Lost from view: the legal invisibility of managers in the U.K.

In this chapter, we explore the evolving relationship between managers, directors, shareholders and companies over the course of the twentieth century. Focusing on the U.K., we show that, during the first half of the twentieth century, an absence of law allowed managers to acquire considerable de facto authority and power within companies, and that this was legitimated by reference to the specific competences that managers possessed. The role of management was not only to rationalize production and to reduce costs, but also to develop new capabilities and to devise strategies by which enterprises would innovate by exploring the unknown, a role which brought with it new social responsibilities.[1] Company law, which predated the emergence of professional management, allowed space for managers to operate with the autonomy necessary to perform these functions, but did not guarantee it, making it vulnerable to later changes that sought to put shareholders back at the heart of the company. The second half of the twentieth century witnessed a succession of hard and soft law reforms which progressively diminished managerial autonomy and authority, transferring power to shareholders and independent directors. This transfer coincided with a move away from managerial conceptions of control, with their emphasis on balancing the competing interests at stake in the enterprise, towards an unbalanced system that creates powerful incentives for executives and managers to transfer value to shareholders (and themselves). As a whole, the chapter shows that law and soft law have exercised a powerful influence over the way in which companies are managed and governed in the U.K.

The chapter is structured as follows. First, we examine how changes to industrial activity drove the emergence of managerial authority in U.K. companies. After that, we show that that new authority was accommodated within existing legal structures but depended on company-specific arrangements for its continuity. Finally, we look at how those arrangements were

undermined and dismantled following changes to U.K. company law and corporate governance policy from the second half of the twentieth century onwards. We examine the legal changes that contributed to the emergence of the hostile takeover, the pressure from policymakers for companies to have boards dominated by non-executive directors and to align executive incentives with shareholder interests, and finally the recent drive to encourage shareholder engagement. A brief conclusion follows.

The emergence of a new managerial authority

The rise of the "modern corporation", which grew in number and size from the end of the nineteenth century, is often associated with both mass production and intensive capital requirements.[2] In the U.K., as elsewhere, incorporation and limited liability were available as a matter of right, allowing companies to raise funds on a massive scale and leading gradually to the well-known "separation of ownership and control",[3] which highlights the changing relationship between shareholders and directors: as the former became more dispersed, the latter gained greater power over the company and its affairs. However, this notion obscures another critical change which occurred at that time: the rise of management as a distinctive function, and the emergence of a distinction between directors and managers.[4]

Whilst it made little impact on the law, the rise of professional management had a huge impact on business operations and industrial relationships.

Under the influence of scientific management, managers first gained authority over workers as they started to prescribe the way work should be done.[5] But as company directors gradually

recruited men from the field from "outside" the company to run the company in their place, professional managers also gained authority over the shareholders. As Berle and Means put it:

> The factory system… brought an increasingly large number of workers directly under a single management. Then, the modern corporation, equally revolutionary in its effect, placed the wealth of innumerable individuals under the same central control. The independent worker who entered the factory became a wage laborer surrendering the direction of his labor to his industrial master. The property owner who invests in a modern corporation so far surrenders his wealth to those in control of the corporation that he has exchanged the position of independent owner for one in which he may become merely recipient of the wages of capital.[6]

The transfer of control to managers

Professional managers probably took control of larger industrial enterprises earlier in Germany and the U.S. than they did in the U.K., where families retained control for longer, although the pattern was far from uniform. Exactly when control of U.K. companies passed into the hands of professional managers has been a controversial issue. Chandler famously claims that under the U.K.'s system of "personal capitalism", entrepreneurs and their heirs "assembled smaller management teams" than their U.S. and German counterparts and continued to "play a larger role in middle- and top-management decisions" until well after World War II.[7] Cheffins follows Chandler and argues that dominant shareholders retained control of the board during the first half of the twentieth century.[8]

However, these arguments were rebutted by Foreman-Peck and Hannah's important empirical analysis of companies listed in the U.K. in 1911.[9] Their data shows that the "evolution of managerial control in the U.K. was substantially complete before 1914" with directors holding office "by virtue of their skills, knowledge, and networks, and promotion or recruitment to the board, not because they held preponderant ownership stakes." A look at the contemporaneous literature shows that these developments were more *ad hoc*, and managerial hierarchies less sophisticated, than they were in the U.S. or parts of continental Europe. However, they were no less real for that. In 1896, Slater Lewis published what Urwick and Brech describe as "the first example of a modern 'organisation chart' in British business literature",[10] showing a hierarchy from shareholders to directors to chairman or managing director, with the latter above a general manager. The general manager headed a large hierarchy, with works manager and chief engineer reporting directly to him. They argue that by 1916, "no writer on industrial management would have given a works manager any descriptions that left doubts about his inclusion among the ranks of the responsible executives."[11] Sargant Florence reports significant growth in the ratio of staff to operatives in the U.K. between 1924 and 1948, noting that management had become "more specialized and more graded into ranks from general manager to foreman and charge-hand".[12] By the middle of the twentieth century, it is clear that professional managers were increasingly being appointed to boards (e.g. up to three quarters in the steel industry in 1947).[13]

These developments are commonly explained on the basis that companies were growing, leading inevitably to shareholder dispersal, or that the complexity of business was increasing rapidly, calling for new strategic expertise. Whilst relevant, neither of these explanations fully explains the emergence and development of the managerial function.

Mechanization and the growing focus on "improvement" and innovation

One fundamental change in the 19th century came from mechanization. As Charles Babbage explained, the "accumulation of skill and science", which he termed "mechanical art", deeply transformed the nature of industrial manufacturing. Babbage called for a closer relationship between science and industry.[14] Engineers and managers were central to industry playing this new role of driving scientific progress.

The design and continuous improvement of machines and methods of working drove the emergence of new jobs and functions for which workers needed to be trained and retrained. The emergence of Taylorism, at the end of the 19th century, was indisputably a consequence of mechanization: the management of the workshop entailed a scientific examination of the work process and the development of new working methods. It changed the nature of the labour relationship: authority was no longer based on ownership but on knowledge and expertise. As Sheldon put it, management's "leadership is based upon knowledge rather than upon force… it operates through the application of a capacity trained in the investigation and solution of problems".[15]

With its relatively late transfer of control from families and incumbents to professional managers, the U.K. may have lagged behind the U.S. and Germany in terms of R&D and technological activity, although this is contested, and the causes of the relative weakness of some sectors of British manufacturing industry are complex.[16] It certainly witnessed the rise

of management-led, technology- or science-driven industries such as Rolls Royce, Leyland Motors, Lever Brothers (commercialising the discoveries of the chemist William Hough Watson) and the synthetic organic chemicals industry (building on discoveries of William Henry Perkin). As Burton noted, "It is chiefly in the manufacturer's appreciation of the scientific branches of his establishment, and of research work that the need lies."[17]

As professional managers organized collective innovation processes, they gradually gained in status and authority (in fact if not in law). The counterpart to this was a reduction in the authority of shareholders, which was driven not only by dispersal but also because the value of modern enterprise lay in its capacity to develop new technologies, to file new patents, and to educate and train new knowledgeable workers, rather than in its financial capital. Likewise, there was no guarantee that incumbent directors (who, as we will see below, were often strongly entrenched) would be able to do this. Hence *de facto* control gradually passed from the hands of shareholders and directors into the hands of salaried managers.

The social responsibilities of this new managerial authority

This transfer of authority required legitimation. Rather than serving private interests, management was presented as serving the collective interest in progress – or as Babbage put it, "the improvement, the wealth, and the happiness of our race".[18] Contemporaneous texts highlight the new role of management as trustee, impartial judge or arbitrator.[19] In forming a "purely neutral technocracy",[20] and carrying on industry "for the service of the public",[21] managers would transcend the division between capital and labour. Numerous writers during the early twentieth century linked professionalization to balancing the interests of capital and

labour.[22] Elbourne, for example, said that "the co-ordination of labour with capital is the outstanding problem of management today. The problem is no longer one merely of supervision; there must be inculcated a spirit of goodwill coupled with an adequate sense of discipline."[23] Similarly, Taylor argued that scientific management proceeds on the basis that "the fundamental interests of employés and employers… are one and the same",[24] and his ideas were gaining currency in management circles in the U.K.[25] Whilst obviously not all managers followed this approach,[26] a "public service" mandate was espoused by influential industrialists in the United Kingdom, including W. L. Hichens, Lord Leverhulme and Seebohm Rowntree, all of whom who claimed to regard industry as a national service. This refrain was so commonly heard that, as late as 1955, Gower, the U.K.'s leading company lawyer stated that "it has become almost an accepted dogma that management owes duties to 'the four parties to industry' (labor, capital, management, and the community) – a dogma which is repeated indiscriminately in the speeches of right-wing company chairmen and left-wing politicians."[27]

The Accommodation of Managerial Authority within the Law

None of these developments sat easily with existing legal frameworks because, for the most part, these managers were neither entrepreneurs nor inventors nor capital owners.

Legally, the gradual development of more sophisticated managerial structures was reflected in the U.K.'s relatively late adoption of the contract of employment, with master and servant laws only abolished in 1875. The subordination of the employee under the contract of employment was an essential component of the managerial hierarchy within the large

integrated enterprise. This allowed managers to direct the employees to different tasks as required. In return for subordination, the enterprise (and gradually the state) took on a growing responsibility for the safety and welfare of the employee.[28]

In labour law, this authority was embodied in the "employer", which by the late nineteenth century was normally a limited company acting through a combination of directors and managers. However, labour law never escaped its conceptual foundations in master-servant relations, so that managers are generally viewed merely as employees to whom management functions are entrusted by the "employer" company, "play[ing] in varying degrees the dual role of both managers and workers; they figure both as employers and employees".[29]

Whilst labour law ensured that the employer company had legal authority to direct employees, whatever the personnel through whom that authority was actually exercised, it fell to company law to determine how far managers would enjoy autonomy from shareholders and directors. Like labour law, its approach was pragmatic rather than systematic. Company law recognised only the directors as relevant actors, granting them by default a very wide power under the articles (i.e. the company's constitution) to manage the business of the company. It was common to require directors to hold "qualification shares" to align the interests of directors with the shareholders, and listed companies often chose to follow statutory companies and grant shareholders pre-emption rights, proxy voting rights and rights to requisition meetings.[30] Beyond these measures, however, the power of the directors to manage was constrained only by fiduciary duties to act in good faith and not to profit from their position, a very weak duty of care and the remote possibility of shareholder intervention in the form of a resolution to remove directors, which normally required a 75 per cent majority.

Shareholder litigation was difficult, as the courts refused to intervene in management decisions where the directors honestly believed that a decision was in the interests of the company (a type of protean business judgement rule), viewing this as an internal matter to be resolved between directors and shareholders in accordance with the company's constitution. Nor would the courts intervene on the grounds of "ultra vires" provided a decision was "reasonably incidental" to the company's business, a principle with wide limits that were very rarely reached.[31] There were also powerful procedural barriers (as well as economic disincentives) to shareholders litigating for breach of duty on the part of the directors. Removal of directors was also, for the most part, impracticable, by default requiring a special resolution of 75% of the shareholders, a threshold which became ever more difficult to reach as shareholders dispersed. This legal and de facto entrenchment of boards was not considered controversial within the investor community at the time,[32] and as late as 1932 the London Stock Exchange only required listed companies to make directors removable by special resolution.[33] Finally, in a series of cases between 1906 and 1935, the courts consistently ruled that shareholders were not permitted to interfere with decisions of the directors. A variety of justifications were offered for this principle, ranging from protection of minority shareholders to the status of the company as a separate legal entity.

These legal structures strengthened managerial discretion, but it was vested in the directors rather than the new professional managers operating below board level. As the directors became less involved in management, real authority was increasingly exercised by managing directors and general managers. Since the Companies Acts made no provision for them, the common law had to determine the extent of the authority associated with these positions, as well as the question of who bore legal responsibility (however limited) for their actions.

Provided there was a power allowing delegation in the articles, which there was by default from 1862, boards of directors were permitted to delegate. By 1906 the law caught up with the common practice of appointing managing directors and managers, and provided for this power by default, although those occupying these positions still had to be directors, preserving an essential link to the board.[34] The courts moved from viewing the managing director as "only an ordinary director entrusted with some special powers"[35] to treating him as both a manager and a director,[36] with managerial functions determined by contract.[37] In contrast, managers below board level were simply viewed as employees,[38] with a limited duty of good faith implied into their contract of employment.[39] The court ruled in 1908 that, under the default articles, it was not permissible to delegate to a manager on terms that he would have full power to conduct the business of the department without interference from the directors except for capital expenditures and litigation.[40] Hence directors had to retain a residual power to intervene, consistent with the current idea that the directors bear some residual responsibility, via their legal duties, for the acts of the person to whom power is delegated. Likewise, in another case, the court ruled that "the only duties which [the board] could delegate to the general manager are those which belong to the management of the ordinary commercial business of such a company."[41] Hence there was a separation between the management function, which could be delegated by the board, and the control function, which could not.

This authority had to be protected against disruption, and in practice this was achieved by widespread adoption of bespoke articles exempting managing directors from retirement by rotation,[42] a practice reflected as a default rule from 1906. Hence, the identity of the managing director was a question for the (entrenched) directors, and the managing director had oversight of the whole managerial hierarchy, which would remain intact for as long as he held

office. The courts later enforced articles giving broad powers to managing directors, even where this effectively gave them a veto over board decisions.[43] Hence, a managing director could "perpetuate their power indefinitely",[44] and not only were the courts unconcerned by this, they appear to have considered it necessary for the business to function.[45]

To conclude, then, the emergence of professional management in the U.K. was accommodated within existing legal structures, rather than supported by a positive legal regime. Their autonomy was entirely dependent upon continuity at board level. As Goyder put it, "Handicapped… by an outworn and defective legal structure, the industrial system works as well as it does only because it is administered by able men who have to make the best of the system as they find it"[46]. As we will see in the next section, this legal ambivalence opened the door for these developments to go into reverse soon after WWII.

Putting Shareholders Back at the Centre of Corporate Governance

The Cohen Committee and the emergence of the hostile takeover

In accordance with its practice of launching periodic reviews of company law, the U.K. government, in 1943, appointed a committee, headed by Mr Justice Cohen, to review "the requirements prescribed in regard to the formation and affairs of companies and the safeguards afforded for investors and for the public interest." Yet, considering shareholders as "owners" and "those on whom the first loss falls", the Committee focused almost exclusively on strengthening shareholders in relation to directors. The emergent role of professional

management during the first half of the twentieth century was not discussed during the reported proceedings of the Committee.

After referring to the growing separation of ownership and control, the Committee concluded that it should be "easier for shareholders to exercise a more effective general control over the management of their companies".[47] Proposed changes included mandatory minimum notice periods for general meetings, facilitating shareholder resolutions and making it harder for directors to solicit proxies. Most importantly for our purposes, the Committee recommended that "any director (…) should be removable by an ordinary resolution, without prejudice to any contractual right for compensation."[48] Following this recommendation, a mandatory power for a simple majority of shareholders to remove the board of directors was introduced by section 148 of the Companies Act 1948. This overrode the provisions in individual companies' articles relating to the removal of directors, which, by default and in widespread practice, required at least a 75 per cent majority on the part of the shareholders. Mandatory rules are very unusual in the U.K.'s company law system, but this rule was introduced with very little by way of debate or critical commentary.[49]

Whilst there is no evidence that the Cohen Committee intended to bring about a wholesale reallocation of the balance of power between directors and shareholders, this was the indirect effect of the 1948 reforms. Before 1948, amalgamations and mergers did not generally result in changes to the directors and managers,[50] with directors only departing by consent and managerial hierarchies frequently remaining intact, particularly in the early, largely anti-competitive amalgamations in which individual companies remained separately managed under a holding company.[51] "Hostile takeovers", in which a "bidder", perhaps a company in a

different industry or even a financier, approaches the shareholders of the target company directly (rather than negotiating with the board of directors) with a view to buying sufficient shares to take control of the general meeting were virtually unheard of before 1948.

A number of reasons explain the absence of hostile takeovers to this point: the difficulty of taking control of the board under the commonly adopted articles, as discussed above; the passivity of individual shareholders, who were only superseded by institutional shareholders from the 1950s; and the inadequacy of accounting information available to would-be acquirers.[52] From 1952, that changed dramatically as a wave of hostile takeovers hit the U.K. After the introduction of section 148, incumbent directors knew that, even if a bidder only acquired majority control of the general meeting, it could remove them from the board, leaving them virtually locked in as mere minority shareholders.[53] In essence, it amounted to a statutory "breakthrough" rule which allowed any shareholder who acquired a majority of the shares to take control of the composition of the board, notwithstanding any provisions in the articles. There is evidence of wholesale removal of directors following takeovers between 1947 and 1960.[54] Companies in which the directors and their associates held more than 25 per cent of the shares, which had previously been immune to changes in control, were suddenly open to takeover, leaving the board and the management vulnerable to change at short notice.

Directors responded to the new threat in a number of ways, including increasing dividend pay-outs and selling off assets,[55] taking defensive measures by issuing new shares or selling off assets, or launching their own bid for majority control.[56] Whilst shareholders in target companies benefitted from the takeover premium (which gave them a tax free capital gain), and much contemporaneous criticism focused on the social implications of takeovers,[57] we

claim that a less commonly observed consequence was that managers lost much of the autonomy they required to design and implement innovative strategies. Being dependent on continuity at board level for their autonomy, managers would have recognised the increased vulnerability of their position. A hostile takeover might result in removal or stricter financial constraints as the new board took control of their access to resources. Even the background threat of takeover led many directors to behave like takeover bidders, increasing payouts to shareholders, thereby, we submit, depriving managers of the resources they needed. Attempts by directors to defend hostile takeovers were circumscribed, first by the courts and later, more comprehensively, by self-regulation in the City of London.[58] The debate about the wider social responsibilities of corporate managers was much quieter in the U.K. during the late 1950s than it had been before the war.

The Drive for Non-Executive Directors

If the emergence of the hostile takeover marked the beginning of shareholder primacy, policymakers' drive for more non-executive directors (NEDs) heralded a deliberate reduction of managerial competence on the board.

As the takeover boom of the 1960s faded, the U.K. appears to have been influenced by U.S. developments, where the SEC began a concerted push for NEDs during the 1970s. A 1973 report by the Confederation of British Industry (CBI) concluded that "inclusion on the board of non-executive directors was highly desirable", in part in order to head off the threat of mandatory two-tier boards with employee representation, as proposed by the Fifth European Company Law Directive. Although the government declined to legislate, the CBI's

recommendations had considerable influence, and ultimately acted as a starting point for the work of the Cadbury Committee. Bank of England encouragement led to the establishment in 1982 of an Agency for the Promotion of Non-Executive Directors (known as PRO NED),[59] chaired by Sir Adrian Cadbury from 1984. Its 1987 Code[60], stated that NEDs were "to contribute an independent view to the Board's deliberations"; "to help the Board provide the company with effective leadership"; "to ensure the continuing effectiveness of the Executive Directors and management; and to ensure high standards of financial probity on the part of the company". In 1992, the Cadbury Report formalised these developments.[61] Thus the foundation on which the various iterations of the U.K.'s corporate governance code have been built is an expectation that directors would act as "stewards", running companies on behalf of shareholder "owners", with corporate governance working "to strengthen the accountability of boards of directors to shareholders".[62]

These efforts bore fruit. In 1976, boards in the U.K. were dominated by management, with around 25 per cent of the largest 1000 companies having no NEDs, but the majority having between one and five.[63] However, by 1979, around 88 per cent of the largest 1000 companies had at least one non-executive director, while 53 per cent had three or more.[64] By 1988, NEDs made up 38% of the board of the largest 250 companies, and 75% of them were independent in the sense of having no previous or present relationship with the company.[65]

So, what was the logic behind the push for more NEDs? It appears to have been pragmatic and *faute de mieux*: according to Walker, an executive director of the Bank of England, something had to be done to prevent the decline of manufacturing industry during the 1970s, and "a good leavening of NEDs", who could prevent drift and provide advice, was within

reach of companies themselves.[66] A more positive justification was also advanced: NEDs constituted a bureaucratic control over management, and were perhaps a precursor to reforming a hostile takeover system that interferes with "managements' ability to plan and develop long term relationships".[67]

With an expectation that NEDs would "rarely if ever be concerned with the detail of managing the business" and that they should "take a more detached view and watch trends over a period",[68] the provision of information to NEDs would be critical. Cadbury noted the importance of information and charged chairmen with ensuring that they received it.[69]

NEDs collectively either have to rely on management for the information they use to hold those same managers accountable, or have to seek information from "alternate information sources… such as the head of risk, head of compliance, internal auditors and external auditors". Their outsider status might also force NEDs to rely primarily on "explicit information" rather than the "more personal information/knowledge" possessed by individual managers which is "less amenable… to the explicit, objective representation" that is a "precondition for its verification and scrutiny by the board".[70] The danger is that explicit information is privileged over the "tacit and incommunicable" knowledge and "inherently ambiguous" information that characterises the management function,[71] so that these important matters are lost from the view of the board.

There has been surprisingly little research carried out on the information provided to NEDs. Johanson's case study found that much of this information came from external financial reports, and was used to evaluate past performance and review strategic initiatives. However,

it was supplemented by management accounts, as well as "subjective, non-financial information" conveyed orally by the CEO.[72] Roy's more systematic research found that internal information on matters such as employee satisfaction, R&D investments and analysis of company strengths and weaknesses was less commonly provided than information about performance, strategy and strategy implementation.[73] Whilst Roy's research is far from conclusive, it does suggest that NEDs receive information that emphasises historic financial performance rather than more intangible, collective processes of innovation within a firm. Since the qualitative aspects of the managerial role discussed above are very difficult to quantify,[74] they might appear to outsider-dominated boards as costs to be reduced rather than the development of capabilities which should be monitored and nurtured. This tendency may be exacerbated by corporate governance codes which require information provided to directors to be "accurate, timely and clear",[75] creating a further danger that the implicit knowledge acquired by managers does not make its way into this accountability process.

Aligning Executive Incentives with Shareholder Interests

The architects of the U.K.'s NED regime almost certainly did not anticipate the massive growth in stock options and other types of performance-related pay for executives from the early 1980s, driven by tax changes and institutional investors,[76] which further financialised the way in which management performance is assessed.

By 1995, the Greenbury Report recommended that remuneration should "align the interests of directors and shareholders in promoting the company's progress", and encouraged the use of performance share plans, with shares awarded based on total shareholder return relative to

comparator institutions. Hence, whether or not NEDs were ever likely to provide support for a long-term, innovation-oriented approach to management, through their role on remuneration committees, NEDs played a key role in ensuring that executive pay gradually took over as the dominant influence on management, setting the time horizons and fixing the objectives of the most senior managers. Hendry points out some of what is lost when managers are incentivised in this way:

> A manager working to tight financial objectives, for example, loses the discretion to respond to threats or opportunities in a way that does not contribute optimally to the specified objectives but is nevertheless in the long-term interests of the company. In general, in management situations people are employed not simply to do as they are told but to create value for their employers by exercising their initiative and judgment. An overprecise specification of objectives may prevent them from doing this.[77]

To the extent that management discretion is being constrained by ever more extensive use of financial metrics, it seems likely that, as the shareholder empowerment agenda, discussed in the next section, proceeds, there will be more focus on "hard" financial metrics (share price, profit margins, turnover, EBITDA) rather than "soft" non-financial metrics (innovation, however that is measured, social responsibility, quality of sustainability strategy).

Encouraging Institutional Investor Engagement

The final factor in the eclipse of management in the second half of the twentieth century is the elevation of institutional investor activism to the status of "corporate governance solution". Like the hostile takeover, the expansion of NEDs and executive incentives, shareholder

activism has been strongly encouraged by policy makers for decades, with little or no regard to the need for managerial authority in modern businesses.

From the mid-1950s onwards, institutional investors began to increase their shareholdings, so that by 1969 they owned 37.8 per cent of listed companies' shares, rising to 58.9 per cent in 1985.[78]

Policymakers took the view that these new institutional investors had the right incentive to hold management accountable. At the prompting of the Bank of England, an Institutional Shareholders' Committee (ISC), consisting of various investor associations, was established. However, the ISC became "virtually inactive" by the late 1980s, leading the Bank of England to express concern that the legitimacy of the system of corporate control might be called into question.[79] Facing an implicit threat of regulation, the ISC issued a 1991 statement on the "Responsibilities of Institutional Shareholders in the U.K.". It was endorsed by the 1992 Cadbury Report, which encouraged the exercise of voting rights and dialogue between shareholders and senior executives on "strategy, performance, board membership and quality of management". After that, institutional investor activism became a progressively more important part of corporate governance policy, culminating in the adoption of the Stewardship Code after the 2008 financial crisis. It was based on an ISC code of conduct, and rebranded institutional investors as "stewards", a role which Cadbury had earmarked for NEDs. The Stewardship Code requires (voluntary) signatories to explain the scope, methods and outcomes of their engagement, as well as their expectations of those who act on their behalf, as well as acting collaboratively to influence companies.[80] Following implementation of the EU Shareholder Rights Directive (SRD), asset managers, pension funds and life insurance

companies must disclose various aspects of their engagement policies or explain why they have not made such disclosures. Engagement policies should set out "how they monitor investee companies on relevant matters, including strategy, financial and non-financial performance and risk, capital structure, social and environmental impact and corporate governance".[81]

This final phase of corporate governance policy potentially represents the ultimate sidelining of management, with institutional investors now invited by policymakers to offer views on strategy from a position even further removed from the company's operations than that of NEDs. Institutional investors (and NEDs) are now expected to have significant input on strategy and to exercise stricter financial control over companies. However, NEDs face little risk of legal liability for business decisions, whilst institutional investors face none. At the same time, managers are now constrained to implement a strategy over which they have little or no say.

Conclusion

During the first half of the twentieth century in the U.K., professional managers emerged, gained authority and took responsibility for collective innovation, a development which rested on a tacit assumption that productive and innovative enterprises could flourish within existing legal structures. In this chapter, we have presented evidence that managers were sidelined by a series of reforms intended to bring shareholders back to the centre of corporate governance. Interventions by policymakers played a part, as did the law's failure to protect the autonomy of managers. At the same time, our historical analysis highlights the absence of any comprehensive vision of the enterprise and its purposes. Classical theories view the firm as an

economic agent, but overlook the role of the manager in developing new capabilities and pursuing collective progress, which requires a degree of autonomy and authority. These legal and theoretical omissions left the door open to reductive strategies that focus purely on financial returns. A fuller account of the purpose of the enterprise properly conceptualises the role of management and their contribution to innovation. Company law should support this by developing a framework that enables managers to innovate whilst ensuring they remain accountable.

Some tentative signs of change in this direction are visible. For instance, in France, the *loi Pacte* introduced the "purpose-driven corporation" (*société à mission*), which can specify in its bylaws a binding purpose (*raison d'être*), as well as social and environmental goals.[82] This prevents managers' mandate being reduced to pure shareholder value. At the same time, managers are held accountable for achieving the specified purpose by a special board. Where the purpose implies a need for innovation, managers will need autonomy and authority in order to act creatively. In principle, then, this new corporate form is capable of supporting a new type of enterprise. Whilst it is currently only one among a number of legal options, the hope is that others follow, with the same aim of supporting innovative management and clarifying the purpose of the enterprise.

Notes

[1] Segrestin & Hatchuel (2012)

[2] Hounshell (1984)

[3] Berle & Means (1932)

[4] Segrestin, Hatchuel, & Levillain (2020)

[5] Taylor (1911)

[6] Berle & Means (1932, p.5)

[7] Chandler (1990, p.240)

[8] Cheffins (2008, chapter 9)

[9] Foreman-Peck & Hannah (2012)

[10] Urwick & Brech (1949, p.81)

[11] Urwick & Brech (1949, p.85)

[12] Sargant (1953, p.140)

[13] Erickson (1986)

[14] Babbage (1832)

[15] Sheldon (1923, p.69)

[16] Jones (1999, pp.108-110)

[17] Burton (1899, p.28)

[18] Babbage (1832, p.31)

[19] Brookings (1925); Dodd (1932); Perkins (1908)

[20] Berle & Means (1932, p.356)

[21] Tawney (1921, p.111)

[22] For an essential overview, see Child (1969, chapter 3)

[23] Elbourne (1919)

[24] Taylor (1919, p.10)

[25] Urwick & Brech (1949, pp. 99-102)

[26] See e.g. Quail (2002)

[27] Gower (1955, p.1190)

[28] Deakin (2009)

[29] Davies & Freedland (2006, p.278)

[30] See Hannah, this volume.

[31] Moore (2018)

[32] Walker & Watson (1894, pp.142-143), a book aimed at investors stated, "'Table A' very fairly fixes the balance of power, but in the articles substituted for it shareholders of course find… everything 'cut and dried' so that shareholders can only change their rights at the sword's point, that is, by means of a hostile 'special resolution'. This in practice is almost an impossibility."

[33] Cheffins (2008, p.170)

[34] Table A (1906, Art 72)

[35] *In re Newspaper Proprietary Syndicate Ltd.* (1900) 2 Ch. 349

[36] *Southern Foundries (1926) Ltd v Shirlaw* (1940) A.C. 701

[37] *Harold Holdsworth & Co (Wakefield) Ltd v Caddies* (1955) 1 All ER 725 at 738

[38] Quail (2002, p.7)

[39] *Robb v Green* (1895) 2 Q.B. 315 at 317

[40] *Horn v Henry Faulder & Co* (1908) 99 LT 524

[41] *In re County Palatine Loan and Discount Company. Cartmell's Case* (1874) L.R. 9 Ch.App. 691

[42] Guinnane, Harris & Lamoreaux (2017, p.20)

[43] *Quin & Axtens, Ltd v Salmon* (1909) AC 442

[44] Guinnane, Harris & Lamoreaux (2017, p.21)

[45] In the Court of Appeal decision in *Quin & Axtens, Ltd*, Farwell LJ noted that "a business does require a head to look after it, and a head that shall not be interfered with unnecessarily".

[46] Goyder (1951, p.25)

[47] Cohen Committee (1945, para 5)

[48] Cohen Committee (1945, para 130)

[49] For further discussion see Johnston, Segrestin & Hatchuel (2019)

[50] Franks, Mayer & Rossi (2005, pp.595-597)

[51] Hannah (1976, pp.86-87)

[52] Hannah (1974)

[53] For a 1953 example of this, see Bull & Vice (1961, pp.109-110)

[54] Singh (1971, p.149)

[55] See e.g. Tabb (1968, pp.61-62)

[56] See e.g. Bull & Vice (1961, pp.166-183)

[57] Bull and Vice (1961, pp.23-24)

[58] Johnston (2007)

[59] Bank of England (1983)

[60] Bank of England (1987)

[61] Cadbury (1992, paras 1.8, 2.1-2.2 and 4.1)

[62] Cadbury (1992, paras 6.1 and 6.6)

[63] Bullock (1977, pp.63-4)

[64] Bank of England (1979, pp.392-3)

[65] Bank of England (1988, pp.243-244)

[66] Walker (1984, p.75)

[67] Davis & Kay (1990, pp.33-34)

[68] Walker (1984)

[69] Cadbury (1992, paras 4.8 and 4.14)

[70] Brennan, Kirwan, &Redmond (2016)

[71] Hendry (2002)

[72] Johanson (2008)

[73] Roy (2011)

[74] Blair & Wallman (2001)

[75] Financial Reporting Council (2018, p.6)

[76] Main (1999, p.84)

[77] Hendry (2002, p.102)

[78] Cosh, Hughes, Lee, & Singh (1989, p.77)

[79] Charkham (1989)

[80] Financial Reporting Council (2020, pp.17-20)

[81] SRD, Art 3g(1)(a)

[82] Segrestin, Hatchuel, & Levillain (2020)

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Table A (1906) Order of the Board of Trade, Dated July 30th 1906 Substituting a New Table A for that Contained in the First Schedule to the Companies Act 1862 (S.R. & O. 1906, No. 596 L.15)

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