Enumerating Old Themes? Berle's Concept of Ownership and the Historical Development of English Company Law in Context

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I. Introduction

> Neither the claims of ownership nor those of control can stand against the paramount interests of the community. . . . It remains only for the claims of the community to be put forward with clarity and force.[1]

This radical statement encapsulates one of the key themes of Adolf Berle's work: stockholders no longer had a role in the corporation that entitled them to extensive claims in the corporation. Heralded in *The Modern Corporation*, his reconceptualization of the nature of ownership in the context of shareholding was based on empirical data on the massive level of share dispersal in America's largest corporations.[2] Stockholders had become too numerous and too dispersed to exercise control over "their" corporation. Instead, managers—the paid employees of the company—controlled the corporations. In this new arrangement, where business was dominated by management-controlled organizations as opposed to owner-controlled organizations—a shift dubbed by Berle as a "revolution"[3]—new guiding principles for corporations needed to be drawn. In this new corporate order the state was required to take the lead to achieve a morally correct balance of interests, a balance which rele-

† Associate Professor of Law, Warwick University, U.K. This paper is the first of two free-standing papers; the forthcoming paper will show how the marginalization of shareholder interests was only briefly achieved through wider social reforms and did not necessarily result from shifts in ownership and control.

1. ADOLF BERLE & GARDINER MEANS, THE MODERN CORPORATION AND PRIVATE PROPERTY 312 (Transaction Publishers 1991) (1932).

2. *Id.*

3. *Id*.

gated to the community both the longstanding interests of stockholders and the new control possessed by corporate managers.[4]

According to Berle in *The Modern Corporation*, these shifts in ownership and control meant that shareholder primacy models for the corporation were outdated: they were based on an outdated model of ownership and entitlement.[5] Shareholder ownership claims should no longer operate as the guiding force behind governance and corporate goals because the nature of that ownership had changed.[6] In the modern corporation, Berle argued, stock ownership had become a "passive" arrangement that was devoid of "spiritual values" and creative input. The owners were not able to directly employ their wealth and its value was dependent on outside forces.[7] Through such mechanisms as limited liability, the owners of stock, unlike the owners of tangible property such as land, bore little responsibility for their property. Correspondingly, owners of stock could not demand the extensive rights generally attributed to private property. Shareholder ownership claims were much more limited and were subject to wider community interest. Accordingly, shareholders were entitled to maintain the liquidity of their assets, protect their assets' unrestricted transferability, and have clear, accurate information on their assets' value—indeed, most of the protections suggested by Berle in his earlier Harvard Law Review piece.[8] However, shareholders' limited relationship and responsibility for their property correspondingly limited their claims. In other words, Berle attributed different normative values to different levels of ownership.

Thus, for Berle, when the large corporation separated ownership from control, "ownership" became a smaller bundle of legal rights that had an historical relationship with property rights but were not property rights themselves.[9] Stock property was, by its nature, more social than private and its owners could no longer claim private property-type rights. The normative values attributable to this level of property were small claims to modest returns after the claims of the community, particularly labour, had been met.

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4. *See* J.R. Boatright, *Fiduciary Duties and the Shareholder-Management Relation: Or, What's So Special about Shareholders?*, 4 BUS. ETHICS Q. 393 (1994). This article discusses some of the policy issues that arose from the Berle-Dodd debate.

5. *Id.*

6. Such sentiments have been voiced in a number of different ways. *See* Jane Wills, *A Stake in Place? The Geography of Employee Ownership and Its Implications for a Stakeholding Society*, 23 TRANSACTIONS OF THE INST. OF BRIT. GEOGRAPHERS 79 (1998).

7. BERLE & MEANS, *supra* note 1, at 79.

8. *See* Adolf A. Berle, *For Whom Corporate Managers are Trustees?*, 45 HARV. L. REV. 1145 (1932).

9. BERLE & MEANS, *supra* note 1, at 297.

In the United Kingdom, this radical theme in Berle's work has been lost. Generally, Berle is cited as an early commentator on share dispersal and the resulting problem of director accountability. This emphasis is particularly misleading, as it gives the impression that Berle was concerned with re-empowering shareholders to act as a bulwark against management power and also enabling them to assert their proper claims as owners. However, while Berle probably maintained a lifelong ambivalence to management power,[10] it seems clear from his work in and after *The Modern Corporation* that he was not concerned with re-empowering shareholders. That ship had sailed and society was the better for it. So why has British scholarship, law, and policy been so blind to the radical theme of downgraded shareholder claims?

This paper offers some tentative suggestions as to why Berle's work has been read and interpreted so selectively in the United Kingdom. I suggest that this must be partly attributable to the historical developments in English company law that entrenched the notion of shareholder ownership claims. Specifically, unincorporated associations' normative values—that members are owners and there is no distinction between small organizations with no share dispersal and large organizations with wide share dispersal—have a continuing influence on this entrenched notion of shareholder ownership claims. Part II will provide an overview of the origins of English company law. Part III will address how the Bubble Act encouraged unincorporated businesses and shareholder primacy. Part IV will discuss the influence of unincorporated business concepts in the early Companies Acts. Finally, Part V will conclude: Berle theorized that the disconnect between shareholder and company resulted in low shareholder entitlement and a corresponding "un-owned-ness" of the company; he further theorized that this could be the basis for social reforms. However, this was not the outcome in Britain. Instead, share dispersal was not a sufficient condition for the reconceptualization of ownership in Britain, given the strength of the legal shareholder entitlement model. A future article will build upon this thesis and will show that this model was only challengeable given the set of wider social reforms introduced in the post-war period.

II. THE ORIGINS OF ENGLISH CORPORATE LAW: AN OVERVIEW

The rudimentary beginnings of company law can be traced to the seventeenth century. Before that time, incorporation did not originally designate a form that was particularly distinct from an unincorporated

10. *See* William W. Bratton & Michael L. Wachter, *Shareholder Primacy's Corporatist Origins: Adolf Berle and the Modern Corporation*, 34 J. CORP. L. 99 (2008).

form.[11] Business associations were merely formed through different mechanisms, with some resulting in an incorporated association and some resulting in an unincorporated association. Incorporation was achieved through the grant of a charter by the crown[12] or, after the English revolution, by an Act of parliament.[13] Statutes were also used to extend the powers of the Royal prerogative so that they could grant charters with enhanced privileges.[14] Unincorporated associations, in contrast, were formed through differing levels of informal understandings. However, in terms of their post-formation characteristics, there were no significant differences between the two forms.

The first corporate form existed as a nexus of contracts and bore little resemblance to corporations as we know them today. Members of incorporated associations frequently made partnership arrangements between themselves, thus operating as unincorporated associations under the umbrella of a body corporate. For example, medieval guilds, which were associations of craftsmen in a particular trade, frequently sought incorporation in order to secure a monopoly over their trade. However, a guild's members would then often form unincorporated associations operating within the corporate body.[15] As early as the fourteenth century, merchant traders sought charters in order to secure monopoly trading rights. Like the medieval guilds, traders entered into agreements with each other as unincorporated merchant trading associations operating under the body corporate. The most famous among these charter compa-

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11. Paddy Ireland et al., *The Conceptual Foundations of Modern Company Law*, 14 J.L. SOC'Y 1 (1987). This article indicates the lack of distinction between shares in incorporated companies and shares in unincorporated companies during the period before the end of the nineteenth century.

12. Until the reformation, incorporation could also be conferred upon English religious bodies by the Pope. Dewey argues that the notion of fiction in respect to corporate personality originated with Pope Innocent IV, who sought to thwart the political power to punish ecclesiastical bodies by conceptualizing them as fictions incapable of guilt or liabilities. *See* John Dewey, *The Historical Background of Corporate Legal Personality*, 35 YALE L. J. 655 (1926).

13. Following the English Revolution, incorporation could also be achieved through statute; however, this route was not popular until the end of the eighteenth century. *See* PAUL L. DAVIES & L.C.B. GOWER, GOWER'S PRINCIPLES OF MODERN COMPANY LAW 19 (Sweet & Maxwell 1997).

14. It did this in the case of the Bank of England and the South Sea Company. *See generally* Peter Temin & Hans-Joachim Voth, *Riding the South Sea Bubble*, 94 AM. ECON. REV. 5 (2004); Julian Hoppit, *The Myths of the South Sea Bubble*, 12 TRANSACTIONS OF THE ROYAL HIST. SOC'Y 141 (2002); Ron Harris, *The Bubble Act: Its Passage and Its Effects on Business Organization*, 54 J. ECON. HIST. 610 (1994).

15. *See* Harris, *supra* note 14. Such associations or partnerships within the guilds fell into two identifiable forms. The first, the *commenda,* described an agreement where a financier of a trader was rewarded with a share of the profits rather than an agreed interest rate—much in the way of a sleeping partner. The latter form of partnership, *societas*, was akin to the modern partnership in that it was more permanent, the liability of partners was unlimited, and each partner was agent of the other. *Id.*

nies was the East India Company.[16] The East India Company began trading in 1600 with a membership comprised of both sole traders and partnerships that invested in joint stock with joint liability that terminated upon the completion of a particular voyage.[17] By 1652, permanent joint stock was introduced, but this coexisted with private trading until 1692 when the latter practice was discontinued.[18] During this period the incorporated body had an identity,[19] the East India Company, but it acted as an umbrella for a number of different commercial arrangements between persons. Thus, unlike the modern company, it really did exist as a nexus of contracts.[20]

The Bubble Act of 1720[21] subsequently conceptualized the incorporated company as a more distinct form. However, by the time it had done so, incorporation had already lost its popularity. In its place, the unincorporated form dominated business. The marginalization of the incorporated form meant that when the legislature sought to make incorporations accessible to all shades of business through the Joint Stock Companies Registration Act of 1844[22] (1844 Act). The Act described the new registered company in terms which actually described the dominant unincorporated forms: the partnership and the Deed of Settlement Company.[23] These post-Bubble Act unincorporated forms were distinguishable from the incorporated forms of this period[24] in a number of key respects. First, both the partnership and the Deed of Settlement Company were private legal arrangements between individuals. They were not, like the companies incorporated by charters, concessions from the state

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16. *See* C.E. Walker, *The History of the Joint Stock Company*, 6 ACCT. REV. 97 (1931).

17. DAVIES & GOWER, *supra* note 13, at ch. 1.

18. *Id*.

19. *See* Murray A. Pickering, *The Company as a Separate Entity*, 31 MOD. L. REV. 481 (1968).

20. It is interesting to note that Jensen and Meckling's new concept of the corporation as just a "nexus of contracts" is radically out of date—it describes arrangements which ceased to exist by the nineteenth century. *See* Michael C. Jensen & William H. Meckling, *The Theory of the Firm: Managerial Behavior, Agency Costs, and Ownership Structure*, 3 J. FIN. ECON 305 (1976); *see also* Melvin A. Eisenberg, *The Conception that the Corporation is a Nexus of Contracts, and the Dual Nature of the Firm*, 24 J. CORP. L. 819 (1999).

21. This Act was originally known as the Royal Exchange and London Assurance Corporation Act of 1719. The Act's full title is "An Act for better securing certain Powers and Privileges, intended to be granted by His Majesty by Two Charters, for Assurance of Ships and Merchandize at Sea, and for lending Money upon Bottomry; and for restraining several extravagant and unwarrantable Practices therein mentioned." Frank Evans, *The Evolution of the English Joint Stock Limited Trading Company*, 8 COL. L. REV. 339, 353 (1908) (quoting 6 Geo. 1, c. 18 (Eng.)).

22. 7 & 8 Vict., c. 109, 110 (Eng.).

23. *See* Geoffrey Todd, *Some Aspects of Joint Stock Companies, 1844–1900*, 4 ECON. HIST. REV. 46 (1932).

24. These incorporated forms differed from the new form of incorporation, which emerged in the end of the nineteenth century.

with all of those implied public responsibilities.[25] Second, they represented the property interests of the members who had contracted for self-interested commercial motives only. Furthermore, and in contrast to members of the later nineteenth-century incorporated forms,[26] members of these types of unincorporated forms were owners of the whole undertaking and thus had the expectations, responsibilities, and claims of private property owners.[27]

III. CORPORATE LAW, THE SOUTH SEA COMPANY, AND THE BUBBLE ACT

By the late seventeenth century, permanent joint stock, exchanging in an active market as a liquid asset, was beginning to emerge.[28] This type of stock was much more akin to our modern company share, and such a development might have heralded modern English company law were it not for the activities of the South Sea Company, a charter company that traded in South America during the 1700s. The South Sea Company's collapse at the end of 1720 and the catastrophic speculative bubble it inflated led to the large-scale abandonment of the incorporated form by businessmen and the contraction of the stock market.[29] At the same time, parliament passed a number of acts to regulate and limit the market in shares, including the Bubble Act.[30] Because of the events following the collapse of the South Sea Company, it was not until the nineteenth century that business regained its interest in the stock market.[31]

A. The South Sea Company

The South Sea Company's scheme to buy government debt was approved by Parliament in April 1720. One of the key aspects of this scheme involved persuading the holders of government bonds and de-

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25. For a full discussion of the Concession Theory, see J.E. PARKINSON, CORPORATE POWER AND RESPONSIBILITY (Oxford University Press 1993); *see generally* William W. Bratton, Jr., *The New Economic Theory of the Firm: Critical Perspectives from History*, 41 STAN. L. REV. 1471 (1989); David Millon, *Theories of the Corporation*, 1990 DUKE L.J. 201 (1990).

26. In modern corporate law, the company has a separate legal personality and shares of stock are titles to revenue, not claims to the whole undertaking.

27. L.C.B. Gower, *The English Private Company*, 84 LAW & CONTEMP. PROBS. 535 (1953).

28. 2 WILLIAM ROBERT SCOTT, THE CONSTITUTION AND FINANCE OF ENGLISH, SCOTTISH AND IRISH JOINT STOCK COMPANIES TO 1720 (1910).

29. *See* A. B. DUBOIS, THE ENGLISH BUSINESS COMPANY AFTER THE BUBBLE ACT 1720–1800 (Commonwealth Fund 1938).

30. The most significant of these acts were passed in 1734, 7 Geo. 2, c. 8, and in 1737, 10 Geo. 2, c.8. However, a number of acts had been passed in 1697 and 1708, prior to the Bubble Act. 8 & 9 Will. 3, c. 32 (Eng.); 6 Ann., c. 68 (Eng.).

31. *See* R. C. MICHIE, THE LONDON STOCK EXCHANGE: A HISTORY (Oxford Univ. Press 1999).

bentures to exchange them for South Sea Company shares.[32] In order to persuade bond holders that these shares were highly valuable commodities, the directors needed to push up the share price. And, as the company did no real trade, this could only be achieved by legal device, hype, and extravagant claims designed to create demand.[33] The South Sea Company set up an imaginative financial scheme which appeared to create money out of nothing. It funded dividends from new issues and offered interest-free loans to buy shares. Through these and other strategies, the company hoped to circulate investors' money profitably and indefinitely.[34] The speculative nature of this activity in which nothing of value was being created meant that share price represented shareholders' demand only. That demand was based on the shareholders' belief that the company was making real value, although that belief was utterly misguided. When shareholder belief in share value vastly exceeds real value because of, for example, successful hype, share prices are known as "bubbles." Bubbles are an apt metaphor because bubbles are delicate and they have little substance for the space that they fill—and when the air that puffs them up eventually stretches their material reality/fabric too much, they will burst.

The success of the South Sea Company spawned a general clamor to buy shares in other companies and unincorporated associations that had equally dubious business purposes.[35] The other companies' inflated stock prices created "mini-bubbles" that threatened the South Sea Company's bubble and profits. As a result, the directors and those involved in the South Sea Company sought government intervention.

B. The Bubble Act and Its Effects

In response to the South Sea Company's pleas for help, the government passed the hastily-drafted Bubble Act, which prohibited the sale of freely transferable shares by associations operating without a charter.[36] The South Sea Company hoped that the more restricted availability of

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32. *See* MALCOLM BALEN, A VERY ENGLISH DECEIT: THE SECRET HISTORY OF THE SOUTH SEA BUBBLE AND THE FIRST GREAT FINANCIAL SCANDAL (Fourth Estate Ltd. 2003).

33. *Id*.

34. *Id*.

35. *See generally* Ron Harris, *Political Economy, Interest Groups, Legal Institutions, and the Repeal of the Bubble Act in 1825*, 50 ECON. HIST. REV. 675 (1997).

36. *See* Bubble Act, *supra* note 21. The Act prohibited the raising of *freely transferable* stock without a charter, an emphasis which allowed the later growth of organizations that had some restriction on the transferability of stock. *Id*.

shares in the market would further enhance the value of the company's shares.[37]

Instead, the Bubble Act had a very different effect. The fearsome tone of the legislation undermined public confidence in share trading per se.[38] So even though the Act gave a temporary boost to the South Sea Company, after just a few more months of trading, the company's share price collapsed, and with it, the national economy.[39] As a result of this financial catastrophe, the Bubble Act—conceived as a short-term device—stayed on the statute books for one hundred and five years. That was the first unintended consequence of the Bubble Act.[40]

The second unintended effect of the Act was to conceptually sever the unincorporated association from the incorporated company.[41] As previously noted, the legal distinction between incorporated and unincorporated associations had not been clearly defined. Partnerships formed and confirmed under seal could provide for the division of interests into shares whose transferability was determined according to the terms of the partnership agreement. Many of the joint stock "companies" selling shares and contributing to the financial bubble were in fact unincorporated associations. This, of course, accounted for the prohibition against unincorporated companies in the Bubble Act.[42]

The third unintended effect was to enhance the role of unincorporated associations in the emerging English capitalist economy.[43] After the financial collapse exacerbated by the Bubble Act, the English gov-

37. There are a number of different perspectives on the passage of the Bubble Act. Some commentators have mistakenly identified its passage as a reaction to the collapse of the South Sea Company. *See* SIR WILLIAM BLACKSTONE, COMMENTARIES ON THE LAWS OF ENGLAND 117 (Univ. of Chicago Press 1979) (1765). These comments have had a huge impact on thinking about this issue. Scott views it as a more general attempt to control speculation in shares. *See* SCOTT, *supra* note 28. More recently, the Act has been discussed as a mechanism for legislatures to achieve higher rents by enhancing charter use, similar to legislative rent seeking in the nineteenth century America. *See* Henry N. Butler, *General Incorporation in Nineteenth Century England: Interaction of Common Law and Legislative Processes*, 6 INT'L REV. L. & ECON 169 (1986). This article does not attempt to assess these perspectives; instead, it follows the more generally accepted and historically verifiable line that the Act was concocted by Parliament to protect the South Sea Company.

38. *See* Harris, supra note 14. Harris argues that because the Act was passed on June 11th—and South Sea Company shares peaked on June 24th before sliding in August and collapsing in September—the Act itself cannot be blamed for the company's collapse. However, while it certainly was true that the company's failure was, at its core, due to the speculative nature of the scheme itself, the rapid decline after the Act cannot discount it is as being contributory to its speed of collapse. *Id.*

39. *See generally* Harris, *supra* note 14; *see also* DUBOIS, *supra* note 29.

40. Margaret Patterson & David Reiffen, *The Effect of the Bubble Act on the Market for Joint Stock Shares*, 50 J. ECON. HIST. 163 (1990).

41. *See* DUBOIS, *supra* note 29.

42. *See* Harris, *supra* note 14.

43. *See* DUBOIS, *supra* note 29.

ernment's shock and embarrassment made it generally averse to granting charters of incorporation.[44] The raising of joint stock had been described in the Act as "dangerous and mischievous to trade," and the ensuing financial collapse of the South Sea Company seemed to evidence the truth of that statement.[45] Companies with freely transferable shares were treated with suspicion by the public and by the government alike, and unincorporated associations became the preferred choice for business.[46] The uneasiness about how to apply the Bubble Act had one final unintended consequence: it created the company lawyer.[47] Businesses increasingly sought legal advice on the Act's applicability to their business and relied on lawyers to draft Bubble Act-compliant business structures.[48] As such, businesses became dependent on lawyers, who in turn developed their skills as business organization lawyers. In the Bubble-Act era, businesses increasingly called upon lawyers to construct complicated forms of unincorporated business organizations that could perform most of the desirable functions of incorporated bodies while remaining Bubble-Act compliant. The Deed of Settlement Company successfully performed this function.[49] Here, a company would be formed under a deed of settlement whereby the subscribers agreed to be associated with the company and held shares in accordance with the terms of the deed.[50] The property of the company was held by a body of trustees. Simple partnerships remained popular for small and medium-sized businesses and the common law honed partnership law as a result. Paradoxically, an Act that was designed to suppress the use of unincorporated business associations resulted in encouraging their proliferation:

> The Bubble Act had decreed a "new deal" for organized business, but the moral tone of the eighteenth century was not sufficiently advanced to appreciate the benefits of the new dispensation. In consequence, entrepreneurs and their legal advisors turned to the device

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44. *Id*.

45. *See* Bubble Act, *supra* note 21. In contrast to Parliament, the English judiciary was more sympathetic to those trading in shares. The first prosecution was in 1808 and it was unsuccessful. *Rex v. Dodd*, 9 East 527.

46. *See* Bishop C. Hunt, *The Joint-Stock Company in England, 1830–1844*, 43 J. POL. ECON. 331 (1935). Hunt examines the deep-set anxiety felt by British businesses regarding the corporate form in the early nineteenth century. However, as DuBois points out, the judiciary became more flexible in their approach to the Bubble Act after some years. *See* DUBOIS, *supra* note 29.

47. *See* DUBOIS, *supra* note 29.

48. *Id*.

49. *See* RONALD RALPH FORMOY, THE HISTORICAL FOUNDATIONS OF MODERN COMPANY LAW (Sweet & Maxwell 1923).

50. *Id.*; *see generally* BISHOP C. HUNT, THE DEVELOPMENT OF THE BUSINESS CORPORATION IN ENGLAND, 1800–1867 (Harvard Univ. Press 1936).

of the unincorporated association to affect their ends, and in this they were remarkably successful.[51]

C. Post-Bubble Act Unincorporated Businesses: The Reason for Enduring Shareholder Primacy

In the Bubble Act era, businesses generally operated as unincorporated associations.[52] Although businesses could be incorporated by an Act of parliament or through a charter grant, incorporation was only used for prestigious or quasi-public activities. The generalized use of unincorporated forms in the eighteenth and nineteenth century, coupled with the early tendency to merge these forms with incorporated forms, explains to a significant degree the enduring power of the shareholder primacy model in the United Kingdom today.[53]

As the legal norms relating to unincorporated associations began to merge with those of incorporated associations, the legal concepts that distinguished the two forms began to blur together. Historically, this developed through a number of points of contact between unincorporated and incorporated associations. For example, unincorporated associations' ownership norms simply continued as incorporated business's norms, even though this was a time when the two forms should have logically developed a new set of norms.

First, as noted earlier, prior to the Bubble Act, members of incorporated companies also operated as partners inter se. Partners were understood in common law to be co-owners of the partnership's property, to be jointly and severally liable for the partnership's debts, and to have a prima facie equal claim to profits and to operational control.[54] For example, members of guild charter companies and early merchant trading associations often operated as both members of an incorporated company and as partners inter se. Thus, incorporated associations were frequently operating as a holding body for many unincorporated associations. Additionally, before the Bubble Act, nearly all joint stock companies were unincorporated. Thus, companies had a long-standing tradition of owners who shared the characteristics of partners in the emerging law on partnerships. Unincorporated and incorporated associations were called "companies" and these business forms organized in an interconnecting fashion.

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51. *See* DUBOIS, *supra* note 29, at 216.

52. *See* Harris, *supra* note 14.

53. *See* D. Gordon Smith, *The Shareholder Primacy Norm*, 23 J. CORP. L. 277 (1998).

54. These principles are now consolidated in statute form and remain in force today. Partnership Act, 1890, 53 & 54 Vict. (Eng.).

Second, both before and after the Bubble Act, joint stock companies were associations of people bound together by joint liability and joint ownership regardless of whether they were incorporated or unincorporated.[55] Under common law, members of all companies, incorporated and unincorporated, were conceived as beneficiaries of the company's property.[56] According to Harvard academic Samuel Williston, shareholders had an equitable interest in both the company's tangible assets and profits.[57] Each share, therefore, was an equitable claim to the company's property: "the corporation held its assets as a trustee for the shareholders, who were in equity co-owners."[58] In respect to shareholder liability for company debts, Williston also showed that unless there were very specific reasons not to do so, shareholders were connected (in equity) to the obligations which the corporation owed to the outside world.[59] This obligation was treated in law as part of a company's assets and could be enforced through equity.[60]

The significance of the common law rule on a member's liability for a company's debts is that it indicates a common understanding that the company and the members had a property interest in the same assets (and therefore similar liabilities) if those assets became deficits, regardless of incorporation. The common law rules established in English courts continued to be applied in America as late as 1826,[61] which indicates how persistent the notion of conjoined shareholder and company property interests really was. In England, the separation of the share-

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55. *See* Harris, *supra* note 14.

56. *Id*.

57. *See* Samuel Williston, *History of the Law of Business Corporations Before 1800*, 2 HARV. L. REV. 105–124, 149–166 (1888).

58. *Id.* at 150. Furthermore, in cases involving the Statutes of Mortmain and Frauds and transfers involving real estate, which hinged on whether property interest in the shares of stock was realty or personalty, Williston found that the nature of the share depended on the nature of the corporate property. *Id*. Thus, he concluded, "if the shareholders have in equity the same interest which the corporation has at law, a share will be real estate or personalty, according as the corporate property is real or personal." *Id*. In respect to a fraudulent or mistaken transfer of shares, the acquisition by a bona fide purchaser for value was protected precisely because shareholders were not legal but equitable owners. *Id*. A transfer made without the knowledge of the original shareholders entitled only them to relief. *Id*. Williston also cites a case involving the shares of the New River Water Company, where the court held that the shares were realty because the company assets were real estate. *See* L.E. TALBOT, CRITICAL COMPANY LAW, ch. 2 (Routledge-Cavendish 2007).

59. Williston, *supra* note 57, at 150.

60. *See* Salmon v. The Hamborough Co. (1691) 1 Ch. 204 (U.K.). Likewise, in a 1673 case, the judge stated:

> [I]f losses must fall upon the creditors, such losses should be borne by those who were members of the company, who best knew their estates and credit, and not by strangers who were drawn in to trust the company upon the credit and countenance it had from such particular members.

Williston, *supra* note 57, at 162 (citing Naylor v. Brown, Finch, 83 (1673)).

61. Williston, *supra* note 57, at 162.

holder from the company's liability was achieved legislatively so that there was a specific intention to differentiate an incorporated company from an unincorporated association in this respect.[62] The common law position did not prima facie distinguish the liability of a member of an incorporated company from those of an unincorporated association.

Thus, before the Bubble Act, all companies adhered to the normative values of unincorporated associations, regardless of size and method of legal formation. The Bubble Act conceptually served those companies that were incorporated and could therefore sell freely transferable shares, and it thus differentiated incorporated forms from those that were not. However, because business rejected the incorporated form as a result of this Act, the normative values that existed for both forms before the Act continued to dominate. This had huge consequences when the legislatures drafted the first Company Registration Acts, which were modelled after the dominant unincorporated forms.

IV. THE COMPANY REGISTRATION ACTS AND UNINCORPORATED NORMS

A. Company Registration Acts: Blurring the Lines Between Unincorporated and Incorporated Companies

The Bubble Act was repealed in 1825. Later, the 1844 Act was introduced to facilitate incorporation through registration, thus potentially removing incorporation from the margins of business.[63] The 1844 Act provides more evidence of the extent that the ownership norms in unincorporated associations, particularly partnerships, continued to infect incorporated forms.[64] The legislation described members in partnership terms and described the company constitution in terms which reflected Deed of Settlement Companies—in other words, the legislation applied unincorporated norms to incorporated associations. The company constitution (the memorandum and articles of association) was said to bind each member as if it was "signed and *sealed* by each member."[65] Members retained full liability for obligations incurred through the company's

62. Limited Liability Act, 1855, 18 & 19 Vict., c. 133 (Eng.). Indeed, even today, a company's constitution must state the limitations of its member's liability. Companies Act, 2006, c. 46 § 9(2)(c) (Eng.) [hereinafter Companies Act 2006].

63. *Supra* note 22. *See* M. S. Rix, *Company Law: 1844 and To-Day*, 55 ECON. J. 242 (1945).

64. *See* HUNT, *supra* note 50.

65. The seal is significant because it was a continuation of the practices of Deed of Settlement companies and unincorporated associations. Indeed, the constitution continued to be termed as if it was a deed until the Companies Act 2006.

activities,[66] as in partnerships. Just as partners are liable for a company's debts, under the 1844 Act, members could also be compelled to pay "the full payment of all the Debts and Liabilities of such Company or Body, and of the Costs of Winding up and finally settling the Affairs of such Company or Body."[67] Finally, the Act explicitly implied that companies registered under the Act were in fact partnerships by providing that they may do such activities as "other Partnerships."[68]

The use of unincorporated association norms in the 1844 Act is unsurprising given the wider historical context in which the Act was passed. The dispersed share ownership in incorporated companies—which led Berle to question the nature and claims of shareholders—had not yet occurred. Therefore, there was no reason to discontinue the conceptual merging of incorporated and unincorporated forms any more than the Bubble Act had already done. In this period, business was closely held and both ownership and control echoed that of an unincorporated form. For example, the shares in these newly incorporated companies were often held in large, oddly-sized values that were not easily transferable and functioned similar to a partnership stake. Thus, owners of shares generally owned a large portion of the business and therefore exercised a high degree of managerial control.[69] This meant that the businesses newly incorporated under the 1844 Act were much more closely akin to partnerships than to the modern company in terms of legal form, judicial understanding of share ownership, ownership patterns, and management.[70] Indeed, aside from perpetual succession and the ability to sue and be sued as an individual, they were quite unlike modern companies. They were closely held organizations without any of the characteristics of Berle's management-controlled organization, which was characterized by limited liability, outside ownership, non-shareholding management, and shares (titles to revenue exchanging on an active share market).

Furthermore, although the Limited Liability Act 1855[71] (consolidated into the Companies Act 1862) might have enhanced outsider ownership, it actually had the effect of bringing more quasi-partnership arrangements under the incorporated umbrella. Because of the connection

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66. Specifically, "any judgement, Decree, or Order for the payment of Money." The Joint Stock Companies Registration and Regulation Act, 1844, 7 & 8 Vict. c. 110, § 25 (Eng.).

67. *Id*. at § 20.

68. *Id*. at § 25; *see also* Hunt, *supra* note 46.

69. This was not the case for the railroad or banking industries, where incorporation was achieved by charter or by a private act.

70. *Supra* note 22. *See* Paddy Ireland, *Company Law and the Myth of Shareholder Ownership*, 62 MOD. L. REV. 32 (1999); *see also* Gower, *supra* note 27.

71. The Act allowed members to limit their liability to the value of their fully paid shares.

between limited liability[72] and unethical business practices, larger, established businesses had eschewed its use.[73] Conversely, limited liability became an attractive option for small businesses[74] (and even, famously, one man companies) where outsider ownership was not a feature.[75] This option was attractive because English law, unlike much of continental Europe and the United States, did not provide for limited partnerships.[76] The Limited Partnership Act 1907 was comparatively late in coming and only provided for limited liability for inactive investing partners. Thus, when incorporation and limited liability through general Acts became popular in the last quarter of the nineteenth century, it was frequently used by people whose only access to limited liability was through incorporation but who in economic terms were either one man companies or small partnerships.[77]

B. Partnership Norms and Share Ownership

The continued use of the partnership norm in companies of different sizes and levels of share dispersal has impacted the legal understanding of the nature of share ownership in England. There are many tens of thousands of companies which are so small that they are described as quasi-partnerships because ownership and control is retained by the same people. However, because English common law does not prima facie distinguish large companies from small companies, the small companies have not been sufficiently conceptually severed from large Berlesian companies, particularly in respect to notions of ownership. Take, for example, the classic case of *Salomon v. Salomon Co. Ltd*. where an (essentially) single shareholder, who was also the only employee, sought to avoid personal liability for the company's debts on the basis that it was a

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72. *See generally* LIMITED LIABILITY AND THE CORPORATION (Tony Orhnial ed., Routledge Kegan & Paul 1982); Amalia D. Kessler, *Limited Liability in Context: Lessons from the French Origins of the American Limited Partnership*, 32 J. LEGAL STUD. 511 (2003); *see also* Walker, *supra* note 16.

73. *See* H. A. Shannon, *The First Five Thousand Limited Liability Companies and Their Duration*, 4 J. ECON. HIST. 290 (1932). Shannon notes that the Limited Liability Act was dubbed "The Rogues Charter." *Id*. The response to limited liability can be considered yet another unforeseen consequence of the Bubble Act.

74. *See* Frank H. Easterbrook & Daniel R. Fischel, *Limited Liability and the Corporation*, 52 U. CHI. L. REV. 89 (1985).

75. As Williston notes, although limited liability had been recognised as early as the late seventeenth century in cases like *Salmon v. The Hamborough Co*., (1691) 1 Ch. 204 (U.K.), this was mainly to protect the company from the member's creditors, and did not protect members from the company's debt because of the company's ongoing right to make levitations or calls for payments from its members. *See* Williston, *supra* note 57.

76. *See* Francis M. Burdick, *Limited Partnership in America and England*, 6 MICH. L. REV. 525 (1908).

77. *See* Shannon, *supra* note 73.

distinct legal person from himself. When the Court of Appeal rejected the separate corporate personality of Salomon Co. Ltd. because "the legislature never contemplated an extension of limited liability to sole traders or to a fewer number than seven,"[78] the House of Lords was quick to point out the fallacy of this position. Instead of distinguishing between large and small companies, the House of Lords pointed out that the number of subscribers and their involvement with the company was irrelevant because none of these members would be liable for the company's debts in a limited liability company.[79] Because a company was an entity (absent fraudulent registration) regardless of the number of members, vast areas of doctrinal company law have developed that are legally applicable to all companies, but which are only practically applicable to small companies. There are partnership norms that apply to all companies, but these norms are only relevant when a company's activity is posited on relationships of mutual trust.[80] Petitions on the basis of unfairly prejudicial conduct, for example, depend on some identifiable relationship between members of the company which are "partnership–like."[81] Furthermore, statutory mechanisms to regulate the fiduciary duties of shareholders or to protect minorities invariably apply to small quasi-partnership companies only.[82]

This means that much English company law doctrine encapsulates the notion of a participating shareholder, for whom ongoing relationships between other members is crucial to the running of the business and who maintains a close tie to the company's management and assets.[83] In short, it equates shareholders in a company to partners in a partnership—

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78. Salomon v. Broderip, (1895) 2 Ch. 323 (U.K.).

79. *Id.*; *see also* Bernard F. Cataldo, *Limited Liability with One-Man Companies and Subsidiary Corporations*, 18 LAW & CONTEMP. PROBS. 473 (1953).

80. *See* Ross Grantham, *The Doctrinal Basis of the Rights of Company Shareholders*, 57 CAMBRIDGE L.J. 554 (1998).

81. *See* Companies Act 2006, *supra* note 62, at § 994.

82. Companies Act, 2008, c. 46 § 994. *See* Bruce v. Carpenter [2006] EWHC 3301 (Ch.); Hawkes v. Cuddy [2007] EWHC 2999, [2008] B.C.C. 390 (Ch.). The Law Commission's empirical research indicated that the more common remedy sought by minority shareholders was for unfairly prejudicial conduct under §§ 459–61. Furthermore, research indicated that this remedy was almost exclusively sought by shareholders in very small companies. Of the court files relating to § 459, petitions presented to the Companies Court between January 1994 and December 1996, 233 out of 254 were inspected. Of these, 70.4% of the petitioners were minority shareholders and 96.6% involved private companies. Nearly 34% of petitions involved companies with only two shareholders and 48.1% of petitions involved companies with less than five shareholders. Only 4.3% of petitions involved companies with more than ten shareholders. THE LAW COMMISSION, SHAREHOLDER REMEDIES, (1997), No. 246 at 177–78.

83. Courts concerned with the statutory contract that exists between company and member occasionally held that a contract exists between shareholders inter se. Rayfield v. Hands [1960] Ch. 1; Hickman v. Romney Marsh Sheepbreeder's Ass'n [1915] 1 Ch. 881. However, in all such cases the company was a small, closely held organization. Ebrahimi v. Westbourne Ltd. [1973] A.C. 360.

this is the type of arrangement present in the facts of these cases and the quasi-partnership conception of small companies infects the notions of companies *per se*. In the early period of company law history, the legal conception of shareholders as partners or quasi-partners bore a reasonable relationship to prevalent business practice. However, as shares became more widely dispersed, such conceptions of shareholders should, as Berle argued, have been radically reformulated.[84] In English law they were not.

This takes us to a curious aspect in the development of English corporate law. Companies in which shareholding was more dispersed were developing contemporaneously with quasi-partnership companies, but the property nature of shares was reconceptualized in widely-held companies. Unlike partnerships, widely-held companies conceptualized their shares as personal property. The modern view of the share as personal property was established in *Bligh v. Brent.*[85] In that case, the plaintiff's assertion that the interest of the *cestui que trust* was co-extensive with the legal interest of the trustee was entirely in line with previous authorities.[86] Shareholders were equitable owners of the whole undertaking. Therefore if the company's assets were real estate, the shares were realty; if the assets were not real estate, the shares were personalty. However, the court held the shares in the company to be personalty rather than realty, regardless of the company's assets.[87] In judgement, Baron Alderton stated that shareholders had no claim on the assets—shareholders only had claim to the surplus that those assets produced. He conceptualized assets and profits achieved with assets into two different forms of property: the company owned the former, and the shareholder owned the latter. Thus, in the larger companies, shares were understood as a property distinct from those interests and claims held by partners. Shareholders' interest was becoming a tradable bundle of claims which were detached from company assets.[88]

Yet despite the reconceptualization of the property nature of shareholders' assets, in England it was not accompanied by a reconceptualiza-

84. *See* BERLE & MEANS, *supra* note 1.

85. Bligh v Brent, (1836) 2 Y. & C. 268. This case in fact involved a charter company with mainly personalty assets. For an assessment of the implications of this for Williston's analysis of the importance of this case, see TALBOT, *supra* note 58.

86. Williston *supra* note 57, at 149.

87. Under the terms of a will, whether shares were personalty or realty determined who could inherit them.

88. *See* Ireland et al., *supra* note 11. The authors here noted that Alderton's view had extended to all companies by the 1850s and cite to Sir John Romilly in *Poole v. Middleton*, 29 Beav. 646 (1861), who stated that shares in joint stock companies were effectively independent property. The authors also refer to Bacon, who stated that shares were no longer personal actionable rights, but were instead "freehold property." Ireland, et al., *supra* note 11, at 159.

tion of the nature of shareholder's claims and entitlement. Shareholders were still conceived as owners with the entitlement of owners, which seems to be more extensive than mere ownership of shares.[89] And, while in modern corporate law it is fully accepted that shareholders do not own the company assets, company doctrine still maintains the seemingly paradoxical position that shareholders are the owners even though they have no insurable interest in the company.[90]

Companies in the United Kingdom may be either small quasi-partnership companies with no outside share dispersal or large Berlesian organizations with a separation between ownership and control. However, the historical development of company law—specifically in the early Company Registration Acts and the continued use of partnership-like legal concepts in company law—has meant that large companies have not been conceptually severed from partnership-like companies. Thus, company law continues to characterize shareholders in all companies as owners.

V. CONCLUSION: BERLE AND THE NORMATIVE IMPLICATIONS OF PROPERTY OWNERSHIP

In the United Kingdom, shareholders continue to be considered the owners of companies and the proper recipients of corporate activity, regardless of the level of share dispersal. This, I have shown, is partly because of the historical development of company law: the interconnectedness of incorporated and unincorporated associations prior to the Bubble Act, followed by the dominance of unincorporated forms in the post-Bubble Act period, resulted in the legal internalization of normative values into company law that more properly belong to unincorporated associations. This continued even after the law itself had reconceptualized the property rights of shareholders so that they were no longer equitable owners of the whole undertaking. Shareholder primacy further developed when the Company Registration Acts introduced incorporation through registration and later allowed members to limit their liability. In the former case, this was because these Acts continued to describe companies in partnership terms, with corresponding implications for ownership; in the latter case, this was because the Acts encouraged small part-

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89. *See* Ireland, *supra* note 70. Ireland argues that the reasons for the continuous conception of shareholders as owners can be found in the conflict between church and economy over the usury laws. *Id.*

90. Macaura v. Northern Assurance Co. Ltd. [1925] A.C. 619. Insurable interest is a key attribute of owning property. *See generally* O. Kahn-Freund, *Some Reflections on Company Law Reform*, 7 MOD. L. REV. 54 (1944).

nership-like businesses to become incorporated companies, thus putting partnership-like disputes in the common law and legislation developing for companies.

Following Berle's thesis, this should have changed with the rise of dispersed shareholding, but it did not. For Berle, the changing nature of shareholding—severed from assets, personal involvement, and liability—has certain normative implications. In illustrating what his normative understanding of property ownership is and the nature of shareholding in the new setting of large corporations, Berle approvingly quoted German minister Walter Rathenau:

> No one is a permanent owner. The composition of the thousand fold complex which functions as lord of the undertaking is in a state of flux. . . . This condition of things signifies that ownership has been depersonalized . . . the depersonalization of ownership simultaneously implies the objectification of the thing owned. The claims to ownership are subdivided in such a fashion, and are so mobile, that the enterprise assumes an independent life, as if it belonged to no one; it takes an objective existence.[91]

Rathenau clearly indicated, as Berle himself maintained, that the shift in the nature of shares—now depersonalized as freely transferable intangible assets—has created a corresponding shift in the nature of the company itself. Now the company "takes an objective existence;" it has an "un-owned-ness" which has implications for future understandings of the claims of shareholders. The disassociation of shareholders' claims in the company—already understood as distinct from company assets and known as the doctrine of separate legal personality—freed the company from any overriding obligation to its shareholders. This "un-owned-ness" opened opportunities for the company to operate in a socially responsible fashion.

But, as the evolution of English companies indicates, the lack of "owned-ness" does not necessarily result in corporate social responsibility and a shift away from shareholder primacy. Indeed, recent company legislation has put directors under a statutory duty to promote the interests of shareholders.[92] The British conception of shareholder primacy, so influenced by the normative values of the unincorporated associations from which company law emerged, is vastly different than what Berle predicted corporations would be like and how he envisioned the nature of ownership. This is partly because share dispersal was not as complete in England as it was in the United States at the time of *The Modern Corpo-*

91. *See* BERLE & MEANS, *supra* note 1.

92. Companies Act 2006, *supra* note 62, at § 172.

ration. But it is principally because the notion of shareholders as owners (thus deserving primary consideration as an entitlement of that ownership) was too grounded in law, and the historical development of that law, to be shifted by such trifling things as the emergence of wide share dispersal. Berle's new ownership required wider social reform so that it could take root. As I will discuss in a future publication, this was partly managed in the context of Britain's shift to corporatism in the post-war period. It is possible that shareholding in widely-held organizations could shift away from the notions of entitlement which underpinned shareholder primacy in the United Kingdom; however, this could only happen in the context of radical reform in ideology, politics, and government policy.