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Limited liability and the modern corporation in theory and in practice

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The catastrophic consequences of a lack of public control over the operations of large private corporations have been thrown into sharp relief by two major events in the recent past: the global financial crisis and the Deepwater Horizon oil spill in the Gulf of Mexico. While these events obviously differ in scope and nature, they nevertheless turn the spotlight on a fundamental problem of contemporary capitalism. An economic system that facilitates the privatisation of gains in the hands of ever smaller elites while also socialising risk (losses) in an anarchic manner to the detriment of the many, is not politically viable in the long run. This is the case, in particular, if a core element of this system's legitimacy is its claim to promote democracy at home and around the world, based on principles of transparency and accountability. Both the global financial crisis and the Deepwater Horizon oil spill have already attained the status of 'watershed' events mainly because the social, economic and environmental risks inflicted by private actors on very large groups of people were extraordinary and the causes of failure to manage these risks were systemic rather than accidental.

At the heart of the systemic nature of these 'watershed' failures lies the gradual evolution of the modern corporation into organisations with the power to re-shape in their favour a changing and varied history of precarious balancing acts between public and private interests in advanced capitalist economies. From its beginnings, capitalism has been defined by the primacy of economic over political organisation, most famously encapsulated in Adam Smith's metaphor of the 'invisible hand'. Much later, Albert Hirschman's insightful account of how 'the interests' gradually came to outweigh 'the passions' (Hirschman, 1977) provides a detailed analysis of such early legitimisation patterns, according to which the pursuit of individual freedom and economic self-organisation would be the driving force of political pacification and collective civilisation. Yet from the beginning such high expectations were curbed by warnings of potential conflicts between private and public interests if the former became too powerful. Thus, Adam Smith himself pointed out that:

> [t]o widen the market and to narrow the competition, is always the interest of the dealers. To widen the market may frequently be agreeable to the interest of the public; but to narrow the competition must always be against it, and can serve only to enable the dealers, by raising their profits above what they naturally would be, to levy, for their own benefit, an absurd tax on the rest

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of their fellow citizens. The proposal of any new law or regulation of commerce which comes from this order ought always to be listened to with great precaution, and ought never to be adopted till after having been long and carefully examined, not only with the most scrupulous, but with the most suspicious attention. It comes from an order of men whose interest is never exactly the same with that of the public, who have generally an interest to deceive and even to oppress the public, and who accordingly have, upon many occasions, both deceived and oppressed it. (Smith, 1776[1981], Book I, Part III, I.xi.p., para 10, p. 267)

Subsequently, there has been no shortage of more urgent warnings as well as more detailed analyses of the detrimental impact of a growing concentration of private economic power on public welfare, long-term growth prospects and political peace. Notwithstanding their differing world views, intellectual roots and specific focus, Marx, Schumpeter, J. M. Keynes, Michal Kalecki and J. K. Galbraith, to name but a few, all worried about growing imbalances between private and public powers in favour of the former, and predicting a more or less violent end to capitalism on this account, or working on ways to avoid this through national as well as international regulation and political cooperation.

Nor has there been a shortage of heterodox economic analyses of the role of large, and increasingly transnational, corporations for the productive organisation and macro-economic dynamics of capitalist economies. For example, seminal contributions have been made from a Marxist perspective by Rosa Luxemburg, Rudolf Hilferding and Stephen Hymer; and from a broadly left-liberal perspective, by Kurt Rothschild, E. S. Mason, J. K. Galbraith, Charles Kindleberger, Joseph Steindl and Paolo Sylos-Labini (see, e.g., Harcourt and Nolan, 2009, for Rothschild and Hymer). Similarly, business and managerial economists, including Alfred Chandler, John Dunning, Michael Porter, Neil Kay, Peter Buckley and Mark Casson, often from a less overtly political economy of capitalism perspective and perhaps less critically, have made invaluable contributions to our understanding of strategic decision-making in large corporations. Of course, Edith Penrose should also be mentioned in this context, albeit that her very original and eclectic approach to large corporations and their investment strategies means that her contribution cuts across the very broad categories mentioned above (e.g. Pitelis, 2002).

Despite this wealth of heterodox and generally critical analyses of the role and workings of large corporations from both macro- and micro-perspectives, their direct contribution to debates about corporate reform and policies to regulate the governance of large corporations are much thinner on the ground than might have been expected, and arguably weaker in their impact on policy making than their intellectual content justifies. Mainstream policy discussion has increasingly been taken over by two main strands of debate, both of which operate at considerable analytical and intellectual distance from heterodox analyses of the political economy of corporate capitalism and the economic workings of large capitalist corporations. The first of these is the debate about 'corporate governance', dominated by management studies, expertise in Anglo-Saxon corporate and company law, and mainstream (contractual and principal-agent) economic theories of 'the firm'; and the second is pressure for greater 'corporate social responsibility' (CSR) coming mainly from social movements, and which is now generating a considerable body of academic literature (e.g. Blowfield, 2008; Crane *et al.*, 2009; Kotler and Lee, 2005; Vogel, 2005).

There are many reasons for this disconnect between heterodox economic and political economy studies of large corporations and oligopolistic market structures, on the one hand, and the theory and practice of contemporary corporate governance, on the other. Nor is this separation at all complete. For instance, heterodox work on corporate finance,

financialisation, takeovers and stock markets (e.g. Singh, 1972; Stockhammer, 2004; Singh *et al.*, 2005; Deakin and Singh 2008; Erturk *et al.*, 2008) has undoubtedly generated important policy insights into corporate governance. However, in our view, one important reason for what remains a surprising disassociation between related subject matters and research themes is the failure, or unwillingness, of much of heterodox economics to engage seriously with the legal concepts, definitions and foundations of what constitutes 'a corporation'.

Hodgson (2002) takes both mainstream and heterodox economic theories of the boundaries between firms and markets to task for 'abandoning a legally-based definition of the firm' (p. 37) without explaining why. While law never tells the whole story of social power relations in production, exchange or elsewhere, it cannot be regarded as merely an empty eggshell of meaningless formalities, particularly in advanced capitalist economies in which the rule of the law *does* mostly prevail. Here the idea that power is located outside the law is plainly mistaken, even if the rule of the law fails to capture all aspects of power relations. As Hodgson notes,

> [a]bove all, without attention to legal relations, social scientists are ill equipped to intervene in the long debate concerning the limitations of abuses of corporate power. They will be less able to evaluate the conditions involved in any legal incorporation of a firm by the state, and the nature of the *quid pro quo* for society in return for the legal privilege of limited liability. Without attention to these features, the social scientist may become dangerously indifferent to the policies that extent or diminish the scope of corporate power or the real market. (Hodgson, 2002, p. 55)

Similarly, Gindis (2009) argues that for the economic theory of the firm to go beyond fictitious, and mainly ideologically inspired, accounts of voluntary contracting amongst individuals, it is necessary to resurrect and build on approaches from outside economics that have long regarded the firm as a 'real entity'. Law and legal theory looms large in this perspective in that 'the role played by the law in creating separate entity status for the firm needs to be recognized instead of being downplayed or ignored' (Gindis, 2009, p. 31); not least because lying behind the law, especially in advanced capitalist economies, is the state together with the whole gamut of power, social and economic relations that shape the balance struck between public and private interests at any point in time.

The purpose of this Special Issue is to add 'voice' to those who advocate closer intellectual links between heterodox economists, legal experts and policy-makers interested in corporate regulation and reform. It does so by bringing together a range of papers on corporate limited liability which, with the exception of that by Konzelman *et al.*, were presented at the international conference 'Corporate Accountability and Limited Liability' organised by the Centre for International Studies & Diplomacy (CISD) at the School of Oriental and African Studies (SOAS), in London, UK.

Corporate limited liability refers to a widespread legal principle that limits the accountability of shareholders-owners for the debts of their companies to the current value of their shareholding. Therefore, for any amount beyond their investment, shareholder-owners are exempt from any claims by creditors whatever the cause of their company's indebtedness. What might, at first sight, appear to be a fairly straightforward financial arrangement becomes on closer inspection a rather more complex matter: as well as constituting a 'veil' obscuring corporate structuring and restructuring, limited liability is at the heart of the formation of the modern corporation as a separate legal and 'real' entity, and many of its most problematic features, including excessive risk-taking and 'shareholder primacy'. The nature of shareholding, and the lack of transparency surrounding it, largely

accounts for a dangerous deterioration of what can be described as an economically and politically viable balancing of privatised gains and socialised risk, and of private and public interests, brought sharply into focus by the evolution of the global financial crisis.

The contributions, by economists and lawyers, gathered in this Special Issue approach the topic from a wide variety of perspectives, including legal history, the history of economic thought, financial economics, the concerns of developing countries and legal reform debate arising, in particular, from limited group liability in multinational enterprises. In the remainder of this introduction, we situate the role and relevance of corporate limited liability in the context of recent debates about corporate governance and theory and point to some of the policy implications arising from re-visiting corporate limited liability for ongoing debates about the regulation of contemporary corporate capitalism.

1. The wider context: corporate theory and the changing face of 'shareholder primacy'

Economic free market theory is renowned for its penchant for fiction. As Stanisland, rather tongue-in-cheek, puts it: according to its critiques:

> liberal economics had floated away into a kind of intellectual Disneyland inhabited by a multitude of industrious dwarfs, happily hammering away at their anvils and humming over their money bags, apparently untaxed, unexploited and untempted by lust, avarice or power. Every story automatically had a happy ending, as it usually had only one character. (Staniland, 1985, pp. 77–8)

The equivalent for corporate theory has been provided by what Ireland refers to as the 'law-and economics movement' (Ireland, 2003, p. 454) in the form of the 'nexus-of-contract' and the 'collection of assets' theories of the corporation (or, in the economist's parlance, of the firm), respectively associated with Jensen and Meckling (1976) and Grossman and Hart (1986). The 'nexus-of-contract' theory (see also Alchian and Demsetz, 1972; Easterbrook and Fischel, 1991) has the firm and the corporation dissolved into a loose ensemble of voluntary contractual arrangements between owners of resources, indistinguishable, in any meaningful way, from contractual exchanges in markets. Instead of economic organisations with a legal and economic history, real relations of cooperation, conflict and power and real effects on the wider economy and society, we are left with the lofty notion of 'firm-likeness' (Demsetz, 1988, p. 155) and a general sense that 'what is or is not a firm is immaterial' (Cheung, 1983, p. 18). Incidentally, this ethereal quality of mainstream analyses of the corporation is in direct contrast to the actual use of the law by corporations to define precisely all aspects of their operations.

The 'collection of assets' approach recognises that voluntary contracting can be 'incomplete' and that, therefore, residual control allocation matters for efficiency. Above all, it resurrects the firm or corporation from being simply a figment of our imagination to the status of an aggregate of assets with property rights defined over them. But it provides few, if any, clues as to what it is that holds this bunching together as an entity distinguishable from others (Gindis, 2009, pp. 29–30). Whether these approaches reduce the corporation to a collection of contracts or to one of assets, there is an analogy with the 'hat-and-rabbit' trick, only in reverse motion: rather than hiding the rabbit in the double bottom of the hat behind closed curtains and then pulling it out in full view of the audience as if from nowhere, the rabbit is in full view until it is slipped into the double bottom of the hat, seemingly dissolving into nothingness (or, in the case of the 'collection of assets' view, with its ears still flopping over the rim of the hat).

As Ireland (2003) points out, not only does this conflate different legal forms—e.g. partnerships with unlimited liability and incorporated public joint-stock companies with limited liability—but it also ignores the role of the state in the creation of economic organisation. One might argue that this, after all, is the point of the magical trick in reverse. In addition, the rapid extension of limited liability privileges to partnerships (LLPs) and companies (LLCs) in recent years[1] both in the USA and the UK, and increasingly beyond Anglo-Saxon jurisdiction, *does* blur the standard boundaries between (private) partnerships and (public) corporations, albeit by giving the state and statutory law an even more prominent role. An important corollary is Ireland's observation that these approaches to corporate and firm theory also tend to conflate company assets with shares under the rubric of 'capital'. The characterisation of corporate shareholders as 'providers of capital', too, 'eliminates the corporate entity as an owner of property other than in a purely formal sense' and ensures that it 'is stripped of substance and more or less conceptualised out of existence'. But, more importantly perhaps, it manages to ignore yet another pivotal role of state regulation and intervention, namely that of creating, in a long drawn-out public and political process, (intangible) *financial* property rights through asset partitioning and 'decontractualisation' (Ireland, 2003, pp. 474, 485–500).

If the much hailed protagonist of economic free market fiction has been the frugal saver–producer, the protagonist of contractual theories of the firm or the corporation is the shareholder–'provider of capital'. The rise to prominence of the latter, not only in theory but also in practice, over the past three to four decades, has been recounted many times (e.g. Lazonick and O'Sullivan, 2000). Those critical of the functionalist explanations provided by mainstream contractualist and agency theories of shareholder primacy have provided alternative explanations for contemporary shareholder primacy. Deakin (2005), for example, argues that, rather than any enshrinement of company law in recognition of its efficiency inducing properties, it was the deregulation of capital markets after the end of the Bretton Woods/New Deal and the European welfarist and corporatist era of public and social control of industry and international economic relations that empowered dispersed shareholders by means of hostile takeover bids. Alternative, and often complementary accounts have been provided by heterodox economic analyses of the rise of financial capital since the 1980s (e.g. Smithin, 1996), and, in particular, Minsky's analysis of the rise of 'money manager capitalism' (e.g. Minsky, 1993; Wray, 2009). These stress the rising importance of fund managers and share options in increasingly financialised corporations as mechanisms to counteract the disciplinary effects of the market for corporate control on corporate management, a point also conceded by Deakin (2005, p. 14). Konzelman *et al.* (2010) make an important contribution to this debate by drawing together, much in the spirit of this Special Issue, insights from different disciplines to a wide-ranging, yet succinct account of long-term changes in macroeconomic as well as corporate governance structures, eventually culminating in the global financial crisis. Analysing the co-evolution of political and economic developments, and of theory and policy in the USA and in the UK, since the 1929 Stock Market Crash, at the level of the macro-economy as well as at the

[1] LLPs combine limited liability with the tax advantages and lower disclosure requirements of partnerships. A conventional limited liability corporation is usually 'double-taxed' through corporate tax on the company and tax paid by shareholders on their dividends. In partnerships, the partners' share of earnings is taxed, but the partnership itself is not taxed. LLPs extend limited liability to the limited partners (the equivalent of shareholder-owners). LLCs have flourished in the USA, and constitute a hybrid between LLPs and fully quoted limited liability corporations. Differently from LLPs, there is no ceiling on the number of limited partners/shareholders, and they are allowed to be active in the management of the company. Thus, business owners can avoid corporate tax while fully enjoying the advantages of limited liability.

level of organisations and corporations, they provide a (very detailed) bird's eye view not only of the rise of neoliberal theory and practice, including shareholder primacy, but also of core factors that have led to what they regard as a definite breakdown of existing governance structures.

Beyond the question of how shareholder primacy came to dominate corporate governance structures as well as influence the wider system of economic governance in most advanced capitalist countries, an important point concerns the changing face of the story's main protagonist: the shareholder-owner. Rather than simply as 'providers of capital', many commentators have traditionally regarded shareholders more specifically as passive financial rentiers from wealthy backgrounds, happy to scoop up dividends but otherwise mere spectators of corporate decision-making, operating through exit rather than voice (i.e. the Wall Street Rule). More recently, this view has been challenged by those who argue that with the increasing importance of institutional investors, such as pension funds, in capital markets, the rentier-investor is being replaced by 'fiduciary capitalism' and its 'universal owners' (e.g. Drucker, 1976; Useem, 1996; Hawley and Williams, 2000; Clark and Hebb, 2005; Deakin, 2005). The basic idea is that the large size of institutional investors' stakes as well as their often more long-term and index-traced investment strategies (spreading this in companies throughout the economy) effectively provides them with an incentive to act in the interest of the economy and society at large. Since increasing numbers of listed shares are indirectly owned by employees, in particular through pension funds, increased shareholder activism in combination with 'universal ownership' is seen to provide the grounds for a less short-termist and more socially responsible and inclusive system of corporate accountability.

While there can be little doubt that the concentration of equity ownership in the hands of institutional investors has changed the nature of share-holding, such optimistic expectations of the direction of this change have, in their turn, come under closer scrutiny. A number of studies (Engelen, 2003; Davis, 2008; Jackson, 2008) have cast doubt on the empirical validity of the assumption that pension funds are, in fact, large stake holders in *individual* companies, and on the extent to which institutional investors have, therefore, been willing or able to promote 'good governance' strategies and corporate social responsibility beyond the short-termist maximisation of shareholder value. Strine (2007) paints a considerably grimmer, yet arguably also more realistic picture of contemporary shareholder capitalism and public corporations, characterising an important and growing contingent of shareholders as 'forced capitalists' (Strine, 2007, p. 6) rather than 'universal owners'. This 'forced capitalist class' of employees, deprived of access to defined benefit pension plans and other public benefits, has 'little choice but to invest in the market' and has to do so 'primarily through intermediaries. It is these intermediaries, and not the *forced capitalists*, who determine how the latter's capital is put to work and how the mountain of shares owned for their benefit is used to influence the management of public corporations' (Strine, 2007, pp. 6, 7, emphasis in the original). Hence, far from activist shareholders with the voice to defend their collective stake in the economy as a whole, a core feature of the new face of 'shareholder primacy', seen thus, is a growing mass of shareholders who are not only as passive as their rentier-colleagues, but are also, *de facto*, excluded even from the Wall Street Rule. The implication is that contemporary public corporations operate, to some significant and growing extent, on the basis of the provision of 'forced capital' in the form of a privatised benefit system for those who 'continue to depend for their economic security on their ability to sell their labor and to have access to quality jobs' (Strine, 2007, p. 6).

2. De-mystifying corporate limited liability

It is against this background that we argue that a re-examination of the original privileges granted to, and constitutive of, the modern corporation is appropriate. If contemporary debate about public corporations is largely dominated by the notions of 'shareholder value' and 'shareholder primacy', one reason is simply that older features of corporations have entered the realm of the dogma. As Deakin (2005, p. 11) notes:

> Britain's industrial revolution took place during a period when few businesses enjoyed limited liability. In the US, many states allowed personal claims to be brought against shareholders for corporate debts late into the nineteenth century. Yet, corporate law scholars, and the normal teaching of both economic history and corporate law, today assert that limited liability and the partitioning of corporate from personal assets are essential parts of the legal "bedrock" supporting enterprise.

– a view of the role of corporate limited liability during European industrialisation also shared by Toporowski (2010).

Ireland (2010) sets the scene for the de-mystification of this 'bedrock' view of corporate limited liability in more detail. In an highly informative and captivating account of the political and economic developments that led to the adoption of corporate limited liability in Britain, he highlights the core role played by a lengthy, politically controversial and contested lobbying process in the interest of a rising rentier class of wealthy investors, wanting to participate in the fast accumulation of industrial and financial wealth without also becoming entrepreneurs. Ireland then proceeds to sketch the gradual shifting of risk (liabilities) away from shareholders to creditors, employees and society at large, mainly through the creation of a separate corporate legal 'personality' and, eventually, the separation of parent companies from their subsidiaries. As Muchlinski (2010) points out, the political motif of protecting rentier interests through legislation does not have to enter into conflict with the economic motif of ensuring adequate financial capital provision for large industrial developments. What Ireland's contribution to this issue shows very clearly, though, is that rentier protection as a driving force of state intervention through legislation can, and eventually did, lead to a politically as well as an economically questionable imbalance of risks and rewards in favour of rentier-investors. The detrimental effects of this growing imbalance are manifest today in the global financial crisis and the Deepwater Horizon oil spill in the Gulf of Mexico. Neither the public impacted by these crises nor the theoretical owner-shareholders have any meaningful way of exerting influence over the financial and oil-industry corporations involved. While the owner-shareholders may risk their capital as share prices dive, they need not fear for their livelihoods as do the shrimp fishermen of the Gulf or state employees being put out of work to pay for the acceptance of liability for banking debts by entire societies.

Moreover, Ireland's emphasis on actual historical process—political, economic, social and legal—is important beyond specific assessments and judgements, in its own right. Engaging with history to improve our interdisciplinary understanding of what actually happened, why and in whose predominant interests, is essential to a theoretically powerful refutation of the functionalism that underlies contractualist corporate and economic firm theory, and its core claims: that public corporations are really private networks of contractual exchange (or else the aggregate sum of private assets), their 'publicness' therefore being no more than a fleeting figment of the imagination, and that the legal constructs that constitute the corporation are what they are because they are economically efficient. This fails to provide any account of *how* supposedly efficient arrangements

emerged, thereby committing the most basic of functionalist sins, that of replacing the 'how' by the 'because', and thus a theory by a mere claim. It also, consequently, fails to recognise the inherently normative nature of the concept of economic efficiency—efficient for whom? We have already stressed the need for heterodox economic analyses of the modern corporation to take the legal foundations of corporations more seriously, on the grounds that, at least in advanced capitalist economies, power resides, to a very considerable extent, in the rule of the law. We now add to this suggestion the observation, on the methodological grounds just outlined, that a more strongly interdisciplinary heterodox approach to the corporation (or the firm) should also pay detailed attention to real historical process. Gindis (2009) and Blair (1999) point to modern revivals of the legal 'real entity theory' of the corporation, with its roots in early twentieth century German cooperative law and American institutionalism, as a useful place to start. There seem to be clear overlaps with 'enterprise analysis', as proposed by Strasser and Blumberg (2009), see also Biondi 2009, and explored by Muchlinski (2010), for the case of group liability by multinational enterprises, certainly in regard to the endeavour of re-instating corporations as entities with a real existence and real properties of their own, as these have emerged from a variety of related political, social, economic and legal processes. In a wider sense, critical realism (Lawson, 1997, 2003) would appear to be an obvious source for providing these approaches to corporate and firm theory with a suitable methodological and philosophical social science-oriented foundation. However, a fuller treatment of these questions is beyond the scope of this particular Special Issue. Its main contribution in this context is simply to provide an example of interdisciplinary and historically informed analysis of a core constitutive feature of the modern cooperation—corporate limited liability.

Another avenue for the de-mystification of the 'bedrock' view of corporate limited liability is the history of thought. Adam Smith's critical verdict on joint-stock companies is well-known:

> To establish a joint stock company, however, for any undertaking, merely because such a company might be capable of managing it successfully; or to exempt a particular set of dealers from some of the general laws which take place with regard to all their neighbours, merely because they might be capable of thriving if they had such an exemption, would certainly not be reasonable. To render such an establishment perfectly reasonable . . . it ought to appear with the clearest evidence that the undertaking is of greater and more general utility than the greater part of common trades. . . . The joint stock companies, which are established for the public-spirited purpose of promoting some particular manufacture, over and above managing their own affairs ill, to the diminution of the general stock of the society, can in other respects scarce ever fail to do more harm than good. Notwithstanding the most upright intentions, the unavoidable partiality of their directors to particular branches of the manufacture, of which the undertakers mislead and impose upon them, is a real discouragement to the rest, and necessarily breaks, more or less, that natural proportion which would otherwise establish itself between judicious industry and profit, and which, to the general industry of the country, is of all encouragements the greatest and the most effectual. (Smith, 1776[1981], Book V, Pt III, Art 1, para 36/40, pp. 757–8)

Similarly, Smith also clearly and explicitly anticipated the Berle–Means hypothesis of the separation of ownership and control by almost 160 years, judging this to be the core disadvantage of joint-stock companies (Smith, 1776[1981], Book V, Pt III, Art 1, para 15–18, pp. 740–1). In this, he was joined by John Stuart Mill and Alfred Marshall, as well as by the Tory Prime Minister, Robert Peel, Britain's richest industrialist in the 1820s, who also was an uncompromising campaigner against corporate limited liability. Goodacre (2010) places Smith's observation on corporate limited liability in the context of his wider political and intellectual outlook. Since, seen from today, this is both too limited and too

weighed down, for example by the idea that slavery is inevitable, Goodacre concludes that it would be inappropriate to use Smith as the basis for a progressive critique of corporate power. Carefully and convincingly argued, this certainly is an important and very valid point to make. Yet, quoting Adam Smith back at those who persistently have misconstrued his work in the partisan interest of promoting efficient market theory, surely it is too great a temptation to resist. And, beyond polemics, our prime purpose in citing Adam Smith remains valid, namely to remove him from his role as the secular patron saint of the modern corporation and to place him amongst the crowd of anti-capitalist objectors outside the doors of corporate AGMs.

Arena (2010) also looks at corporate limited liability through the prism of the history of economic thought, albeit at a much later stage, namely Cambridge economics in the interwar period, and in particular the contributions by Dennis Robertson, J. M. Keynes and Piero Sraffa. For Sraffa scholars hitherto unpublished excerpts from Sraffa's manuscripts in the Wren Library at Trinity College, Cambridge, will be of particular interest, over and above the very fact of Sraffa's here documented interest in and reflections about the evolution of the modern industrial corporation. Arena demonstrates in considerable detail, that all three of these economists were clearly well aware of the importance of corporate limited liability and the concomitant separation of ownership from control for both corporate governance and wider macroeconomic policy concerns. While their conclusions and answers differ, with Sraffa, not surprisingly, the most acerbically critical (in places) of shareholder capitalism, Arena shows that they nevertheless shared concerns about very similar micro- and macroeconomic issues raised by corporate limited liability.

3. The policy challenge: corporate limited liability in the context of contemporary global capitalism

If the de-mystification of corporate limited liability, through historical analysis and a closer look at the history of economic thought, is an important contribution to the debate about corporate theory as well as corporate power, an equally important and obvious sequitur concerns policy implications. If corporate limited liability is not an untouchable dogma or 'bedrock' of efficient corporate governance, either in theory, in history or in contemporary practice, what follows for corporate and more general policy reform?

A first point to be made, on which all contributors to this Special Issue who address this question explicitly agree, is what does *not* follow: calls for a blanket abolition of corporate limited liability and a return to the full liability norm of early nineteenth century partnerships are as a-historically blind and counter-productive, both politically as well as economically, as the insistence of mainstream corporate theory on the 'bedrock' nature of corporate limited liability.

Such calls have traditionally been the preserve of the Libertarian Right, and for a reason. For instance, in *For a New Liberty: The Libertarian Manifesto*, Murray N. Rothbard approvingly quotes Robert Poole, a fellow libertarian who states that '[a] libertarian society would be a full-liability society where everyone is fully responsible for his actions and any harmful consequences they might cause' (Rothbard, 1973[1978], p. 268). For Libertarians, corporate limited liability is an obvious thorn in the side of their radically individualist and subjectivist free market view of the world.[2] Corporate limited liability is simply

[2] See also van Eeghen, 2005, for a sophisticated and balanced version of the Libertarian position on this point

incompatible with the invisible hand and, in this, Libertarians are at least more honest than their contractualist brothers-and-sisters-in-arms. Crucially, though, the call for a return to full liability norms and partnerships is, of course, based on the idea that, in the absence of interference by statutory law and the state into the private affairs of individuals, free markets would cease to be a fiction and the 'Disneyland inhabited by a multitude of industrious dwarfs, happily hammering away at their anvils and humming over their money bags' would join the real world.

In this vein, Toporowski (2010) points to the limited impact, not to say sheer futility, of simply eliminating corporate limited liability in advanced capitalist economies. Arguing from the perspective of heterodox economic analyses of firm finance, in which firm behaviour is affected by the composition of financial liabilities, Toporowski contends that shifts in corporate liabilities towards debt instruments with limited liability and/or towards insurance premiums, in response to a wholesale elimination of corporate limited liability, will lead to a reallocation of liabilities amongst shareholders, and that a stabilising overall effect on highly speculative financial markets might follow. More important, however, is Toporowski's observation that, in the context of today's over-capitalised corporations operating complex group structures, the successful evasion of unlimited liability through a management of balance sheets that 'off-loads' difficult liabilities to companies, which can be bankrupted without damaging core business interests, is easily possible.

That said, limited liability in the context of corporate *group* structures certainly enormously facilitates, and essentially encourages, irresponsible investment strategies. For instance, a report prepared for Synapse Energy Economics by STAR Foundation Riverkeepers states with striking and lapidary matter-of-factness:

> Over the last ten years, the ownership of an increasing number of nuclear plants has been transferred to a relatively small number of very large corporations. These large corporations have adopted business structures that create separate limited liability subsidiaries for each nuclear plant and, in a number of instances, separate operating and ownership entities that provide additional liability buffers between the nuclear plant and its ultimate owners. The limited liability structures being utilized are effective mechanisms for transferring profits to the parent/owner while avoiding tax payments. They also provide a financial shield for the parent/owner if an accident, equipment failure, safety upgrade, or unusual maintenance need at one particular plant creates a large, unanticipated cost. The parent/owner can walk away, by declaring bankruptcy for that separate unit, without jeopardizing its other nuclear and non-nuclear investments. (Synapse Energy Economics, 2002, p. 2).

Muchlinski (2010) focuses specifically on the unacceptable consequences arising from limited liability and corporate separation doctrines in the context of claims made by tort victims against multinational enterprises. Alongside other contributors to this Special Issue, Muchlinski argues that, generally speaking, the wholesale abolition of corporate limited liability is neither feasible nor would it be effective in stemming abuses of corporate power. Differently from Ireland (2010), he also maintains that the economic motif of providing capital for the finance of ongoing industrialisation concerns was the main driver behind the emergence of the original limited liability and corporate separation doctrines, even if he concedes that rentier interests also played their part. For cases of claims made by tort victims against multinational enterprises (e.g., after the 1984 Bhopal gas disaster and, of course, the Deepwater Horizon oil spill) he argues, however, that the current state of affairs amounts effectively to a state of no-liability, and advocates a statutory rule that attributes liability to the parent for negligent acts of the subsidiary.

Das Gupta (2010) raises a rather different aspect of the fall-out from 'globalising' corporate limited liability that has so far received very little attention: the impact of the transfer of legal concepts, created for specific purposes in post-industrialisation Europe and the USA, to developing countries, as yet in the difficult process of capitalist transformation under very different conditions from their European and US predecessors. Much in the vein of Ireland's focus on historical process and the interaction of economic, political and legal emerging processes, but from a much lesser historical distance, Das Gupta tells a gripping story of the changing relationship between the state and capital in India before and after neoliberal liberalisation. She highlights the importance of major changes in the legal provisions of capital for the rise and consolidation of 'new' business houses since the onset of liberalisation and neoliberal globalisation, and illustrates 'the unrestrained forms of corporate take-over' of the Indian economy in this period through the examples of two specific forms of corporate legal liability: managerial compensation and the formation of limited liability partnerships.

If these contributions provide a wide-ranging, and in their detail often fascinating, account of the global ramifications of corporate limited liability, a century and more after the emergence of this doctrine in specific historical circumstances and contexts, mass torts by multinational enterprises do thankfully remain the exception rather than the rule, notwithstanding their devastating consequences, and the impact of the 'legal transfer' of corporate limited liability to developing countries' emerging capitalisms (as opposed to the role of multinational companies) is still far too under-researched to allow one to arrive at any definite assessment. Thus, perhaps, the most important damage done by corporate limited liability is to its 'ordinary' victims in the context of contemporary financial globalisation, so far largely unimpeded by the global financial crisis. First, there are the 'involuntary creditors'—the unpaid ex-employees, suppliers and the not-compensated customers—of companies whose bankruptcy has been engineered, negligent or fraudulent under the 'privileges' of shareholder limited liability and the separation of the corporate legal 'personality' from that of its shareholders. The pressures of the global financial and economic crisis—itself brought on by the failure of financial markets, operating the principle of shareholder primacy, to assess or even take note of systemic risk—ensure that the ranks of such 'involuntary creditors' are swelling rapidly. Second, there are the more 'indirect' victims of excessive risk-taking, encouraged by corporate limited liability and subsequent doctrines of 'shareholder primacy'. This includes employees made redundant in the wake of corporate 'consolidation waves' driven by the short-termist dictate of financial markets, those made redundant as a direct consequence of the subsequent financial crisis, and those made redundant as a consequence of the fact that global financial capital still not only roams the world more or less undisturbed, but actually is allowed to raid whole regions—such as the Eurozone—and thereby impose severe austerity programmes on their populations. It also includes those 'forced capitalists' whose pension claims have evaporated in the hands of financial intermediaries and speculators at any stage of financial globalisation.

Taken together, this makes for rather a formidable 'reserve army' of the victims of corporate limited liability, and of the rise it eventually gave not only to irresponsible management and risk-taking generally—of which we have been warned since the times of Adam Smith—but more perniciously to the short-termist activism of institutional investors, in control of a growing influx of 'forced capital' diverted to capital markets through the privatisation of public benefit schemes. This is a sinister spectacle indeed, presided over by what Strine (2007, p. 9) refers to as the 'corporate governance industry'—a 'strange

mixture of public pension fund administrators, proxy advisory and corporate governance ratings organisations, corporate law scholars and business journalists'.

Clearly, if this accurately describes the challenge faced, it is profoundly unsurprising that initiatives aiming at voluntary reforms in favour of enhanced 'corporate social responsibility' (CSR) by large corporations, mainly through the adoption of codes of 'good corporate governance', have fallen flat. While the CSR movement remains popular, doubts about its effectiveness are fast gaining a growing audience (e.g. Christian Aid, 2004, CORE and Save the Children, 2007). Appeals to voluntary conversion to CSR simply are no match for the 'corporate governance industry' and of little, if any, consolation to the 'reserve army' of the victims of corporate limited liability and shareholder primacy in its various and changing manifestations over the decades. The corporate veil, so firmly rooted in limited liability law, has become far too impenetrable to lend any credibility to self-reform. Quite the contrary, concerns about corporate fraud and illicit activities, greatly facilitated by the secrecy of the corporate veil, are sharply on the increase, and the focus of civil society activism has, in fact, started to shift to a preoccupation with corporate fraud and illicit international capital flows (e.g. Kar and Cartwright-Smith, 2008). Even the OECD concludes in its 2001 study *Behind the Corporate Veil: Using Corporate Entities for Illicit Purposes* that:

> [c]orporate entities – corporations, trusts, foundations and partnerships – are often misused for money laundering, bribery and corruption, shielding assets from creditors, tax evasion, self-dealing, market fraud and other illicit activities. The veil of secrecy they provide in some jurisdictions may also facilitate the flow of funds to terrorist organisations. (quoted in Plesch, 2004, p. 162).

Similarly, broad calls for 'qualified board oversight' and 'robust risk management', emanating from the corporate governance literature in response to the global financial crisis (e.g. Kirkpatrick, 2009), fail to grasp the severity of the crisis of corporate governance and the futility of appealing to internal, still essentially voluntary reforms of corporate management. Finally, even the much harsher stand-off between the current US administration and BP in the case of the Deepwater Horizon oil spill in the Gulf of Mexico, while at least pitting the progressive administration of the most powerful capitalist country against a multinational enterprise, carries all the hallmarks of an *ad hoc* response to a sudden crisis, rather than a considered approach to corporate reform. While the *de facto* imposition of corporate liability to the sum of US$20 billion (to start with) by way of political power makes perfect political sense from the point of view of the Obama administration and the constraints under which it operates, it is by no means clear that the probably rather complex distributional effects of an eventual takeover of BP by the US oil industry will improve the overall 'lot' of the various and manifold victims of the flawed decision-making process at the heart of this particular crisis.

The contributions to this Special Issue cannot and do not resolve this mismatch between contemporary policy discourse and the severity of the economic, social and political crisis of shareholder capitalism. Muchlinski's proposal (2010) of a statutory rule to attribute liability for negligence by subsidiaries to the parent is a very welcome concrete proposal to pursue. A relevant question is which international body could be lobbied to second this, since, as with all policy proposals in the age of globalisation, their viability rests on their advocacy and implementation, if not at an international level, strictly speaking, at least by leading capitalist governments in cooperation.

Ireland (2010) makes a more general point. He argues that, rather than going directly against *de facto* no liability shareholding in the context of modern financialised and globalised corporations, with an endless array of accounting and financial diversification mechanisms at the tips of their fingers, we should turn the tables on corporate limited liability. Actually *reinforcing* the real separateness of the corporation from its shareholders, and thus further limiting their rights of control, should open the way to reclaiming the public corporation as a social institution. This raises a core policy challenge for any process of 're-socialisation' of public entities: corporate limited liability and *de facto* no liability shareholding have meant that gains are privatised in the hands of few, by virtue of statutory privilege, while risk is socialised anarchically, through political and economic crises. 'Re-socialising' gains, at least to some extent, will obviously meet with political contestation from potential losers in the process. But the much more difficult question is how public corporations, as truly social institutions, should socialise *losses* in a way that is not anarchical, yet does not stifle necessary risk-taking (as opposed to recklessness through *ex ante* exemption from responsibility and accountability)?

This relates to a similar, yet slightly less ambitious proposal of an avenue to reform: Rather than focusing on corporate limited liability as something to get rid off, this emphasises the fact that a privilege granted to one section of society—those with vested interests, not too forcefully imposed upon them, in capital markets—provides very good grounds for the demand of privileges to be granted to other sections of society in equal measure. If equality before the law means anything, there surely has to be a *quid pro quo* of corporate limited liability for society (Hodgson, 2002, p. 55) or a balance of rights across different sections of society (Plesch, 2004, p. 176). What this might be is obviously a question for different societies to resolve differently, although enforceability will likely depend on international cooperation here, too. Konzelman *et al.* (2010), against the backdrop of their very encompassing analysis of developments, over many decades, of the economic and political interplay between politicians, corporate leaders and intellectual commentators in advanced (Anglo-Saxon) capitalism, leave us with little doubt that whatever reform strategy we might favour will have to aim at building an 'international floor' for policy (see also Strine 2008) as well as be inspired by interdisciplinary research.

4. By way of conclusions

Questioning corporate limited liability takes us back to the legal and political roots of modern corporate capitalism. In so doing it undermines theoretical dogma and thus helps to pave the way toward a less ideologically informed, more open-ended and relevant approach to corporate and firm theory, rooted in an interdisciplinary understanding of the historical emergence of the doctrines of corporate limited liability, the partitioning of corporate from personal assets and the changing face of 'shareholder primacy'. Addressing corporate limited liability also means pointing the finger at a long-established but therefore no less partisan political privilege that requires, at the very least, re-balancing in favour of the less privileged members of society, and in the interest of a politically and economically viable balance between the public and the private interest. The contributions to this Special Issue raise many of these issues and provide some tentative answers. Its main purpose, though, is to provide ideas for future debates on the theory and reform of the public corporation.

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