation. The dispersed shareholding and increasing use of institutional shareholders is at odds with the notion that shareholders exercise any real control or hold any power. From this position of deconstruction, the thesis is therefore free to explore, if the notion that the corporation is to be run for the shareholders is flawed, what alternatives are there. These alternatives is the reconstruction, through reconceptualising, the thesis explores within its proposals.

5.1 Methods of data collection

The volume of data available from Companies House annual statistical release is substantial. This data which is available, covers a wide spectrum of data from ownership, management and financial data. This chapter will focus on analysing both quantitative and qualitative data. The data in the subsequent analysis is predicated on is that of ownership and financial data. The reason for obtaining and analysing these types of data is that they provide a framework to comprehend how companies structure their business organisations and, furthermore, these may be related. This data collection and analysis is essential to testing the hypothesis of links between corporate groups, growth and the use of subsidiary companies. The quantitative data analysis consists of a data set sourced from the 100 largest private and public companies, '*dataset1*'. This will allow for comparison between the public and private structures as a comparative size. Moreover, it provides for a definitive list and subsequent analysis of a defined data set. It will collect data to give an overall picture of companies, and this will prove a lens from which to analyse a subset of data. Following on from this, the chapter will proceed to provide in-depth qualitative analysis with the case studies of 10 companies which are deemed to be the most valuable, the '*dataset2*'. The analysis of this data will support the theory that corporate groups are used more frequently in larger organisations where power and control are already widely dispersed, thus further exacerbating the challenges of corporate power.

This research has evaluated the power within large companies and the unique features which provide the capacity to further extend this power. As outlined in chapter three, corporate power is the ability held by corporations to wield their will on wider societal stakeholders. Moreover, this research has identified that often this power is held by a finite number of corporate managers. Chapter four considered how this power manifested in the group context, establishing that corporate power in the group context presents both additional challenges due to its unique features and the magnification of existing challenges within corporate law. This relates directly to the data evaluated in this chapter, considering both the financial strength of corporations and also evaluating how embedded the use of group companies has become in the modern corporation.

Therefore, this chapter will focus on the analysis of larger companies, as this is where both financial and socio-political power is most likely to be possessed and wielded. This chapter will divide the analysis into both public and private companies to determine differences, if any, between the structures of ownership and the correlative group relationships.

As analysed in the preceding chapters, public companies are seeing exponential growth in shares held by institutional investors, institutionalisation. When combined with hierarchical group structures, additional challenges of the legitimacy of corporate power appear. Corporate power is exercised by managers at varying levels of the hierarchical group structure; however, where companies are wholly owned, shareholder activism for the non-parent companies becomes diluted. The public companies which have been selected to form the data set are the FTSE 100 companies as of the 10 of February 2021.[19] The data set for private companies has been compiled from the Top Track 100 league table 2020.[20] These two data sets (*dataset1)* will be utilised to demonstrate patterns and structures within both private and public companies to ascertain if there are significant differences in relation to their structuring. Following an analysis of the largest 100 private and public companies to identify patterns and trends, the chapter will proceed to case studies for a more in-depth analysis of company structures. This analysis will be derived from companies listed in the 'most valuable brands in the UK as identified by Statista.[21] This will provide a more detailed, qualitative analysis of companies and allow for a greater understanding of the way in which large corporations are structured. In ascertaining ways in which large valuable companies structure their business, will provide a framework for potential reform and legitimisation of power utilised within the corporate group context.

The study in this chapter will be data refined for two purposes as outlined above. The aim of the chapter is to ascertain and provide evidence to the widespread

[19] London Stock Exchange, 'FTSE 100' <https://www.londonstockexchange.com/indices/ftse-100/constituents/table> accessed 10th February 2021.
[20] The Sunday Times, 'Top Track 100 league table' (*The Sunday Times*, 2021) <https://www.fasttrack.co.uk/league-tables/top-track-100/league-table/> accessed 10 February 2021.
[21] Statista, 'Brand Finance. Most Valuable Brands in The United Kingdom (UK) as of May 2020' (*Statista Inc*, 2020) <https://www-statista-com.uoelibrary.idm.oclc.org/statistics/292024/most-valuable-brands-in-the-united-kingdom/> accessed 22 February 2021.

use of corporate groups in large organisations. Additionally, the research from this chapter will provide an understanding as to the ultimate beneficial owners of shares within the parent companies. This serves two purposes, the first providing the support for the overall thesis that corporate groups are an economic reality and increasing in their use. Secondly, the study seeks to understand and ascertain the ownership structures of companies within the group.

5.1.1 Methodological approach

The methodological approach for collecting the quantitative data (*dataset1*) involved obtaining data from Companies House and mining for particular fields. Data was collected on public companies from the FTSE 100 and the 100 largest private companies. The data sourced was the following: whether the company had subsidiaries, how many companies were in the group, how many companies were in the subsidiaries and over how many levels. In addition to this, data was collected on the turnover of the company. The same data was collected for private companies, but an additional field of data was collected for private companies, that of ownership and the percentage of ownership. This data was then put into SPSS and Microsoft Excel to produce graphs to identify patterns.[22] The approach to the qualitative analysis involved selecting 10 companies deemed to be the most valuable in the UK and mining specific data. The data collected for each of the qualitative data involved collecting data on the following fields: ownership structure, subsidiary ownership by country, subsidiary shareholding, shareholding of the ultimate parent and data on the architecture of each company.

5.2 Statistical data analysis

5.2.1 Corporate groups data

This section will review available data as to the make-up of the whole group. It will first evaluate the available data of all companies to ascertain what proportion operate as part of a group. The aim is to provide an understanding of how

[22] Details of the full dataset is outlined in appendix A.

widespread corporate groups are across incorporations generally. The section then moves to evaluate overall use of groups in larger organisations. This will provide a comparison for how the use of the corporate group is implemented across the market generally and if this changes within larger companies.[23]

The register of companies within the UK has demonstrated steady growth over the last 50 years, growing from under 1 million companies in 1979 to the most current figure of 4,350,913.[24] This thesis considers the use of corporate structures as a contributor to this growth. The analysis provided below suggests that there is a direct correlation between growth and the use of the corporate form. The use of corporate groups provides the ability to judgment-proof assets through group structuring alongside other benefits outlined in chapter four. These unique features drive growth in corporations, and this is important as the argument presented by this research is that groups lack the legitimacy required to wield such corporate power. A likely consequence of this is the use of corporate subsidiaries to further the ultimate needs of the parent at the detriment of subsidiaries. The ability to create subsidiaries 'at will' and dispose of them in the same regard mitigates losses for parent organisations, further facilitating financial growth.

Companies House does not record details of companies that operate as a group, or companies that operate as stand alone.[25] Therefore, from the data available from Companies House, it is not possible to provide an overview on the complete register as to the divide between standalone companies and those who operate as part of a group. Some data is available from the Business Registers Strategy and Outputs department in the Office for National Statistics (ONS) in respect of a more complete overview. Figure 5, below, displays data from the ONS, and 89% of companies operate as a standalone corporation whilst the remaining 11% operate within the confines of a group. There are some qualifications to this data supplied by the ONS. Firstly, this is data collected through businesses paying VAT or PAYE tax in the UK. Therefore, some companies may be omitted by virtue

[23] The companies within *Dataset1.*
[24] Gov.uk, 'Statistical Release Incorporated Companies In the United Kingdom' <https://www.gov.uk/government/statistics/companies-register-activities-statistical-release-2019-to-2020/companies-register-activities-2019-to-2020> accessed 22nd February 2021.
[25] Standalone meaning the corporation is not part of a larger network of interconnected companies.

of their size. Companies with a turnover of less than £85,000 need not register for VAT, and as a result these companies would not feature in the data set supplied by the ONS. Moreover, companies which operate with no employees will also not feature due to the absence of PAYE payments. Additionally, the data is limited to companies which are domestic: it is therefore plausible that companies which fall within the 89% may have subsidiaries in different jurisdictions, as this chapter proceeds to demonstrate is a regular theme. The threshold for including a company as part of a group is 50% of the share value or voting rights, and therefore connected companies with less than 50% will also not feature in this data from the ONS. It is submitted that this set of data is therefore not fully representative of companies on the register; it is, however, the most complete data available.[26]

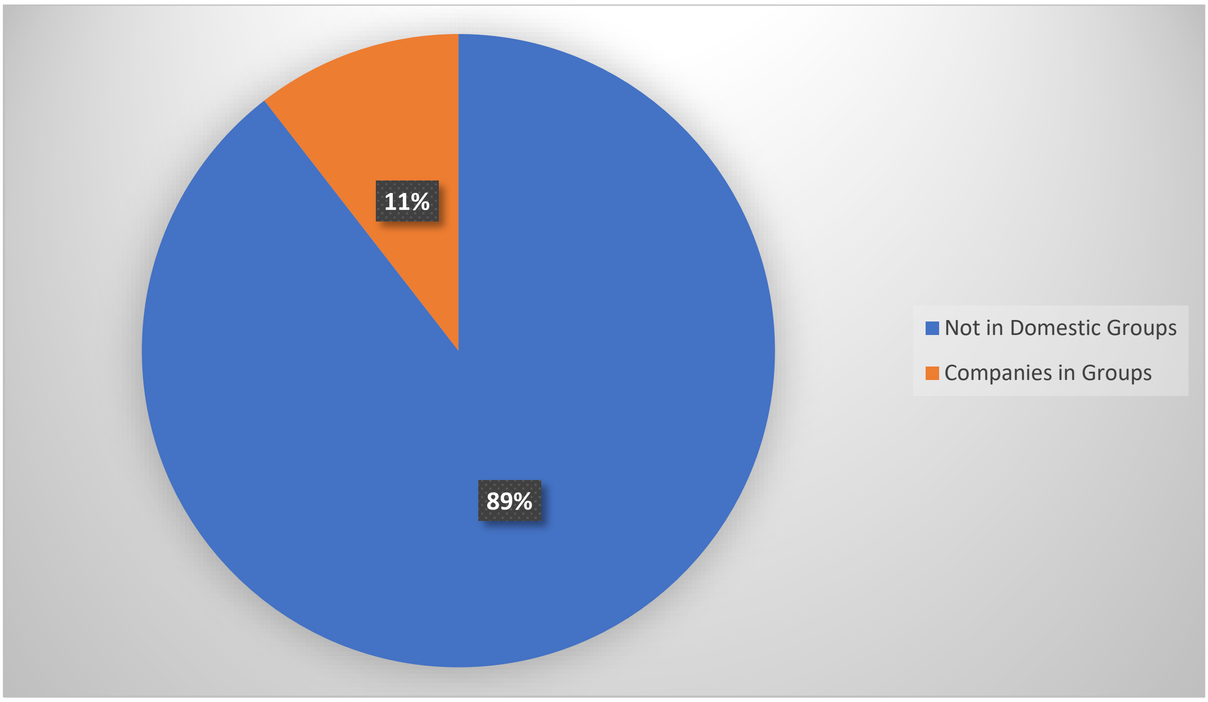


Figure 5 ONS Data on Companies

The data from the ONS presents the picture that companies operating within corporate groups represent a small proportion of companies. The purpose of this analysis is not to ascertain how many groups exist, as collection of this data would be both incomplete and inherently difficult to obtain. The information from the data here is that in utilising the 'best available data' of all operating enterprises, a broader picture of the use of groups can be seen. In this respect, the vast

[26] At the time of writing.

majority[27] of companies do not operate within a group. This collected data, of this broader picture, can be contrasted with the use of corporate groups within larger companies with greater financial strength. The aim here is to demonstrate from the available data that whilst the use of corporate groups may at first appear to represent the minority of companies, this is not conducive of the market when financial power and size is considered. In this respect, the larger companies who operate within this minority have the capacity to benefit from their unique construction which facilitates their accelerated growth, for which this thesis argues lacks legitimacy.

This can be demonstrated by the number of companies from *dataset1* operating as a group. In both the 100 private companies and FTSE 100 groups in *dataset1*, the use of both corporate groups and subsidiaries was significantly higher than the 11% presented by the ONS data. In both cases, as displayed in Table 1 and Table 2 below, the use of groups was 100%. That is, in each of the larger companies, irrespective of private or public, the use of corporate groups was present in each company. Given this disparity between the data from the ONS compared with the *dataset1*, some further analysis will follow to determine why such a disparity exists and if the size of the company maintains a correlation to the use of group structures.

Group = FTSE

Case Processing Summary[a]

	Cases					
	Valid		Missing		Total	
	N	Percent	N	Percent	N	Percent
Companies in Group	98	99.0	1	1.0	99	100.0
Subsidiaries	98	99.0	1	1.0	99	100.0

a. Group = FTSE

Table 1 Public Companies Operating within a Group

[27] Determined by quantity not financial size.

Group = Private

Case Processing Summary[a]

	Cases					
	Valid		Missing		Total	
	N	Percent	N	Percent	N	Percent
Companies in Group	100	100.0	0	0.0	100	100.0
Subsidiaries	100	100.0	0	0.0	100	100.0

a. Group = Private

Table 2 Private Public Companies Operating within a Group

5.2.2 Corporate groups analysis

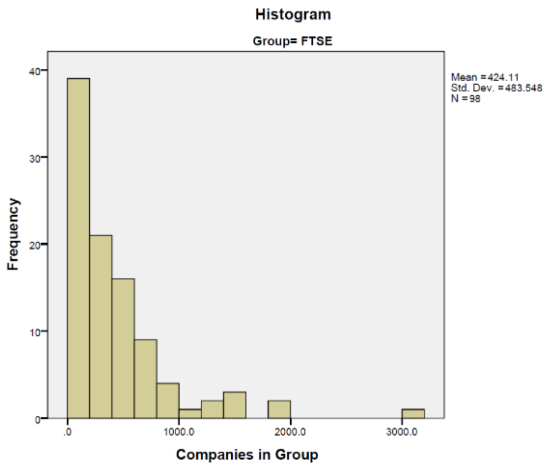
The preceding paragraphs present the argument that the use of corporate groups is more prevalent within larger corporations than smaller companies when compared to the 'all companies data'. Whilst corporate groups appear more embedded within larger organisations, this is not simply because groups are exclusively available to larger organisations. Witting claims that the insolvent entity problem lends itself to smaller and medium size business due to reasons of commerciality.[28] Witting argues that smaller companies might become insolvent by virtue of their position within a group, and this could be to the benefit of the parent, irrespective of size. This chapter's analysis will proceed to demonstrate that smaller companies appear to be utilised as part of a group, as opposed to the controller of the group. Whilst it is feasible for smaller companies to operate as a corporate group, the agency costs of this are argued to be disproportionate to the benefit. In this regard, corporate groups will be required to submit group accounts[29] and ensure the relevant management structures are in place. This has operational and agency costs which might be extensive for smaller companies. The use of corporate groups for larger companies is therefore more viable, and this viability is demonstrated in the preceding data provided. Furthermore, this section seeks to reinforce this argument, that there is a strong correlation between turnover, and thus financial power, and the use of corporate groups. Moreover, it aims to utilise statistical modelling to draw conclusions and

[28] Christian A Witting, *Liability of Corporate Groups and Networks* (1 edn, Cambridge University Press 2018) 1.
[29] Companies Act 2006, ss 403–405.

identify patterns within *dataset1* of the 100 largest public and private organisations. The data demonstrates not just that larger enterprises are more likely to put operations in the hands of subsidiaries, but that with an increase in size there comes an increasing certainty that group structuring will occur. Additionally, once the structures are in place, the growth of further subsidiaries seems to expand. Whilst this is analogous to Adam Smith's position[30] on what we would expect with the division of labour predicated on the extent of the market, the use of subsidiaries is not needed for this division. Austin contends that groups are not necessarily required to create these structures. He maintains that different divisions could be obtained through divisions without the need for incorporation.[31] The data analysed suggests this is not the case and the overwhelming majority of large corporations utilise incorporation and group structures to facilitate their corporate strategy. These patterns and structures are identified by utilising *dataset1* and processing this data utilising the methodological approach to produce graphical visualisations. The links between companies are based upon a connection through the ultimate owner holding >50.00% of the voting shares.

Utilising a histogram, the dispersion of the number of companies within a group can be seen in Figure 6 and Figure 7. The diagram on the left shows the dispersion of public companies, whilst the chart on the right is private companies. The majority of companies within a group in the private context were limited to the first two bins, less than 500. Therefore, the number of companies within the group for private companies is significantly less than the average for its public law comparator. There is also a greater range among public companies, demonstrating that public companies show a general trend of using more subsidiaries and connected companies than their private company counterpart. This is significant given the observation in the previous chapters that the dispersion of shareholders in public companies presents additional challenges to corporate governance. The greater the number of companies within a group, the more power wielded has the capacity to grow, which in turn lacks control by shareholders with rights over the parent company.

[30] Adam Smith, *The Wealth of Nations* (1776) vol 11937.
[31] Robert Austin, 'Corporate Groups' in Ross B Grantham and Charles Rickett (eds), *Corporate Personality in the 20th Century* (Bloomsbury 1998).



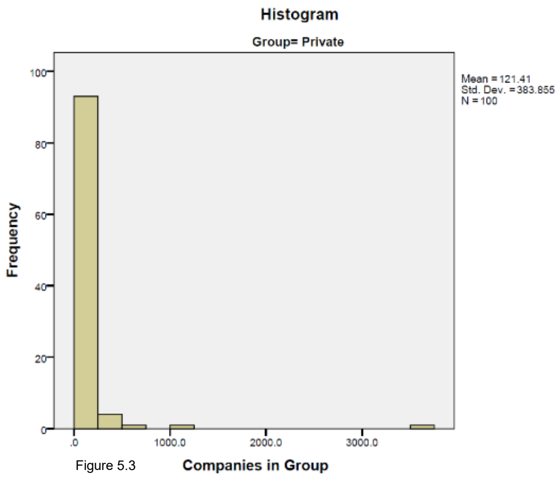


Figure 6 Public Companies Histogram

Figure 7 Private Companies Histogram

Condensing these two histograms down into a comparable bar chart with the average number of companies with a group presents the differences more clearly. The average size of a corporate group in the FTSE public companies was 424, whereas in the private companies, the group size was 70% smaller in terms of companies within the group. When looking at direct subsidiaries between public and private companies, the pattern is also substantially different. The number of subsidiaries for a public company is analogous to the companies within the group. However, the subsidiaries for private companies are 70% lower than companies within a wider corporate group and over 90% lower than public companies. This data, therefore, suggests that private companies are more likely to be subsidiaries than have subsidiaries. This argument is supported by both Figure 8 and Figure 9. The higher number of private companies being part of a group is due to the difference between the data of companies in groups and companies with subsidiaries. This is significant and supports the hypothesis of the thesis, as public companies largely operate with subsidiaries that remain subservient. This subservience is greater in public companies, which results in diluted shareholder activism due to the widely dispersed shareholders within public companies.

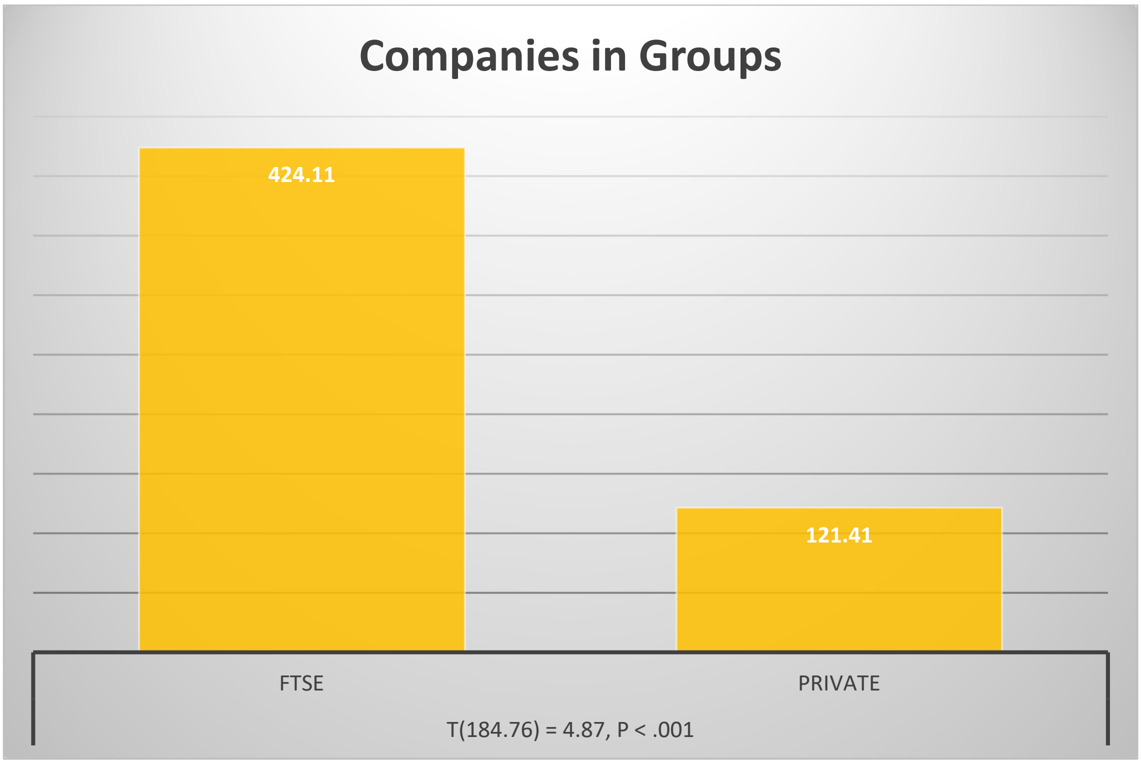


Figure 8 Companies in Groups

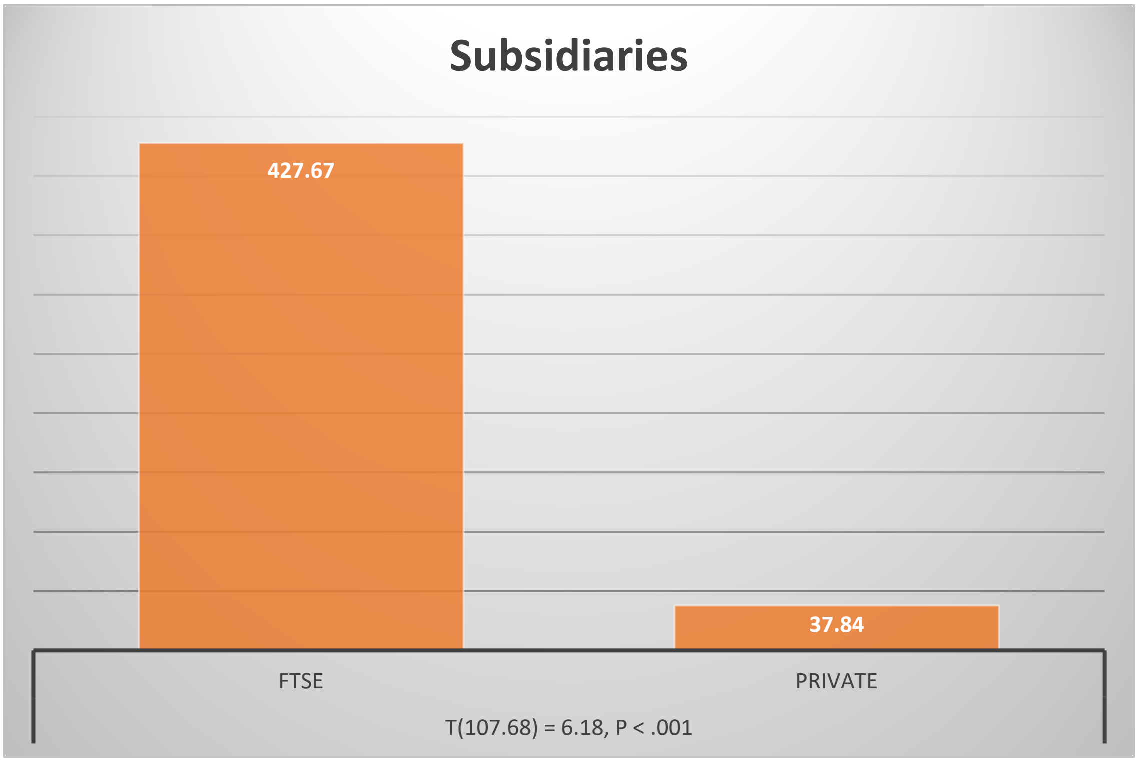


Figure 9 Companies with Subsidiaries

Furthermore, it is submitted that the use of these structures through subsidiaries and the creation of groups drives higher turnover, from which financial power results. With larger turnover, greater financial benefit for corporations can be derived and from this financial position, greater power wielded.[32] Figure 10 displays the disparity between the turnover of public companies and the turnover of private companies. This figure is based upon the average turnover of the private and public companies within *dataset1.* Mikler presents the argument that the financial strength of corporations drives their political influence,[33] , which further solidifies the power held. The large-scale turnover of public corporations, therefore, results in greater influence. This influence is significant within the public company due to the widely dispersed shareholders which exist at the ultimate parent company level. Public companies are, therefore able to make use of this financial position and further strengthen it by utilising corporate groups and subsidiaries.

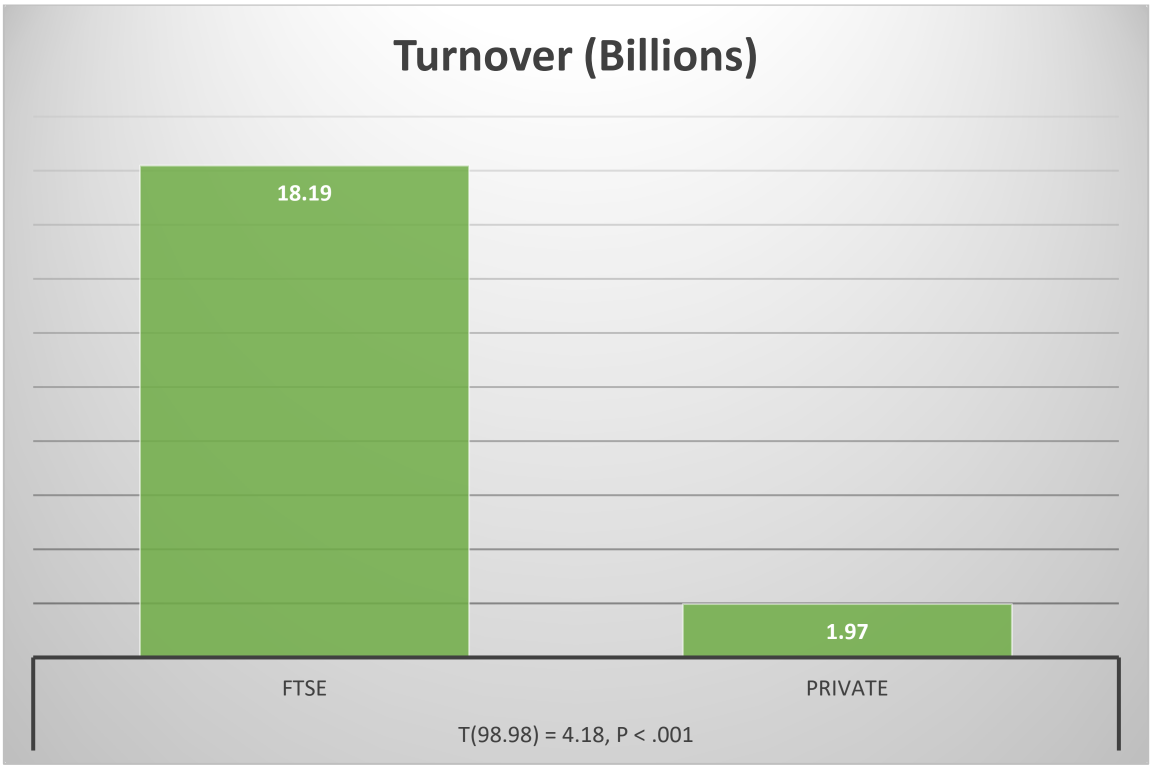


Figure 10 Company Turnover

This submission is that public companies are utilising subsidiaries to grow their turnover, and as a result they are able to multiply their financial strength and, subsequently their power. This can be represented with regression analysis. Regression analysis suggests that public companies' turnover can be predicted from subsidiaries and companies within the corporate group. Therefore,

[32] John Mikler, *The Political Power of Global Corporations* (John Wiley & Sons 2018).
[33] ibid.

regression analysis for Turnover by Companies in Group and subsidiaries is successful for FTSE public companies; however, regression analysis for Turnover by Companies in Group and subsidiaries was not successful for private companies. The result is that the use of corporate groups and subsidiaries for public companies is directly correlated to turnover. This is not the same in private companies where the correlation is not present. This data is represented in Figure 11 and Figure 12**.** Where in Figure 11 in relation to the public companies the line of best fit is clearly positive, in Figure 12 with private companies, this is not the case. This data analysis supports the theoretical underpinning in the preceding chapters. The use of subsidiaries within large public groups is overwhelming, the result of which is increased turnover that subsequently results in greater financial power. This ability for private companies to spawn subsidiaries presents greater challenges in public companies due to the diverse shareholding which exists in modern public companies. This presents particular challenges due to the power which is exercised by a small number of individuals within the ultimate parent company's board. The parent company is subject to controls and checks by its shareholders; however, the subsequent companies which are subsidiaries of the ultimate parent are not subject to these controls. This is supported by Robé, who argues parent companies are not held to the same standard.[34] Using the data it can be argued that the 427 subsidiaries each public company controls lack legitimacy due to the reduced checks on power which is exercised on behalf of the wider group.

[34] Jean-Philippe Robé, Robé J-P, 'The Legal Structure of the Firm' (2011) 1 Accounting, Economics, and Law 1, 21.

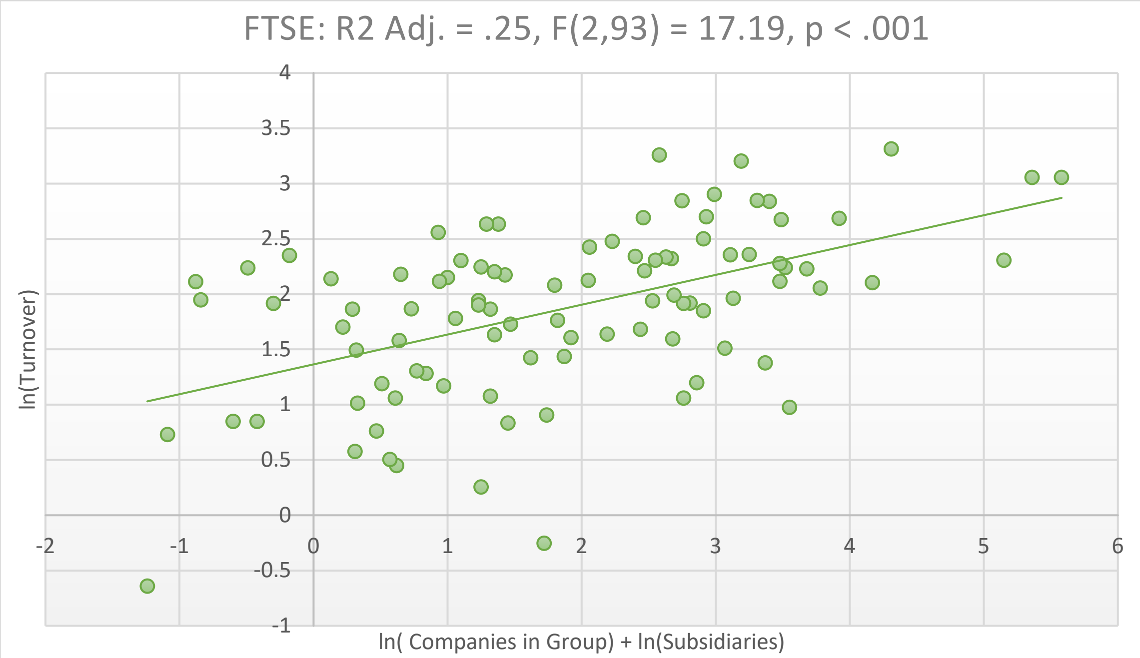


Figure 11 Public Company Regression Analysis

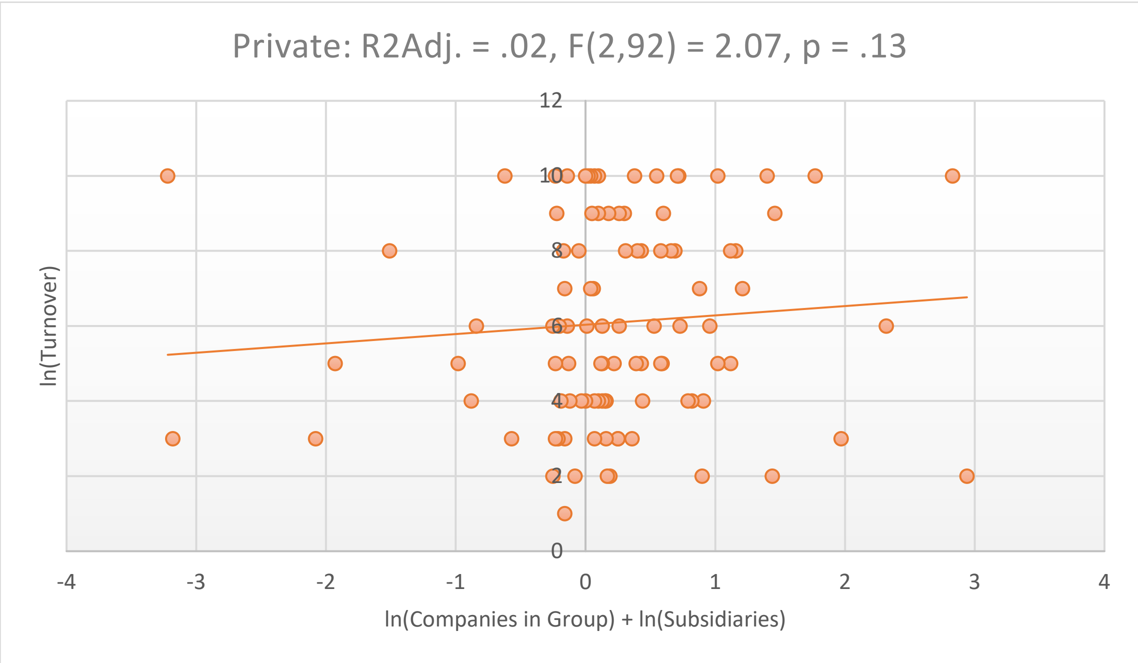


Figure 12 Private Company Regression Analysis

This section has provided empirical data analysis utilising data sourced from both Companies House and wider sources such as Fame.[35] This data analysis has evidenced the prevalence of corporate groups and that they extend further than merely a theoretical possibility. Moreover, the data has shown the widespread use of groups which in turn results in higher revenue from public companies. The

[35] Fame <https://fame.bvdinfo.com/> accessed 26 February 2021.

use of groups within public companies presents challenges due to a more widely dispersed shareholding. Furthermore, the correlation between value and the use of subsidiaries is disproportionate between private and public companies. This analysis supports the hypothesis that the close correlation between value and the use of subsidiaries has been the driver of the more laissez-faire economic style resulting in the widespread use of corporate groups. Moreover, this analysis provides the support to consider a framework for more correlative accountability within corporate groups. In ascertaining the disproportionality of groups within public companies, alternative frameworks for accountability should be considered in the context of publicly held corporations. Following this section, having identified the widespread phenomenon of groups and how they are used differently between private and public companies, and their difference in size, the next section will seek to deepen this understanding. This section will consider case studies of 10 of the most valuable companies, which will provide a further understanding of how groups function within powerful organisations.

5.3 Case studies

This section will evaluate case studies looking at the structures of 10 of the most valuable companies within the UK. The selection of these companies has been derived from a list from Brand Finance of the 10 of the most valuable brands and companies in the UK.[36] The purpose of this data study is to ascertain ownership structures of these larger corporations. The ownership structures are broken down into two distinct categorisations: the ownership of the subsidiaries and their geographical location, and the ultimate shareholding of the parent. This allows for two perspectives: it will first allow conclusions to be drawn as to the method of holding subsidiaries, that is, wholly, minority or majority owned. More significantly, the purpose of this study is to demonstrate the shareholding of the ultimate parent to allow chapter six to consider theories of ownership of the firm.

This data set (*dataset2*) has been selected due to the correlation between the use of groups and size as identified above. The preceding sections identified

[36] Statista, 'Brand Finance. Most valuable brands in the United Kingdom (UK) as of May 2020' (*Statista Inc*, 2020) <https://www-statista-com.uoelibrary.idm.oclc.org/statistics/292024/most-valuable-brands-in-the-united-kingdom/> accessed 22 March 2021.

patterns within the largest 100 private and public companies to identify some common themes, and this section aims to build on this with a more in-depth analysis of some off the largest companies. The data set selected, *dataset2*, has been identified in Figure 13 below. The analysis will be broken down into four key themes: the general structure of the company, the jurisdictional location of the parent's subsidiaries, the holding of shares in its subsidiaries and the shareholding of the parent company.

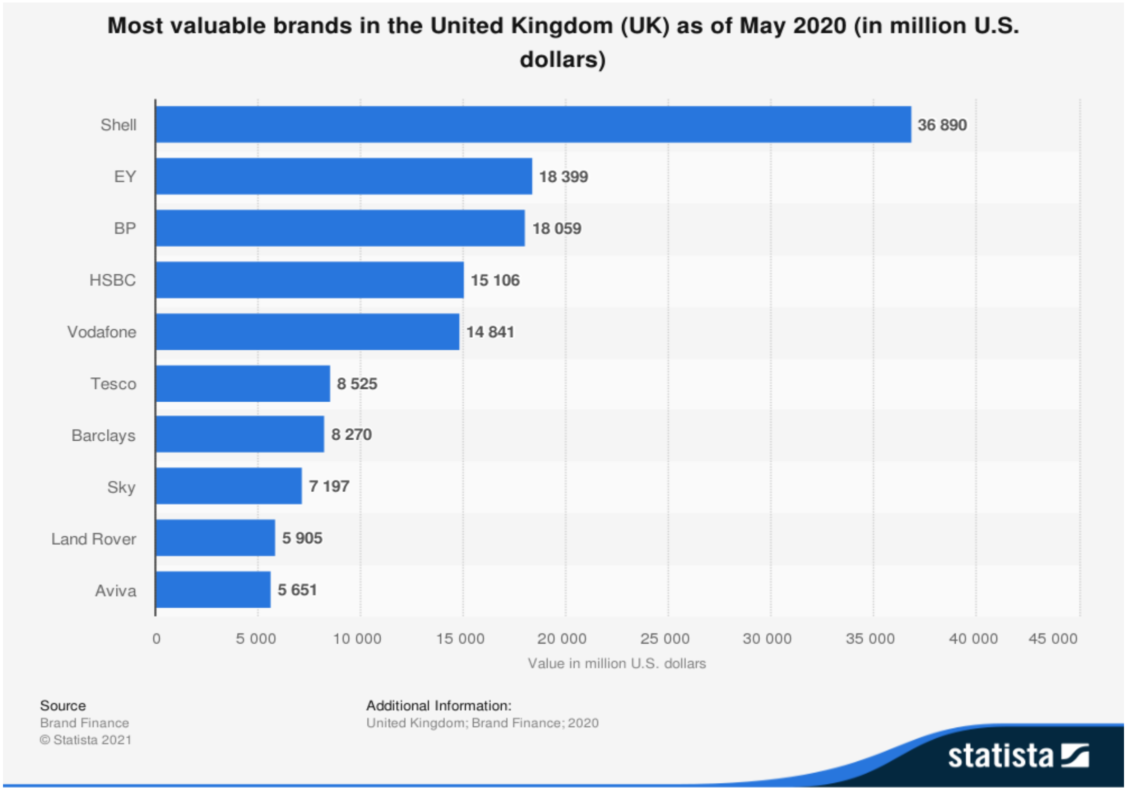


Figure 13 Most Valuable Companies in UK

5.3.1 Structures and patterns

This section will provide a descriptive analysis on the structures and patterns identified from the companies within the selected *dataset2*. This presents an overview of the types of structure we see within the largest corporate groups. This in turn will provide an underlying framework for the chapter to proceed to consider further statistical analysis. The chapter has thus far established the correlative link between size and the use of corporate groups. The regression analysis and bar charts establish that within public companies, the use of these groups and subsidiaries is greater, averaging around 400 companies within their group. The

10 companies with this *dataset2* consist of eight public companies and two large private companies. The public companies within this smaller data set have an average of 1,145 companies within their corporate group. This is an increase in the number of companies within the group average in *dataset1* of 170%. This further supports the argument being made by this chapter that there is link between numbers of companies within a group and the financial position of the company. The two private companies from this data set, Aviva insurance Ltd and Ernst & Young (EY) LLP, also demonstrate a higher proportion of companies within their group than the average in *dataset1*. The average between these two was 554, which again is significantly higher than the 121 we saw in the *dataset1*. This further supports the preceding argument of correlative growth with the use of corporate groups and financial strength.

As the preceding chapters have identified, there are many reasons for the structuring of groups and two principal methods of structuring they might follow: vertical and horizontal. This *dataset2* will now be analysed to identify patterns of types of structures amongst these large organisations.

5.3.1.1 Categorisation of subsidiaries

Some key themes have been identified with the corporate groups selected in the *dataset2*. One theme is that companies within these large groups fall, largely, into three categories of subsidiary: jurisdictional, divisional and financial. This section will now proceed to consider the *dataset2* to ascertain these different categories and how they are utilised.

Mining and extraction

The two largest groups in terms of companies within the group are Shell and BP. Both operate the activity of mining and extraction, a universally accepted high-risk industry.[37] Royal Dutch Shell have recently been subject to a high-profile appeal in the Supreme Court regarding one of their subsidiaries and its

[37] For example, in the year ending 2019, Shell reported nine deaths directly related to their activities.

operations.[38] One of the key themes which is more prominent in both Shell and BP is the use of 'development' companies to carry out their operations. The high-profile Supreme Court case was in relation to one of these companies, The Shell Petroleum Development Company of Nigeria Ltd. A common theme from both Shell an BP is the use of development companies where oil extraction activities are carried out. These fall into the jurisdictional and operation types of subsidiaries. Both Shell and BP have companies in Oman, Nigeria, the Middle East, Hong Kong, Canada and Russia. The jurisdictional subsidiary allows mining activities to be carried out whilst remaining legally separate from the parent. This type of structuring allows the parent to judgment-proof the parent to the possible detriment of the subsidiaries or their creditors.[39]

In additional to this jurisdictional structuring, there is also a common theme of divisional structuring within these companies. Divisional structuring is where operations of the organisation are broken down into divisions which carry out specific tasks. Within Shell and BP, common divisions are upstream and downstream. Upstream divisions extract raw product, and then downstream produce raw materials into a product for retail sale. In addition to both these upstream and downstream divisions, there are also distribution and retail companies within their groups. Financial structuring is also present in Shell and BP, where assets and finance companies operate as part of the organisational structure. Therefore, what can be determined from these two case studies is that in this large organisational structure, all three categories of subsidiary are present. It can be inferred from these complex structures that the benefit in this structure is that of isolating risks to specific divisions and jurisdictions, and the cases of *Vedanta* and *Okpabi* support this inference. This isolating of risks provides a platform for the organisation to expand, and with expansion comes financial reward and with this, increased corporate power.

Banking and finance

[38] *Okpabi and others v Royal Dutch Shell plc and another* [2021] UKSC 3.
[39] See *Okpabi and others v Royal Dutch Shell plc and another* [2021] UKSC 3 and *Vedanta Resources plc v Lungrove* [2019] UKSC 20.

Having analysed the structures of BP and Shell in the context of mining and extraction, this section will proceed to analyse the two banks within our data set to establish if patterns emerge. It is noteworthy that the complexity of the structure of HSBC prevented the system Fame from mapping the group structure. HSBC and Barclays operate on both a horizontal and vertical structural basis with differing levels of complexity leading back to the ultimate parent. Unsurprisingly, the key theme of the subsidiaries within these banks is that of financial subsidiaries. In this sense, the division of subsidiaries is broken down into investments, trusts, assets, holding and asset management companies. These are categorised as a 'financial' style of group structure. In addition to the financial subsidiaries, there are jurisdictional subsidiaries within the group. As identified in preceding chapters, the requirement of a local incorporated company will often result in these jurisdictional subsidiaries being incorporated, as this is such an example of a reason for corporate groups as outlined in the previous chapter. Given the global footprint of both HSBC and Barclays, it logically follows that local divisions will be incorporated to comply with local financial regulations.[40] Therefore, what can be surmised from both Barclays and HSBC is that they operate on two key themes for subsidiaries, financial and jurisdictional. A similar theme occurs in EY and Aviva; however, the groups structural architecture differs. EY contains financial subsidiaries alongside jurisdictional ones, which appears analogous to that of HSBC and Barclays. The main difference here is that EY is an LLP and the way in which subsidiaries are utilised differs from that used in the banking company examples. EY has 217 subsidiaries within the group, which is significantly less than the average for this data set. The way in which those subsidiaries are organised also differs: there are more layers and subsequently a more complex structure as opposed to either horizontal or vertical structuring. In both EY and Aviva, the theme is that of financial subsidiaries, such as investment and holding subsidiaries. It necessarily follows there is a logical correlation between parent companies which operate financial services and their structuring of the corporate group, with financial and jurisdictional subsidiaries.

Goods and services

[40] The consideration of worldwide banking regulations is beyond the scope of this thesis.

The remaining companies within *dataset2* will now be considered collectively: Vodaphone, Sky, Tesco and Land Rover. These companies provide goods and services largely to the retail markets. Much like the previously considered companies, there are jurisdictional subsidiaries in each of these organisations. The nature of jurisdictional categories of companies within the group demonstrates the global remit of all of these companies within *dataset2*, and this appears to be a prominent feature of all 10 of the companies within this data set. The common theme with Vodaphone, Sky, Tesco and Land Rover is their use of divisional companies within the group. This use of divisional structure is the prominent feature of structural organisation within these companies. For Tesco, there are direct subsidiaries for a division then further companies working down a vertical structure for sub-divisions of operating. Sky UK represents a similar structure whereby operations and divisions are divided in a vertical manner, such as Sky News and Sky Retail operating as companies within the collective group. This theme is similar in both Vodaphone and Land Rover. This suggests that companies which offer goods and services in a tangible format structure the organisation in a predominantly divisional structure which differs from companies such as HSBC, EY and Barclays whose structure is largely financial. This analysis demonstrates that there is no single organisational structure for large companies and that the type and size of the organisation renders different structural design.

Therefore, what can be established from this analysis is that whilst there may be some significant differences in the way groups are architecturally structured, the types of subsidiaries which exist within these structures largely fall into three categories. These three categories are jurisdictional, divisional and financial, and from the analysis carried out on the sub-data set at least one of these categories was present in each group of companies. Some of the companies within the data set contained group companies within all three categories and others used different combinations, such as jurisdiction and financial or jurisdictional and divisional. This analysis provides an insight into why groups may structure their organisations, and what benefit can be derived from the chosen structure. This level of understanding will permit the thesis to make recommendations based on the types of groups which are seen in practice and the patterns which present themselves.

5.3.2 Locations of companies within the corporate group

The preceding section identified the three categories of the company within a group and how the use of these categories differed amongst different corporate groups depending on their industry. One common theme identified amongst all the companies within the data set was the use of jurisdictional companies within the corporate group, companies registered or operating within other jurisdictions. This section will proceed to evaluate if there are common jurisdictions within *dataset2* and how ubiquitous the use of jurisdictional group companies is. The section will proceed to evaluate jurisdictional companies by identifying the companies within a corporate group and how these are divided by country. To display this data, each of the 10 companies within our data set have been converted into a pie chart to demonstrate the jurisdictional locations in which the groups operate.

First is the evaluation of the jurisdictional structures of both Shell and BP given their similarity in business activity. Figure 14 below displays the global reach of Shell, which operates across 124 countries, whilst Figure 15 displays the jurisdictional reach of BP, which extends to 84 countries. Therefore, Shell appears to have a larger presence globally, though both Shell and BP demonstrate a large global footprint.

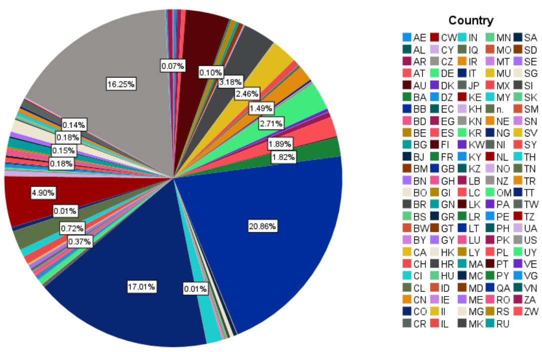


Figure 14 Shell Pie Chart of All Countries

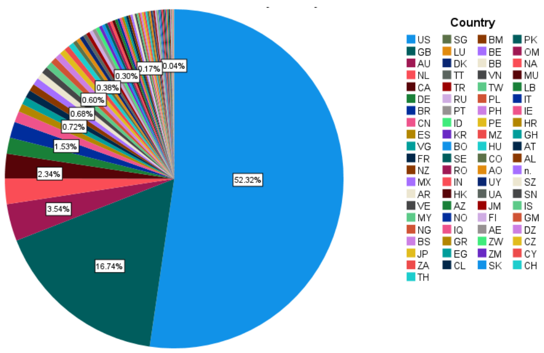


Figure 15 BP Pie Chart of All Countries

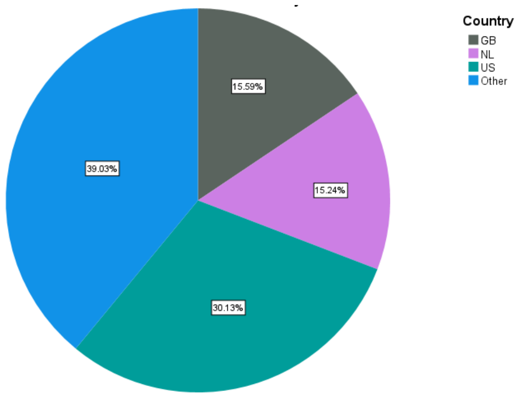


Figure 16 Shell Companies Condensed

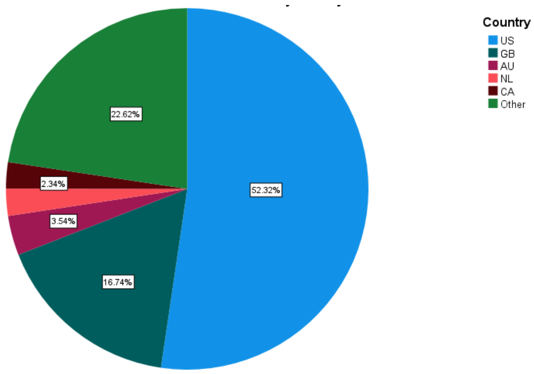


Figure 17 BP Companies Condensed

Given the volume of data on the full pie chart analysis of group companies, it is difficult to ascertain patterns; therefore, in Figure 16 and Figure 17 (above), where jurisdictional countries amount a trivial number these have been collapsed into the category 'Other'. Condensing the data in this way permits a greater analysis in terms of comparison. In both Shell and BP, it can be identified that there are three common jurisdictions: GB, USA and the Netherlands. The USA in both groups maintains a larger number of subsidiaries than in GB, and in both the GB companies within the group represented less than 25% in both case studies. The volume of companies which are controlled and owned by the group largely operate outside the jurisdiction in which the ultimate parent company is registered. This section will proceed to present the argument that this is the case for the majority of the *dataset2*. In the successive companies within the data set, the average number of jurisdictions utilised within the corporate group is 41, which is 50% less than BP and 70% less than Shell. It can therefore be surmised that the use of jurisdictional companies is more widespread in the mining and extraction industry than the other types of industries within the *dataset2*.

Groups of companies by location

In appendix B Figure 28 to Figure 36, the data from the remaining companies within the *dataset2* demonstrates a consistent pattern. The pattern which emerges is that once condensed,[41] all these companies operate largely from an average of 3.6 jurisdictions, which is significant given the average of 41

[41] The jurisdictions which amount to an all but trivial amount are placed into the category 'other'.

jurisdictions utilised by these groups. Therefore, despite the relatively large global footprint of these 41 jurisdictions, the majority exist within just 10% of the total number of jurisdictions in which the groups operate. This data suggests that the use of jurisdictional companies could be utilised for either compliance with local regulations – as identified in earlier chapters – or for judgment proofing, as was the case in both *Okpabi*[42] and *Vedanta*.[43] The use of subsidiaries in the latter context is an example of the use of corporate power identified in the group framework as defined in chapter four.

Moreover, the large global footprint of corporations allows corporate power to transcend multiple jurisdictions and utilise corporate power in one jurisdiction with the ultimate parent operating from another jurisdiction. This can be supported by the data in the above figures with respect to the number of companies within the same jurisdiction as the ultimate parent company. In each of the case studies within the *dataset2*, with the exception of Tesco, the companies within the same jurisdiction of their parent, England and Wales, was less than a third. This ranged from around 10% of all group companies operating within England and Wales to a maximum of 33%. This data demonstrates that the jurisdictional category of group companies is significantly utilised with the majority of group companies operating outside of the jurisdiction of the ultimate parent. This affords additional protection in terms of judgment proofing, as in addition to the corporate veil there is also the jurisdictional veil affording protection for parent companies. In addition to the patterns already identified, there is a significant commonality of group companies operating in the USA and Luxembourg. This further supports the argument of corporate groups expanding their geographical footprint, which ultimately provides a jurisdictional privilege.

This section has emphasised the widespread use of jurisdictional companies within large organisational groups. There is a significant use of group companies operating in diversified locations of over 120 unique locations in some corporate groups. This diversified portfolio exists despite the majority of group companies operating in three or four primary jurisdictions. Moreover, the majority of

[42] *Okpabi and others (Appellants) v Royal Dutch Shell plc and another (Respondents)* [2021] UKSC 3.
[43] *Vedanta Resources plc v Lungrove* [2019] UKSC 20.

subsidiaries and group companies operate outside the primary jurisdiction of the ultimate parent company. This structuring strengthens the global and multinational influence of large companies and further strengthens their political and financial power. The ability to have companies operating on different levels and in different jurisdictional locations affords group companies benefits which are not possible with standalone companies.[44] This in turn, adds to political pressure and the need for jurisdictions to compete to maintain companies for tax revenue purposes. This section has therefore demonstrated that the global reach of large group companies is both substantial and furthers the power held by corporate groups due to the ability to operate on a multinational level. This ability to operate across jurisdictions affords protections to group companies by being legally separate but at the same time appearing as one global business, supporting the short-term focussed schizophrenic corporation.[45]

5.4 Shareholding of group companies

The preceding section analysed the vast global footprint of large group companies and their omnipresence on a global scale. Given the footprint and capacity to operate and control group companies on this global scale, this section will proceed to evaluate the ownership of group companies to ascertain levels of control by the ultimate parent. The section intends to establish levels of control by identifying the shareholdings within the corporate group, the ultimate parents' shareholding of the group companies. Data will be displayed on histograms to analyse and investigate how parent companies hold their subsidiaries. Histogram analysis will clearly demonstrate patterns in the holding of subsidiary companies.

In *dataset2*, the overwhelming majority of companies within the corporate group are wholly or majority owned. This can be demonstrated by Figure 29 to Figure 38 in appendix C, which presents histograms for each of the 10 case studies within our *dataset2*. The mean ranges from 88 to 98 across all of the examples, suggesting significant control by the ultimate parent as a common theme. The

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[44] See chapter 4.

[45] See: William T Allen, 'Our Schizophrenic Conception of the Business Corporation' Lawrence Mitchell (ed) *Corporate Governance* (Taylor and Francis 2017); Paddy Ireland, 'Corporate Schizophrenia: The Institutional Origins of Corporate Social Irresponsibility' in Nina Boeger and Charlotte Villiers (eds), *Shaping the Corporate Landscape Towards Corporate Reform and Enterprise Diversity* (1 edn, Hart Publishing 2018).

preceding chapters have outlined the challenges of separation of ownership and control and the ability to divide the organisational group but maintain control over these subsidiaries. The data has also demonstrated the regular use of high-volume wholly or majority-owned subsidiaries. This ability to incorporate subsidiaries but maintain control has the potential to increase parent company opportunism and corporate managers seeking deviant goals.[46]

5.4.1 The effects of control

The concept of control has featured prominently thus far in this research, both in terms of utilising control to define a corporate group and the subsequent effects that result from parent company control. The ability of corporate parents to maintain control of subsidiary companies to serve their own interests is unique to groups. This is notorious, with parents able to dispose of underperforming companies with ease. The result of maintaining majority or whole control presents specific challenges for corporate groups, which were outlined in the previous chapter.[47] One such challenge is that of judgment proofing, the holding a significant amount of control in one subsidiary that results in the specific subsidiary becoming subservient to the needs of the parent. This is linked to the challenge of opportunism and excessive risk-taking, the problem of short-termism. The parent company is able to exert its power and control over the subsidiary to ensure it carries out the will of the parent to the possible detriment of the subsidiary. These subservient practices and structuring present challenges which are unique to the group company and as a result, require further consideration and analysis.

The ability to control the group companies by virtue of their shareholding also can saturate a market and derive benefits by seemingly allowing one group to appear as multiple brands. By way of example, if a particular brand has been operating with undesirable practices, the goodwill attached to that specific company may have been lost but this is unlikely to affect the parent company. This can be demonstrated by looking at a company such as Unilever PLC.[48] If negative press

[46] Parkinson, (n 9) 71.
[47] Chapter 4.
[48] Unilver, ‘All brands’ (*Unilever*, 7 June 2021) <https://www.unilever.com/brands/view-all-brands/> accessed 7 June 2021.

resulted in PG Tips, one of their brands of tea, becoming less favourable due to negative press or leaked practices, this is unlikely to affect the brand Lipton Tea because they are seen as separate, and few individuals will be aware of the link between the two and that they are ultimately controlled by the same parent company. This could be despite there being a very close link between the two brands or products. This is a specific challenge to corporate groups and allows market saturation and control of large proportions of the market, with consumers seemingly unlikely to be aware this is the case. This affords the parent company a unique ability to utilise subsidiaries to their own means without substantial risk to their own financial viability or subsequent power wielded by the parent. The challenges within parent companies also extend to where a 'brand persona' may be presented but a subsidiary is the main contracting party. In this scenario, a third party could think they are dealing with the parent due to the use of branding, but in fact they are dealing with the subsidiary. This affords the parent company to further proof their assets by utilising subsidiaries in this manner, especially in more risky operations. This is to the possible detriment of the third party, who may be an unsophisticated creditor or lack the negotiating power to adjust the terms.

5.4.2 Shareholder monitoring of subsidiary companies

There exist further agency challenges with the context of corporate groups within the type of structures which have been identified in this chapter. Shareholders are able to hold directors and their representative company to account through retained shareholder rights as the 'beneficial owners of the company. The terminology 'beneficial owner' in this context refers to those who are entitled, subject to profit, a return on their investment and who maintain residual voting rights. Given that the majority of companies within the group context appear to be majority or wholly owned, there is significant control with the managers of the parent company, who can exercise this over the subsidiaries within the group. This presents additional problems of asymmetric information and a further dilution of control by the shareholders of the ultimate parent company. Whilst the parent company may be able to control the subsidiaries, the shareholders may be acutely unaware that a subsidiary may be being utilised in a certain way. Moreover, if the shareholders are aware, the ability to hold the parent to account for the use of the subsidiaries is inherently difficult, and this links directly to the argument Robé presents.[49] The ability for both the ultimate shareholders to be aware of the actions of the parent in respect of subsidiary action, and the ability to take action to hold them to account is diminished by the control of the parent, which results in asymmetric information. This information and activism gap further dilutes any ability shareholders may have to exercise their residual rights for the company to be run in their interests. Moreover, given the large scale of companies, an average of 425 companies within a group, reprimanding parent companies or their managers for the use of a subsidiary which is all but a small part of the enterprise is unlikely to be an avenue shareholders will engage in activism over.

This section has established the common theme of how subsidiaries and related companies are owned and controlled within corporate groups of *dataset2*. It has identified that the majority of companies within the corporate group are wholly or majority owned, which affords the ultimate parent company the significant ability to exert their control over the subsidiaries. This common theme suggests that large companies maintain significant control and as such this increases both company and managerial opportunism. This opportunism has the potential to lead to damaging practices such as short-termism, and in some instances could be contrary to the interests of the beneficial owners. This ability to control subsidiaries with asymmetric information reduces the ability for shareholders to engage in activism, which further strengthens the position of the parent company and its managers.

5.5 Shareholding of parent companies

This chapter has thus far demonstrated common themes in types in terms of horizontal and vertical structuring as well as the financial, divisional and jurisdictional patterns that have been identified. Moreover, the use of these types of company operates on a large global scale, and often within this scale the control is maintained by the parent through whole ownership or majority ownership. This has addressed the question as to the application of corporate

[49] Robé (n 34).

groups and the economic reality in which they operate. Given the scale of these large corporations and the likely power they are to wield, this section now proceeds to evaluate the ownership structure of the parents themselves to identify any patterns which might exist.[50] This will provide a framework to ascertain the levels of activism which might be possible to hold corporations and their managers to account. Additionally, it will provide a basis to consider further changes, if any, in the next chapter, given the types of ownership which are seen within companies of this size. In each of the case study examples utilised, the shareholding has been broken down into types of shareholders and displayed on a pie chart to ascertain each category of shareholder.

Royal Dutch Shell PLC shareholding

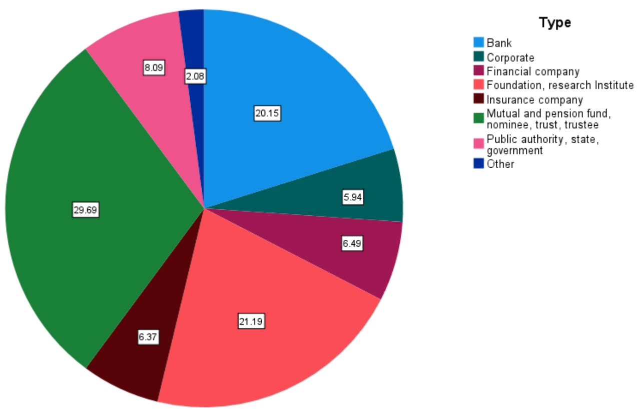

Figure 18 Shareholding of Royal Dutch Shell PLC

First, looking at the shareholding of Shell (Figure 18), the majority of shareholders fall into the category of mutual and pension funds. This suggests that the shares are likely to be held by a third party or trustee. The second largest classification of shareholder is a foundation or research institute, closely followed by banks. Only 2.08% are held by 'Other', which includes individuals. The result is that most shares for Shell are held by institutions, other companies, or banks. There will likely be further beneficiaries within these categories, for example, the pension fund may have beneficiaries within its fund. The corporations who hold shares may have shares as capital investment and they themselves will have beneficial shareholders. Therefore, what can be identified from the case of Shell is that the

[50] Data collected represents ownership of the 10 case studies as of March 2021.

rights for voting and other rights vested in shareholders will be exercised largely by those who are exercising these rights on behalf of other beneficiaries, adding further dilution between ownership and control.

BP PLC shareholding

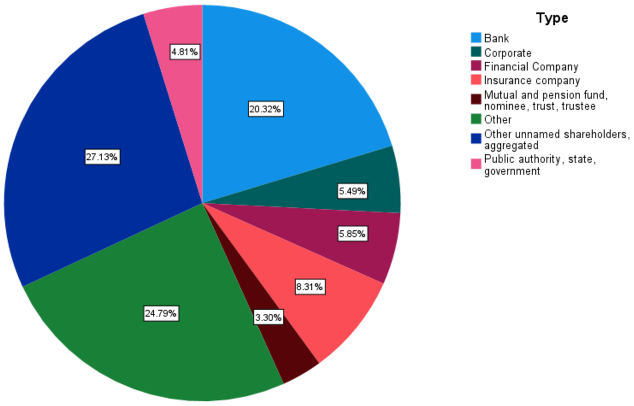

Figure 19 Shareholding of BP PLC

The shareholding of BP PLC is depicted in Figure 19. The category of ‘Other unnamed shareholders, aggregated’ is the largest shareholding. Upon further investigation of such a large individual sharing, it can be discovered that this is held by JP Morgan Chase bank, an institutional shareholder. Moreover, another large shareholder is that of the banks more generally, alongside insurance companies and pension funds. One noticeable difference between BP and Shell can be observed: the category of ‘Other’ is larger in Shell than in BP, suggesting a large representation of individualised or unregistered shareholders. One key feature remains the same that the majority of the shares are held by those in capacity who hold them on behalf of another party.

Barclays PLC and HSBC shareholding

Comparing the two banks within *dataset2* in Figure 20 and Figure 21 (below), in Barclays it can be seen that the largest category of shareholders is ‘Banks’. However, for HSBC, it is the ‘Other’ category. This could be due in part to HSBC being more global and having a more global ‘negligible’ shareholding. The second largest category of shareholding for HSBC is also ‘Banks’; therefore, within both bank case studies in *dataset2* there is significance in other bank ownership.

Insurance and financial companies also contain large shareholdings.[51] In both cases, with both HSBC and Barclays, there is a larger proportion of 'Negligible/Other' than can be seen in BP and Shell. However, there remains a large holding in the categories where shares are held for third parties as likely beneficiaries. This is consistent with what has been identified in both BP and Shell.

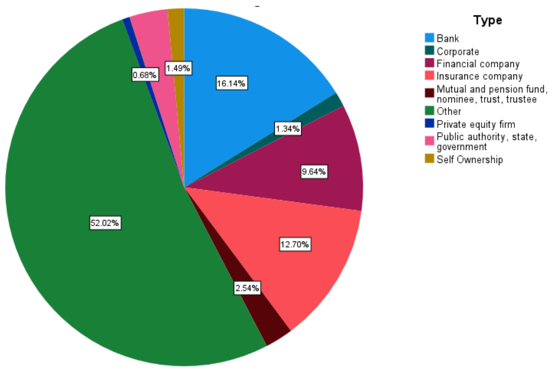

Figure 20 Shareholding of HSBC

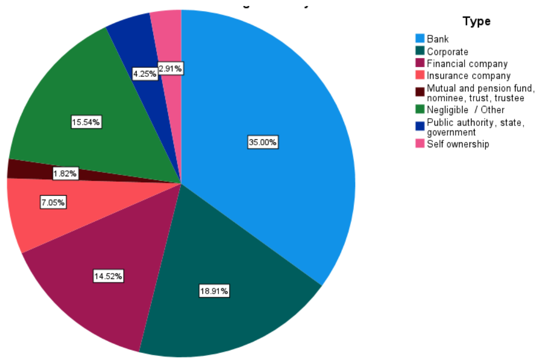

Figure 21 Shareholding of Barclays PLC

Tesco PLC shareholding

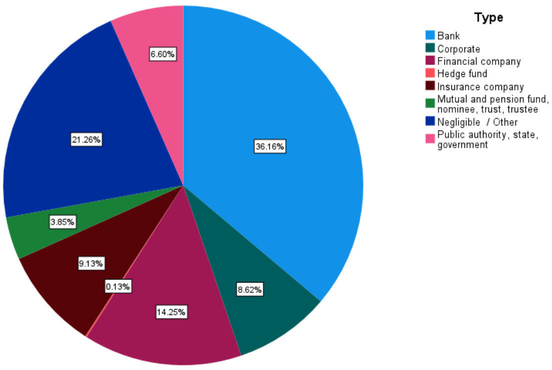

Figure 22 Shareholding of Tesco PLC

Tesco (Figure 22) demonstrates a similar position to that of BP and Shell. A large proportion of shareholders were in the category of a bank, representing over a third of the overall shareholding. Moreover, other significant shareholders of Tesco were insurance companies and financial companies. Much like Shell and BP, there is a significant presence of shareholders who hold shares on behalf of beneficial shareholders.

[51] A large shareholding in the context of private companies is considered anything over 5%.

Land Rover shareholding

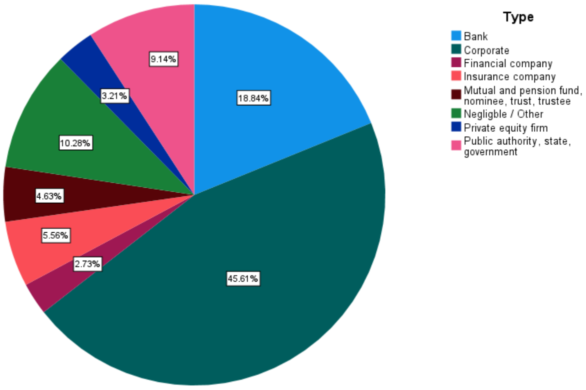

Figure 23 Land Rover Parent Company Shareholding

The category of shareholding with the group of companies associated with Land Rover (Figure 23) consists mainly of corporate shareholders. Analogous to the previous companies, the majority of shareholders fall into the category where shares are held for the benefit of others. In the case of Land Rover, other prominent categories include public authorities, banks and insurance companies. The combined shareholding for 'Negligible/Other' is 10%, which will be made up of a significant number of both individual shareholders and institutional shareholders who hold greater numbers of smaller proportion shares.

Sky Group shareholding

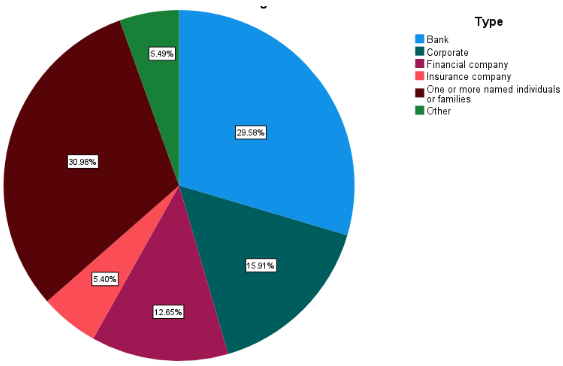

Figure 24 Sky Parent Company Ownership

Furthermore, analogous patterns can be derived from the share ownership categories of Sky (Figure 24). Sky itself is a private company subsidiary of Comcast and as such this data is from the ultimate parent company. A similar pattern emerges whereby the bank and financial companies occupy the largest category of shareholding. In the case of negligible or smaller shareholdings, when combined these amount to just over 5% of the total shareholding. In a similar vein to BP, there is a significant party who occupies a large proportion of the shareholding. Brian Roberts, an American business tycoon, maintains around one third of the voting rights. This is the only company within *dataset2* where an induvial maintains a significant proportion of the shareholding.

Aviva and Vodaphone shareholding

In the categories of shareholding with Aviva (Figure 25) and Vodaphone (Figure 26) the majority of shareholding falls into the category of 'Other/Negligible'. This category covers all remaining categories of shareholders and those who own negligible shareholders: as such, it is not easy to ascertain who the 36% and 41%, respectively, are. Despite the large proportion of shareholders falling into 'Other/Negligible', other patterns from the remaining distinguishable categories can be recognised. In a similar pattern to the previous case studies from the data set, the category of 'Bank' maintains a large proportion of the category of shareholders. In Aviva and Vodaphone, despite there being a large 'Other/Negligible' amounting to over a third, both companies have 'Bank' as a category of shareholder, representing over 25% of the types of shareholders. There is also a large representation from corporate, insurance and financial categories, which combined occupy a significant proportion of the classification of shareholding.

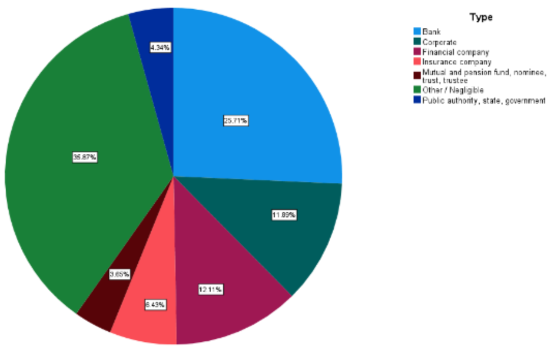

Figure 25 Shareholding of Aviva PLC

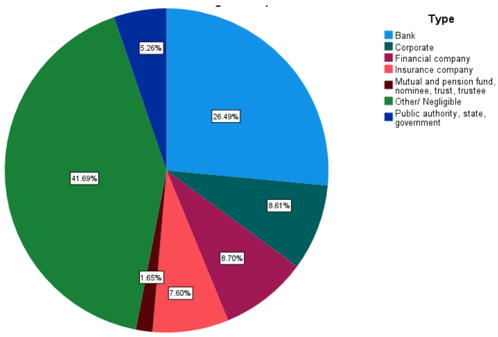

Figure 26 Shareholding of Vodaphone

5.5.1 Results

The analysis of the preceding case studies within *dataset2* demonstrates a clear pattern amongst all the companies within the selected data set. This pattern is a significant number, and in most cases, a majority are held by those who likely hold these shares for the benefit of other third parties. In all cases where the 'Negligible/Other' category was substantial, the breakdown of this further demonstrated that this was shareholders where the shareholding was so trivial that it could not be registered, defined as <0.01%. It is possible, therefore, that the cumulative value of these shareholdings of <0.01% amounts to some significance, as identified above. The individual rights which can be exercised, shareholder activism, are somewhat diminished. Therefore, it can be determined that with the companies within *dataset2*, the majority of shares are held by those who fall into the category of holding the shares on behalf of other beneficiaries, institutional shareholders. In the instance where the category of shareholder is a public or state body, it is submitted that these are held to benefit society at large, and as such the beneficial interest is separated from the legal one.

The register of shareholders also displays patterns within the categories identified in the pie charts. In the category of mutuals and pensions, a key single shareholder was identified: the Diverse Income Trust PLC featured in two of the companies within our data and various trusts and schemes managed by JP Morgan appeared in over half of the companies. The Universities Superannuation Scheme (USS) also featured, which is one of the largest pension schemes in the country with a substantial membership of 450,000 members.[52] The result is that institutional shareholders represent a large proportion of shareholders, and that those beneficially entitled to the income and benefits are further removed from the company. By way of example, it is unlikely that those who pay into the USS pension scheme are aware that their contribution has allowed USS to purchase a significant control in Thames Water and Heathrow Airport.[53] Moreover, significant power appears to be vested in institutional shareholders in a further

[52] USS, 'Who we are' (*USS*, 2021) <https://www.uss.co.uk/about-us/who-we-are> accessed 16 April 2021.
[53] In this instance, >10%.

separation with ownership and control. Therefore, those who provide the capital, those beneficially entitled, are likely to be unaware and unable to engage in activism due to even more dispersed and disengaged shareholding.

This further separation can be further seen through the category of 'Bank': the above ownership analysis has demonstrated that Banks hold a significant proportion of shares within these large corporations. This is specifically demonstrated with the example of Blackrock Inc, which is an investment bank specialising in asset management. An activity carried out by asset managers, such as Blackrock, is managing pension funds amongst other forms of management. As alluded to above, the average pool of beneficiaries for pension funds is widely dispersed, which further dilutes the ability to engage in activism.

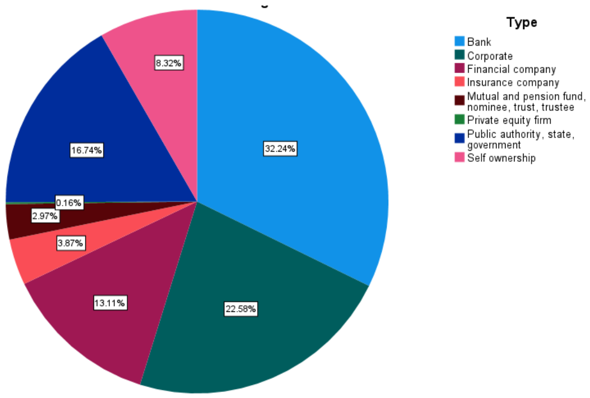

Figure 27 Shareholding of Blackrock Inc

Blackrock Inc (Figure 27) held significant proportions of shareholding in each of the companies within *dataset2.*[54] These range from as low as 2% increasing to 12% throughout the data set. Therefore, the institutional investment company maintains a significant proportion of control in these companies, being the legal owner where beneficial interest is held elsewhere. This increases the separation between ownership and control and further dilutes the financial interest from the control rights. In the group context, this is magnified because further dilution increases as the subsidiaries progress down the hierarchy. This combination of an already diminishing group of rights holders is then further exacerbated by use of funds such as those of Blackrock. Blackrock itself is owned by a majority of further banks, corporate owners, financial companies and public or state bodies.

[54] Excluding EY who operate as an LLP.

The result of this is potential further dilution, such as funds who buy investments through Blackrock. This section has demonstrated that the shareholding of the parent companies within *dataset2* is largely held by those who hold the shares beneficially for others. Irrespective of the 'combination' of majority categories, one key theme remains: the majority is held by these types of institutional owners for which activism on behalf of its beneficial owners may prove difficult. Moreover, this section has identified that within the categorisation of shareholders, there is a significant number of categories which are not held by specific or named individuals. From the widespread ownership identified, the shareholder-centred approach to corporate governance as the main conceptualisation of the company becomes fragmented.[55]

5.6 Prioritising Stakeholder interests

The data in this chapter supports the argument that growth is intrinsically linked with the use of the corporate group. Moreover, this growth leads to increased power and as such lacks the legitimacy due to the dilution of control mechanisms. A realignment of the of the shareholder primacy doctrine therefore becomes necessary to displace illegitimate use of corporate power. The categorisation of shareholders is more aligned with a representation of society and therefore this justifies greater consideration of stakeholders due to the diminishing individualistic ownership. Stakeholder ownership must, therefore, be better prioritised to support a realignment to re-couple legitimacy with corporate power.

One method of how could be better prioritised is through a more pluralist inclusion model, whereby shareholders and stakeholders' interests are considered on equal footing. This could be achived through a greater voice in the bo ardroom, but ultimately requires a reconcepulaision as to the purpose of the corporation. Presently, section 172 required the board to consider shareholder interests above all else, and they are required to report on this. Increasing stakeholder voices and enforcing report on stakeholder considerations in parity with shareholders will assist in this the departure from the shareholder primacy model as the board would no longer reporting in capacity of 'having regard too' but more

[55] Julian Franks, 'Institutional Ownership and Governance' (2000) 36 Oxford Review of Economic Policy 258.

expressly asserting how they have complied and in what format. In sum, the increased shareholders interest would be through stakeholder voice[56] and mandatory reporting that the board have considered these duties, greater transparency.

This increased consideration of stakeholders affects the power dynamic as it requires directors to consider stakeholders on parity with shareholders and report on such. In doing so, the power is legitimised by the public interest who would be able to enforce their interest. This departure from a 'shareholder first' approach adjusts the power as when faced with decisions, directors may be less oportunistic in their decision making and less self-serving. Presently, few shareholders would object to directors high salarlies, benefits and position provided they are delivering value on their investment. The investment from other stakeholders, such as human capital, cannot be qualified in the same way and as such greater justriiccaitons for certain actions will be required. Therefore, whilst the power main remain in concentrated hands, the way in which it is exercised shifts when departing from a shareholder primacy model as the focus is more on overall value opposed to financial return.

5.7 Summary

This chapter has provided both a qualitative and quantitative analysis of the ownership structures of large corporations and their structural architecture, that is, how these groups are constructed. The purpose of this data study was firstly to demonstrate and support the theory that groups, and networks, are extensive and how this manifests itself in the current market. Secondly, the study shows that shares which are held in parent companies are significantly diluted and diffused. This wide level of shareholding supports the argument away from the shareholder-centred approach, which will be analysed in the subsequent chapter.

The quantitative analysis provided a framework to consider group companies within the largest private and public companies. The patterns identified within this quantitative analysis were only further exacerbated when a qualitative analysis of

[56] Assisted with New Technologies as per chapter 6.

the 10 companies within *dataset2* was carried out. This chapter has identified the key role corporate groups play in expanding corporate power through growth of financial power resulting in managerial power. Moreover, it can be identified that the use of corporate groups occurs in all large company structures, and the use of such structures extends past divisional and jurisdictional reasons.

The statistical analysis shows the clear and consistent relationship between the use of corporate groups and their financial strength. The positive outcome on the regression line supports this theory to the causal link between corporate groups and financial strength. Moreover, what can be identified from the statistical analysis is the omnipresence of large corporations operating within a group. Whilst groups may not be present in all corporations, the data suggests that subsidiaries and related group companies are present in the largest 200 companies, both public and private, in the UK. This is of significance due to the power corporate groups are able to hold, and not being held to the same standard in the group context. The challenges of corporate power and deficiencies within corporate governance are magnified in the group context. Therefore, this widespread use of corporate groups within large corporations merits further consideration.

Within the case studies considered, *dataset2*, the prevalence of corporate groups was further expanded and featured more prominently than the average, which was seen when looking at *dataset1*. One of the features of the modern company which was identified was the commonality of the types of subsidiaries: jurisdictional, divisional and financial. The jurisdictional nature of the companies was present in each of the companies within *dataset2*, and as such, this presents an even further separation. The separation jurisdictionally and the volume coupled with control means there is a greater separation of ownership and control between the ultimate beneficial owners and the subsidiary. This supports the idea that control mechanisms of the subsidiaries may not be in place and that ownership is even further divorced from control. In each of the companies within *dataset2*, the scale and structures of the corporate group were of considerable complexity.

Patterns were also established with respect to subsidiary company ownership, and the majority of companies within *dataset2* were either majority or wholly owned. This is of significance due to the control that the parent company can exert on its subsidiary companies. By maintaining a majority, the parent company can utilise the subsidiary to serve its own means, which is both detrimental to the subsidiary and to creditors.[57] This is one of the challenges of corporate groups identified in the preceding chapter: this chapter establishes this as a common practice amongst large corporations. The ability to utilise this control without adequate legitimisation is not consistent with the theoretical framework which supports the use of limited liability and separate legal personality. The companies within *dataset2* also have their requisite ownership of the ultimate parent company. The analysis of the ownership of the parent company presents some further interesting results. The categorisation of the type of shareholder in the parent companies within *dataset2* demonstrated a further dispersion. The shareholders who were the legal owners of the shares were largely institutional shareholders managing pension funds and investment funds. This shareholding supports the theory for a broader conception of the company due to the wider dispersion of shares being held in large corporations.

This chapter has demonstrated that the use of corporate groups allows for inflated growth which may not otherwise be possible with the ability to utilise subsidiaries. The creation of corporate groups within corporations is prominent in all large corporations, with the creation and interweaving of group structures evidenced in all groups evaluated. Moreover, further analysis from the qualitative research demonstrated greater use of group structures. The large geographical footprint of large organisations, coupled with the close connections through corporate groups, challenges the legitimacy which should be present for companies which wield power.

This is challenging because legitimising power becomes increasingly difficult the more dispersed a group operation is. This presents challenges in the ultimate parent because shareholders cannot engage in activism to ensure compliance within the actions of a subsidiary. This in turn means the power which is held by

[57] Andrew Muscat, *The Liability of the Holding Company for the Debts of its Insolvent Subsidiaries* (Routledge 2016); Blumberg and others (n 16).

large parents and their managers is largely unchallenged, especially in the context of power exercised within a subsidiary. This is significant because the divisions which are separated result in the inability to make meaningful use of activist-control mechanisms. This is further exacerbated by additional layers of dilution by institutional investors.

The data supports growth within corporations and that there is a correlation between group use and growth. This thesis maintains the argument that the use of the group is more than a mere coincidence in that structures result in growth. The concentration of power held with the parent companies affords greater opportunity risk taking which can result in fast short term growth. It is argued that the data supports that arrangement of enterprises within groups affords advantages which further facilitates growth and with growth increased power. The increased opportunism, and ability to control subsidiaries removes control mechanisms which may otherwise have been present but for the group structure. This aligns with the argument of the thesis that the facilation of these groups has resulted in growth groups which has excaserbated the challenges they pose. A corollary of this is that dilution of control for the whole enterprise results in a legitimacy failure. Therefore, the data within this section supports the argument that there is dilution of control mehacnisms and these can stem from complex structural architecture concentrating power and perpetuating the legiitomacy failure.

This chapter has contributed to the thesis by providing a framework as to how the corporate group is constructed. Whilst the wider dispersion of shareholders and a greater dilution present problems of activism, it also provides a justification for a wider social conception due to the ultimate ownership of these large companies. This chapter, therefore, serves two principal purposes: establishing and supporting that corporate groups are present in all large organisations and that they maintain control of their subsidiaries. Additionally, the very nature of the shareholders of the modern corporate group supports a departure from the shareholder-centred approach. Shareholdings are widely held, often through financial institutions, and as such social considerations become more justifiable. Given the large dispersion of shareholding in these groups of companies, the next chapter will evaluate if additional societal conceptions can be applied in the majority-owned subsidiary to legitimise corporate power within the corporate group. It will achieve this by postulating the theory of the firm and propose the parameters for reform.

Chapter 6: Democratising the Corporate Group to Attain Legitimacy

> *'The most effective way to restrict democracy is to transfer decision-making from the public arena to unaccountable institutions: … modern corporations.'*[1]

Thus far, this thesis has focussed on the evolution of the corporate form into the corporate group and how this affects the corporate power within the ultimate parent. The research has argued that the wielding of this power in the context of corporate groups is illegitimate, and the exercising of this is predicated on assumed norms which lack a substantive legal footing. This chapter moves to investigate and propose ways in which legitimacy can be achieved. It does this through analysing the very conception of the corporation, and if the current dominant theory of shareholder primacy truly represents the modern corporation. First, the chapter investigates the dominant theory and how it has reigned supreme for the last century despite challenges from other theories. The chapter considers these alterative theories to ascertain if a new theory could provide legitimacy for corporate power which, to date, is absent in group companies. The chapter argues that legitimacy can be derived from an alternative theory ensuring that those who exercise power have it legitimised. This chapter then provides the parameters for how this theory could be utilised within the modern corporation and how it can be reconceptualised. The chapter evaluates adaptions to current legislation and constitutions, and other forms of support which can be introduced to give corporate managers the confidence to depart from the dominant model. Moreover, in evaluating how social and societal inclusion could be implemented, the chapter considers how new technologies could be implemented to support this process. This chapter considers justifications and frameworks for a realignment of the dominant theory to legitimise power which is currently wielded by groups.

[1] Noam Chomsky, *Profit over People: Neoliberalism and Global Order* (Seven Stories Press 1998).

The need to legitimise through democratic inclusion arises due to the failure of legitimising corporate power. Chapter four emphasises these problems and how they become both magnified and unique in the context of the corporate group. Chapter four argued that the corporate groups are not legitimate for three reasons. Firstly, control is fundamental to corporate power, and given the dilution of shareholders and their respective relinquishment of property rights, control mechanisms on corporate power lack substance. Secondly, the boards of subsidiary companies are not held to the same standards, so breaches of fiduciary duties are inherently difficult to enforce. Thirdly, the use of subsidiaries to serve the means of the ultimate parent the company defies the 'spirit' of the privilege of incorporation where the reality is a single economic unit. The preceding chapter, chapter five, made two significant observations. The first was that the use of corporate groups is widespread, and this supports the theory of corporate groups as an economic reality. Secondly, the chapter argued that the shareholders of large corporations are so widely dispersed that the shareholder primacy model becomes less persuasive as the dominant theory. This is due to identifying beneficial interest holders being inherently complex. The result is that the role of shareholders becomes less important, and this provides support for the argument of realigning the theory of the firm with the practical realities of the firm.

This chapter builds on the preceding chapters to provide some parameters of how the challenges and problems identified could be mitigated. Chapters three and four presented the argument that corporate power is ubiquitous within the corporate group, and the current controls are inadequate. This inadequacy has arisen from the historical evolution which has permitted corporate features to be extended to groups without sufficient debate or consideration. This chapter seeks to contribute to the thesis by considering how the realignment of the theory of the firm could address the inadequacy highlighted. It aims to consider how the conceptualisation of the firm can be challenged and if reconceptualisation is possible. Moreover, this chapter will evaluate the parameters of a more social conception of the corporation and how this might be achieved. One method of achieving greater stakeholder democracy within the corporation is to include this through new technologies. The chapter will explore how this may be implemented, with one significant consideration being the use of artificial intelligence and blockchain technologies.

The chapter is structured as follows: first, the chapter considers the dominant theory of the corporation. This evaluates how it became the leading theory and how it has been defended. It then proceeds to assess if this dominant theory serves the economic reality of the modern corporation. The chapter then discusses how governance failures have resulted in the legitimacy crisis within the corporate group. Having considered the deficiencies with the dominant theory, alternative theories of corporate conceptions are evaluated. The chapter analyses whether either alternative theories evaluated can provide greater legitimacy to corporate groups than the dominant model. The social conception of the corporation is then discussed to study how such a broad conception can be adopted. This leads to an analysis of 'social', and how it could be defined and achieved. Having considered the dominant model, and its deficiencies and alternative models to mitigate for these, implementation methods are considered. New technology is introduced as offering the tools to allow directors to implement an alternative conceptualisation model. New technologies provide the capacity to collect and process large data sets, making a more democratic corporation feasible. The chapter then moves to assess how legislation and regulation can facilitate an alternative conceptualisation, and the use of technology to achieve them. The chapter concludes by evaluating challenges to the proposals made and if they are unsurmountable or if these challenges can be mitigated to support implementation.

6.1 The shareholder-centred approach

This section will proceed to consider what the dominant theory of the corporation is and how it has reigned supreme since the inception of the company. This links directly to the objective of the chapter to reconceptualise the theory of the firm. The foundations of the current leading theory must be explored to enable them to be challenged. The deficiency of the dominant theory has resulted in the pursuit of profit which has in turn, contributed to significant failures of governance, resulting in economic and environmental damage. This section will proceed to define what the shareholder approach is, and the considerations of this theory of the firm. The section will then consider how it became the dominant theory of the firm, and why it has become so enshrined within corporate governance. Finally, the section will go on to consider why this approach has been defended as the leading theory. This will provide a framework to compare and contrast with other theories of the firm to ascertain if realignment from this dominant theory is feasible.

6.1.1 Defining the shareholder-centred approach

The shareholder-centred approach or 'shareholder primacy' theory of the firm dictates that the firm is to be run in the interests of the members. The shareholder primacy model is the leading theory.[2] This can be seen as an extension to the traditional partnership model whereby the partners or co-owners carry on a business for profit. The difference is that in the limited company, there is a division of management and ownership whereby the roles may be held by different people. In the context of the limited company, the directors will therefore seek to return profits to shareholders, as they are considered to be the owners of the corporation. This is as they are the residual claimants of the company. In the UK, there has been a codification of this principle within the Companies Act. The statute provides guidance to the directors as to how they are to discharge their duties. It states that 'a director of a company must act in the way … for the benefit of its members as a whole'.[3] This provides a clear and codified directive that the directors must act in ways which favour the shareholders, the members. Conversely, Stout argues that no such provision has ever existed in the USA, and that this inclusion provides for a shareholder's paradise.[4]

This doctrine has been developed through the common law prior to its codification within the statute. In *Hutton v West Cork Railway Company*,[5] Bowen LJ opined, 'The law does not say that there are to be no cakes and ale, but there are to be no cakes and ale except such as are required for the benefit of the company'.[6] In

[2] Elisabet Garriga and Domènec Melé, 'Corporate Social Responsibility Theories: Mapping the Territory' (2004) 53 Journal of Business Ethics 51.
[3] Companies Act 2006 s 172.
[4] Lynn A Stout, *The Shareholder Value Myth: How Putting Shareholders First Harms Investors, Corporations, and the Public* (Berrett-Koehler Publishers 2012).
[5] *Hutton v West Cork Railway Company* (1883) 23 Ch D 654.
[6] ibid 673.

Parke v Daily News,[7] there were ex gratia payments; however, the court held that these will only be valid if they are for the benefit of carrying on the business and to promote the business. These cases are analogous to the wording in the 2006 Act where the position is that any other considerations of stakeholders are subservient to those of the shareholders. The common law and the statute, therefore, make it clear that shareholder primacy is the dominant purpose, and directors must discharge their duties in ways which benefit the shareholders.

In addition to this history and the derived statutory provisions above, there has been extensive academic debate as to the theory of the firm, as this chapter will demonstrate. Writing in 1970, Milton Friedman introduced his Friedman doctrine, where he claimed that the social responsibility of business is to increase its profits.[8] This is justified on the basis that this differs from partners or an individual proprietor, as if they chose social responsibility, it is their money they are spending and not someone else's.[9] Friedman is therefore advocating that corporations must focus on returning the maximum investment return, dubbed 'shareholder maximisation'.

Therefore, what can be deduced from the above analysis is that shareholder primacy is keeping the interests of shareholders above any other party, including the officers of the company. There appears to be an emphasis within this definition that the way to achieve this preference is through delivery of profit, 'shareholder wealth maximisation. This emphasis is disingenuous: whilst many shareholders invest for return, this need not be their only intention. Voting rights remain important within this model; shareholders preferences can be exercised through more than return of profits, and they can be achieved through voting rights. Therefore, the definition of shareholder primacy extends further than shareholder wealth maximisation, as it encompasses an element of control in the corporation.

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[7] *Parke v Daily News (No.1)* [1961] 1 WLR 493.
[8] Milton Friedman, 'A Friedman Doctrine: The Social Responsibility of Business Is to Increase Its Profits. A Friedman Business Doctrine' (*New York Times*, 1923 – Current file, New York, N.Y., 13 September 1970) <https://www.proquest.com/docview/117933451?accountid=10792&parentSessionId=DI71KmQxaqB%2FL4JGBScmExL6MyN6CHiqUHTV225mVeo%3D> accessed 15 March 2022.
[9] ibid.

6.1.2 Development as the leading theory

The shareholder primacy model has reigned supreme as the dominant theory of the corporation for the last century. Whilst, as identified above, there is now a legal basis on which to consider shareholders as having a preference, this leading theory has been through an evolution. The example of directors discharging their duties for the benefit of the members was cited above; however, it is important to note that duties are not owed to shareholders but to the company itself.[10] This nuance is important, as it rebuts arguments of the directors being the agents of the shareholders. Whilst agency in this context may not be express, the development of the theory has arisen due to this relationship and previous considerations of agency. The question of agency arose in *Automatic Self-Cleansing Filter Syndicate Co v Cuninghame*,[11] where members sought a course of action from the directors. The court upheld that the directors are not agents of the shareholders and are only bound so as far as the constitution provides for. In *Shaw & Sons (Salford) Ltd v Shaw*,[12] the court agreed that directors' actions could not be overridden by a mere resolution of the shareholders. The key feature is that the power to run the company is vested in the managers and if managers were agents of the shareholders, as principles, they could instruct them to carry out specific tasks. Therefore, despite it being clear that managers are not the agents of shareholders, the contention within the case law suggests that this is the perceived reality, even if it does not match the legal one. This historical confusion as to the role of directors and the shareholders sets the scene for the shareholder primacy model. Directors consider themselves obliged to act in the interests of the shareholders, and it is argued that this finds it origins within the principles of agency.

This concept of ownership and control is one of Anglo-American design, and the features of determining the interests of shareholders proved equally problematic in the USA. This is best demonstrated by the case of *Dodge v Ford Motor Co*,[13] where the claimants brought an action to force the defendant to pay a more substantial dividend. This appears to be the classic example of shareholder

[10] Companies Act 2006 s 170 (1). See also, *Foss v Harbottle* (1843) 2 Hare 461.
[11] *Automatic Self-Cleansing Filter Syndicate Co v Cuninghame* [1906] 2 Ch 34.
[12] *John Shaw and Sons (Salford) Limited v Peter Shaw and John Shaw* [1935] 2 KB 113.
[13] *Dodge v Ford Motor Co 204 Mich. 459.*

maximisation whereby shareholders demand a return on their investment. The consideration for withholding some of the capital earnings was to reinvest in the company and consider humanitarian activity. This was not well received by the shareholders who sought to have these considerations reversed and a larger dividend paid on their investment. The outcome in *Dodge* was that an arbitrary refusal to distribute to stockholders was not valid, and dividends plus interest should be paid to the shareholders. This is a significant ruling which affirms the importance of shareholder primacy and wealth maximisation. This builds on the historical basis of the confusion of agency in considering that the shareholders are the primary beneficiary of surplus proceeds. Furthermore, a significant judgment such as this set a precedent and provided guidance to corporate managers to ensure shareholders rank first in their considerations.

Berle and Means[14] identified that this separation of 'ownership' and control was increasing, predicated on business norms before the introduction of codified principles. They argued that in the early stages of the company, key features could have been established through contract, which would have provided greater control. They provided an analysis as to the theory of the firm and considered in whose interest the corporation should be run, stating that this was 'the greatest question'. The argument presented is that the logical answer is that if the shareholders receive the profits, the corporation should be run in their sole interest. Berle and Means identified the potential problem within this position, and this was the concept of property ownership. They argued that the concept of traditional property ownership does not apply in the modern corporation due to the surrendering of the investor's wealth. According to Berle and Means, the result is that this is more akin to supplying capital and taking on a risk, which in turn renders a different outcome to traditional property rights. The outcome of this separation, however defined, is two distinct parties: those who 'own' the corporation and those who 'control' the corporation. The analysis from Berle and Means highlights the growth of this separation, and with this growth came a greater need to ascertain the owners of the corporation.

[14] Adolf Augustus Berle and Gardiner Means, *Modern Corporation and Private Property* (Macmillan 1932).

Moore maintains that there are two legal dimensions of the shareholder primacy doctrine: shareholder status as the ultimate collective beneficiary of the duty of loyalty and the intervention rights and control through voting.[15] To this end, Moore argues that s 172[16] is simply a codification of the previous terms, and the express wording of s 170 (4)[17] supports this by the wording within the provision. This is supported when cases such as *Hutton* and *Parke* are considered. The importance of this is that there appears to be a duty of loyalty, which is analogous to the shareholders' money argument. The directors feel a loyalty to the shareholders, as it is their capital they are managing and as such will have them first in mind when considering discharging their duties. Furthermore, in addition to this more passive 'duty of loyalty', there is the reality of intervention rights where shareholders can intervene. This chapter has touched upon the 'shareholders paradise' whereby shareholders can hold meetings and remove directors should they be underperforming. This has the capacity to instil some more direct pressure on corporate managers to act in favour of those who can ultimately remove them from office.

Therefore, the development of the approach has been due to three primary considerations: firstly, the concept that shareholders own corporations. This can be determined by the stock in which they buy and the capital invested, the 'shareholders money' claim. Secondly, shareholders are residual claimants, as per the argument in *Dodge*. They are entitled to surplus capital in the form of a dividend. Thirdly is the assumption that directors are agents of the shareholders and the directors must act in their interests as the principle. This was evidenced from the cases of *Hutton* and *Parke*: even this mistaken belief could result in indirect behaviour in favour of the shareholders. The historical development and the separation of ownership and control has further emphasised the importance of the need to appease shareholders. The managers endeavour to run the company in the interests of the 'owners' irrespective of broader considerations. This development and continued expansion of the principle[18] has rendered the shareholder primacy model the dominant model, which has become the standard

[15] Marc T Moore, 'Shareholder Primacy, Labour and the Historic Ambivalence of UK Company Law' in *Research Handbook on the History of Corporate and Company Law* (Edward Elgar Publishing 2018).
[16] Companies Act 2006.
[17] ibid.
[18] Expansion into the statute, its 'codification'.

which most corporations consider to be the purpose of the company. The next section will move to consider the justifications for adopting this theory of the corporation.

6.1.3 Defending the shareholder-centred approach

The preceding sections have evaluated both a working definition of the shareholder primacy model and its development since its initial introduction. This section will proceed to consider the factors which have facilitated the development of this model, which have rendered it the dominant theory of the firm. This will, in turn, allow the subsequent sections to question the applicability of the dominant model to ascertain if other theories will result in greater legitimacy for corporate groups.

One of the fundamental concepts which has permitted the shareholder primacy model to dominate is the development of forms of business. Whilst, as chapter two illustrated, corporations have been used since the 18th century, the levels of use today differ significantly from the initial corporation. This presents two primary justifications and defences for the shareholder primacy model: the first is the conversion of businesses from partnerships and sole traders into corporations, and the second is investment from shareholders who seek returns on their investment. The increase of the corporate form has experienced significant growth over the 19th and 20th century, with the use of partnerships and sole traders decreasing.[19] This change of business format has resulted in a more widespread and broad use of the corporation. The result of this is inherited norms from alternative business formats such as sole traders and partnerships. These were essentially to carry on business to make a profit. This concept of profit making is analogous to the shareholder wealth maximisation concept within the shareholder primacy model. These social norms of what partners or business owners may expect has been a driver of the profit maximisation; it is what would be expected and as such, is what directors will seek to achieve. The purpose of business, and the corporation in this example, is to derive profits for those who have invested, those akin to partners. This is well identified and categorised by

[19] See chapter 2.

Friedman, where he introduces his doctrine. The development of the corporation has, therefore, partnership norms embedded within the purpose of the corporation, which has resulted in greater importance being applied to the ideology of ‘making a profit.

The second primary argument favouring the shareholder-centred approach is that the directors are managing the ‘shareholder’s money’ and the company should be run solely in their interests. The concept of the shareholders’ money argument dictates that any policy other than profit maximisation takes wealth from the shareholders, which is itself morally improper.[20] This links to the social norms which have developed through the traditional concepts of business. The shareholders are perceived to be entitled to residual beneficiaries, in that surplus capital is returned to them by way of dividend. In this regard, spending this capital on profit-sacrificing endeavours would be contrary to the interests of members, and taking income which they are entitled to. The basic concept with the shareholders’ money argument is that as providers of capital who are entitled to dividends, expenditure which does not maximise their interests is not action which ought to be taken.

In addition to these primary justifications for the dominant position of shareholder primacy conception, Parkinson contends there are two further reasons why this theory has arisen as the leading theory.[21] The first is the ‘efficiency’ argument, which dictates that investment in alternative social purposes at the expense of shareholders could make investment unattractive. If investment in the company is unattractive then stock prices could be affected, which is detrimental to shareholders and opens the company to takeover. The concept of this argument is that expending capital on more social purposes could ultimately render the company less desirable to investors. This argument feeds into the idea that shareholder wealth maximisation is of paramount importance and that damage to share price should be avoided. The second concept Parkinson puts forward is the ‘difference’ argument. This is where a clear division of private and public forums are introduced. The argument is that a company is a private entity, and

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[20] John E Parkinson, *Corporate Power and Responsibility: Issues in the Theory of Company Law* (Oxford University Press 1993) 309.
[21] ibid.

therefore, its focus should be fixed on what is agreed between private parties. In the context of capital expenditure for a public purpose, this should be paid for by public bodies and authorities, not private individuals or organisations. This further supports the shareholder wealth maximisation theory by suggesting that private capital should remain in the hands of private individuals in line with the constitution and purpose of the company.

This section has defined the shareholder primacy/shareholder-centred approach whereby the shareholders maintain the right for the company to be run in their interest as ‘owners’. The section has also provided some analysis as to how this approach has developed as the leading theory and the reasons behind this. Finally, it has considered why the approach has been defended as the primary theory and its justifications. This has provided a framework for the subsequent analysis to consider realignment of this theory. This includes a stronger emphasis on societal attributes to attain greater legitimacy for the power corporate groups wield. This will be the focus of the next section, to consider how a departure or realignment from this theory could be achieved and justified.

6.2 Realignment of the dominant theory?

With the dominant theory identified, this section looks to challenge the acceptance of the shareholder primacy approach. The section will consider the failures of the theory, investigating why it may be problematic, specifically in the group context. Moreover, it will consider how shareholders become increasingly difficult to ascertain in the modern corporation. The section will link to the data study in chapter five to outline that the theory is not representative of the modern corporation, and the economic reality does not align with the corporate theory. Following this critique, this chapter will then consider if alternative theories more closely align with the economic reality of the group and if these alternative theories can provide greater legitimacy for the corporate group.

6.2.1 Systematic failures of governance

The failures of corporate governance are the most significant challenge to the acceptance of shareholder wealth maximisation. Ireland has described shareholder primacy as:

> a shareholder's paradise: a body of law able to combine the ruthless pursuit of 'shareholder value' without any corresponding responsibility on the part of the shareholders for losses arising out of the corporate failure or the damage caused by corporate activities or malfeasance.[22]

The argument here arises due to the myth of shareholder ownership: there is no ownership in the traditional sense and the structure in place to support this model encourages short-termism within corporate. The problem is that shareholders are more like bondholders than owners and are considered outsiders instead of insiders. The argument here is that it is possible to attain the best of both worlds. Shareholders can have the company run in their interests, for short-term profits, without suffering the consequences of longer-term actions. This is analogous to the arguments put forward by Stout, who argued that there are many examples where this problem affects corporations.[23] One example given is the Deepwater Horizon disaster, which resulted in significant environmental and economic damage including the loss of life. In this infamous example, cost-saving measures were carried out, which resulted in the disaster. The short-term gain was a larger bottom line; however, the longer-term effects resulted in far greater costs than would have been required if safety measures were correctly carried out. The VW emissions scandal was another example of focusing on short-term results, the sale of more cars. The ultimate long-term effects were detrimental to the company. The focus on short-termism is therefore resulting in failures of governance predicated on the need to deliver a return for shareholders. Contextualising this into the corporate group, the greater the emphasis on shareholder value, the greater the need for corporate managers to exercise their power to benefit the shareholders. With shareholder wealth maximisation at the centre of policy decisions, a greater need for legitimacy arises to ensure accountability.

[22] Paddy Ireland, 'Limited Liability, Shareholder Rights and the Problem of Corporate Irresponsibility' (2010) 34 Cambridge Journal of Economics 837, 848.
[23] Stout (n 4).

6.2.2 Enlightened shareholder value

The Companies Act of 2006 introduced the enlightened shareholder value.[24] This concept was to include a wider group of stakeholders in the decision-making. The deficiency here is in the provision's wording and its inability to usurp the shareholders in their right to wealth maximisation. Moreover, Lynch argues that this provision is a codification of the common law principles to promote the success of the company, but in its introduction, it weakens the position of shareholders.[25] The provision requires directors to 'have regard to' additional considerations when discharging their duty to promote the success of the company. Listed within this provision are wider stakeholders such as suppliers, customers and employees, and in addition to this, the environment and longevity are all to be considered. Whilst this prime facie, appears to provide and indeed advocate for a more inclusive spectrum of stakeholders, the reality is somewhat different. The criticism of the provision is that there remains an emphasis on 'have regard to' with the focus being on the members. Therefore, directors should only consider other facts insofar as they will benefit the members as a whole. Given the preceding discussion on shareholder wealth maximising, directors are unlikely to utilise capital to benefit employees to the detriment of shareholders. A recent example of the power of shareholder wealth maximisation was seen in FirstGroup.[26] Shareholders who were not content with the sale of part of the business sought to pressure the executive board to resign. This was directly because of shareholders believing a better deal could have been attained. The chief executive stepping down due to this pressure demonstrates the significance of shareholder wealth maximisation and that despite sustained efforts, shareholder interests remain unchallenged as the primary consideration. Lynch contends that the reality of the enlightened shareholder could result in the opposite of what was intended. In providing wider considerations, this could provide what Lynch dubs a 'get out of jail free card' whereby directors can justify alternative behaviour.[27] In this regard, the directors could utilise this provision to

[24] Companies Act 2006 s 172.
[25] Elaine Lynch, 'Section 172: A Ground-Breaking Reform of Director's Duties, or the Emperor's New Clothes?' (2012) 33 Company Law 196.
[26] Bryxe Elder, 'FirstGroup chief executive bows to investor pressure and resigns' (*Financial Times*, 27 July 2021) <https://www.ft.com/content/8b9917a3-82d3-479a-85aa-505fd51d5868> accessed 27 June 2021.
[27] Lynch (n 25).

justify a departure for which in turn the shareholders would have difficulty in pursuing action for breaches of duty. This paradox presents the position whereby the control mechanism can be avoided by utilising a provision which in and of itself is inherently flawed. Therefore, whilst the enlightened shareholder value approach has demonstrated appetite for a wider consideration, the reality is that 'having regard to' does not result in wider considerations. The shareholder-centred approach thus reigns, and the enlightened shareholder value has failed to attain any significant change.[28]

6.2.3 Systemic focus on short-termism

Short-termism is broadly defined is making quick decisions for the immediate benefit at the expense of longer-term best interests. Professor Kay describes this behaviour as 'myopic behaviour [that] is the natural human tendency to make decisions in search of immediate gratification at the expense of future returns: decisions which we subsequently regret'.[29]

The pressure to focus on short-term results in the corporate context increases this myopic behaviour. The systemic focus on short-termism supports an argument in favour of realigning the dominant theory. It is predicated on the basis of shareholder wealth maximisation and can be detrimental to the company itself and society more broadly. Short-termism is the focus on short-term returns irrespective of longer-term consequences. The pursuit of short-term gains to appease shareholders is often at the expense of sustainability and has tangible environmental and social costs, as can be observed from the Deepwater Horizon oil spill. The challenge of short-termism is particularly problematic due to the separation of ownership and control: those who control the company are focussed on returns from investment. This is pertinent as if the corporate managers do not focus on returns, their position is under threat, as was the case with FirstGroup, as discussed above. Parkinson contends that the problem of short-termism is only further exacerbated by the introduction of performance-

[28] See: David Milman, 'Stakeholders in Modern UK Company Law' [2017] Company Law Newsletter 1; Moore (n 15).
[29] John Kay, *The Kay Review of UK Equity Markets and Long-Term Decision Making* (Gov.uk Final Report, 2012) 14.

related pay.[30] The argument is that by focusing on shareholder wealth maximisation, which will prevent removal from the board and provide some security of office, the executive directors can now profit directly. The data analysed in chapter five supports this, as directors of large organisations receive a significant proportion of their salary through share schemes interlinked with performance-related pay. The result is short-termism, which is dictated by the very conception of the firm, and shareholder wealth maximisation is enhanced by performance-related pay. The executives of the company, therefore, have dual incentives to provide short-term returns for their own financial benefit and for shareholders who demand such a return.

This focus on short-termism has received significant scholarly and more widespread criticism. Parkinson has claimed that short-termism is a disease.[31] The recent corporate scandals and mismanagement which have occurred over the last two decades since Parkinson's claim suggest that this disease is starting to permeate. In the early 2000's, clients of Arthur Andersen – both Enron and WorldCom – collapsed into bankruptcy,[32] , ultimately resulting in the demise of Arthur Andersen. This is a significant example with accounting practices, as the auditor itself collapsed. Arthur Andersen was one of the 'Big Five' accounting firms at the time, which demonstrates the reach and commonality of creative accounting reporting. More recently, following the collapse of the global bank Wirecard, their auditors Ernst & Young have come under the spotlight for the clean bill of financial health issued. There are parallels between the scandal with Enron and Wirecard:[33] this has led to increasing pressure to break up the 'Big Four' and review auditing practices.[34] This is supported by Bowdren,[35] who identifies the importance of maximising long-term value and that there ought to

[30] Parkinson (n 20) 115.
[31] ibid 136.
[32] These companies were MNEs based in the USA: the term bankruptcy denotes the procedure followed in this jurisdiction.
[33] At the time of writing, a full report on the collapse of Wirecard was not finalised.
[34] See: Jonathan Ford, 'After Wirecard: Is It Time to Audit the Auditors?' (*Financial Times*, 3 June 2021) <https://www.ft.com/content/b220719a-edca-4ebf-b6bc-5f7a67078745> accessed 27 June 2021; Tabby Kinder, 'Regulator Outlines Plans to Break Up Big Four Accounting Firms' (*FT.com*, 07/02/2020) <https://www.ft.com/content/1ddf7430-5987-11ea-a528-dd0f971febbc> accessed 27 June 2021.
[35] Andrea Bowdren, 'Contextualising Short-Termism: Does the Corporate Legal Landscape Facilitate Managerial Myopia?' [2016] UCL Journal of Law and Jurisprudence 285.

be a greater emphasis on reducing short-termism for which the regulator should evaluate.

This subsection has considered the focus on short-termism and the failures which can result because of this focus. Short-termism is the product of the shareholder-centred approach, which has further developed over time. Realignment or reconceptualising the theory of the firm will mitigate for some shortfalls of short-termism. Whilst there is no legislative requirement for short-term decision-making, it has become the default position. This is despite the fact the opposite is mentioned with the Companies Act. This short-term nature is a result of market pressures and institutional investors seeking quick returns. Considerations of wider stakeholders and correlative consequences are likely to organically reduce the impact of short-termism and progress in curing ‘the disease’.

6.2.4 Asymmetric information

The dominant approach is constructed upon the notion of returns for shareholders and their wealth maximisation. This separation of ownership and control results in significant power being wielded by corporate managers.[36] The legitimacy of this power is derived from control mechanisms and checks being in place. In the context of the corporate group, the difficulty of transparency renders these checks and controls more difficult to exercise. In this context, the lack of available information is a legitimacy failure that asymmetric information contributes towards. Corporate managers possess far greater knowledge than shareholders, and by selectively distributing such knowledge, puts shareholders at a disadvantage when exercising their rights. This is magnified in the corporate group, where shareholders of the parent company are unlikely to be privy to information and the workings of subsidiaries further down the chain. This level of imbalance between information results in a failure of the shareholder primacy due to the inability of shareholders to exercise their votes, specifically in respect of wholly owned subsidiaries. In this regard, corporate managers are able to isolate parts of the business and shield it with opaque transparency of knowledge. There are, of course, genuine reasons for corporate managers to not to release

[36] See chapter 4.

sensitive data on a wholesale level to ensure they can remain competitive in the market, and indeed to comply with directors' duties. One control mechanism for information transparency is the use of auditors to check financial records, including group accounts. There are, however, inadequacies in the auditing process and these are well known, such as the examples of Enron and Wirecard as discussed above.[37] Moreover, Sikka argues that even with intensive auditing, accounting policies can distort the picture.[38] It is submitted, therefore, that shareholders who do exercise their vote may often be doing so premised on false, inadequate or out-of-date information, based on the problem of asymmetric information. This problem becomes more prominent in the corporate group where the relationships between companies is complex, and the shareholders are reliant on information presented to them. This is a failure of one of the very mechanisms which is there to support shareholder primacy, in that shareholders have an ultimate say on corporate strategy and behaviour. The lack of transparency and that of available data supports the realignment of the dominant theory into something which represents the modern corporation.

6.2.5 Failure of capital market

The capital market is central to the shareholder primacy model, as satisfied shareholders are likely to retain shares, whilst those who are not satisfied are likely to dispose of them. A corporation with significant rates of disposal could indicate to the corporate managers that shareholders are dissatisfied, and this could be reflected in a reduced stock price. The capital market provides an additional corporate governance mechanism, being able to control governance through share pricing. Stokes argues that the growth of the corporate enterprise has shattered the presumption that power is able to be legitimised by a competitive market.[39]

This links to the challenge of short-termism, as the focus on the market, is to allow for increased returns either by increased stock value or return by way of dividend.

[37] A detailed discussion and analysis of auditing is beyond the scope of this research.
[38] Prem Sikka and others, *A Better Future for Corporate Governance: Democratising Corporations for their Long-Term Success* (2018).
[39] Mary Stokes, 'Company Law and Legal Theory' [1986] Legal Theory and Common Law 155, 158.

This problem of short-termism and the separation of ownership and control have changed the way in which business is carried out. This argument is supported by Jensen, who asserts that in shutting down effective capital markets for motivating change, there still remains a reliance on internal control, which is problematic.[40] Internal control relies on corporate managers to evaluate and self-regulate their own conduct given the reduced impact of the market. The market as a governance mechanism should operate to increase good corporate governance; however, the systematic focus on short-term returns has significantly reduced the impact of the capital market as a governance mechanism. This failure is largely due to exit being preferred over voice. The exit right for shareholders is one of the most important rights a shareholder can have: if they so wish, they can liquidate their investment and move on to another if they are not satisfied. This exit over voice has become increasingly prominent, and the effect is that shareholders prefer to exit over engaging in activism. Whilst disposal of shares on a wholesale level might adversely affect the corporation, the reality is that this in and of itself is insufficient as a governance mechanism and greater activism is required. In sum, the focus on short-term returns results in pressure on corporate managers, which in turn renders the capital market as a governance mechanism illusory due to preference of exit over voice.

6.2.6 Shareholder primacy v economic reality

This subsection proceeds to consider how the dominant theory of the firm aligns with the economic and modern reality of the corporation. In smaller corporations where the shareholders and the executive offices are one and the same, or closely linked, the shareholder primacy model aligns with this structure. In the larger corporation this picture is less clear, and it is widely reported that shareholdings within larger corporations are widely dispersed. The data study within chapter five highlighted the wide-ranging shareholder democratic make-up of parent companies. The data study showed that the economy reality is that the category of 'individual' was trivial in these large companies, unless the company was categorised as a family-run corporation. The lack of individual shareholders within the companies in the data set identified a large classification of institutional

[40] Michael C Jensen, *A Theory of the Firm: Governance, Residual Claims, and Organizational Forms* (Harvard University Press 2003) 37.

shareholders for which each would have its own beneficiaries. Shares in the corporations analysed were largely held by pension funds, insurance companies, hedge funds and banks. This wide array of institutions presents its own challenges for the shareholder primacy model. The first challenge is ascertaining what shareholders really want: the focus from a hedge fund may be on short-term gains, whereas a pension fund might see longer-term growth. The challenge this presents is in ascertaining the following: what it is the shareholder's desire, and how can this be achieved through the traditional approach? Utilising one of the key arguments in favour of shareholder primacy, the shareholders' money argument, further analysis can be undertaken. If it is accepted that there is a significant weight attached to the argument of 'providers of capital' and the need to consider these providers, how does this function in the context of institutional investors and corporations?

Institutional investors by their very nature will invest capital on behalf of others, the 'beneficial interest holders'. The analysis in the data study carried out demonstrated that there was not a singular institutional investor in each larger company, in fact there was an average of three to four larger institutional shareholders and the same in smaller holdings. In any event, the largest share held by an institutional investor was circa 5%. Utilising the shareholders' money and providers of capital argument to justify corporate policy presents its own challenges in ascertaining what beneficiaries want, and how they wish for their interest to be used. By way of example, Company X PLC has two large institutional shareholders, both in the 'Bank' category. If one of these banks is Barclays PLC and the other is Triodos Bank, the interests of these two intuitions are diametrically opposed. This is a hypothetical example, and the reality is that a bank such as Triodos, with its focus on sustainability and ethical banking, and Barclays would have different capital investment strategies. However, in the case of other institutional investors this problem becomes exaggerated. Hedge funds, pension funds and other financial funds manage the beneficial interests of thousands of members. The USS,[41] for example, has half a million members who contribute to the fund which is invested. Hargreaves Lansdown, a popular hedge fund company, invests on behalf of 1.5 million clients. This is a significant divergence of interests. Given that the data study shows that often there are

[41] The largest pension scheme by asset value.

between 5 and 10 institutional investors by category, and in each category multiple types of fund, the number of small and trivial interests is overwhelming. The applicability to the shareholder primacy model, when viewed through the lens of the shareholders' money defence, becomes significantly weakened. Identifying such a vast array of differing interests where alignment of a majority may be seemingly impossible presents a significant challenge. The reality is that acting in the best interests of shareholders and putting their interest to the fore is misplaced, as the shareholders' interest has become so difficult to define. The shareholder wealth maximisation lens as a defence is equally problematic. Short-term investors will seek wealth maximised on a short-term basis where long-term investors such as pension funds may seek longer-term benefits. Where there exists such a diffusion of interests, ascertaining what is in the best interests of shareholders becomes inherently problematic. This is the case for two substantive reasons, identifying what is 'best' is challenging depending on the type of investor, and secondly, identifying the shareholder or ultimate beneficiary[42] is equally difficult. The result is a corporate managers and short-termist paradise where increased profits and returns demonstrate 'a good job' despite potential damage through the long-term environmental or societal costs.

This section has worked through justifications to consider a departure and realignment from the dominant theory analysed in the first section. It evaluated the failures of governance which have occurred due to the dominant model being utilised. The introduction of enlightened shareholder value was also critiqued and it was concluded that the theory did not match the reality of the introduction. Moreover, the focus on short-termism as a result of shareholder wealth maximisation has the capacity to be at the expense of the long-term interests of the company, which is contrary to promoting its success. Furthermore, asymmetric information and the capital market do not function with control mechanisms for this governance method, which undermines its credibility. The section then considered the economic reality, looking at how the modern corporation is structured. The result of the data study suggests that shareholders are widely diffused and even further dispersed in the context of institutional investors. This in turn advocates for a realignment of the dominant theory. The shareholder-centred approach functions where there are a small number of

[42] The providers of capital.

shareholders, akin to a partnership; however, with a wide dispersion of shareholders, identifying what is best and who they are destabilises the acceptability of the approach. The next section will move to consider alternative theories of corporate law, asking, how else could the corporation be theorised? This will then allow the subsequent section to explore alternative theories to legitimise the corporate power that group companies wield.

6.3 Alternative theories of corporate law

The preceding sections have analysed the dominant theory and the challenges it presents in the context of the modern corporation and within corporate groups. Whilst this shareholder-centred approach has remained the dominant theory over the last century, there have been alternate theories which have challenged it. This chapter will proceed to consider how alternative theories could address the legitimacy failure of corporate group power. This section will therefore consider alternative theories which may have the capacity to attain greater legitimacy and more closely represent the modern corporation. The shareholder-centred approach has not been the singular theory over the last century, and the theory of the firm has been long debated in the context of what purpose the corporation serves. This section will explore the additional theories of two main challengers to the dominant theory, namely the nexus of contracts theory and the social conception theory. The objective of exploring these additional theories will demonstrate that although there is a dominant theory, there are alternative theories which have been proposed. Moreover, the shareholder primacy model, whilst dominant, is not a settled and undisputable theory. This in turn will provide a framework for the research to consider an alternative theory to support the overarching aim of the thesis.

6.3.1 The nexus of contracts theory

The nexus of contract theory differs from the shareholder-centred approach, as it refuses to consider the company 'a thing'[43] the same way the shareholder primacy model does. The shareholder primacy model dictates that the company

[43] For example, a juridical person.

as an incorporated entity must act to maximise the shareholders' utility. In contrast to this, the nexus of contracts model, or the contractarian model, refuses to acknowledge the company as an entity. This theory of the firm dates to 1937 with the seminal work of Ronald Coase entitled ‘The Nature of the Firm’.[44] Coarse was an economist who identified that economics has no positive theory as to the bounds of the firm. Furthermore, these bounds, he argued, were a range of exchanges over which a suppressed market was used for authority and exchanges. Alchian and Demsetz consider that the notion of the role of governance is not governed by the authority and exchanges identified by Coarse. They object to this concept of authority and contend that the role of contracts is for voluntary exchange.[45] The focus of their argument is on joint input production where one party is common to all the contracts of the joint inputs.

Evolving from this historical theorising of the firm, Jensen and Meckling developed the leading literature on the nexus of contracts,[46] building from Coase, Alchian and Demsetz. Jensen and Meckling sympathised with Alchian and Demsetz and their perception of team production; however, they conclude that it is too narrow. They argue that only a small fraction of the behaviour of individuals can be explained by joint production. It is within this paper that Jensen and Meckling proposed the popularised definition of the nexus of contracts. They claim the following:

> It is important to recognize that most organizations are simply legal fictions which serve as a nexus for a set of contracting relationships among individuals …. By legal fiction we mean the artificial construct under the law which allows certain organizations to be treated as individuals.[47]

Jensen and Meckling build on the argument from Coase, Alchian and Demsetz to argue that the corporation is a mere fiction which serves as a nexus for contracting relationships. The focus of this definition is not on determining those who are inside and outside the firm, but on objectively understanding the function. Furthermore, they claim that asking questions around areas such as ‘behaviour’

[44] Ronald Coase, ‘The Nature of the Firm’ (1937) 4 Economica 386.
[45] Armen A Alchian and Harold Demsetz, ‘Production, Information Costs, and Economic Organization’ (1972) 62 The American Economic Review 777.
[46] Michael C Jensen and William H Meckling, ‘Theory of the Firm: Managerial Behavior, Agency Costs and Ownership Structure’ (1976) 3 Journal of Financial Economics 305.
[47] ibid 311.

and ‘social responsibility are misplaced and dubbed an error by Jensen, because they are not persons with motivations and intentions. The definition of a firm is offered thus: ‘the firm is a “black box” operated so as to meet the relevant marginal conditions with respect to input and outputs, thereby maximising profits, or more accurately, present value’.[48] This black box is facilitative and provides a platform to transaction, which through contract law alone costs would increase. The use of this theory reduces agency costs as ‘norms’, and standard terms can be achieved without extensive negotiation. This reduction of cost to achieve optimal outputs is in line with one of Kraakman’s objectives of corporate law, to reduce agency costs.[49] Jensen claims that the nexus of contracts theory allows us to dispel the tendency to treat corporations as if they were persons.[50] The nexus of contracts theory as described by Jensen is a platform for individuals to conduct transactions based upon their negotiating position. Writing in 1985, Easterbrook and Fischel, in discussing limited liability, agreed with the definition set out by Jensen and Meckling.[51] Easterbrook, in defining limited liability, considers the ‘limited’ nature by the fact that the corporation is not real. The claim is that the corporation ‘is no more than a name for a complex set of contracts amongst managers, workers and contributors of capital’.[52] One example used by Easterbrook is that of a bank, claiming that if a bank loans $100 to a company, its liability is for the $100 loaned and this is the most they could lose, which is the same as shareholder or provider of capital. The argument is put forward that limited liability reduces the cost separation between assets of those contracting.

The nexus of contracts theory therefore dictates that the corporation is not an entity and is not capable of exercising rights itself: it is merely a way of exercising the rights of those contracting through the black box. Hansmann and Kraakman provide an argument countering this view, stating that the corporation cannot be strictly achieved through contract alone.[53] They argue that organisational law offers solutions where contract law would be unable, and one of these is that of

[48] ibid 308.
[49] Reinier H Kraakman and others, *The Anatomy of Corporate Law: A Comparative and Functional Approach* (Oxford University Press 2017).
[50]Jensen (n 40) 136.
[51] Frank H Easterbrook and Daniel R Fischel, ‘Limited Liability and the Corporation’ (1985) 52 U Chi L Rev 89.
[52] ibid.
[53] Henry Hansmann and Reinier Kraakman, ‘The Essential Role of Organizational Law’ (2000) 110 Yale LJ 387.

asset partitioning. This functions in two ways: one is the traditional viewpoint of the providers of capital, whose own personal assets are not at risk once shares are fully paid up. Hansmann and Kraakman make an additional observation in that corporate assets are also not at risk from the shareholders. Therefore, if the shareholders were to get into financial difficultly, there would be no risk of the corporation's assets being at risk. This provides a level of reassurance for creditors and other stakeholders who contract with the company. Hansmann and Kraakman contend that the asset partitioning is an essential function of organisational law. Furthermore, it should be enabling in its nature to assist contracting parties to contract with one another. Asset partitioning needs to do this with mandatory, as opposed to optional 'rules'. The argument is that organisational law is more akin to property law because the creditors are looking to secure credit against property which is moving and changing which contract could not facilitate, for example, stock. Therefore, the essential role of organisational law is to facilitate this partitioning to reduce contracting costs, which is enabling in nature. Stout also opposes the theory of the firm presented by Jensen and Meckling.[54] She argues that the model which they discuss includes some mistaken assumptions. The key argument presented opposing the nexus of contracts model is that they are natural persons and as such cannot be considered the black box Jensen puts forward. Corporations own themselves, they maintain their own rights, and as such these rights preclude them from being a 'nexus of contracts'.

Therefore, the nexus of contracts theory dictates that the company is not a 'thing' but a black box from which legal persons can contract. This black box provides norms and standard features that support the exercising of rights to reduce the cost of contracting between those transacting. This theory has attracted criticism due to its inability to accept the company as a legal entity which has its own rights and is capable of exercising them. Moreover, it has also been criticised as without organisational law, which does accept the corporation as a 'thing', many features of company law would not exist. Additionally, the ability of the corporation to have its own rights provides security for all stakeholders through the use of standard terms and rights, and this would not be attainable without organisational law. This theory of the firm has consequently received much debate, continuing from

[54] Stout (n 4).

Coarse[55] in 1937 until today.[56] In the context of the corporate group, much of the debate against the nexus of contracts theory is more persuasive. The complexity of group arrangements prevents a platform for contracts from taking place, and the individuality of each subsidiary on multiple levels does not align with this theory. Each subsidiary is a separate legal entity with its own rights, and a contracts model would not function given the relationship between each of these subsidiaries.

6.3.2 The social conception of the corporation

The preceding sections have considered the corporation as a legal entity which promotes shareholder wealth maximisation and the corporation as being little more than a black box to conduct complex transactions. This section proceeds to consider the corporation, which encompasses a more social conception of the corporation that deviates from both theories discussed thus far.

The social conception of the corporation is one which has received several differing definitions. At its narrowest, the definition is that there ought to be a mere social consideration in board decision making and at its broadest is where societal interests take priority. There are several justifications for the use of a more social conception of the corporation. One such justification is that features such as limited liability and separate legal personality are granted by the state, and as such, the use of these rights should be exercised in a way which benefits society more broadly. This proposition is based on the idea that companies should not be able to profit at the expense of the state and society, given that the benefits of incorporation are provided by the state. In this example, the creative tax compliance[57] , which has recently been widespread, would not be compatible with this view of the corporation. Another definition provided by Parkinson and Kelly,[58] is that of a more pluralist 'investment' view of the corporation. The

[55] Coarse (n 44).
[56] See: Richard N Langlois, 'The Corporation is not a Nexus of Contracts: It's an iPhone' in *Institutions and Evolution of Capitalism* (Edward Elgar Publishing 2019); Marios Koutsias, 'Shareholder Supremacy in a Nexus of Contracts: A Nexus of Problems' (2017) 38 Business Law Review.
[57] Anna Donovan, *Reconceptualising Corporate Compliance: Responsibility, Freedom and the Law* (Bloomsbury Publishing 2021).
[58] John Parkinson and Gavin Kelly, 'The Conceptual Foundations of the Company: A Pluralist Approach' (1998) 2 Company, Financial and Insolvency Law Review 174.

argument which is presented within the shareholder-centred approach is that the shareholders are the bearers of residual risk; that is, they could lose their investment. This remains one of the justifications for the shareholder primacy model, stating that as their capital is at risk, the company should be run in their interests so that they do not lose their investment. Parkinson and Kelly present the argument that the pluralist viewpoint rejects the shareholders as the only bearers of residual risk. There is human or social capital which is attached to a company and which will be impacted by corporate decision-making. One example of human capital is an experienced employee who has a specific skill set for very specialist machinery. If the factory is moved, or the company falls into insolvency, then the skills this employee has gained become redundant, and their human capital which has been invested is likewise lost. There are further stakeholder considerations, such as customers who are invested with companies with specialist arrangements. These represent investment but not in the same sense as capital investment by shareholders. The shareholder primacy model would reject this as a type of investment, but the pluralist view considers it to be a valid investment. This pluralist conception is that the two concepts of profit maximising and stakeholder interest do not need to be mutually exclusive. It is possible for the interests to coincide and run together as one to benefit all parties. The argument presented by Parkinson and Kelly is that the aim should be to increase wealth which can serve social welfare, and in doing this there are benefits for both shareholder and stakeholder.

In addition to the argument of human and customer capital investment, another justification for social considerations within the corporation is due to the power held by large companies. This thesis has already discussed how closely held power can be challenging. Parkinson contends that this level of power held by large corporations results in greater bargaining power in the hands of the corporation.[59] His seminal work claims that as a result, corporations should be thought of more as a social enterprise, and he rejects the idea that the argument against interfering in private corporate affairs is indefensible.[60] This concept is an extension of the ‘creature of the state's argument and considers corporations as social entities. This is a strong assertion from Parkinson, as the claim is that all

[59] Parkinson (n 20).
[60] ibid 23.

consideration should be in the social interest of society more broadly. Whilst this appears heterodoxical, it has gained support. Stout contends that the shareholder primacy model is on the brink of intellectual failure and that there is a greater need for a complex evolution.[61] Professor Colin Mayer considers the shareholder-centred model to be misplaced and that there should be a greater emphasis on corporate purpose.[62] The argument presented by Mayer is that the corporation is not a nexus of contracts between the parties to the firm, it is the opposite, if the nexus of relations is based on trust. The social conception of the corporation posits that the public interest requires something more than profit maximisation, and this should be reflected within the law.[63] Moreover, employee and stakeholder interests are not served by the policy of profit maximisation, and the managerial pressure towards this goal is detrimental to the longevity of the company and to stakeholders more broadly.

The term public interest has been used within this thesis, following on from the use of Parkinson in his seminal works on legitimacy. The notion of public interest could be aligned to the 'three P's''; People, Profit and Planet' which have been the focal point of much corporate scholarship over the last half century. In more recent times, the third 'P' has become increasingly significant. Facing a global challenge of keeping the global climate temperature rise below 1.5° has become globally controversial. The understanding of public interest has also substantially developed over the last decade. Therefore, this concept of 'Public Interest' which this thesis advocates for built on the notion of "doing good by doing well". In this regard in addition to the philosophical arguments for social interpretation[64] there is the additional enormous climate change challenge which must also be considered as part of this public interest.

Some scholars have highlighted the importance of fundamentally rethinking what the public interest means. Raworth contents that economic theory must reflect the ecological realities of the 21st century.[65] In order to achieve this she proposes

[61] Stout (n 4).
[62] Colin Mayer, *Prosperity: Better Business Makes the Greater Good* (Oxford University Press 2018).
[63] Parkinson (n 20) 364.
[64] See Section 6.5.
[65] Kate Raworth, 'Doughnut economics' (2nd ed Penguin, 2022)

‘Doughnut’ economics which explore seven ways in which to think like a 21st century economist. Raworth challenges the notion of growth and being motivated by cost of and price arguing that historically, and in some cultures, the concept of living well in nature brings its own value. The use of the earths resources has depleted many of the earths resources and Raworth argues that this is where life imitates art. In this regard the modern economist, and way of thinking has developed from a ‘model of man’ to a ‘model for man’ and this is significant, according to Raworth, because it shapes human nature. This is analogous to the historical point Ireland made about changing terminology in the Companies Act in relation to the formation of a company. In presenting the ‘Doughnut’ in her form of economic model, Raworth argues that there is a safe place to occupy between social foundation and the ecological ceiling. The ‘no pain, no gain’ when exploring the long-term growth is damaging to the doughnut, and indeed to the current climate challenges faced currently. Raworth’s doughnut model presents what she calls a radical new compass for guiding humanity this century. Focal to this economical model is not only fundamental human needs, but the need to not overshoot the ecological ceiling.

Naomi Klein[66] wrote specifically about the challenges of pitting climate against capitalism. This capitalist nature is one Raworth identifies as the pressure on growth, development and profit. Klein claims that many operate in climate change denial despite the fact that it will change everything about our word.[67] Klein presents the argument that the decades of corporate interests have exploited crises and forcing large scale privatisations of the public sphere. Klein is concerned that the climate crises may well be outsourced to the private sector so ‘solve’ which would be catastrophic given the capitalist foundations that corporations are often built on. The focus on the individualist is problematic, according to Klein and a greater collective consideration is required. This appears to challenge the notion of Adam’s smith invisible hand notion. Smith’s notion was prior to widespread economic failure and where wider considerations may not have been considered. This can be especially true, within corporations’ senior managers and leaders may be competing not only internally to retain their post, or seek promotion but also to give their corporation an advantage over

[66] Naomi Klein, *‘This Changes Everything : Capitalism Vs. the Climate’* (London, Penguin, 2014).
[67] Ibid.

competitors. It is this type of individualist focus which Klein seeks a departure from. Klein contends that the reason simple actions are not taken is because of this fundamental conflict within deregulated capitalism. This is the square peg of social responsibility trying to fit through the round hole of capitalism. In the 'battle' between capitalism and the planet, Klein claims that capitalism is winning hands down. According to Klein a different strategy is needed and a climate revolution is required.

These two perspectives from Klein and Raworth have made their way formally toward the policy agenda. The recent proposal by the EU, a Directive on corporate sustainability and due diligence directive[68] explores companies integrating environmental matters into their policies. It also provides for a method of enforceability if companies are not engaging with the directive. Whilst, in the context of the United Kingdom, this is merely a proposal and one which will not be automatically enforced, it demonstrates wider policy direction. Moreover, many large corporations which this bill seeks to encompass operate in the UK and across Europe and many corporations may seek to embed policies throughout all of their operating jurisdictions. The public interest, and policy direction, therefore must contain environmental considerations and reporting on those considerations. Villiers claims that good company reporting is essential and that it is a device which should be increasingly relied upon a method to control corporate activity. One reason for this is that can often change business priorities.[69] In this regard could do in departure of the shareholder maximisation model favouring a more social conception, incorporating these critically important environmental considerations.

The public interest therefore plays a significant role within the CSR theoretical framework. The very nature of considering the planet and taking action is 'social responsibility' within the CSR framework. Within the model proposed by Carroll's pyramid public interest could fit into the any of the layers from the 2nd layer up. Whilst this might be challenged by the likes of Klein and Raworth following

[68] European Commission, *Proposal for a*
DIRECTIVE OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL
on Corporate Sustainability Due Diligence and amending Directive (EU) 2019/193
https://ec.europa.eu/info/sites/default/files/1_1_183885_prop_dir_susta_en.pdf Accessed 30th September 2022
[69] Charlotte Villiers, '*Corporate Reporting and Company Law*' (5th ed, Cambridge University Press, 2006).

economic responsibilities, without this foundation it becomes difficult to produce meaningful change. Aligning this with the 'doughnut' from Klein, the distributive economy can only function if there is economic stability to do so. Therefore, the environmental public interest could be mandated to fall within the legal responsibilities, within Carroll's pyramid which would mitigate for some of the challenges of capitalism v climate highlighted above. This placement of the climate within the CSR framework provides further support for the adoption of a greater social conception which is achieved through CSR.

The social conception of the corporation, however, theorised, includes greater societal inclusion than the shareholder primacy or the nexus of contracts permit. It considers the importance of wider societal inclusion on the basis of investment through relations, the wielding of corporate power and the greater good. Given the widespread separation of ownership and control and the inability for shareholders to hold managers to account, the importance of societal inclusion to legitimise this power become increasingly more justifiable.

This section has considered the two leading alternative theories of corporate law, the nexus of contracts model and the social conception model. These two theories demonstrate that the dominance of the shareholder primacy model is not unchallenged or universally accepted. These alternative conceptions consider broader perceptions of the corporation, which this research argues can provide an improved platform to attain legitimacy for corporate groups. The shareholder primacy model is not unchallenged and not undisputable, and this chapter sought to build on alternative theories to legitimise corporate power. The following section will evaluate if either of these theories can provide legitimacy which currently is absent in corporate groups. The objective is to ascertain a theory of the corporation which can justify the wielding of substantial power by groups of companies.

6.4 Utilising an alternative theory to achieve legitimacy of corporate power

The preceding section considered alternative theories of corporate law and how they have been defined and defended. This section will build on this to establish if either of the two theories evaluated can be utilised to attach legitimacy to corporate groups for the power they wield. This research has maintained that control is at the centre of legitimacy and that the holders of such power must have it legitimised. This can be done through control mechanisms. This section puts forward an argument in favour of an alternative theory of conceptualising the corporation as one of these control mechanisms.

6.4.1 Nexus of contracts to attain legitimacy?

The nexus of contract model allows for contracting parties to choose terms and the way to control management costs. The concept of the model is that it provides a place whereby transactions can be carried out with reduced costs of contracting. In the context of the corporate group, the contracts become more complex due to the relationships between the parties within the group. The nexus of contracts model is likely to result in additional costs to contracting, not less. If it can be accepted that the corporation is not an entity, then conceptually, neither are the subsidiaries. The nexus of the contract model dictates that there ought to be contracts between each party, and therefore each subsidiary and related company would require clear contractual terms to operate effectively. As demonstrated by chapter five, given the average number of companies within a group is 400, this web of contracts between each of these 400 companies and their suppliers and employees becomes unduly complex. The concept of 'legal fictions' becomes more indefensible due to the inherent nature of the group and the structural architecture which is only made possible through the use of separate legal personality. This is supported by Hayden and Bodie, who contend that features such as limited liability cannot be replicated by contract, and as such the nexus of contracts argument of freely negotiated contracts is somewhat 'self-defeating'.[70]

The largest challenge with the nexus of contracts model is the relationship with wider stakeholders and how these relationships can be contracted. The concept of a contract only accounts for a limited proportion of the rules for company and

[70] Grant M Hayden and Matthew T Bodie, 'The Corporation Reborn: From Shareholder Primacy to Shared Governance' (2020) 61 BCL Rev 2419, 17.

corporate law.[71] Moreover, as identified, Mayer argues that the corporation is not a nexus of contracts between the parties to the firm, it is the opposite, if the nexus of relations is based on trust.[72] It is these relations which are unable to be met by contract law alone for two principal reasons. Firstly, the nexus of the contract model does not adequately deal with the unequal bargaining power between the parties. This model functions where there are two businesses dealing with one another on a commercial basis and the nexus of contract theory provides a platform for this to take place. Where there is an employee or a small trade supplier, there is likely to be an inequality of bargaining power. An employee is unlikely to be able to negotiate terms upon which they are to be employed, for example. In this scenario, the nexus of contracts provides a platform to facilitate unequal bargaining platforms. Secondly, there are parties which may not be in a position to contract with the company on a voluntary basis. These involuntary parties to contracts are those such as tortious claimants and wider society. Tortious claimants will be unable to enter a contract by the very nature of the relationships, and the model does not adequality provide for this. More significantly, the challenge of wider societal inclusion becomes difficult to achieve. By way of example, how would the environment enter into a contract with a corporation? Moreover, how can longevity be achieved when many contracting will be concerned with immediate contracts? The very nature of wider societal inclusion does not fit with the nexus of contracts model.

The nexus of contracts model does have the capacity to remove the fictions of separate legal personalities between parent and subsidiary; however, it fails to engage with the broader range of stakeholders. The inability of all stakeholders to contract does not provide the platform to derive greater legitimacy. Moreover, the use of this model could result in CSR being removed from consideration altogether, furthering the challenges of short-termism. When evaluating legitimacy through the theoretical framework of CSR, this removal is fatal to the success of the nexus of contracts model to be successful in attaining legitimacy. Therefore, this model is insufficient to overcome the challenges outlined in this research thus far.

[71] Parkinson (n 20) 181
[72] Mayer (n 62).

6.4.2 Social conception of the corporation as the route to legitimacy?

This research has maintained that corporate groups lack legitimacy due to the inadequate controls on senior managers and the historical basis upon which power is attained. This subsection considers how the use of a more social conception could address these challenges of legitimacy deficiency. It will proceed to evaluate which definition of a more social conception could be utilised to attach legitimacy and how these considerations resolve the challenges of legitimacy failure of the corporate group. Those who have power must have it legitimised, and this has traditionally been done through control mechanisms. However, this research has argued that these have all but been eroded, and as such a requirement for social considerations could be a control mechanism which can be utilised to derive legitimacy.

6.4.2.1 The parameters of the social conception

This chapter has considered multiple definitions of the social conception, from mere stakeholder inclusion to stakeholder priority over shareholders. Parkinson maintains that the public interest is the foundation of the legitimacy for companies and as such, society is entitled to ensure corporate power is exercised in way which is consistent with that interest.[73] Establishing the parameters to manage this control mechanism is therefore of significant importance. The balance of shareholder and stakeholder interests needs to be delicately managed, as corporations are reliant on shareholders for capital investment. The introduction of stakeholder-centric provisions could disrupt the capital investment market, whereas the model currently adopted is threatening the rights of others.[74] This research sets the parameters for the social conception along the pluralist model. In 2002, the Company Law Steering Group considered two alternative approaches: one was the enlightened shareholder value, and the other was pluralism.[75] The enlightened shareholder value principle was adopted and as this thesis has argued, not to great success. The pluralist approach was considered

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[73] Parkinson (n 20) 23.
[74] Mayer (n 62).
[75] Trade and Industry Committee, Trade and Industry – Sixth Report' (1 March 2002) <https://publications.parliament.uk/pa/cm200203/cmselect/cmtrdind/439/43902.htm> accessed 4 August 2021 3 [12].

to require a more fundamental change in company law, whereas the enlightened shareholder value would require each stakeholder to have their interest considered. Since this introduction of the enlightened shareholder value, this consideration has not been the case, and the benefit to stakeholders has been negligible. The pluralist view was rejected on the basis that the enlightened shareholder value could be more easily adopted and less litigious. Given that the enlightened shareholder value has not been the success that the Company Law Steering Group had hoped for, this opens a discussion for the introduction of a pluralist view.

Defining the pluralist view

This research advocates for a more pluralist model of the corporation and how directors should consider all stakeholders. The pluralist view received consideration by the Company Law Steering Group prior to the 2006 Act, before the enlightened shareholder value principle was adopted. The pluralist view can be justified on the basis that it has capacity to benefit both shareholders and stakeholders. Moreover, this view of the corporation will allow the corporation to fulfil its purpose. This is the view put forward by Mayer, who argues that firms only exist to fulfil this purpose. This purpose is not restricted to making profit, although profit comprises part of it.[76] Corporations have purposes, and this stems from the early inceptions of the corporation when they were permitted by Acts of Parliament to fund public functions, such as building railways, etc. The purpose that would be fulfilled in this example would be the construction of a railway: providing benefits to the users of the railway and that those employed in its construction all contributed to its purpose. There can, therefore, be additional beneficiaries to the output of corporations than the shareholder-centred approach would suggest.

The pluralist viewpoint rejects the idea of shareholder wealth maximisation and replaces it with maximation of total wealth.[77] In this regard, the interests of shareholders and stakeholders need not be mutually exclusive, and they can be evaluated in parity to generate overall wealth. This wealth can then be returned for the benefit of shareholders and stakeholders. This pluralist perspective is

[76] Mayer (n 62).
[77] Parkinson and Kelly (n 58).

preferable to a pure social model, as it can be incorporated into the capitalist economy in which the modern corporation functions. It builds on the failures of the enlightened shareholder value and allows for greater social inclusion into corporate decision making without overturning significant rights attached to shareholders. Moreover, this broader perspective to include wider stakeholders fits with the economic reality of the modern corporation. As chapter five argued, individual and identifiable shareholders are decreasing in numbers and relevance. The pluralist view protects the purpose of the corporation whilst acknowledging that societal and group ownership is the reality of the modern corporation.

The parameters of the pluralist social conception encompass an equilibrium of considerations within the theory of the firm. These considerations include the members, employees, suppliers, customers, society, environment and longevity. The consideration of these parties allows the corporation to generate wealth and fulfil its purpose. Moreover, the use of this model affords the corporation to derive greater legitimacy for corporate power in the group context; the next subsection will consider this further.

6.4.2.2 Deriving greater legitimacy

The preceding subsection advocated for a pluralist definition of the social conception of the corporation. This subsection will proceed to consider how this definition could provide greater legitimacy for corporate groups and their exercising of corporate power.

This research has considered the role of corporate power within the corporate group and has established that corporate power becomes magnified in this context. Coupled with the accidental extension of limited liability to groups, this power lacks legitimacy. The entrenchment of fundamental principles[78] of corporate law renders significant reform unpersuasive.[79] Therefore, a reconceptualisation as to how the corporation is perceived becomes

[78] Such as limited liability and separate legal personality.
[79] See: *Prest v Petrodel Resources Ltd* [2013] UKSC 34, *Hurstwood Properties (A) Ltd v Rossendale BC* [2021] UKSC 16.

convincing,[80] as it can be justified on historical and empirical evidence whilst also not disrupting the market. Those who exercise power must have it legitimised, and this can be done through control mechanisms; the control mechanism this research advocates for is a pluralist social conception of the corporation. Legitimacy is the rightful possession of power,[81] and the public interest is the foundation to ensuring that it is complied with in a way which is consistent with society. [82] This pluralist social conception model of the corporation can act as a control mechanism by providing a platform to hold those to account, which in turn will legitimise the power wielded. This approach can achieve this for four reasons: firstly, this will allow the corporation to achieve its purpose,[83] , which extends past purely profit maximising. Secondly, this conception requires social considerations from corporate managers as opposed to offering it as an option for consideration in regard to advancing members' interests. Thirdly, in considering a more social outlook, longevity can be included, which regulates the challenges of short-termism. Fourthly, this conception can justify the exercising of power, as it is exercised to benefit society more generally as opposed to the narrow shareholder approach. This aligns with the results seen from the data study carried out and links economic reality to the conception of the firm.

The corporate purpose has historically been conceived as shareholder wealth maximisation; however, Mayer presents a persuasive argument that this is not an accurate depiction. This can be best illustrated with an example, where the corporation should be recognised for what it is.[84] From a historical context,[85] corporations were initially set up to perform and fund public functions, such as the construction of the railways. The purpose of the corporation in this context was to add value by constructing these railways, and this value presented itself by way of a return for investors, but also for those who used the railways and built them. The purpose is more than returning capital and aligning interest: it is achieving the purpose of the corporation. Adopting a pluralist social conception of the corporation aligns with the idea of purpose. The managers can consider

[80] Donovan (n 57).
[81] Adolf A Berle, *Power without Property: A New Development in American Political Economy*, vol 56 (Harcourt, Brace & World Inc 1959) 99.
[82] Parkinson (n 20) 23.
[83] Mayer (n 62).
[84] ibid.
[85] See chapter 2.

wider stakeholders in achieving the company's purpose and are not shackled to focussing on returns for investors irrespective of social consequence.

In seeking to accomplish the purpose, the social conception can promote stakeholder considerations and the long-term effects of the company. In considering these perspectives, the wielding of power becomes more legitimised because it is to be wielded subject to the consideration of those whom decisions affect. This is legitimised due to the role companies play in society. This model considers the impact on society and requires directors and corporate managers to consider the impact of their decision-making on parties external to shareholders. This is stronger than the enlightened shareholder model, as there is a requirement, and not merely an option, to consider relevant parties. Under the social pluralist model, there is more than a requirement to 'have regard to', there is a greater level of parity between shareholders and stakeholders. This model also removes the requirement for corporate managers to consider shareholder wealth maximisation; the removal of this is likely to reduce the challenges of short-termism as considerations of the longer become more primary than secondary.

The economic reality of large corporate groups is that their shares are widely held, and this broad nature results in challenges of establishing who the shareholders are and what their interests are. Moreover, the level of activism within these large corporations is negligible, resulting in illegitimate wielding of corporate power due to the dilution of the exercising of this power. The use of the pluralist social conception closes the gap between the abstract corporate managers and the beneficiaries of the corporation. This model provides a framework for corporate managers to evaluate broader stakeholders and has the capacity to legitimise corporate power by providing a platform for society to ensure that power is exercised in a way which is consistent with this public interest.

Corporate managers exercising power with the social conception borne in mind provides legitimacy because it allows public interest a right to question and challenge the directors for breaches. This availably of a route to correct behaviour serves to provide the absent legitimacy. This right to ensure power, exercised in a way which is consistent with the public interest, serves to provide legitimacy. This functions in two principal ways, firstly as the direct requirement for directors to consider more than just shareholder interest.[86] Secondly is the indirect consideration where directors are aware of consequences for breach and adjust behaviour accordingly. This provides an avenue to 'punish' behaviour which is not consistent within this model and provides guidance for directors to encourage compliance. The result is a more resilient corporation contributing to the circular economy.

This section has evaluated how utilising an alternative theory could provide legitimacy, addressing the current deficiency. It first considered the nexus of contracts model, though concluded that this would provide no more or less legitimacy than the current dominant model. The section then proceeded to consider the social conception, specifically the pluralist adaption of this model. The argument was made that this theory can legitimise the power wielded by groups because it introduces checks and controls on the power wielded for those who are affected by corporate decision-makers. It provides a framework for unchecked power to be checked and evaluated. Having outlined the theoretical model, the pluralist social conception, this chapter will now proceed to consider how these stakeholders are defined and how this model can be practically adopted and incorporated.

6.5 Determining 'social'

The previous section identified that legitimacy can be derived from a social pluralist model of the corporation. This section proceeds to consider the parties included within the 'society' label and how these can be identified. The corporation is a key actor within society, creating jobs, employment and wealth. Otteson claims that businesses when operating in an honourable manner are good for society and can create and promote prosperity and eudaimonia.[87] The power of corporations is analogous to that of the state, and recent research has

[86] Discussed further in section 6.6 below.
[87] James R Otteson, *Honorable Business: A Framework for Business in a Just and Humane Society* (Oxford University Press 2019).

identified that many corporations have greater wealth than states.[88] The role corporations play in society is therefore of significant importance, and the rules governing these entities should reflect this power and role within society. This section will proceed to consider how corporations should include societal considerations into their decision-making processes. It will achieve this by evaluating jurisprudentially what are the desired outcomes for society and how these are to be reached. It will consider theorists Bentham, Rawls and Nozick, with further considerations of Marx. These theories align to the moral framework of CSR as introduced in chapter one. The chapter will conclude that the theory advocated for is the Rawlsian approach, as this fits within the social conception of the corporation. This will in turn address the question, how do we determine what is optimal for society? In answering this question, the chapter provides a framework for social inclusion into corporate decision making.

Jeremy Bentham[89] is considered the founder of utilitarian theory. This theory holds that private action is only justifiable insofar as it produces the greatest happiness. The focus of this theory is collective utility, and that the 'greatest good for the greatest number' is the principle which should be adopted. Whilst Bentham recognised the importance of individual liberty, he likewise recognised that individuals could consider their own self-interest, and the legislator should introduce clarity. This is comparable to the position which is currently identified in modern corporations where self-interest[90] is advanced to the potential detriment of third parties. This utilitarianist approach, therefore, focusses on maximising total utility and achieving the best for the majority. The challenge to this position is that within the minority, there could be significant harm executed for the purpose of benefitting the majority. The majority in this perspective could be the thousands of shareholders who benefitted at the expense of employees, the environment or creditors. The inability to attach weight to each side of Bentham's 'pleasure' and 'pain' renders this argument unpersuasive in the context of the corporation. This inability to quantify and add weight to pleasure and pain was

[88] Jake Johnson, '157 of World's 200 Richest Entities Are Corporations, Not Governments' (*Inequality.org*, 19 October 2018) <https://inequality.org/research/richest-entities-corporations-governments/> accessed 8 August 2021.
[89] See: Jeremy Bentham, *An Introduction to the Principles of Morals and Legislation* (Batoche 2000).
[90] In the form the shareholders, by virtue of the shareholder primacy position.

identified by John Stewart Mill,[91] who advanced Bentham's argument by advocating for the best quality of pleasure. Mill recognised that not all pleasures were equal, and consideration should be applied in this context. However, judging the weight to be attached presents challenges in achieving maximum utility. For example, would this require more stakeholder pain then shareholder pleasure to achieve utility? Mill's work focussed on harm and regulation requiring the intervention to prevent harm, for which the threshold was set high. Ultimately, Mill progressed the argument of greatest happiness introduced by Bentham. Given the advancement of greatest utility and the ability for the minority to be adversely disadvantaged, it is submitted that this is not the most optimal determinative of society for the purposes of this research.

Robert Nozick, in contrast to utilitarian theory, was individualistic and expressed a very liberal theory of society. The underlying argument presented by Nozick was that individuals have rights, and these rights should be interfered with in a minimal way.[92] This theory poses some interesting questions in respect to its applicability to the corporate context. The corporation being a separate legal person would presumably have their own rights, which are to be respected and not interfered with. From this perspective, the imposition of additional requirements to consider wider stakeholders would be in opposition to the theory of justice presented by Nozick. The individualistic and liberal theory presented by Nozick does not align with collaborative interests and working for the benefit of a wider group of stakeholders. The argument put forward by Nozick is that state imposition infringes upon the rights of individuals, and the state should operate a 'night watchman' state. This level of minimum interference from the regulators does not align with the social conception of the corporation. It fails to account for all the stakeholders within the corporation and the need to adopt a pluralist outlook to achieve this. This renders the libertarian position unpersuasive.

John Locke's position centres around private property and the belief that everyone has natural rights.[93] Where individuals mix their labour with nature, they obtain a legitimate claim to property rights. Locke's theory is based on fairness,

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[91] John Stuart Mill and Jean Bethke Elshtain, *On Liberty* (Yale University Press 2003).
[92] Robert Nozick and Thomas Nagel, *Anarchy, State, and Utopia* (Basic Books 1974).
[93] John Locke, *An Essay Concerning Human Understanding* (Kay & Troutman 1847).

and that the route to private property was one aligned with nature. In this sense, the concept of private property and state interference with this did not correlate with Locke's position. These obtained rights were unalienable and not able to be given away, and were unique to the individual and nature, a principle predicated on morality principles. Karl Marx considered that property should be owned and operated by the state to ensure complete parity amongst citizens.[94] Marx was a critic of capitalism and believed that it resulted in 'primitive accumulation', with wealth being held by a small number of individuals and low levels of wealth for workers. This argument contended that the talent of the workforce should not be capitalised for profit, as this is more akin to theft and exploitation. Marx's work focussed on the challenges of capitalism and how this imbalance resulted in moral injustice. Whilst these concepts of egalitarianism from Marx and Locke provide a strong case for moral and individual freedom, their opposition to ownership of private property and to capitalism presents challenges for the social conception of the corporation. The inclusion and equality of all stakeholders is of importance within the social conception; however, this is paired with rewards for the corporation for performance. This would not be considered acceptable for Marx and Locke, and therefore this theory for societal inclusion is not appropriate for the social conception of the corporation.

John Rawls, also liberal in his theory, presented an argument based upon freedom and equality.[95] The argument presented by Rawls was that individuals needed to cooperate, and this was the society in which most justice could be achieved. This could be achieved by equal distribution to all regardless of their position. Rawls argued that this could be achieved by seeking to arrive at the original position, and this in turn could be arrived at by using the veil of ignorance. The concept behind Rawls's theory is that at the original position everyone would be treated fairly and be able to work collaboratively. The way this is achieved is by creating an agreed set of principles upon all would agree. This is more sophisticated than the greatest good for the greatest number, or indeed individualism. It requires consideration to a wider set of characteristics which would be universally accepted once arbitrary factors have been removed. Each

[94] Karl Marx and Serge L Levitsky, *Das Kapital: A Critique of Political Economy* (H Regnery Washington 1965).
[95] John Rawls, *A Theory of Justice SE - Oxford Paperbacks* (Original edn, Belknap Press 1971).

person behind this veil has an equal right to the basic liberties, and the position allows for those who wish to advance their position in the infrastructure to do this. This principle exists to allow benefits to those who are disadvantaged, and further allows for equality of opportunity. This theory when applied to the corporate law context aligns with the pluralist model of the corporation. It considers the need to act fairly amongst all parties involved and provides a platform for this to be exercised. The sophisticated consideration of disadvantaged parties due to arbitrary features ensures parity amongst shareholders and stakeholders can be achieved irrespective of position. The argument to provide greater fairness amongst parties involves makes the Rawlsian position persuasive in determining societal fairness amongst shareholders and stakeholders.

This section has introduced three conceptions of the 'social contract', utilitarianism, libertarianism and Rawlsianism. Whilst there is much debate as to the applicability of theories, this research advocates for the Rawlsian approach due to the persuasiveness of the original position and the ability to consider all those involved with parity of position. Moreover, the approach presented by Nozick and the libertarianism approach do not align with the social conception. Under the libertarian perspective, the corporation and its managers would be free to utilise their property with minimal state interference to advance their position, irrespective of impact on other individuals. This is the very position which can currently be utilised to the detriment of wider stakeholders. Additionally, the utilitarian model presents two extreme sides of the spectrum: at one end, the greatest good for the greatest number could render shareholders' interest so trivial they cease to have any tangible interest. This conception is likely to disrupt the capital market and have an adversely negative effect on investors. Conversely, detrimental decisions for employees could result in less collective pain than the pleasure derived for shareholders. The calculation here would result in preference for the shareholders over the stakeholders, with the result depending on who benefits the most with greater loss. This paradoxical position renders utilitarianism an unpersuasive theory to adopt.

6.6 Implementation of the social conception

This chapter thus far has evaluated the dominant theory of the corporation and established how this theory became the dominant model. It has furthermore presented justifications for a realignment of the model, citing failures of governance and the systemic problem of short-termist behaviour. The chapter presented alternative models of the corporation and advocated for a pluralist social conception of the corporation. Within this model, a more social outlook is to be considered at parity with shareholders. The chapter has also considered how this social outlook is to be achieved. Having presented the argument in favour of realignment towards a pluralist social conception, this section will proceed to consider how this can be implemented. It will consider who ought to be included within the remit of stakeholders. It will then consider potential weighting to these parties to ensure the parity sought under the pluralist model. Having established the key actors and their role, the section will proceed to consider how this can be achieved. Given the failure of implementation of the enlightened shareholder value, a more substantive tool is required. This section will evaluate tools to implement the pluralist social model, considering directors and new technologies. Moreover, it will consider how new technologies can assist the implementation process to successfully implement the social pluralist model.

6.6.1 Defining the stakeholders within the pluralist social conception

This research has maintained that the reach of large corporate groups has the capacity to affect a wide range of stakeholders. Therefore, establishing a definitive list of stakeholders who ought to be considered is inherently difficult. It is argued that the term ‘stakeholder’ is to be construed within the confines of the specific corporation in which they are applicable. The benefit of this definition is that it is fluid to encourage the wider consideration advocated for. Whilst a definitive list would more likely exclude some stakeholders, an indicative guide can be used to foster an encompassing group of stakeholders. In comprising this guide, the list within the current enlightened shareholder value[96] can provide a good foundation. Specific stakeholders within this categorisation include employees, creditors and the community. More broadly, the environment and high standards of business conduct are also included. In addition to these parties,

[96] Companies Act 2006 s 172.

B Lab UK in their partnership with B Corp have proposed further inclusions which can be drawn upon.[97] In addition to those included above, wider society can be included to extend post the immediate community. Moreover, B Lab suggests that the reduction of harm should be within the goal of the corporation. This is an interesting proposal and should be included within the remit of stakeholders, though not as the purpose of the corporation as alluded to by B Lab. A reduction of harm can be a by-product or a route to achieving corporate purpose; however, existing as the sole purpose, this is not persuasive when contrasted to the argument of Mayer.[98] The aim of B Corp and B Lab is the admirable pursuit of ethical business and societal improvement. However, whilst their proposals align with the arguments of this research, they fail to fully engage with the need for shareholders and capital. For the purposes of this research and its proposals, when stakeholders are discussed, it is to include as an indicative guide the employees, creditors, communities, business conduct, environment, wider society affected by the corporation, and mitigation of harm caused by the corporation in achieving its purpose.

With the indicative definition of stakeholders outlined, there remains the important question of balancing these interests both internally amongst themselves and externally with shareholders. This research advocates for a pluralist social conception of the corporation: in this sense, the balance between shareholders and stakeholders should be equal in pursuit of the purpose and goal of the corporation. It must remain an attractive investment whilst ensuring that profits are not returned at the expense of long-term stability or at the expense of stakeholders. The proposal is therefore for an equal weighting of consideration for both stakeholders and shareholders. The accumulation of all the stakeholders within the above definition should be considered collectively as half of the consideration for corporate executives. The remaining half of consideration factors will continue to be on behalf of the shareholders and members. This affords equal consideration and allows for flexibility within the stakeholder proportion of the weighting for consideration.

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[97] B Lab UK and B Corp are the drivers and organisers of a report from the Better Business Act, 'The Better Business Act: An Act to Amend the Companies Act 2006' (*Better Business Act*) <https://betterbusinessact.org/wp-content/uploads/2021/04/The-Better-Business-Act-2021.pdf> accessed 9 August 2021.
[98] Mayer (n 62).

6.6.2 New technologies to support implementation

The breadth of categories of stakeholders and potential for sub-categories within the definition of stakeholder consideration provides a significant set of data to be considered. This results in challenges for the executive board in considering all these parties and interests, as each will need to be considered in corporate decision making. Coupled with significant data sets of considerations, and the the optional nature the board of directors can claim in defence that it is inplausible to consider the volume of public interest this thesis advocates for. New technologies can be utilised to facilitate this inclusion, as they have the ability to process large data sets and can augment the skills of directors in evaluating all interests outlined above. This section will proceed to consider what new technologies can adequately support this model and how it can be attained. This consideration of New Technologies provides a theoretical method of 'how' the reconceptualization could be achieved. A more comprehensive analysis of 'CorpTech' is beyond the scope of this thesis. The inclusion of the proceeding discussion seeks to introduce New Technologies as a plausible way of achieving the changes proposed which have previously not been viable.

Robotic process automation

Robotic process automation (RPA) is utilised to operate applications like a natural person and works to complete a process. It is rules based and often works on the basis of processing routine work.[99] Alberth and Mattern maintains this is similar to a form of 'macros' in that it does not replace existing systems or their code but operates akin to the human user of a system. In this regard, the RPA needs to learn the processes much like a human user, and it is guided by a rules-based approach rather an artificial intelligence (AI). One of the main benefits of RPA is that it can work 24 hours of the day, carrying out the same functions as its human counterparts. In addition to this, as the RPA is carrying out traditional functions but in an automated way, the functions and practices which have been automated do not require substantial change. Once the RPA has been 'taught' the rules to

[99] Markus Alberth and Michael Mattern, 'Understanding Robotic Process Automation (RPA)' (2017) 46 Journal of Financial Transformation 54.

carry out a sequence, the existing procedures and policies remain in place. With this new technology, there are several caveats to its application. The first is that once automated, the processes are out of site, and therefore determining how a decision has been reached is impossible due to this process. In addition to this, the RPA still requires human supervision and as such cannot be considered as a like-for-like replacement for a human user.

The largest challenge for an RPA is that it is currently only for rules-based and routine work; in this regard, manual processes will be required at either end to complete the process. In the context of its applicability for the corporate context and its ability to support the implementation of proposals, significant challenges remain. The RPA could be utilised to collate and file responses from stakeholders and shareholders. It would, however, require evaluating by a human agent to comprehend the data. Given the idiosyncratic nature of each corporation, the RPA would not be able to complete specific tasks given the uniqueness of each corporation. Therefore, the RPA does not advance the current position for current directors, as the largest challenge is in analysing and processing the data. As this is not a process which can be facilitated by a rules-based approach, this renders the RPA of trivial benefit to executives in implementing the pluralist social conception of the corporation due to the volume of data left to process.

Artificial intelligence

AI has developed extensively since Alan Turing's test of machine thinking in 1950.[100] The acceptance of AI has witnessed dramatic growth with the introduction of driverless cars.[101] This has been further realised by the Department for Transport legalising 'driverless cars' on a national scale.[102] AI can encompass and mean many things given its broad applicability, and defining AI is difficult with different definitions offered. The definition this research adopts is taken from the industrial strategy government white paper. It offers the following definitions:

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[100] Alan Turing, 'Computing machinery and intelligence-AM Turing' (1950) 59 Mind 236 433.
[101] For a more extensive discussion see: Matthew Channon, Lucy McCormick and Kyriaki Noussia, *The Law and Autonomous Vehicles* (Taylor & Francis 2019).
[102] Gov.uk, 'Government paves the way for self-driving vehicles on UK roads' (Gov.uk, 2021) <https://www.gov.uk/government/news/government-paves-the-way-for-self-driving-vehicles-on-uk-roads> accessed 28 April 2021.

> Artificial intelligence: technologies with the ability to perform tasks that would otherwise require human intelligence, such as visual perception, speech recognition, and language translation
>
> Machine learning: a type of AI that allows computers to learn rapidly from large datasets without being explicitly programmed
>
> Data-driven economy: a digitally connected economy that realises significant value from connected, largescale data that can be rapidly analysed by technology to generate insights and innovation[103]

These definitions make a clear separation between the overarching definition of AI and how machine learning is a derivative of AI. Moreover, the white paper provides a definition on how AI can act as a driver for the economy. AI can be described to be a technology which can perform the same tasks as human beings. This form of AI could be rules based or a form of machine learning. Machine learning is where technology can learn from data received, a more advanced form of AI. With technology more akin to human intelligence, AI has the capacity to offer more than RPA as a new technology due to its ability to be more than manual processes. Additionally, the capacity of AI to be able to adapt and develop to include the idiosyncratic features of corporation results in AI becoming a persuasive tool. This section will now proceed to consider how AI could function in the context of the corporation to implement the social conception.

Artificial intelligence as an implementation tool

The definition of AI allows for a wide remit of application within the corporate landscape to achieve the social conception. The key feature to enable the implementation of the social conception of the corporation is the inclusion of wider stakeholders. This subsection will therefore proceed to consider how wider stakeholders could be included and if there is any support for this level of implantation.

The most significant challenge within the RPA technology was the inability to adapt to the unique nature of each business and analyse data. AI, conversely,

[103] HM Government, 'Industrial Strategy: Building a Britain Fit for the Future' (2017) <https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/664563/industrial-strategy-white-paper-web-ready-version.pdf> 37, accessed 9 August 2021.

has the capacity to carry out both of these functions to promote the social conception of the corporation. Given this availability of technology and its advance technical state, it poses the question, can AI perform the tasks of directors independently? The RPA technology sat in place of a human operator to automate procedures. The question, therefore, remains: can AI do the same and operate as a director to achieve the social conception of the corporation and full autonomy? This topic has been the subject of rising and significant debate. In 2014, venture capitalist firm Deep Knowledge Ventures appointed an AI called Vital to its board.[104] This has led to increasing debate as to the applicability of AI as an autonomous director.[105] This discussion has resulted in the conclusion that currently an AI cannot perform the role of a director and as such its applicability in the context of the corporation is to enhance the functions of the existing board, and assist them as a tool.

AI as a tool has a broad scope to address some of the challenges posed throughout this research and to support the model for a more social conception of the corporation. This tool offered by AI needs to be conceptualised to enable directors, shareholders and stakeholders to understand its capabilities and limits. Chiu and Lim[106] recognised that in the context of the corporations there are several frameworks which could be considered. They presented the argument that 'CorpTech' will develop over time in three forms, narrow AI, general AI and super AI. Narrow AI details complex rules which can develop into machine learning. General AI is ambitious and relates to machines with holistic and integrated capacity simulating human reasoning. An example of this type of AI can be seen in self-driving cars. Super AI occurs where AI is indistinguishable from human sentience and capacity. Super AI, whilst perhaps a long-term goal, is not feasible in the corporate context. This would result in fully autonomous AIs

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[104] BBC News, 'Algorithm appointed board director' (*BBC News*, 2021) <https://www.bbc.co.uk/news/technology-27426942> accessed 4 February 2021.

[105] John Armour, Richard Parnham and Mari Sako, 'Augmented Lawyering' (2020) European Corporate Governance Institute - Law Working Paper 558/2020 <https://dx.doi.org/10.2139/ssrn.3688896> accessed 2 April 2022; John Armour and Horst Eidenmuller, 'Self-Driving Corporations?' (2020) 10 Harv Bus L Rev 87; Florian Möslein, 'Robots in the boardroom: Artificial Intelligence and Corporate Law' in *Research Handbook on the Law of Artificial Intelligence* (Edward Elgar Publishing 2018) 1; Adolfo Paolini, 'Robots in the Boardroom: would AI Beat Their Creators? D&O Insurers Please Think Deep!' (SLS conference, Exeter, 3 September 2020).

[106] Iris H-Y Chiu and Ernest WK Lim, 'Technology vs Ideology: How Far will Artificial Intelligence and Distributed Ledger Technology Transform Corporate Governance and Business?' (2021) 18 Berkeley Bus LJ 1.

operating as directors who are indistinguishable from human counterparts. This position is not achievable in the foreseeable future. Therefore, the type of AI which would enhance the social conception of the corporation sits between narrow AI and general AI. The use of narrow AI is freely available on the market,[107] which poses real possibilities of AI to operate in the corporate context. The framework of AI and its implantation into the corporation, according to Chiu and Lim, falls into three categories, incremental/facilitative, radical/disruptive and fundamental/structural. Each of these operates to implement AI on progressive levels. The incremental and facilitative framework is based upon automation of what Chiu and Lim dub low-level work such as manufacturing. This type of AI can be freely adopted and implemented, as it is operating to replace automated functions, much like the RPA new technology. The incremental framework therefore is more of a processing of automated functions, as opposed to the more executive level and qualitative judgements. Radical and disruptive AI is the displacement of the human agency rules which were thought incapable of assumption by robots, for example, not the assistant but the judge.[108] Applying this to the corporate context, this type of AI can provide reasoning and processing akin to directors in making decisions which relate to the idiosyncratic nature of the corporation. Lastly, the fundamental/structural category is whereby current governance systems are eradicated and replaced by new governance systems. Whilst this structural change has the capacity to develop as super AI, this framework is not suitable for AI in the corporate context, due to the inability for AIs to attain legal capacity and consciousness.

This framework can be utilised to achieve a more social conception which encompasses features from both the facilitative and disruptive frameworks identified above. As the corporation is idiosyncratic, in order to drive change, there is a requirement for a greater development than automating existing processes. This can be balanced with the need to ensure commercial certainty and gain acceptance from those who utilise it. AI, therefore, can provide the platform to automate some practices, such as the collecting of data, and likewise process this data using qualitative judgements. This level of enhancing the skills

[107] IBM, Watson Studio <https://www.ibm.com/cloud/watson-studio/ai-capabilities> (2021) accessed 4 June 2021.
[108] Chiu and Lim (n 100).

of directors is one which is supported by Armour, Parnham and Sako, who present the argument of augmented AI.[109] This is the concept that as corporations are idiosyncratic and the technology is not developed enough, replacement of traditional human roles is not likely. The role AI can play, however, is improving the intelligence of the human agents. In the context of the social conception model, the AI can be utilised to process data from each party and produce a report or recommendation for consideration by the board. This complements the board of directors, allowing a more informed decision to be made to fulfil a more social conception.

This augmentation provides the platform for AI to process a large set of data which would have been incomparable by human directors due to their limited ability to process large data sets. This allows for the identified stakeholders to feed into the decision making of the board and ultimately support the pluralist social conception of the corporation. Utilising the AI to assist and carry out tasks has received support, with some scholars arguing that this not only supports human decision making but frees directors for alternative genuine business tasks.[110] Moreover, that augmentation and the complementing of existing skill sets could actively support important strategic decisions.[111]

The use of AI as a tool can therefore operate to facilitate corporate decision making in considering the inputs from the wider stakeholders. The proposal put forward by this research is for a pluralist social conception of the corporation, and the ability to process big data provides a strong argument for the use of AI. This chapter has considered the weighting of each shareholder and stakeholder and concluded that parity between the two provides legitimacy for corporate power. The AI can consider each stakeholder and their respective weight and calculate outcomes and recommendations for the board of directors to adopt. This provides a route to feasibly consider all stakeholders and have these views considered in decision making. This process, due to its objectivity, will provide support to directors in their decision making, knowing factors have been considered and evaluated in accordance with the company's agreed parameters. AI in this regard

[109] Armour, Parnham and Sako (n 99).
[110] Gian Domenico Mosco, 'AI and the Board within Italian Corporate Law: Preliminary Notes' (2020) 17 European Company Law.
[111] ibid.

makes a more social conception of the corporation more realistic than previously thought attainable due to the ability to consider this wider breadth of stakeholders.

Blockchain

The preceding paragraphs in this section have considered how new technologies can be used as a form of automating processes, supporting decision making. This subsection will consider another new technology, blockchain, which could support the collection of data to be analysed. Blockchain and distributed ledgers are synonymous with Bitcoin, a system of secure digital currency. Blockchain can be defined as the following:

> [C]omprised of blocks of information or records that store data using sophisticated algorithms. The blocks are connected or chained together and distributed to a peer network of multiple trusted sources. Each member of the network has a key or an individualized digital signature that is assigned to the transactions made by that member.[112]

The benefit of blockchain is that data can be stored and transferred in a way which can survive corruption, and hacking. Whilst synonymous with digital currencies, it has expanded beyond payments in helping support new autonomous systems where the need for intermediaries exist.[113] The use of blockchain technology to manage important private documents has the capacity to revolutionise democratic participation within a corporation due to the ease in obtaining and storing data.

Chapter five identified that the shareholders were significantly diffused and as such identifying the beneficiaries of shares is complex. The inability for these beneficiaries to have their voice heard results in a democratic deficiency, impacting control mechanisms. Panisi, Buckley and Douglas contend that not only is this identification possible but that simple real-time identification of

[112] Susan Alman and Sandra Hirsh, *Blockchain* (American Library Association 2019) 15.
[113] Primavera De Filippi and Aaron Wright, 'Introduction' in Primavera De Filippi and Aaron Wright (eds), *Blockchain and the Law* (Harvard University Press 2018) <http://www.jstor.org/stable/j.ctv2867sp.3> accessed 10 August 2021; De Filippi and Wright, 'Smart Contracts as Legal Contracts' in Primavera De Filippi and Aaron Wright (eds), *Blockchain and the Law* (Harvard University Press 2018) <http://www.jstor.org/stable/j.ctv2867sp.7> accessed 10 August 2021, 72.

shareholders could be achieved.[114] This ownership transparency could streamline the entire share ownership architecture.[115] This streamlining could enhance shareholder participation by way of encouraging activism. It could provide a framework whereby beneficial shareholders can make their interests known to the legal interest holders who then remain under a fiduciary duty to consider these interests. Shareholders may also become more aware using technology where their ultimate investment is being distributed, that is, the hedge fund composition. Increased awareness could result in indirect influence on participation. In this regard, blockchain provides a platform for greater ownership transparency which has the capacity to increase activism from shareholders.

In addition to this ownership transparency to enhance shareholder participation, the combination of blockchain voting systems with AI could be beneficial. Blockchain can provide the platform to feed in what shareholders and beneficial interest holders want. Moreover, this could be considered by the directors or an AI algorithm in conjunction with stakeholders to evaluate options for the board of directors. Advanced encryption can be used to facilitate secure voting and mitigate the risks of malware and other cyber-security risks. One such example of these features in practice is with the 'i-voting' system Estonia that is used for political elections. Using a smart government-issued card, this allows users onto a voting system whereby votes can be cast securely.[116] This has the benefit of encouraging activism due to the ease of the process, but also an automated calculation based on result. These features are more advanced than current electronic voting systems due to their well-established security, and blockchain technology has the potential to address current electronic voting issues.[117] Recent analysis provides support for blockchain as a facility to enable electronic voting. Dhillon and others argue that blockchain supports this in three ways:[118] securely storing large voting data, tracking votes using accounts, and by using smart contracts. With vast shareholdings coupled with frequent transfer of

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[114] Federico Panisi, Ross P Buckley, and Douglas W Arner, Blockchain and Public Companies: A Revolution in Share Ownership Transparency, Proxy-voting and Corporate Governance? [2019] Proxy-Voting and Corporate Governance 19.
[115] ibid.
[116] Valimised (2021) <https://www.valimised.ee/en/internet-voting/internet-voting-estonia> accessed 10 August 2021.
[117] Amrita Dhillon and others, ''Voting over a Distributed Ledger: An Interdisciplinary Perspective' (2021) 12 Foundations and Trends in Microeconomics 3 48.
[118] ibid 42.

shares, the large storage support is highly beneficial for corporate application. This has been trialled recently by UK bank, Santander, who sought to revolutionise the AGM and increase participation.[119] The use of this blockchain technology in a private context provides support for its application for a shareholder application.

Technology and Corporate Power

This section has sought to demonstrate that the proposal of realignment is more conceptually possible with technologies than previously has been. One argument presented by this thesis is that where power is concentrated and is controlled by those who are the beneficiaries the control mechanisms are significantly diluted. One such benefit that New Technologies offers is the ability to shift the power dynamic through transparency and reporting in controlling the concentrated power. Where power is to be exercised for the public interest, or to generate wider social value the ability to hold directors to account is greater. If technology allows for transparency this would decrease asymmetric information and have the ability to hold directors to account. This could function in two ways; the first through publicity and reputational damage. If technology can highlight underperforming companies in relation to their consideration of the social conception of the corporation, this could change consumer and end user habits. This was famously displayed where Starbucks UK avoided taxation and the backlash resulted in closure and shrinking of market size in the UK. This affects share price and may affect shareholders who may engage in activism. This power dynamic change is indirect as the increased disclosure and availability of information impacts board decisions. Thisis especially the casein an economic climate where consumers are becoming increasingly aware of corporate impact, specifically on climate crises.

The second way in which technology can adjust the power dynamic is to give greater voice to those who have been 'voiceless' historically. This is not the same as the supervisory board which is seen jurisdictions such as Germany but more

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[119] Attracta Mooney and Nicholas Megaw, 'Santander shows potential of blockchain in company votes' (*Financial Times*, 17 May 2018) <https://www.ft.com/content/c03b699e-5918-11e8-bdb7-f6677d2e1ce8> accessed 26 April 2021.

so in providing a platform for opinions to be considered. Wider stakeholders, including environmental factors, can be programmed into an algorithm for decision making assistance for the board of director. This can be through either direct input and computation, or through norms and patterns of voting from stakeholders. This combined with increased reporting, and the proposal for complaints to an external body has the capacity to change and alter board decision making as they become increasingly required to include wider stakeholders or justify their non consideration. Stakeholders being aware of this through feeding in information and being able to ascertain the advancement of such public interests can be achieved through new technologies and the increased flow of information it affords. In summary, the increased ability to provide data, through transparency and reporting, and feedback to the board affords benefits which may have historically not been possible. This can allow the focus to me more on the creation of value not profits. This value is not necessarily predicated on shareholder returns but need not exclude them either. Value is the benefit the corporation can provide to both shareholders and stakeholders through their enterprise. One such example could be Tesla, someone may buy an electric car as they want to play their part in a more economical viable transport future. They may purchase this car due to the positive press and reporting that Tesla presents. The value to the purchaser is a greener method of transport and their contributon to the climate crisis. The value to Tesla is the sale of the car and growth of their brand, and the benefit to the shareholder is any profit returned to due to the sale . In this regard value need not be downward facing but can be all encompassing and the ability for technology to provide more real time information could provide a platform for a wider conception of value, thus working towards the pluralist notion the thesis advocates.

The introduction of new technologies is not without its own risks, questions such as ownership and liability need to be further discussed.[120] These challenges are not unsurmountable and policy direction here is key. The government in a recent

[120] For a further discussion on Liability see Joseph Lee, Peter Underwood, Peter, 'AI in the Boardroom: Let the Law be in the Driving Seat', International and Comparative Corporate Law Journal, Available at SSRN: https://ssrn.com/abstract=3874588

white paper [121] have set out proposals whereby the users. Therefore, whilst the use of new technologies does pose its challenges and risks, with well programmed algorithmic steps it could transform the corporate governance landscape. It can commence progressive steps to ascertaini how changes to the landscape can be made to increase overall value. Whilst it might present risks and some challenges of initial conception, the transparency and ability to bring a theoretical position, a social conception, to reality outweighs the risks of the incremental technologies proposed in this chapter.

Combination of new technologies

This section has presented three new technologies which can assist the implementation of the pluralist social conception of the corporation and in turn generate greater legitimacy. It has considered the new technology of RPA, which despite being basic could be utilised to collect and file data. Arguably the largest advancement of the social conception can be achieved through 'general AI' and its ability to complement the skills of the directors of corporations. The use of AI systems to attach weight to all related stakeholders allows for a wider conception, and for stakeholders' views to be processed and presented to the board. This in turn can be utilised in combination with blockchain technologies which can be utilised to collect data from the shareholders on their interests. The shareholders' interests can then be considered against the interests of the stakeholders through AI processing, and recommendations for adoption presented to the executive board. The use of new technologies removes elements of objectivity and allows the AI to consider shareholder and collective stakeholder interests equally in the running of the corporation. This results in the implementation of the pluralist social model due to the adoption and real time consideration of stakeholders, which enhances a more social conception of the corporation. The result is real engagement with a broader set of considerations which legitimises the power held by corporations.

6.7 Proposals to facilitate reconceptualisation

[121] Department for Digital Culture Media and Sport: Establishing a pro-innovation approach to regulating AI (White Paper CP 728), 2022.

This chapter has considered how a more social conception of the corporation can provide legitimacy for corporate groups wielding power. It has advocated for a pluralist social conception of the corporation to achieve this legitimacy. This realignment from the dominant model can be justified based on failures of governance and the economic reality of corporations from the empirical data collected. Moreover, this chapter has presented the argument that new technologies can be a catalyst for change in achieving this reconceptualisation. Having presented the theoretical underpinnings of how new technologies can support the social conception model, this section will move to consider proposed changes to facilitate the new technologies and conception. First this section will consider how amendments to legislative frameworks such as a reformulation of directors' duties can support this model. Then it will evaluate encompassing the corporate group to ensure amendments are unable to be circumvented.

6.7.1 Amendment of directors duties

Within the corporation, separation of ownership and control results in power being wielded by a concentrated number of individuals, the executive board. Directors' duties operate to ensure that directors exercise their duties in a way which is compatible with the interests of those whom they are acting on behalf of. This separation of ownership and control, and the requirement for control mechanisms, is more pronounced in public companies. Therefore, the amendments this section proposes will apply to public corporations, subject to subsidiaries discussed in 6.7.2 below. This section will proceed to consider amendments which can be made to facilitate the reconceptualisation into a pluralist social conception.

Duty to promote the success of the company

The duty to promote the success of the company has been considered one of the most revolutionary inclusions within the Companies Act 2006. Lynch contends that the duty is a codification of previous common law and adds very little to the principles which were already in place.[122] This research has presented the

[122] Lynch (n 25).

argument that this provision has been diluted by the inclusion of the phrase 'have regard to' which gives executives free reign to discard external interests provided the outcome benefits the members. The duty to promote the success of the company introduced the enlightened shareholder value. Whilst this principle has received criticism, it does make a theoretical argument to consider wider stakeholders. Given this, a reform of s 172 could provide the legislative framework to support the social conception model. B Lab have drafted an amendment to this principle launching a campaign for 'The Better Business Act'.[123] The primary aim of the revision proposed by B Lab is the focus is on the directors promoting the purpose of the company that benefits wider society. The provision states that, 'a director of a company must act in the way the director considers, in good faith would be most likely to advance the purpose of the company, and in doing so must have regard'.[124]

The proposal then provides a list of factors almost identical to those outlined in sub-s 1 of s 172. The change of terminology in this proposal is that these factors must be considered to advance the purpose. The purpose has been defined as benefitting wider society and reducing costs. Whilst this amendment does address the need to consider societal interests, describing this as the purpose of the company is misplaced. If the very purpose of the company is to benefit society and reduce harm when considering the members, this does not align with the historical conception of the corporation. The purpose of the company is to serve an outcome which can benefit society and its members as a result. This amendment provided by B Lab UK appears to be the opposite of the shareholder primacy model. Mayer contends that the purpose is not to serve either of these needs and exists to set out what it intended to do, build the railways for example. Moreover, whilst widely drafted principles allow for some flexibility, they need to be sufficiently clear to allow directors to discharge their duties and be held to account. The purpose of eliminating harm or costs is subjective and may result in directors taking a more liberal approach, given the wording under the proposal remains 'have regard to'. This research proposes a more conservative

[123] Better Business Act, 'The Better Business Act: An Act to Amend the Companies Act 2006' (*Better Business Act*) <https://betterbusinessact.org/wp-content/uploads/2021/04/The-Better-Business-Act-2021.pdf> accessed 9 August 2021.
[124] Ibid 1.

amendment to the provision to achieve greater parity amongst stakeholders and shareholders.

Proposal 1 – Reform to Section 172

This proposal requires directors to consider members and stakeholders 'as a whole', a collective unit and consider them equally. It retains the list of considerations for the factors currently within s 172. This adjustment to the framing requires directors to consider stakeholders on greater parity and give them an equal share in executive consideration. This would be applicable only to public companies given that the justification for this change is predicated on ownership structures and corporate power. The proposal is therefore that the current s 172 would remain unaltered, and this provision is supplementary to apply specifically to public companies. It is proposed that the provision is amended to the following:

172A Duty to advance the purpose of the company
(1) A director of a public company must act in the way they consider, in good faith, would be most likely to promote the success of the company for the benefit of its members and stakeholders equally as a whole, and in doing so have regard (amongst other matters) to—
(a) the likely consequences of any decision in the long term,
(b) the interests of the company's employees,
(c) the need to foster the company's business relationships with suppliers, customers and others,
(d) the impact of the company's operations on the community and the environment.

Proposal 2 – Amendment to Duty to Exercise Independent Judgment

This research has highlighted the benefits of and encouraged the use of new technologies to achieve the social conception model of the corporation. The challenge with the use of these new technologies arises in relation to knowledge transferred from the new technology to the natural director. Section 173, for example, provides that directors must exercise independent judgment. If the decisions they are making are guided and directed by new technologies, this could result in accidental breach of their duties as a director. Executives will often take advice from professional services such as accountants and legal counsel. The proposal of this provision seeks to extend this to the use of digital advice provided by new technologies. It can achieve this by way of an exclusion within s 173 such as the following:

(2) This duty is not infringed by their acting—

…

(c) in accordance with using authorised technology systems to assist the decision-making process.

This inclusion provides protection to directors by including it as a statutory defence. The authorised technology systems should be defined and regulated by external bodies to ensure this is kept up to date and monitored by a suitably qualified regulator.

Proposal 3 – Enforcement of Duties

The social conception of the corporation requires directors to consider wider society in their decision making. This section has argued this can be achieved through a re-framing of s 172 to encourage participation by directors. In order for this reformulation to be effective, there needs to be a route to enforce these duties. Shareholders have minority protections and can bring a derivative claim should a director breach one of their duties.[125] Without similar enforcement measures, the wider consideration is a right without a remedy. One method of enforcement is having a way in which a stakeholder can bring action should a breach occur. Given the breadth of stakeholders, widening the derivative claim to all stakeholders is not a persuasive argument due to the number of stakeholders who could be included within the definition.

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[125] Companies Act 2006 s 260

This research proposes that an external body, as the representative of stakeholders, be permitted to enforce the duties. Parkinson highlights that historically, there was a power held by the Secretary of State to bring civil actions on a company's behalf;[126] , however, this was subsequently removed with the latest iteration of the Companies Act.[127] Moreover, a 2017 report from the BEIS[128] put forward the proposal that an external party such as the FRC be permitted to bring actions for breaches. The report argued in favour of legislation to give the FRC sufficient power to hold directors to account for a breach of their duties. In 2021, a consultation on restoring trust in corporate governance was carried out.[129] It was acknowledged that the FRC does not have powers to enforce duties. Proposals were advanced for new reporting to 'sharpen' directors' accountability.[130] The report also proposes that the regulator have effective civil enforcement powers for public interest entities. This appears a progressive proposal. However, the focus on public interest entities limits the scope of the proposals and sets a higher bar for the corporation to fall within this category. This research advocates for a similar proposal where an external party can bring an action for a breach of directors' duty. This would be an independent body such as the FRC who would be able to bring a claim on behalf of the company for a breach of directors' duties. The inclusion of New Technologies and the ability to report on non-compliance or consideration can provide the platform for complaints to be made.

The use of an independent body can also function to include the wider stakeholder base. The independent body can collect complaints of breaches from stakeholders and evaluate pursuing them. This benefits stakeholders, as they gain not only a voice, but a platform for complaint if this is consistently ignored. Moreover, groups of stakeholders could have similar complaints, and an independent body would be more efficient in collating these and bringing an action, resulting in a more efficient process. This proposal is, therefore, an

[126] Companies Act 1985 s 438.
[127] Companies Act 2006 s 1179.
[128] Publications.parliament.uk., 'Corporate governance: Government Response to the Committee's Third Report of Session 2016–17 - Business, Energy and Industrial Strategy Committee'.
[129] Energy and Industrial Strategy Department for Business, 'Restoring Trust in Audit and Corporate Governance: Proposals on Reforms' (*gov.uk*, 18/03/2021) <https://www.gov.uk/government/consultations/restoring-trust-in-audit-and-corporate-governance-proposals-on-reforms> accessed 11 August 2021.
[130] ibid 16.

independent body who have the legislative backing to bring an action for a breach of directors' duties. This proposal, when coupled with the amendment to broaden s 172, provides a stronger framework for stakeholders to have their interests considered. These broader interests provide for greater legitimacy for the power held by corporate groups.

6.7.2 Encompassing group coverage

The proposals outlined in 6.7.1 are centred around the public company. This is due to the wide diffusion of shares and the public interest, which is intrinsically linked; this in turn justifies a departure from the pure shareholder primacy model. The BEIS proposals have likewise focussed reforms on public interest entities. Therefore, the proposals applying to public companies are academically defensible. However, as identified by this research,[131] large corporations operate exclusively as corporate groups, and therefore a narrow definition of public company will be problematic in achieving the aims these reforms seek. Therefore, this thesis advocates for a broader definition of public company for the purposes of directors' duties to correlate to the larger economic enterprise they are a part of. Insofar as a private company (Ltd) is wholly or majority owned by a public parent, the duties will be commensurate to that of the parent company irrespective of the private incorporation. Majority owned can be defined as the parent company controlling more than 50% of voting stock, irrespective of this being directly or indirectly held. The justification for this more comprehensive definition is to ensure correlative accountability on the part of directors. The risk remains that if the proposals above only relate to public companies (PLCs) then the parent might operate as a holding company and the subsidiary, a private company, will avoid the requirements for a more social conception. Therefore, by widening this definition it considers the reality of the group, substance over form. If a private company operates as part of a larger group, for which the parent is a public company, the directors of the private company will be subject to the same enhanced duties of the ultimate parent.

[131] See chapter 5.

This expansive and inclusive definition of what is considered public for the purposes of these proposals is more persuasive than applying them to all companies, both public and private. This is due to the volume of companies on the register. Private limited companies make up 93% of all companies on the register, whereas public limited companies equate to less than 1%.[132] Many of the companies on the register are small and medium enterprises and as such, enforcing societal considerations is not as defensible. They are likely to have fewer stakeholders and less power wielded. The cumulation of these renders the argument in favour of these principles applying equally to be unpersuasive. The superior approach is to have the amendments over those with a public interest and provide an avenue to include links to private subsidiaries and connected companies.

This section has considered how the implementation of the social conception can be facilitated by legislative reforms. It has considered how providing support for directors delivers an obligation to consider wider stakeholders. Moreover, if this obligation is not adhered too, extended routes exist to bring a claim against a director for a breach of their duties. It is submitted that these proposals provide the guidance and framework for directors to adopt the social conception of the corporation giving greater inclusion to stakeholders and shareholders. This can be achieved through the use of new technologies to fully support the implementation and consider big data and wider societal factors. This shift in paradigm will result in wider societal and environmental factors being considered at board level. This consideration provides the justification and legitimacy for wielding power in the corporation due to the increased control mechanisms introduced.

6.8 Challenges of reconceptualisation

The implementation of changing the way in which the corporation is conceptualised brings with it challenges which require further consideration. This section will evaluate the significant challenges that present themselves when

[132] Gov.uk, 'Companies register activities: 2020 to 2021' (Gov.uk, 2021) <https://www.gov.uk/government/statistics/companies-register-activities-statistical-release-2020-to-2021/companies-register-activities-2020-to-2021> accessed 11 August 2021.

considering this more social conception. To this end, it will evaluate if these can be mitigated, or if they are unsurmountable, rendering the proposals unfeasible.

One challenge to this reconceptualisation relates to the capital markets and the potential effect on the capital market with the inclusion of a more social model. The shareholder primacy model asserts that the shareholders, as the owners of the corporation, are entitled to dividends as residual claimants. A realignment poses the challenge of the wealth maximisation being diluted and less capital invested into corporations. Investors may consider that they are beneficially entitled to the profits of the company and that a deviation of this is not justifiable. This argument, however, can be rebutted. The context of capital investment is based on returns, and the market regulates corporations. The reconceptualisation would apply to all companies[133] equally, therefore levelling the market and still enabling the market to offer regulation. Enforcing all companies to adopt this change prevents significant disruption to singular companies. This is partially due to the changing in market needs. Kay contends that there is a clear distinction between 20th and 21st-century companies and, as a corollary of that, their market needs.[134] Companies in the 20th century required capital as they were producers of goods, such as General Motors and Britain's ICI. However, of the largest companies currently – such as Apple, Amazon, Alphabet and Microsoft – none are large producers. They largely provide services, and as such, there is a decreased need for capital due to leased warehouses and stores. The need for working capital has all but disappeared. Moreover, Stout contends that the convention of measuring success on the basis of the stock market single metric is puzzling.[135] The result is that any opposition to a reconceptualisation based on market capital is misplaced, given the landscape of the current market.

A further challenge exists in identifying the relevant stakeholders to be considered within the more social conception. Given the impact large corporations have on society, if every connected party was to be considered, this would not be an

[133] Within the proposed definition of public.
[134] John Kay, 'RIP PLC: The Rise of the Ghost Corporation' (*John Kay*, 3 March 2021) <https://www.johnkay.com/2021/03/03/rip-plc-the-rise-of-the-ghost-corporation/> accessed 12 August 2021.
[135] Stout (n 4).

efficient or economic method of conducting business. Therefore, establishing the correct parameters of the stakeholders to be considered is of significant importance. This can be established by utilising a definition whereby those who have directly invested human capital gain automatic consideration within the model. Wider stakeholders are to be covered by the consideration of society in general; this viewpoint is to be determined by the Rawlsian approach. Irrespective of the way in which stakeholders are identified, the requirement to consider stakeholders as a whole on parity with shareholders provides for a more social conception due to the departure from shareholder maximisation. Therefore, whilst identifying specific stakeholders might be difficult, the inclusion of them as a 'class' for consideration supports the pluralist social conception. Moreover, the use of new technologies provides the platform to consider a wider set of data and feed into the decision making of the board, resulting a more informed board complemented by this technology.

Acceptance of this reconceptualisation is a further challenge, as the dominant theory of the corporation has been in place for a century. Despite this dominance, this theory has been challenged, Stout contends that this conventional view is on the brink of intellectual failure.[136] Donovan contends that this has been based upon historical norms which require reconsidering to realign with the modern corporation.[137] This research has presented its own empirical analysis to evidence the widespread dispersion of shares, which demonstrates this narrow view to be misplaced. The public company is a creature of the state and operates to serve the public interest, and the conception of the corporation should align with this interest. Therefore, whilst acceptance of the model might receive criticism from investors, there remains a legal basis upon which to justify the consideration of more social conceptions.

The challenges of this reconceptualising can, therefore, be rebutted with considered responses and methods of implantation. Additionally, research carried out by Hanbury Strategy investigated UK public responses to corporations and their 'operating system'.[138] This research identified that 72% believe that

[136] ibid.
[137] Donovan (n 57).
[138] B Lab, 'Our economic "operating system" needs upgrading' (*Hanbury Strategy*) <https://bcorporation.uk/system-upgrade> accessed 12 August 2021.

business should have a legal responsibility to the planet and people alongside profits. This supports the pluralist approach advocated by this research. Furthermore, research carried out by McKinsey & Company asserts that following the recent COVID-19 pandemic, firms need to be more resilient to survive and that this importance has translated into board considerations.[139] This resilience can be derived from longer-term considerations and wider considerations as opposed to a short-term focus on shareholder returns. Therefore, the challenge of acceptance within the firm appears more feasible than ever before due to the requirement to change following COVID-19.

6.9 Summary

This chapter has considered how legitimacy for corporate groups wielding power could be achieved. It first considered the dominant theory, that of the shareholder-centred approach which focuses on maximising shareholder wealth. The chapter identified why this theory has become the leading theory and how it has historically been defended. This provided the chapter with a framework to depart from the traditional theory. The chapter moved to consider how the theory of the firm could be realigned. In doing this, it considered the failures which had arisen as a result of the dominant theory. This section provided justification to consider alternate theories of the corporation. The chapter advocated for an alternative conception which deviates from the shareholder primacy model. The failures of governance and the capital market, when coupled with the empirical economic reality support this realignment.

Alternative theories of corporate law were considered with the aim of deriving legitimacy where the dominant theory had failed to do so. The chapter evaluated the nexus of contracts model, though the inability to recognise the corporation as an entity rendered this argument futile. The second theory that this chapter considered was the social conception of the corporation. This social conception had been theorised differently by scholars and had a broader approach. The

[139] Celia Huber, Frithjof Lund and Nina Spielmann, 'How boards have risen to the COVID-19 challenge, and what's next' (*McKinsey & Company*, 29 April 2021) <https://www.mckinsey.com/business-functions/strategy-and-corporate-finance/our-insights/how-boards-have-risen-to-the-covid-19-challenge-and-whats-next> accessed 12 August 2021.

pluralist social conception of the corporation was argued to have the capacity to generate legitimacy for power held by corporate groups. This pluralist model was considered to be the most persuasive due to its ability to provide equilibrium to both shareholders and stakeholders. The chapter also considered how the 'societal' could be included and how this could be quantified, calculated and included within wider considerations. The Rawlsian approach to determining societal interests was favoured given its ability to consider liberal ideologies without a significant imbalance of weight between stakeholders.

New technologies were introduced as implementation methods. The result in including a wider societal consideration is more data and information to process. The use of technology can support the collection of this data and its processing. It was argued that AI could be used to calculate and weigh up respective parties and report back to the executive board. Legislative amendments were proposed to facilitate both the social conception and the use of new technologies to achieve these.

This chapter has investigated alternative methods of conceptualising the corporation and evaluated how an alternative theory could provide the legitimacy which corporate groups lack. The chapter argued that legitimacy can be derived from an alternative theory, ensuring that those who exercise power have it legitimised. This legitimacy which can be derived from an alternative theory permits the wielding of power corporate groups current exercise. The introduction of checks and balances allows corporate groups to utilise this power; however, this is only insofar as it is beneficial to a wider set of beneficiaries which extends past shareholder wealth maximisation. The shift in the conception provides the legitimacy which has been absent since the inception of the corporate group.

Chapter 7: Conclusion

'For the foreseeable future, we probably have to acknowledge the likely continuation of capitalism and the dominance of traditional corporations so we need to look for ways to improve their behaviours and graft features from the alternative organisational forms.'[1]

The significance of corporate power has undoubtedly increased since the expansion of the separation of ownership and control. The introduction of Corporate Governance Codes and increased governance mechanisms demonstrate that the demands of governance are firmly on the international agenda.[2] This thesis has sought to explore the notion of corporate power in its magnified state, the corporate group, to ascertain the legitimacy of the wielding of such substantial corporate power. The change in the growth of the corporate group has been impressive, resulting in this structure's ubiquitous use throughout large organisations. The focus of this thesis has been to explore how legitimacy can be understood in relation to corporate group power. In responding to this focus, the thesis explored four research questions to elucidate the understanding of group power.

This thesis argues that there is a legitimacy deficiency, when analysed through a CSR framework, of corporate power within the context of a corporate group. This results from a failure of debate and inclusion of control mechanisms to curtail potential abuse from the use of the corporate form in the group context. Furthermore, this thesis advocates that this legitimacy deficiency can be addressed in reconceptualising the corporation. Moreover, it argues that this is not an abstract ideology and is feasible through the use of new technologies.

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[1] Nina Boeger and Charlotte Villiers, 'Conclusion' in Nina Boeger and Charlotte Villiers (eds), *Shaping the Corporate Landscape: Towards Corporate Reform and Enterprise Diversity* (1 edn, Hart Publishing 2018) <http://www.bloomsburycollections.com/book/shaping-the-corporate-landscape-towards-corporate-reform-and-enterprise-diversity/conclusion/> accessed 29 January 2018, 371.

[2] See for example, OECD, *G20/OECD Principles of Corporate Governance* (OECD Publishing 2015); David Walker, *A Review of Corporate Governance in UK Banks and Other Financial Industry Entities* (HM Treasury 2009); Financial Reporting Council, *The UK Corporate Governance Code 2018* (London: Financial Reporting Council, 2018); Financial Reporting Council, *The UK Stewardship Code 2020*.

7.1 Synopsis of the thesis

Chapter one set out the thesis's key research question, namely, whether the legitimacy of corporate power differs in the group context and if so, if this requires reconceptualisation. The argument presented by this research is that legitimacy can be challenged in the group context based on evolution and an alternative framework introduced to attain legitimacy. Chapter one set out the CSR theoretical framework through which the research would be approached. This framework provided a definition and approach to how the term legitimacy would be used throughout the thesis. Moreover, chapter one introduced the interdisciplinarity methodology adopted throughout the thesis in addressing the research questions. This methodology is premised on the basis that law is autopoietic and evolves with the society in which it operates.

Chapter two examined the historical evolution which contributes to the legitimacy deficiency of corporate power. It contended that the lack of debate in the expansion of the bedrock principles of company law to groups is a significant contributor. This failure is twofold: first, corporate groups were not considered from the outset of company law principles, coupled with a lack of debate in the extension. This is analogous to Blumberg's historical accident principle he identifies in the American corporation. Second, the evolution of the corporate form has allowed significant power to be concentrated with parent companies. Chapter two contributed to the thesis by addressing the research questions, as it provided a historical framework to review historic legitimacy from the inception of the corporation. This framework allowed subsequent chapters to make comparisons when contrasting groups with their historical counterparts.

Chapter three delved into the role of corporate power, seeking to define how power in the corporate context may differ from others. It offered parameters through which power would be evaluated in addressing the research questions. Having outlined what corporate is within a corporation, the chapter proceeded to identify the holders of this power. The identification of holders of power within the corporation led to a further analysis of the Berle and Means corporation. This analysis from Berle and Means identified that there was an increasing separation between ownership and control. This thesis argues this is further separated within the modern corporation with increased dispersion of shareholders and even further dispersion in the corporate group. This separation requires legitimisation for the continued wielding of corporate power. Chapter three explored the Companies Act and its provisions to monitor and control power and further examined its applicability following the evolution of the modern corporation. This chapter provided a platform for the thesis to evaluate how corporate power can be understood. This allowed the legitimacy of corporate power to be analysed through the CSR theoretical framework.

Chapter four explored the dynamics of the corporate group, investigating the unique characteristics of the group and how power manifests itself. The construction of the corporate group offers unique benefits such as the ability to asset partition and judgment-proof assets whilst maintaining economies of scale. Following the analysis as to the unique benefits of the corporate group, the chapter moved to ascertain the reasoning behind the construction of the group. The structuring of a group is not inherently nefarious, and legitimate reasons for group structuring are often utilised. Legal, practical and political reasons are often cited as the cause for group structuring. The chapter advances the argument that given the addition of these unique benefits, there should be correlative control mechanisms placed on corporate groups. The benefits afforded to groups grant an advantage to group companies which further challenges the legitimate holding of corporate power. The chapter also argued that following the corporate power analysis in chapter three, the separation within the group between owners and controllers was even further removed.

Chapter five demonstrated the result of the extension of the modern corporation into the corporate group through statistical analysis and case studies of large enterprises. The argument was presented that this extension is without legitimacy and the use of the group is mapped out through statistical analysis and case studies of companies with the FTSE 100. The chapter included qualitative and quantitative analysis of the ownership structures of large corporations and their structural architecture. This structural architecture provided the thesis with a platform to view the practical construction of the group and the shareholding and control at varying levels. This demonstrated that the theory of extensive use of corporate groups and complex structures was a reality in the modern market. In addition to this visual representation, the study highlighted that shareholdings within parent companies are significantly diluted and diffused. This presents significant challenges in legitimising corporate power in the corporate group due to the weakened application of control mechanisms. The statistical analysis showed the clear and consistent relationship between the use of corporate groups and their financial strength. This is of significance due to the power corporate groups can hold, and this not being held to the same standard in the group context. Moreover, when analysing the subsidiary ownership through parent companies, the majority of companies within *dataset2* were either majority or wholly owned. This is of significance due to the control that the parent company can exert on its subsidiary companies. Further challenges of stakeholders within subsidiaries were also presented, as wider dispersion and narrower control reduces the ability of successful activism. The chapter also provided support for a realignment of the shareholder primacy doctrine to be further evaluated in chapter six. The considerable dispersion, and categorisation, of shareholders, is more aligned with a representation of society. This provides justification for greater consideration of stakeholders due to the departure of individualistic ownership. Therefore, the chapter progressed the research in two ways: firstly, in the omnipresence of the corporate group, and secondly, in identifying owners and controllers of powerful corporations as a study.

Chapter six explored ways in which the legitimacy deficiency could be addressed in the context of corporate group power. It commenced this from the current legal conception of the corporation, the shareholder primacy doctrine. From this, the chapter investigated any causal links between shareholder primacy and the facilitation of company law resulting in the widespread adoption of the group structure. To facilitate this analysis, the chapter identified why this theory has become the leading theory and how it has historically been defended. The chapter then progressed to consider other conceptions of the corporation and if in reconceptualising, greater democratic inclusion could be achieved. This greater inclusion is a pluralist model of the corporation and based upon this model, it was proposed that heightened levels of stakeholder inclusion could address the legitimacy deficiency. This is defensible on the grounds the shareholder primacy model has contributed to the failures of governance and the legitimacy deficiency which flows from this. Chapter six, therefore, challenged the notion of the Friedman doctrine, proposing alternative theories to give a greater social context to corporations operating in a social setting. This allowed the chapter to progress to consider alternative theories, from which the pluralist social conception was advanced as a model to achieve greater legitimacy for the use of corporate power. Moreover, this social conception can be justified on the basis that the beneficial owners of the large companies are analogous to that of society with increased shareholder diffusion. The chapter then progressed to consider how these wider stakeholder democracies could be introduced. The proposal is the use of new technologies in supporting the collection and analysing of the data inputs. AI and blockchain can provide the platform for shareholder and stakeholder voting for greater activism. Moreover, new technologies offer valuable tools for the board of directors in their decision making. It was submitted that these new technologies can support the implantation of this pluralist conceptualisation and that this can be done without wholesale reform to corporate law. Reform proposals to facilitate this change were presented, to include an obligation on s 172 compliance, an exclusion for the use of new technologies when exercising independent judgment. Furthermore, the chapter recommended the external enforcement of duties to ensure that more than lip service is paid to this new conception. This reconceptualisation affords greater inclusion to wider stakeholders and shareholders, which in turn generates greater legitimacy. As power is to be exercised for the benefit of more than just shareholders, greater controls are introduced. These controls and conceptions can be implemented through new technologies and enforced with minor amendments to existing provisions.

7.2 Responding to the research questions

The first task of the research was to explore the bedrock principles of company law which have facilitated the growth of the corporate group. The purpose of this analysis was to determine how these features have been extended to corporate groups and, if so, was this an accident resulting in illegitimate holding of corporate power? To address this question, the thesis surveyed the historical rise of the modern group. It evaluated the historical evolutionary development of the modern corporation and the importance of this evolution in the group context. In analysing this legal evolution, it also considered the judicial interpretation over time to draw parallels with the evolution of modern business. This provided a platform to demonstrate that attempts were made to recognise corporate group activity.[3] This was, however, contradicted as the courts returned to the principles in *Salomon*. In addressing the question as to the evolution of law, the thesis also sought to address the significance of specific company legislation. The findings of this historical analysis were that the evolution into the corporate group form failed to adequately debate the applicability of these bedrock principles to corporate groups. This failure has resulted in corporate groups not being held to the same standard as their 'non-group' counterparts and as such, has contributed towards a legitimacy deficiency. The focus on shareholder wealth maximisation has resulted in company law becoming facilitative of corporate groups without requisite specific legislation to govern their unique features.

Having established the historical significance underpinning the accidental extension to corporate groups, the thesis explored the nature of the corporate group and its power. The thesis sought to address the question, to what extent is corporate power magnified in the corporate group? A definition of corporate power was presented as an ability held by corporations to wield their will on stakeholders. With a definition established, the magnification of power was further evaluated. This is poignant, as the use of corporate power is permitted subject to adequate controls. Therefore, a corollary of magnified power should be accompanied by enhanced controls. The thesis identified unique challenges applicable to corporate groups, the most significant being the dilution of stakeholder interests increasing as subsidiaries become further removed from the ultimate parent. This exacerbates the already challenging position of corporate managerial power: coupled with diluted control mechanisms, the outcome is a legitimacy deficiency. The cumulation of accidental extension of bedrock principles to corporate groups without correlated control mechanisms has resulted in corporate groups wielding significant power without adequate controls. The control mechanisms were, historically, fundamental to the granting of limited liability and separate legal personality, which is the gateway to corporate power. The thesis, therefore, concludes that corporate power is magnified in a group context, and moreover, this magnification results in a legitimacy deficiency of corporate power for group companies.

[3] See for example: *DHN Food Distributors v Tower Hamlets LBC* [1976] 1 WLR 852.

This thesis sought to address the accidental extension of the benefits of incorporation to groups and the resulting magnified power resulting in a legitimacy crisis. To this end, two further questions were posed: firstly, can greater legitimacy be derived from an alternative framework or conceptualisation of the company? Secondly, if this alternative framework can resolve the legitimacy crisis, how can this be realised? To address these two questions, the research explored both the theoretical basis upon which company law is premised, through the lens of the CSR theoretical framework, and combined this with empirical analysis. The empirical analysis provided support for arguments in favour of alternative conceptions.

The remaining research questions revolved around deriving greater legitimacy and how this might be achieved. To answer these questions, the research explored two key facets: what drives the current illegitimacy and can this be rectified. To address these, the thesis collected empirical data and analysed the construction of corporate groups. This demonstrated the ubiquitous nature of the corporate group and their omnipresence amongst the most powerful corporations. The data also provided support for a departure from the Friedman doctrine of ultimate shareholder primacy. The data analysis identified a departure from individual ownership of corporations, which supports the proposition of a pluralist model of the corporation. The use of corporate groups allows inflated growth and financial power, which requires legitimising. This wide growth and dispersion provide the very basis for additional societal conceptions through a pluralist model to legitimise the corporate group. The thesis builds upon this data analysis by proposing ways in which the legitimacy deficiency within the corporate group can be addressed. It argues that there is a need to legitimise through democratic inclusion due to the increased corporate power and subsequent legitimacy crisis which arises from group structuring. Additional theories of corporate governance were evaluated with a pluralist social conception advanced as the most desirable and defensible. This conception was desirable as the eroded control mechanisms could be re-introduced to ensure power is not granted without checks and balances. It is also the most defensible, as a wide pool of shareholders within a PLC is analogous to societal ownership with multiple disconnected shareholders as the ultimate beneficiaries. Therefore, the thesis advocated for a pluralist social conception of the corporation which gives decision-making weight to both shareholders and stakeholders. To achieve this alternative conception, new technologies were explored to ascertain their suitability to facilitate a change in conceptualising the corporation. The research argued that with amendments in directors' duties, the use of new technologies as tools could enhance the use and uptake of this pluralist conception.

This thesis has explored the historical origins of the bedrock principles of company law and how the benefits of incorporation were extended to the corporate group. The conclusion drawn is that, in the UK, this was done with little to no debate and the corporate group is a product of evolution. This has in turn, diluted the control mechanisms initially linked with the benefits of incorporation. The result of this is that corporate groups maintain power and benefits, which are unique to corporate groups. However, despite this uniqueness, the governing principles remain the same in each and every company due to the iron grip of *Salomon*.[4] Having explored empirical data, the use of groups is synonymous with large organisations facilitating further growth with unfettered power. This results in a legitimacy failure due to the deficiency of control mechanisms. To address this failure, the research explored alternative conceptions and considered that a pluralist model of the corporation would reintroduce a legitimate basis upon which to hold and use corporate power. This model could be achieved through new technologies and the ability to consider wider stakeholder interests in conjunction with shareholder interests. This departure from the Friedman doctrine, shareholder primacy, can be justified based upon the construction of the ultimate beneficiaries of the corporate group.

7.3 Contribution of the thesis

This thesis set out to critically evaluate the role of power within corporate groups. Corporations often maintain power analogous to the state, and corporate collapse and failure have wide reaching consequences. A significant finding of this thesis is the omnipresence of the corporate group form, demonstrating its wide-ranging use. The way in which these groups operate means they do so without the

[4] *Salomon v Salomon & Co Ltd* [1897] AC 22 (HL).

legitimacy which should be attached to this power. The extension of bedrock principles of company law has been extended to the group without debate and consideration. This results in a legitimacy deficiencyMoreover, when evaluated against Carroll's pyramid of CSR,[5] corporate groups fail to ascend past the 'economic' and 'legal' elements of the pyramid. Viewed through this framework, the way in which the corporate group has been constructed lacks legitimacy. This thesis advances arguments to rise to the ethical and philanthropic elements of the pyramid resulting in greater CSR and thus correlative legitimacy.

The legitimacy deficiency argument has been central to the thesis. The concept is that the iron law of responsibility suggests those who exercise power must do so within the social context it is granted. The contribution this thesis makes is the advancement of the pluralist model of the corporation achieved through new technologies. It advocates for an alternative conception of the corporation in departure from the shareholder primacy doctrine and argues that this will address the legitimacy failure. This realignment into this pluralist model can be justified on the basis that legitimacy deficiency arises from a failure to wield power in the social context in which power is granted. Moreover, the data study carried out that revealed the use of the corporate group in all large corporations also identified significantly diffused shareholdings within parent companies. This diluted and diffused shareholder of parent companies challenges the notion of the shareholder priority nature of ownership.

This research, therefore, has contributed to knowledge through its demonstration of a legitimacy deficiency within the context of corporate group power. Moreover, it proposes a pluralist conception of the company to rectify this deficiency. This reconceptualisation is grounded in a robust CSR theoretical framework and is further supported by empirical data presented by this research. The contribution this thesis has made to the field is the enhanced understanding of how legitimacy is evaluated in relation to corporate group power. Moreover, it has introduced attainable methods, through new technologies, of achieving this, subject to further detailed studies.

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[5] Archie B Carroll, 'The Pyramid of Corporate Social Responsibility: Toward the Moral Management of Organizational Stakeholders' (1991) 34 Business Horizons 39.

7.4 Limitations and scope for future research

The coverage of this thesis has maintained some limitations. The focus of the research was to explore and analyse how legitimacy can be understood in the context of corporate group power, and as such there are limitations to what the thesis has been able to investigate.

One such limitation was that of the selected data set for the statistical analysis. Indeed, many more companies and corporate groups could have been included into the data set. This limitation is both logistical and methodological. The logistical limitation rests on the ability to collect and analyse the data. This thesis has collected the data for over 100 companies and analysed the structure and paradigms within them. Additional collection of data from a broader data set would present challenges of collecting and analysing within the scope of this research. The data collected and utilised within this research represents a broad range of companies and as such it is maintained that this sample size was sufficient to draw conclusions and address the research questions. The methodological issue was to identify the relevant companies to make up the data set. The hypothesis of the thesis is that corporate groups maintain illegitimate power given their size and structure. To test this hypothesis, a range of companies operating with corporate power within a corporation needed to be selected. The methodological approach was, therefore, to collect data from companies which were likely to exercise corporate group power on wider stakeholders. The *dataset1* was selected using the 100 largest private and public companies and *dataset2* was selected for a more in-depth analysis of high-value corporations. Whilst a broader set of data could have, theoretically, been sourced and included, for the purposes of the research questions posed, the methodological approach was to limit the data sets. The justification for this limitation lies within the socio-financial position in which they operate.

This research also discussed new technologies as tools to support implementation of a reconceptualised corporation. Whilst new technologies were discussed, the primary focus of this thesis was that of corporate group power and its legitimacy. The research provided potential avenues for implementation through RPA, blockchain and AI. The discussion and analysis as to the implementation of such tools was limited to their capacity to improve corporate governance and realise the new conception proposed by the research. Given the focus on corporate group power and legitimacy the analysis in this regard was limited to this. Analysis as to the technical implementation and alternative considerations for the use of new technologies would occupy its very own research paper. The discussion on self-driving corporations and these new technologies is a rising area of research and greater levels of interdisciplinarity will further enrich this field.

A final limitation of this research is the integration of private equity companies as parent companies, or as companies within the corporate group. There has been substantial growth in recent years within the private equity market,[6] with Reuters claiming the 'UK is for sale'.[7] This meteoric rise of the private equity market presents challenges of corporate governance due to the disparity in shareholders, with residual property rights, and investors. These challenges can manifest themselves in several ways and challenge the notion separation of ownership and control. With shareholders, able to hold managers to account through voting, the use of exit with diminished voice is increased within the private equity model. The primary aim of this thesis was to evaluate corporate group power and structural architecture of corporate groups. This structure within the private equity model differs from that of the group as identified in this research. Private equity takeovers are likely to include pre-existing groups, one such example is WM Morrisons Supermarkets take-over by CD&R, which operates with 96 companies within the group. This research has not explored how private equity companies as parent corporations operate and if this differs from public company ownership, for example. This thesis has presented proposals to achieve the reconceptualisation through additional obligations on public companies as parent companies. These proposals were based upon the preceding analysis of the data set comprising of mostly public companies. Notwithstanding specific proposals for public companies, the reconceptualisation of the corporate group is applicable to corporations wholly owned and controlled by private equity

[6] Robin Wigglesworth, 'Private Capital Industry Soars beyond $7tn' (*Financial Times* 11/06/2021) <https://www.ft.com/content/4d0e6f18-2d56-4175-98c5-e13559bdbc25> accessed 24 January 2022.
[7] '"UK for sale": Britain's year of private equity buyouts' (*Reuters*, 16 August 2021) <https://www.reuters.com/business/uk-sale-britains-year-private-equity-buyouts-2021-08-16/> accessed 24 January 2022.

investment funds. Further research into specific provisions is required for tailored proposals,[8] to align this with the theoretical framework presented by this research. The implementation of pluralist model of the corporate group in a private equity scenario has not been considered and would be the subject of further research.

Several key themes have arisen from the preceding chapters. It is hoped that this work will be capable of enhancing the understanding of corporate groups and the legitimacy of their power, which is not limited to the UK. This thesis has explored corporate group power and its legitimacy, and how these deficiencies could be addressed. It also introduces the notion of new technologies as a tool to assist in reconceptualisation. The new technologies and their intersection with corporate law as introduced have much scope for future research. This research advances the proposal that new technologies could be implement within the governance structure of the corporation. With this framework introduced, this provides further scope for research into how new technologies could be implemented and in what form. Research into capacity, bias and operational functions of new technologies within the company are areas which can be explored further with future research.

The preceding paragraphs identified limitations of the research, and with limitations comes with scope for further research. A further area with scope for future research is that of private equity. As elucidated above, private equity is growing, and with this growth is changing the corporate landscape. With the increase in the use of private equity, made available through ease of entry into the marketplace, there is scope for further research into legitimacy of power in private equity funds. The framework for understanding legitimacy within corporate groups can be transferred, with the implementation methods to be explored. The increasing investment into private equity has the capacity to further exacerbate short-termism and transfer concentrated power to those fund managers. Exploring how this power manifests itself in the context of private equity brings scope for an empirical study in this differing structure.

[8] Such as 'Proposal 1' for a reform of s 172 presented in chapter 6.

7.5 Concluding remarks

In conclusion, I hope this thesis is capable of offering an alternative academic conception of the corporation and how the legitimacy of corporate group power can be rationalised. Many of the key drivers for corporate group structuring are to afford benefits to beneficiaries and this thesis has sought to address both the 'how' and 'why' questions of group structuring and the legitimacy challenges of powers. It sought to challenge the notion of legitimacy of corporate power in the group context and explore alternative methods of analysing this legitimacy. It does not seek to offer a comprehensive depiction of influences upon management and their motives on group structures. However, this thesis takes issue with the shareholder primacy doctrine being the driver for such power given the separation between owners and controllers of large corporate groups. This research has sought to reconceptualise how the company is viewed and in so doing, addresses the legitimacy deficiency. This is achieved through a pluralist conception of the corporation through which wider stakeholders have consideration. This heterodox position may be challenged based on the historical proprietary nature of shareholding. However, I hope this thesis has been able to offer a justification from this departure from a position of orthodoxy.

Although the alternative suggestions put forth in chapter six, for the future of company law and governance, may be the subject to some scepticism. I believe the recommendations are capable of responding to problems identified in this thesis. They have the capacity for further development and refinement having opened new avenues of research. I hope that this work contributes to more social legal themes of work within the corporate field, especially considering a renewed rigour on sustainability and corporate responsibility. Whilst the proposals presented in chapter six may be the subject of contention and further refinement, they should not divert the attention from the central focus of the thesis. This is, firstly, to provide a clear definition of how we understand legitimacy of corporate power in the corporate group; and secondly, to devise regulatory mechanisms for controlling the power held by corporations. Only once these two are fully realised will economic democracy be achieved.

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Appendix A

Public companies (FTSE100)

Code	Name	Subsidiaries	How Many Companies in Group	How Many Subsidiaries	On how many levels	Turnover (bn)
AAL	ANGLO AMERICAN PLC	Yes	500	475	10	22.5
ABF	ASSOCIATED BRITISH FOODS PLC ORD 5 15/22P	Yes	525	384	8	13.9
ADM	ADMIRAL GROUP PLC	Yes	32	37	3	1.36
AHT	ASHTEAD GROUP PLC	Yes	126	109	3	5.05
ANTO	ANTOFAGASTA PLC	Yes	74	66	7	3.74
AUTO	AUTO TRADER GROUP PLC	Yes	9	11	4	5.57
AV.	AVIVA PLC	Yes	900	1,436	8	27.5
AVST	AVAST PLC	Yes	61	33	6	0.657
AVV	AVEVA GROUP PLC	Yes	1208	61	7	0.834
AZN	ASTRAZENECA PLC	Yes	233	222	8	18.4
BA.	BAE SYSTEMS PLC	Yes	628	586	5	18.3
BARC	BARCLAYS PLC	Yes	803	1,795	10	30
BATS	BRITISH AMERICAN TOBACCO PLC	Yes	716	214	10	25.9
BDEV	BARRATT DEVELOPMENTS PLC	Yes	195	526	6	3.42
BHP	BHP GROUP PLC	Yes	58	69	7	34.7

BKG	BERKELEY GROUP HOLDINGS (THE) PLC	Yes	392	345	5	1.92
BLND	BRITISH LAND CO PLC	Yes	407	422	8	0.613
BME	B&M EUROPEAN VALUE RETAIL S.A.	Yes	20	22	8	3.49
BNZL	BUNZL PLC	Yes	605	567	6	9.33
BP.	BP PLC	Yes	1395	1,493	7	213
BRBY	BURBERRY GROUP PLC	Yes	84	78	6	2.63
BT.A	BT GROUP PLC	Yes	315	194	10	22.9
CCH	COCA-COLA HBC AG	Yes	59	47	5	5.71
CPG	COMPASS GROUP PLC	Yes	1047	1,337	3	19.9
CRDA	CRODA INTERNATIONAL PLC	Yes	138	125	3	1.38
CRH	CRH PLC	Yes	1806	1,719	1	24.2
DCC	DCC PLC	Yes	424	113	10	14.8
DGE	DIAGEO PLC	Yes	436	316	10	11.8
ENT	ENTAIN PLC	Yes	285	181	6	3.41
EVR	EVRAZ PLC	Yes	169	162	9	8.97
EXPN	EXPERIAN PLC	Yes	255	192	10	3.73
FERG	FERGUSON PLC	Yes	645	30	7	15.77
FLTR	FLUTTER ENTERTAINMENT PLC	Yes	131	55	9	2.17
FRES	FRESNILLO PLC	Yes	54	28	3	1.6
GLEN	GLENCORE PLC	Yes	811	124	10	172
GSK	GLAXOSMITHKLINE PLC	Yes	632	156	10	33.8
HIK	HIKMA PHARMACEUTICALS PLC	Yes	86	81	3	1.66
HL.	HARGREAVES LANSDOWN PLC	Yes	15	814	2	0.551

HLMA	HALMA PLC	Yes	242	218	4	1.34
HSBA	HSBC HLDGS PLC	Yes	1932	2,529	10	74.4
IAG	INTL CONSOLIDATED AIRLINES GROUP SA	Yes	122	181	6	21.6
ICP	INTERMEDIATE CAPITAL GROUP PLC	Yes	447	185	10	0.414
IHG	INTERCONTINENTAL HOTELS GROUP PLC	Yes	427	399	8	3.49
III	3I GROUP PLC	Yes	390	288	10	1.14
IMB	IMPERIAL BRANDS PLC	Yes	339	353	10	32.6
INF	INFORMA PLC	Yes	428	39	7	2.89
ITRK	INTERTEK GROUP PLC	Yes	456	456	6	2.99
JD.	JD SPORTS FASHION PLC	Yes		161		6.11
JET	JUST EAT TAKEAWAY.COM N.V.	Yes	83	9	5	0.337
JMAT	JOHNSON MATTHEY PLC	Yes	161	146	7	14.6
KGF	KINGFISHER PLC	Yes	183	168	8	11.5
LAND	LAND SECURITIES GROUP PLC	Yes	252	257	5	0.741
LGEN	LEGAL & GENERAL GROUP PLC	Yes	463	3,019	8	11.7
LLOY	LLOYDS BANKING GROUP PLC	Yes	948	569	10	50.4
LSEG	LONDON STOCK EXCHANGE GROUP PLC	Yes	117	64	6	2.31
MNDI	MONDI PLC	Yes	231	147	9	6.15
MNG	M&G PLC	Yes	162	801	7	12.5
MRO	MELROSE INDUSTRIES PLC	Yes	603	290	10	11
MRW	MORRISON (WM) SUPERMARKETS PLC	Yes	91	75	5	17.5
NG.	NATIONAL GRID PLC	Yes	468	468	9	14.5
NWG	NATWEST GROUP PLC	Yes	1447	474	8	15.7

NXT	NEXT PLC	Yes	53	42	5	4.27
OCD O	OCADO GROUP PLC	Yes	31	28	4	1.76
PHNX	PHOENIX GROUP HOLDINGS PLC	Yes	405	314	6	4.18
PNN	PENNON GROUP PLC	Yes	51	113	4	1.39
PRU	PRUDENTIAL PLC	Yes	632	1,369	10	32.8
PSH	PERSHING SQUARE HOLDINGS LTD	Yes	2	13	1	0
PSN	PERSIMMON PLC	Yes	738	781	4	3.65
PSON	PEARSON PLC	Yes	395	381	6	3.87
RB.	RECKITT BENCKISER GROUP PLC	Yes	485	403	10	12.8
RDSB	ROYAL DUTCH SHELL PLC	Yes	1403	1,459	1	265
REL	RELX PLC	Yes	629	398	9	7.87
RIO	RIO TINTO PLC	Yes	457	396	10	32.5
RMV	RIGHTMOVE PLC	Yes	6	4	2	0.289
RR.	ROLLS-ROYCE HOLDINGS PLC	Yes	341	130	6	16.6
RSA	RSA INSURANCE GROUP PLC	Yes	130	107	7	6.46
RTO	RENTOKIL INITIAL PLC	Yes	379	323	10	2.71
SBRY	SAINSBURY(J) PLC	Yes	108	123	5	29
SDR	SCHRODERS PLC	Yes	343	3,120	6	2.54
SGE	SAGE GROUP PLC	Yes	162	134	5	1.9
SGRO	SEGRO PLC	Yes	270	256	4	433
SKG	SMURFIT KAPPA GROUP PLC	Yes	340	368	10	7.75
SLA	STANDARD LIFE ABERDEEN PLC	Yes	460	2,292	10	3.99

SMDS	SMITH (DS) PLC	Yes	331	314	6	6.04
SMIN	SMITHS GROUP PLC	Yes	352	322	6	2.55
SMT	SCOTTISH MORTGAGE INV TST PLC	Yes	0	82		28.9
SN.	SMITH & NEPHEW PLC	Yes	167	162	7	3.87
SPX	SPIRAX-SARCO ENGINEERING PLC	Yes	192	165	6	1.24
SSE	SSE PLC	Yes	144	199	6	6.8
STAN	STANDARD CHARTERED PLC	Yes	1568	192	10	18.8
STJ	ST.JAMES'S PLACE PLC	Yes	51	142	3	15.8
SVT	SEVERN TRENT PLC	Yes	71	66	8	1.84
TSCO	TESCO PLC	Yes	334	342	5	64.8
TW.	TAYLOR WIMPEY PLC	Yes	191	192	6	4.34
ULVR	UNILEVER PLC	Yes	283	392	6	44
UU.	UNITED UTILITIES GROUP PLC	Yes	27	29	4	1.86
VOD	VODAFONE GROUP PLC	Yes	415	391	10	39.8
WPP	WPP PLC	Yes	3107	647	5	13.2
WTB	WHITBREAD PLC	Yes	239	227	7	2.07

Private Companies

Name	Subsidiaries	How Many Companies in Group	How Many Subsidiaries	On how many levels	Turnover (bn)	Ownership
INEOS	Yes	477	2	10	5.87	Sir Jim Ratcliffe (60%), John Reece (20%), Andy Currie (20%)
EG Group	Yes	55	9	10	`16.9	Issa family (50%), TDR Capital (50%)
Greenergy Fuel	Yes	3624	28	10	0.04	Brookfield Business Partners (85%), management (15%)
Swire - JOHN SWIRE & SONS LIMITED	Yes	584	823	5	0.145	Swire family (67%), others (33%)
John Lewis Partnership	Yes	27	3	6	10.2	Employees (100%)
Pentland Group	Yes	0	88		6.44	Rubin family (100%)
Arnold Clark	Yes	53	37	2	4.24	Clark family and trusts (100%)
MFG	Yes	52	17	10	4.07	Clayton, Dubilier & Rice (>50%), management including Alasdair Locke (<50%)
Dyson	Yes	34	12	5	0.377	Sir James Dyson and family (100%)
JCB	Yes	74	66	3	0.0417	Bamford family interests (100%)
Bestway Group	Yes	46	2	9	4.31	Sir Anwar Pervez and family (88%), management (12%)

Iceland	Yes	37	12	8	3.19	Sir Malcolm Walker, Tarsem Dhaliwal, other management (100%)
Heathrow Airport	Yes	52	46	8	3.07	Ferrovial (25%), Qatar Investment Authority (20%), CDPQ (13%), GIC (11%), Alinda (11%), others (20%)
bet365	Yes	36	6	5	3.06	Coates family (93%), Will Roseff (7%)
Specsavers	Yes	1218	1092	5	1.53	Perkins family and joint venture partners (100%)
EMR	Yes	118	67	7	3.36	Sheppard family (100%)
Prax Group	Yes	37	19	7	2.42	Sanjeev Kumar Soosaipillai (50%), Arani Kumar Soosaipillai (50%)
Westcoast	Yes	13	2	4	2.26	Joe Hemani (100%)
Virgin Atlantic	Yes	77	1	10	2.78	Virgin Group (51%), Delta Air Lines (49%)
Rigby Group	Yes	84	9	5	2.77	Sir Peter Rigby (60%), family trusts (40%)
Laing O’Rourke	Yes	117	7	8	1.93	Ray O’Rourke and Des O’Rourke through Suffolk Partners Corporation (100%)
2 Sisters Food Group	Yes	87	4	9	1.2	Baljinder and Ranjit Boparan (100%)
Marshall Group Conglomerate	Yes	59	44	4	2.48	The Marshall family and family trusts (75%), others (25%)
Radius Payment Solutions	Yes	40	31	6	2.62	Bill Holmes (44%), Inflexion Private Equity (24%), Roy Sciortino (11%), other management (21%)
ISG Construction	Yes	93	2	10	0.538	Cathexis (100%)

Home Bargains	Yes	7	4	2	2.47	Tom Morris and family settlement (100%)
Mace Construction	Yes	74	3	5	1.78	Mark Reynolds (34%), Stephen Pycroft (14%), Gareth Lewis (13%), other management (39%)
Rubix	Yes	91	1	10	2.04	Advent International (>50%), management (<50%)
Thames Water	Yes	21	5	6	2.08	OMERS (32%), USS (11%), ADIA (10%), KIA (9%), others (38%)
Cobham	Yes	162	132	10	2.06	Advent International (100%)
Pension Insurance Corporation	Yes	4	1	3	7.14	Reinet Investments, CVC Capital Partners, Luxinva
The Very Group	Yes	66	14	8	1.99	Sir David Barclay and Sir Frederick Barclay family settlements (100%)
Chrysaor	Yes	31	0	8	1.54	EIG Global Energy Partners (90%), others, including management (10%)
Arcadia	Yes	84	76	9	1.82	Lady Tina Green and family, other shareholders
Mott MacDonald	Yes	137	47	8	1.78	Employees (92%), trust (8%)
Merlin Entertainments	Yes	226	200	10	1.74	KIRKBI Invest A/S, Blackstone, CPPIB, management
Neptune Energy	Yes	47	5	4	2.2	China Investment Corporation (49%), Carlyle Group (30.6%), CVC Capital Partners (20.4%)

Arup	Yes	92	76	5	1.81	Employees through trusts (100%)
Bloor Investments	Yes	85	62	6	1.7	John Bloor (100%)
Wates	Yes	60	21	4	1.55	Wates family (100%)
Healthcare at Home	Yes	165	5	9	1.35	Vitruvian Partners (73%), Erebus Holdings (17%), management (10%)
McLaren Group	Yes	141	1	8	1.49	Bahrain Mumtalakat Holding Co (57.8%), TAG Group (14.7%), Michael Latifi (7.7%), others (19.9%)
Clarks	Yes	73	46	5	1.47	Clark family (85%), employees and institutions (15%)
Wilko	Yes	21	2	3	1.43	Wilkinson family (100%)
Finastra	Yes	46	7	8	0.22	Vista Equity Partners (100%)
Anglian Water Group	Yes	66	2	10	1.455	CPPIB (32.9%), IFM Investors (19.8%), ADIA (16.7%), CFSGAM (15.6%), Camulodunum (15%)
Willmott Dixon	Yes	40	7	5	1.25	Family & management (100%)
W&R Barnett	Yes	63	15	8	1.36	Robert Barnett and family (100%)
William Grant & Sons	Yes	53	0	6	0.778	Grant and Gordon families
NES Global Talent	Yes	301	2	6	1.3	AEA Investors (>40%), management (<50%), Akastor (>10%)
Rontec	Yes	21	1	3	1.29	Ronson Family Trusts/Charitable Foundation (100%)
JCT600	Yes	26	19	3	1.28	Jack Tordoff (100%)

New Look	Yes	13	5	4	0.97	Alcentra, Brait, CQS, Avenue
Listers	Yes	5	4	2	1.21	Bradshaw family (50%), Lister family (50%)
Menzies Distribution	Yes	4	2	2	1.19	Endless Private Equity (90%), management (10%)
M Group Services	Yes	131	11	9	1.3	PAI Partners (85%), management (15%)
Greenhous Group	Yes	18	2	3	1.17	Derek Passant (52%), Kerry Finnon (46%), Mike Pawson (2%)
Lamex Food Group	Yes	76	14	4	1.17	Phil Wallace & family trusts (24%), Steve Anderson (24%), Colin Dicker & family trusts (16%), others (36%)
THG	Yes	66	22	6	1.14	Matt and Jodie Moulding (20%), management (6%), institutional investors (67%), others (7%)
A.F. Blakemore & Son Retail	Yes	23	17	4	1.14	Blakemore family (100%)
Paysafe	Yes	71	1	10	1.07	Blackstone, CVC, management
Matalan	Yes	11	0	5	1.13	Hargreaves family (100%)
Inmarsat	Yes	83	78	9	1.05	Apax (25%), Warburg Pincus (25%), CPPIB (25%), Ontario Teachers' Pension Plan Board (25%)
Reed Global Recruiter	Yes	21	5	4	1.07	Reed family and Reed Foundation (100%)
Yorkshire Water	Yes	31	3	7	1.06	GIC (34%), Corsair Infrastructure (30%), Pan-European Infrastructure Fund (23%), SAS Trustee Corp (13%)

Samworth Brothers	Yes	32	3	4	1.16	Samworth family trusts (100%)
KCA DEUTAG Group	Yes	91	32	10	1.02	Pamplona Capital, Al Qahtani Investments, BlackRock, Golden Tree, EIG Partners, other funds
Bourne Leisure	Yes	80	1	10	1.11	Family of Peter Harris, families of the late John Cook and David Allen, management
Nando’s	Yes	33	9	9	1.1	Dick Enthoven and family through Yellowwoods Investment Group (100%)
OVO Energy energy supplier	Yes	31	6	5	1.14	Stephen Fitzpatrick (66%), Mitsubishi Corporation (20%), Mayfair Private Equity (11%), management (3%)
Harrods Group	Yes	493	2	10	1.04	Qatar Holding (100%)
Collinson	Yes	55	3	6	1.01	Colin Evans (100%)
Arqiva	Yes	77	79	10	1	Canada Pension Plan Investment Board (48%), Macquarie (25%), other investors (27%)
LCC Group	Yes	7	9	2	0.924	Loughran family (100%)
Stoneacre Motor Group car dealer	Yes	9	3	4	0.826	Richard Teatum (51%), Christine Teatum (49%)
City Facilities Management	Yes	26	2	4	1.11	Haughey family (99%), others (1%)
OCS Group	Yes	60	2	6	0.432	Goodliffe family (100%)
Rothesay Life	Yes	13	7	2	18.9	Blackstone (36%), GIC (36%), MassMutual (26%), management & staff (3%)

Morson	Yes	31	7	8	0.952	Ged Mason and family (80%), Paul Gilmour (7%), Kevin Gorton (7%), others (6%)
Bowmer + Kirkland	Yes	53	31	3	1.07	Kirkland family and family trusts
WSH	Yes	34	2	10	0.873	Clayton, Dubilier & Rice, Alastair Storey and management
The Range	Yes	14	6	4	1	Sarah Dawson and family (100%)
River Island	Yes	104	6	5	0.88	Bernard Lewis and family (100%)
Henderson Group	Yes	20	5	3	0.563	Geoffrey Agnew (12%), Martin Agnew (12%), Ardbarron Trust (76%)
Pertemps Network Group	Yes	125	5	6	0.873	Management and employees (42%), Tim Watts (31%), LDC (27%)
AMC Group	Yes	34	6	4	0.889	Harold Sher (26%), Giles Robbins (11%), Charles Rowan (11%), others (52%)
Sir Robert McAlpine	Yes	40	2	7	1.04	McAlpine family (100%)
Stonegate Pub Company	Yes	74	74	1	0.853	TDR Capital (100%)
Vue International	Yes	66	56	7	0.848	Special purpose vehicles for OMERS and AIMCo (74.2%), management (25.8%)
Miller Homes housebuilder	Yes	45	2	8	0.841	Bridgepoint (>50%), other shareholders & management (<50%)
Bibby Line Group conglomerate	Yes	103	13	6	0.822	Sir Michael Bibby and family (89%), management and others (11%)
John Clark Motor Group	Yes	16	0	3	0.125	John Clark and family (100%)

Trailfinders Travel organiser	Yes	7	4	3	0.849	Mike Gooley (100%)
Domestic & General	Yes	18	2	4	0.413	CVC Capital Partners (>50%), ADIA (30%), management (<20%)
Fircroft Technical	Yes	105	2	9	0.8	Johnson family and management (66%), Equistone Partners (34%)
Park's Motor Group	Yes	13	9	3	0.813	Douglas Park and family (100%)
Dhamecha Foods Cash and carry wholesaler	Yes	5	1	3	0.794	Dhamecha family (100%)
Moto	Yes	16	15	2	0.781	Universities Superannuation Scheme (60%), CVC (40%)
Edrington	Yes	49	27	5	0.792	The Robertson Trust (71%), employees, former employees (19%), Suntory Holdings (10%)
Peel Ports Group	Yes	312	4	10	0.792	John Whittaker and family (50.1%), DWS Group (49.9%)

Appendix B

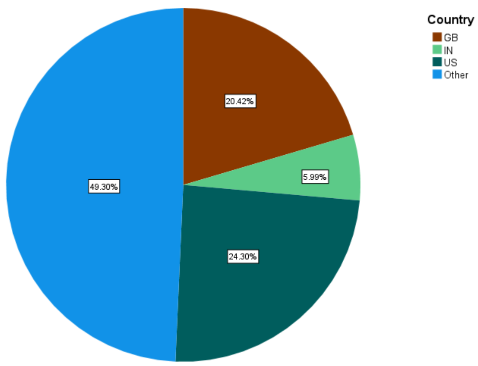

Figure 28 Land Rover Group of Companies

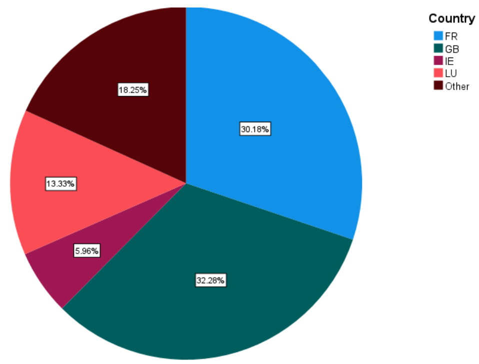

Figure 29 Aviva Group of Companies

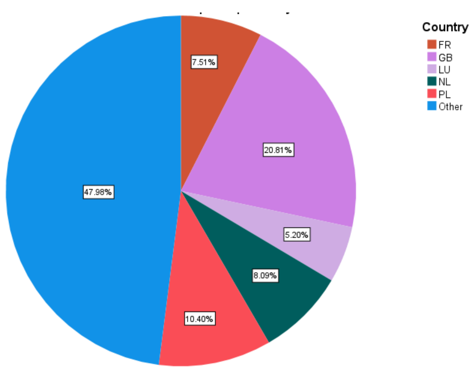

Figure 30 EY Group of Companies

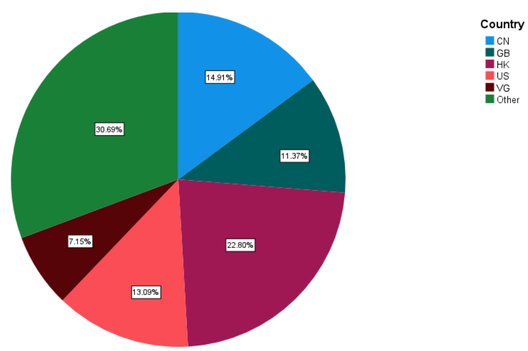

Figure 31 HSBC Group of Companies

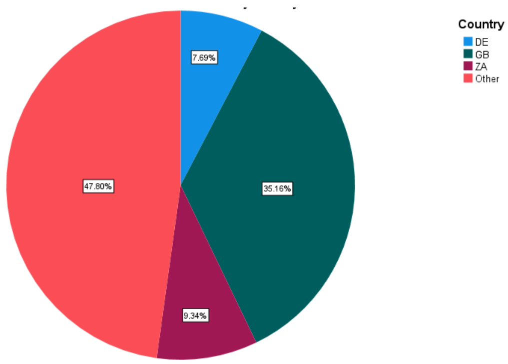

Figure 32 Vodaphone Group of Companies

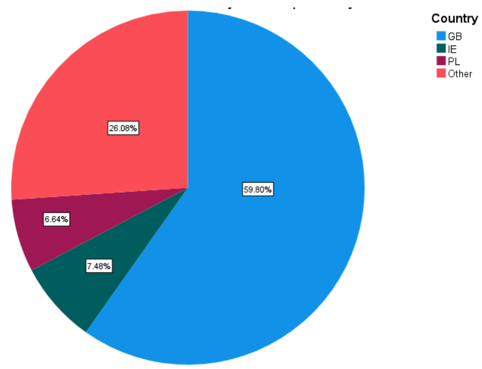

Figure 33 Tesco Group of Companies

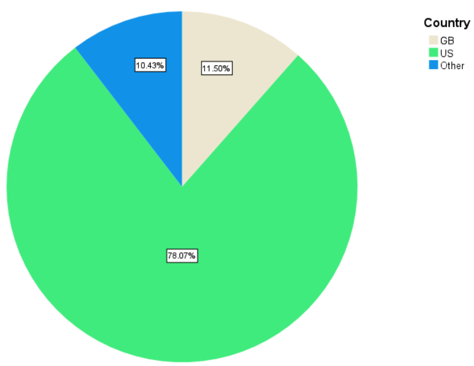

Figure 34 Sky Group of Companies

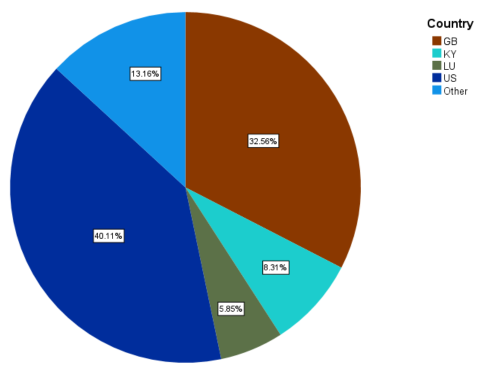

Figure 35 Barclays Group of Companies

Appendix C

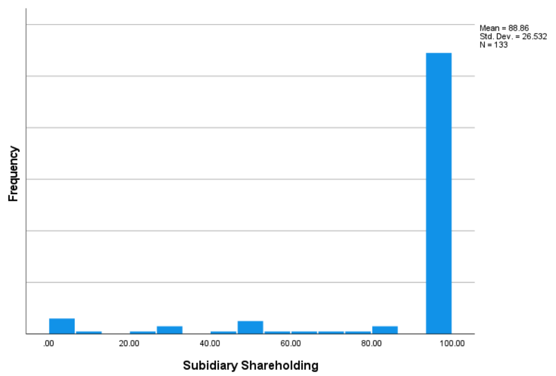

Figure 36 Figure 29. EY Histogram on Subsidiary Ownership

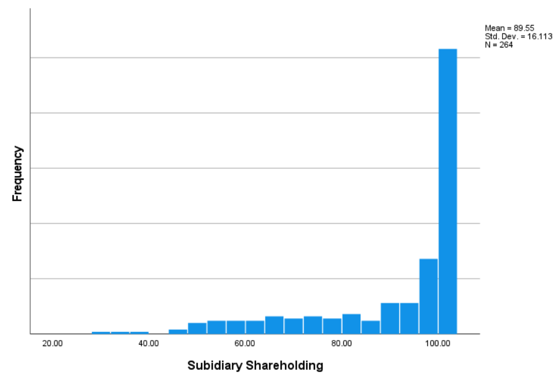

Figure 37. Aviva Histogram on Subsidiary Ownership

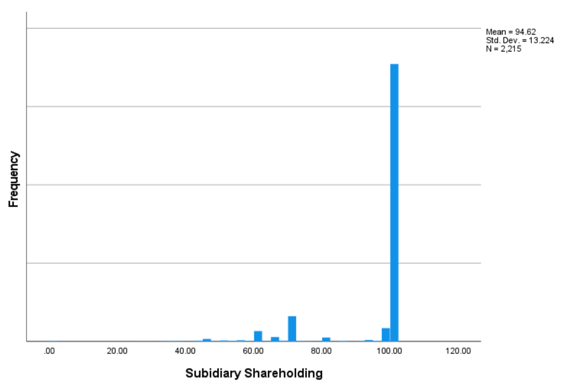

Figure 38 HSBC Histogram on Subsidiary Ownership

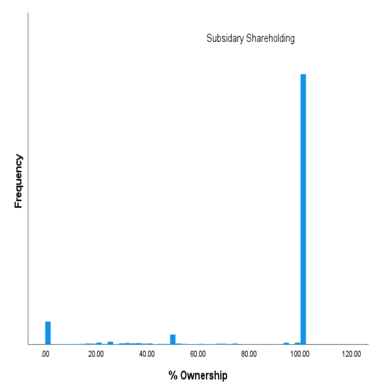

Figure 39 Shell Histogram on Subsidiary Ownership

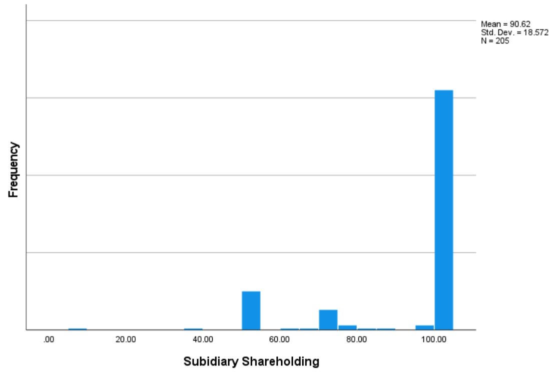

Figure 40 Land Rover Histogram on Subsidiary Ownership

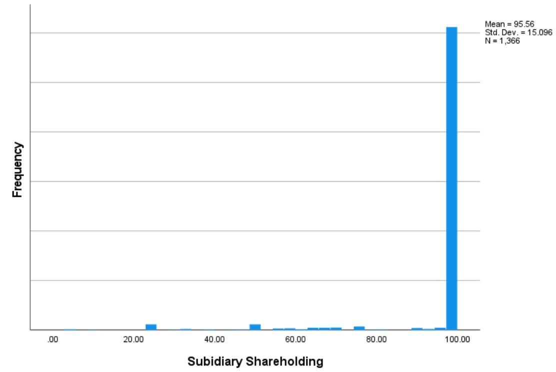

Figure 41 BP Histogram on Subsidiary Ownership

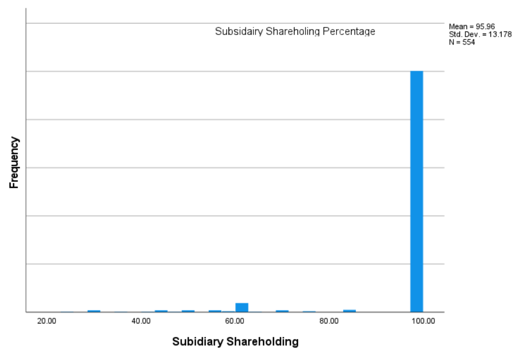

Figure 42 Vodaphone Histogram on Subsidiary Ownership

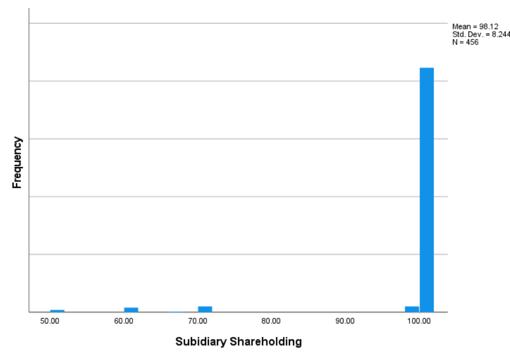

Figure 43 Sky Histogram on Subsidiary Ownership

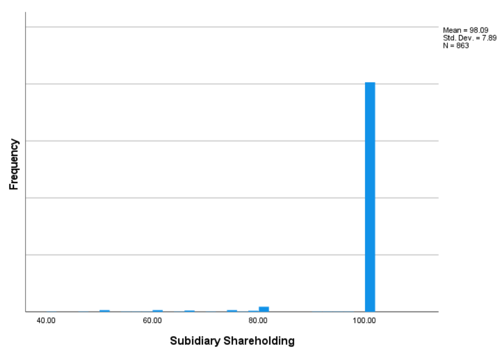

Figure 44 Barclays Histogram on Subsidiary Ownership

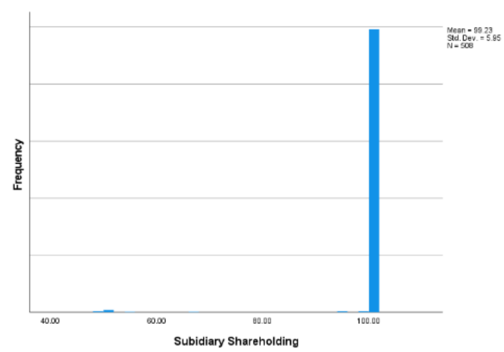

Figure 45 Tesco Histogram on Subsidiary Ownership

End