CONFLICT BETWEEN MODERN MANAGERIAL PRACTICE AND COMPANY LAW

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The word 'conflict' in the title of this essay may be misplaced, for, in many of the aspects of managerial practice, with which we are here concerned, company law is almost irrelevant and demands little more than ritual observance.

Those formulations of company law which are based on the British model have a clear and explicit concept of the company with two primary organs, the members in general meeting and the directorate.[1] Supreme rule making and policy determining authority rests with the general meeting but the general meeting may confer on the directorate the right to exercise all the company's powers, except such as the general law expressly requires to be retained by general meeting. In return for this delegation of managerial power the directors are formally required to act in the interests of the members or shareholders, or, rather, to consider other interested groups only in so far as this may also advance shareholders' interests. 'There are to be no cakes and ale except such as are required for the benefit of the company: *Hutton v. West Cork Railway*.[2]

This statement of the devolution of authority, and of consequent responsibility, is simple and clear. It is also largely unrealistic. It is based on a concept of the power relationships in a company that may have been related to economic reality in the nineteenth century. The company, as an idealized concept, was small with respect to its market; it was one of a number of companies that competed in this market and the market was perfect in that no one company was large enough to dominate the market by its individual decisions. The chief scarce resource of the company was capital and, therefore, the owners of capital had the major power in the determination of company objectives. There were other groups with power to affect the operation of the company—labour, government, suppliers—but these were essentially peripheral. The function of the directors as the managing organ was to work towards the economic end of maximizing the return of the investment of capital in the interests of the shareholders, through arms length relationships in a competitive market.

As companies have grown larger and industries more concentrated,[3] several things have happened to distort this simple notion. Fewer and

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[1] Gower, *The Principles of Modern Company Law* (2nd ed. 1957) 16.

[2] (1883) 23 Ch.D. 654, 673.

[3] Karmel and Brunt, *The Structure of the Australian Economy* (1962) for discussion of the Australian situation.

bigger firms in the market have tended toward imperfect competition, to oligopoly and monopsony and to increased uncertainty about market reaction. Larger firms with widely distributed shareholdings have led toward the familiar divorce of ownership from control and a consequent diminution of the central power of capital; a large company with dispersed shareholding can retain more capital from its earnings and can borrow more effectively. Organised labour has gathered power and government has become an active agent in the business environment. Far from its earlier passive role of ringholder, government is now the regulator of the economy, a critical influence through tariff and subsidy machinery, a proponent of innovation through research organizations and taxation policy and a substantial customer.

This new world is very different from the earlier notion. The older certainties of competition in the market through price, quality and delivery have yielded to the many-faceted marketing concept with complexly interacting variables and consequent uncertainties. The director or manager increasingly sees himself as the point of convergence of a number of interests, powers and pressures that are involved in the operation of the firm. Wilson[4] summarily labelled these areas of interest and power as: Government, Distributors and Consumers, Competitors, Shareholders, Material Suppliers, Labour, Sources of employees especially managers and technologists, Groups within the firm. All of these—with the manager himself— form part of a single community with a pervading general interest and many individuals and groups would appear, in different aspects, in more than one of the areas listed.

In this frame of reference the manager's central tasks may be described as those of formulating agreed policies and strategies that will maintain movement toward the general objectives of his company. He needs, therefore, to build and maintain an appropriate pattern of relationships and transactions between himself and others within the company and with the groups and institutions external to the enterprise. It should be noted that this model treats shareholders as an external group and gives primacy to the objectives of the firm itself rather than to the interests of any one of the groups. The model in fact invests the legal personality of the corporation with volition and ambition. Such attribution, incidentally, is in accord with the assumptions of sociology that any integrated co-operative group does establish goals and objectives that are intrinsic to itself and which are not entirely predicated by the goals of its component members.

This 'managerial' model of the relationship between the enterprise and its environment therefore sees the manager as the dominant figure

[4] Wilson, 'The Manager and his World'. *Symposium on Executive Development,* Massachusetts Institute of Technology, April 1961.

and dominant because of his involvement in, and commitment to, the objectives of the enterprise. None of the external interests have any permanent dominance and the director-manager's task is to satisfy them all according to the relative marginal power of each at the time of decision and in accordance with the long-run achievement of company goals. He draws his authority to manage from each and all of the interests in return for at least minimally satisfying their needs. These satisfactions are not seen as necessarily economic. The rewards to labour, for instance, may reflect a wide range of physiological, sociological and ego-satisfying as well as monetary returns and the same complexity of satisfaction can be seen in relation to all the other groups: the government has interests in the firm for many other reasons than its economic efficiency; customers may seek status rather than utility through its products; shareholders may value the associations and their investment for reasons that are not wholly economic.

All of these complex satisfactions have to be taken into consideration and distributed by the director-manager. Profit for shareholders remains an important consideration but only one among many. Profit assumes far more importance as an internal management criterion; the test and index of performance against plan and policy. It is necessary for survival but it is not the sole end of the enterprise.

We have, then, two distinct models of the relationship of the enterprise to its environment, the 'classic' economic model, which is the basis of British style company law, and a 'managerial' model. It is in the nature of such idealized constructs that neither is wholly realistic; there are companies where the objectives and practices approximate very closely to the classic concept. These tend to be small and middling-size enterprises where there is little real divorce in share-holding and control—the companies of owner-managers, and family businesses. The larger corporation tends toward the managerial notions though it is clear that even those companies that do have single dominant interests, for example some family businesses, may very often define the rewards to those interests in terms far wider than simple economic ones. The owner-manager may well value independence, status, a base for political activities, family security, a quiet life at least as highly as profit maximization.

It would be generally admitted that the managerial notion is more closely in accord with actual practice in most companies. Here is the first root of 'conflict' between company law and managerial practice. Directors pursue, and it is widely recognized that they ought to pursue, a much wider range of objectives than those comprehended by law. The Institute of Directors[5] say that: 'A director's responsibilities extend to the company, its shareholders, its employees, customers and creditors, as well as to his fellow directors and, to some degree, to the

[5] Institute of Directors, '*Standard Boardroom Practice*' The Institute 1962.

State'. Mr Harold Wincott, editor of the *Investors Chronicle* told the Jenkins Committee on Company Law: 'In my own philosophy, any company that forgets that it has three co-equal interests to serve—those of its shareholders, its employees and its customers—will be failing in its duty and could not achieve the maximum degree of success, and it seems to me to be sterile to attempt to rank the claims of any one of these interests above those of the others'.[6]

American law has gone further than British and Australian law in recognizing the claims of the other interest groups. Many state laws recognize that corporations should, to quote one decision, 'Acknowledge and discharge social as well as private responsibilities as members of the communities within which they operate'.[7] However, it is important to question whether the deficiency in our law is of any practical significance. Fogarty[8] comments: 'The fact that British company law does not yet recognize the wider objectives of a company is, in itself, only of marginal importance. It weakens the law in its role as indicator of what ought to be done . . . But none of this is of great practical importance: practice rides over the defects of the law. What is important is that behind the over-long survival of the narrow legal statement of the company's objectives there lurk at least two major unsettled issues, one over the destination of company surpluses and one over the criteria appropriate at levels respectively of strategy and tactics'.

These are important issues and both raise the question of the responsibilities of directors. The classic model is quite clear: directors are responsible to the shareholders. Until recently directors were treated merely as agents of the company and the shareholders in general meeting *were* the company. Directors were required to obey their direct instructions. Obviously in a large company, shareholders cannot direct and directors must make decisions on their own authority and can expect little useful guidance on supervision from shareholders. Shareholders may still dismiss directors and change the articles but 'the members in general meeting cannot give directions on how the company's affairs are to be managed nor can they over-rule any decisions come to by the directors in the conduct of business . . . provided that they are matters not expressly reserved to a general meeting by the Act or the articles'.[9] But despite this evolution toward parallel powers between the two organs of board and general meeting there remains a definite concept of directorial responsibility.

Under the managerial approach, however, the director becomes the arbiter of interests and is the servant of none. The question is there-

[6] Minutes of evidence to the Committee on Company Law—Supplement to *Report of Company Law Committee* Cmd 1749/1962.
[7] *Smith v. Barlow* (1953) N.J.Sup.
[8] Fogarty, *Company and Corporation—One Law?* (1965).
[9] Fogarty, *op. cit.*

fore immediately posed: to whom or what is the director responsible? If the answer is given that he is responsible to all the interests then there is a serious deficiency in that many of the interests can only exert their influence by indirect or cumbersome over-powerful ways. A strike is not necessarily an efficient mechanism by which labour can comment on the directors' decisions. A fuller recognition by the law of the wider objectives of the company – a recognition of the totality of interest groups – could lead to a more efficient representation of these interests on the body concerned with the review of the company's achievements and in the distribution of its surpluses. There in fact seems to be no inherent difficulty in the recognition of groups, other than shareholders, as having rights and claims on a company on an equal footing with shareholders or, indeed, of giving them membership rights, including rights to elect directors and to control objectives and distribution. The case of *Short v. Treasury Commissioners*[10] has disposed of the mythology of the shareholder as 'owner' in any legal sense and thereby disposes of their *a priori* right to sole membership.

The law governing public or statutory corporations does often comprehend wider 'managerial' objectives for the corporation and does often provide for the effective representation of interests such as the state, labour, and consumers. It should be noted that the German law for private corporations has the same effect of providing machinery for the participation of such groups in the overall direction of the company. However, such effective participation does not yet exist under our present law and the director is therefore without clearly defined responsibilities.

An alternative answer is that the director is responsible to the company and there is no doubt that some such concept is of considerable operational importance in determining the conduct of the boards of many corporations. Yet this is a very imperfect responsibility, for the high degree of involvement of the directors in the definition of the corporate objectives suggests in effect that the directors are responsible to themselves. Do we have here an example of the familiar case of inadequately constrained subordinate jurisdiction leading to the 'over-mighty subject'? Much of the case for nationalization arises from such consideration. If there is no effective way in which the varied interest groups can participate in control over, and enforce responsibility on, the directors then it is the clear duty of the most generalized of the interest groups, the state, to take over control.

Some radical revision of the distribution of authority in the review and appraisal organs of the company may be a vitally necessary condition in any alternative to widespread nationalization, or other more subtle forms of substantial government control. The gap between the

[10] [1948] A.C. 534; Gower, *op. cit.* 131, 139.

forms of objective, and responsibility imputed by company law, and those extant in the real world creates a power vacuum that needs to be and will be filled.

This question of responsibility is raised again in the second of the major deficiencies in the concepts of our style of company law. We noted earlier the growing independence of the directors from the members in general meeting and the guarded recognition of this independence by the law. We have, however, skirted a substantial issue by reference to 'director-managers' — for the law does not properly take cognizance of the growth and development of professional management, of the executives who are employees of the company. In theory the board determines policy and the subordinate managers execute it. In theory again the board delegates power to the managing-director as the chief executive giving him some limited independence but constraining him by their direct determination of policy. Admittedly the law shows an increasing tendency to recognize the acts of the managing-director as the acts of the company itself rather than the acts of a servant[11], but in reality the direction of the flow of authority may be different and more complex.

Just as the power of boards has grown to parallel the power of the general meeting because of the complexity and size of the company, so the power of the managers has grown to parallel that of the board for the same reasons. The board cannot make the whole of policy itself; it cannot have adequate information on the resources of the company to enable it to do so. Top managers do not merely run the company from day to day within a framework of policy, but to a significant extent they initiate and determine that policy. It is wholly consonant with experience to consider management as a third organ of the company, acting together with the board and the general meeting but having independent and separate spheres of authority.

It is noteworthy that the great majority of the voluminous writings on management and administrative theory pay little, if any, attention to the role of the board of directors. Their attention is concentrated on the executive roles in the company. Peter Drucker[12] says: 'Management is the specific organ of the business enterprise . . . it sets management apart from all other governing organs'. Lord Brown in the most stimulating book yet written by a practising manager goes even further for he explicitly sees the board of directors as an *external* influence group on the management of the company: 'The power position of consumers, trade unions, staff groups and Boards of Directors is real: in the long run it effectively prevents unilateral decisions being taken by managers except within agreed policies'.[13] This is a far cry from the manager as executor of board policy. In part, this

[11] Gower, *op. cit.* pp. 131, 139.
[12] Drucker, *The Practice of Management* (1955).
[13] Brown, *Exploration in Management* (1960).

growth of managerial authority stems from the growing professionalization of managers. The complex corporation in a complex environment must put a premium on competence, training and experience which is not necessarily related to ownership of a substantial shareholding in the company. The costs of inadequate decision-making amount with integration, increasing capital investment and increasing stocks necessary to back a marketing campaign. A Warrandyte potter mistakes a market opportunity and may be hungry for a week; the Ford Motor Company spent $US300 million on the disastrous Edsel project. These costs moreover no longer affect the company alone, they become significant social costs. General Motors disorganization in 1921 greatly exacerbated a financial slump and came close to creating chaos.[14]

There is a tendency to recruit men into companies specifically as potential managers and to develop increasingly sophisticated methods and systems for training them for their responsibilities. There is admittedly no compulsory qualification for management and no body with binding power to decide who is to be allowed to practise in any particular management field. To this extent, the truly professional manager does not exist. But there is a powerful body of general opinion about how a manager should operate. This knowledge is based not only on experience but also on specific knowledge and specific skills and it tends to be focussed in management institutions and in universities as well as in the operating companies. Managers are no longer superior technicians but they are trained to act as decision-makers; men using discretion and judgment in the choice of alternatives. It is mainly as top managers that they can expect to deploy their knowledge and skill in arbitration between the interest groups; modern theories of delegation and decentralization open up the opportunities to accept such responsibility at an early stage in a career. The management cadet can hope for early achievement of professional responsibility.

The manager is also conscious that he may be in fact the true limiting factor to the growth of the enterprise. Trained and experienced men with the necessary personality characteristics and attitudes are relatively rare in a world that has an insatiable demand for managers in so many spheres. Drucker talks of the manager as the central resource of the modern world[15], and this attitude is reiterated, less forcibly, in much of the more recent approaches to the industrialization of the developing nations or, in Canada, to the problem of escaping from U.S. domination. To the degree that this thesis is true, and we may accept it in substantial part, the growing power of managers may reflect their scarcity.

[14] Sloan, *My Years with General Motors* (1963).

[15] Drucker, in an unpublished lecture at University of Melbourne, 2nd August, 1966.

Thirdly, managers increase their relative power because of new theories and operational procedures within the companies. The classic model envisages a devolution of authority from the top of the organization, from the primary organs of board and general meeting, down to chief executive and on down a hierarchy to the operator. This concept of formal, structural authority delegation has some validity but it does not describe the total pattern of authority and influence relationships within the firm. Above all it is not a framework in which the most effective style of operational relationships can be developed.

Recent theory is much concerned with the relationship of real authority with the possession of information. It sees that expert authority may be located in the person of superior knowledge rather than with the person of superior status. By virtue of his knowledge of day to day operation, of existing potential and constraints, the executive has considerable power in relation to a board of directors. Much the same phenomena are observable in the field of public administration, in the relationship of public servants and their ministers.

Modern theory is also concerned with the fact that the unidimensional flow of authority from on high downwards creates organizational group resistance at various levels in the organization. This body of knowledge is not concerned with the existence of formal protective institutions such as trade unions and quasi-professional associations but rather centres attention on the informal group structures. The formal authority system is inevitably a merchanistic one in that it instructs subordinates to carry out tasks that will further the attainment of organization goals; since it flowed downward, it can have little real regard for the objectives of the subordinates themselves. Classic theory overcomes this problem by assuming a very simple pattern of motivation—employees are profit maximizers in the same way as the theory assumes that companies are profit centred. As a basis for a theory of motivation this assumption is too naive; there is ample evidence that men seek a number of need-satisfactions at work.[16] Important among these needs are needs for recognition as a person, as a contributor, rather than as a pair of hands. If the employee is denied recognition as an individual, and is treated as an element in a productive machine, he will seek that recognition within his immediate work group. The work group will defend itself from depersonalization by generating its own authority over the activities of its members by prescribing their response to management, by limiting production and restricting creativity. From this pattern flow concepts of 'a fair day's work'; 'why sweat so that the boss can buy his wife a new fur coat'; 'if you make bonus they will retime the

[16] See, among others, Whyte, *Money and Motivation* (1955); McGregor, *The Human Side of Enterprise* (1960).

job'.[17] From this attitude also stems a flood of creative endeavour devoted to anti-organizational ends.

The modern manager therefore needs a sophisticated concept of the authority-flows in his organization. He needs to realize that his company has a system of social relationships as well as a system of technical and economic relationships and that only by achieving healthy social relationships can he hope for effective economic relationships. The tendency is toward 'participative' management to 'management by objectives'[18]. Broadly this entails the creation of a consultative process whereby the employees are involved in the establishment of corporate objectives or of sub-unit objectives. From true consultation and involvement stems commitment and responsibility, and hence effective performance.

Any full development of these ideas is rare admittedly, but the tendency in management thinking is clear. Glacier Metal under Lord Brown[19] has become an outstanding example. In Glacier there is a taut authoritarian 'Executive system' that ensures that work is done, performance standards are attained and schedules are met. This system is paralleled by a 'Legislative system' which is a body with representation of all levels in the company and which meets to formulate policy and to assess the results of the implementation of that policy. The 'Legislative system' legitimizes the authority of the Executive system. It should be noted that the 'Legislative system' works in parallel with the board and not as its subordinate. Other examples with more or less precision in the degree of rigor with which the role of the participative process has been analysed and codified could be cited by any management scholar[20].

Such trends are new. Most of previous organization theory was based on assumptions that were familiar to Aristotle. The assumptions are that if an economy depends on human muscle and sweat a large part of the work will have the character of slaving: of monotonous, repetitive, narrowly defined tasks. In this way the pyramids were built and in this way Henry Ford built motor cars. A large part of the human race cannot be offered work which makes full use of their capacities or which gives scope for their development. The worker was necessarily alienated from his work. It is a taskmaster to which he must submit and expect to find his satisfaction outside of work or outside of the world. More recent management theory gives greater freedom to experiments in the tailoring of productive processes to human attributes. It does seem possible to reconcile productivity with

[17] Whyte, *op. cit.* Part 1.

[18] Drucker, *The Practice of Management* (Heinemann, 1955) Chs. 11, 20.

[19] Brown, *op. cit.* Ch. XVII.

[20] See, among others, Vauxhall Motors Ltd., Lincoln Electric Co. Inc., International Business Machines Inc. and General Motors Inc. at senior management levels. See also National Institute of Industrial Psychology, *Joint Consultation in British Industry* (1962).

human values; indeed the two may even be directly variable. The organization and the employee need not be in irreconcilable conflict; concepts of dual loyalty to company and union can replace notions of class war, and management's interests may be perceived as not necessarily inimical to employees' personal interests. It is not suggested that a state of perfect identity in which there is no conflict is either an attainable or desirable goal. Modern theory does suggest structures and systems that minimize conflict and turn it to socially desirable ends.

The fact that these theories and the limited experiments in their application exist creates a growing insistence that they should be realized. Society begins to demand that work should be something in which man participates as a full human being; as an activity in which he not only produces goods and services, but one in which he creates a fuller person in himself. The logic of the advanced industrial organization reinforces this social drive toward participative management. We are only beginning to understand the processes of efficiently managing an educated work force at tasks which essentially call for knowledge rather than sweat and skill. 'Knowledge'—work, as Drucker terms it[21], is a new phenomenon in large scale organization. Previously it was axiomatic that knowledge was a small scale activity. The Medici's downfall was treated as proof that no organization could control ninety-six employees at intellectual work in sixteen countries and Reubens was delated to the Inquisition on the grounds that no one could manage one hundred and twenty-three craftsmen and apprentices without the aid of Satanic powers.

In the last few years management literature has strongly suggested that the type of management that will optimize productivity, profit and morale in an advanced and technologically changing industry is that which keeps employees fully aware of the objectives of the enterprise, demands their involvement in the definition of those objectives and allows them to develop their own ways of achieving that necessary and agreed contribution to the objectives[22]. This style of management gives little reliance to threats, to compartmentalized formal auhority and to atomized rigidly programmed jobs. Though this management concept evolved in the advanced and technologically mobile industries, it has application, as Glacier and Vauxhall Motors show, in stable mass production industries. It is a management style that has attractions in its morality and social ethic but, happily, it is also and primarily, justified on economic grounds. Clarke Kerr in a graphic, if overstated phrase, notes that 'the University becomes more the model for the enterprise than the enterprise for the University'[23].

Hence we have powerful changes in theory and in practice which

21 Drucker, unpublished lecture at Melbourne University, 2nd August, 1966.

22 Burns and Stalker, *The Management of Innovation* (1961).

23 Kerr, *et al, Industrialism and Industrial Man* (1960) 289.

tend to reinforce the power of the senior executives, who are at the apex of this consultative process, in their relationship with the board of directors. The consultative system becomes yet another interest group with rights and claims on the company and in the multiplicity of such groupings the executive finds freedom.

The apotheosis of this freedom and the direct inversion of the classic theory is in the wholly 'internal' board of directors. When all directors are executives and are appointed to the board by virtue of the executive office to which they are promoted then the general meeting has only residual powers which can only rarely be involved. In such a company the assumptions of company law on power relationships and responsibility are indeed irrelevant. The board is the creature of the manager and the shareholder has little but a passive role to play, for his only intervention can be to discharge the top management group.

This situation may also arise where there is an intermediate board, dominated by executives but with a few external directors. Often the outsider directors are nominated by the executives and hold their appointments by grace and favour. Such directors have limited value.

It is difficult for an executive dominated board to function effectively for it must be remembered that though managers are the arbiters between the interest groups, they are themselves one, and a powerful one, of those groups. The problem arises in British-influenced company law because of a lack of discrimination between several different activities. The top management or direction of the company involves the activities of setting objectives and priorities, determining strategies for the achievement of these objectives, implementing action plans and the appraising of achievement.

Some of these activities are functions of managers acting as executives, as members of the hierarchy of authority. Some are consultative participative activities in which all the interest groups, both internal and external, have a necessary contribution to make if the most effective policies and plans are to be made. In these policy making functions the executive authority system is a distorting factor. To quote somewhat extensively from Brown, who uses different but intelligible language: 'The board is a *committee* elected by the shareholders and is responsible to them. But, such a board can be confused with a command meeting and I suspect that this happens not infrequently, particularly when all or the majority of its members hold executive posts in the company. If, in addition the managing director is also chairman of the board, then role confusion will be very difficult to avoid; for the managing director's immediate command will embrace all, or nearly all, the members of the board and the board meeting will almost entirely consist of the managing director and some of his immediate subordinates. It is open to doubt whether those subordinates who held their executive roles at the discretion of the managing

director can effectively take up the role of director, where one of their major responsibilities the appointment of the managing director'[24].

Sound management theory and practice sees a number of specific functions for a board of directors. These include[25]:

a. Trusteeship—safeguarding the assets of the company.
b. Selection of the senior managers of the company.
c. Determination of basic enterprise objectives and policy.
d. Ensuring that major plans are designed to achieve these objectives.
e. Approval of major commitments of resources.
f. Appraisal of results.
g. Dispersion of profits and assets.
h. Acquisitions.

It is clear that these functions are most effectively carried out by a group of people who are in some substantial measure independent of office in the executive hierarchy and who do represent the more significant of the interest groups. It is clear that an effective board carrying out these functions is a valuable asset to the enlightened chief executive for he can use his board for guidance and advice. It can be a mechanism for ensuring that proposals and plans are checked by a body that does not have the same degree of organizational myopia and to ensure additional and detached review of achievement. It is unfortunately also clear that our company law does little to ensure the reality of the separation of these functions from the executive functions.

American and German law both have recognized and attempted to solve this problem. American law has the clear separation of the board's functions from the functions of the company officers, the president, treasurer and the vice-presidents. It separates the functions but does not ensure that the different functions shall be exercised by different people. In German law there is explicit recognition of the three primary organs of the company—shareholders, board and management—and a considerable degree of differentiation of the membership of these organs. German law creates a Supervisory Board (*Aufsichtsrat*) between the general meeting and the Executive Board (*Vorstand*). The supervisory board appoints the executive board: it may question them, call for reports, accounts and papers but it is formally forbidden by the Act to take management decisions. It is the executive board that manages 'on its own authority'. The supervisory boards represent other groups as well as shareholders; since 1920 employees have been included and the Volkswagen board, for instance, also includes federal and state government, the universities and consumers.

The German example is one indication of a world wide trend for

24 Brown, *op. cit.* p. 130.
25 Koontz, 'Functions of the Board' mimeograph U.C.L.A. (1962).

an evolution from two primary organs—shareholders in general meeting and directors—to three: shareholders, directors and managers. Van Ommeslaghe[26] traces this development in other European countries' company law and practice and it is clear that the realities of the distribution of effective power cause and will reinforce this trend. In a company with more than, say, one hundred thousand shareholders, these shareholders are unlikely to deploy anything except a crude influence, and then only at a moment of crisis.

The division of functions between these three organs is not yet clear, or rather the division between the directors and the managers is not yet crystallized. German practice and law sees the division between supervision and execution; the evolving practice in Britain and America seems to be in terms of time horizons. In a company such as General Motors[27] the full board with a number of external directors, has a much longer term and 'trusteeship' responsibilities whilst the executive board tends to make shorter-term decisions within the broad strategic decisions of the full board.

There seems to be little legal or structural inhibition in British, American or Australian companies that would prevent the representation of interest groups other than shareholders on a board that is essentially concerned with 'trusteeship' functions. However, such representation will do little to clarify the roles of directors and executives. Managerial theory is faced with a substantial problem in formulating a coherent body of principles that will determine which interest groups should have the right to intervene within what limits in the direction of business enterprises and the mechanisms that will provide for adequate representation of the interests and still leave room for the necessary freedom for executive action of the professional manager.

Fogarty[28] points out that the typical British nationalized industry has generally solved the problem of the inadequacy of the objectives contemplated by company law by a much broader formulation. It has often gone a long way toward meeting the problem of adequate representation of the interest groups but it still faces unresolved conflict in the relation of the executive managers of the industry and the 'trusteeship' function in the hands of the minister and Parliament. This remains a challenge to management theory and to the law.

Company law therefore appears to have three defects which vitiate its proper impact on the conduct of corporate enterprises. It assumes inadequate objectives, it fails to recognize and to invest with responsibility major power groups that can wield a significant influence on the conduct of the affairs of the company and it pays scant regard

26 Van Ommeslaghe, *Régimé des Sociétiés par Actions et leur Administration en Droit. Comparé* (Bruylant Brussels 1960).
27 Sloan, *op. cit.* Ch. 23.
28 Fogarty, *op. cit.* Ch. 8.

to the separate existence of the senior professional manager who must often act as arbiter between the interest groups. The first two of these defects can be remedied in law as they frequently are in practice. This may mean the absorption of company law into a more general corporation law as Fogarty suggests. Such an absorption would end the interesting deviation over the past two hundred years of company law from the law of corporations but it would probably be of advantage. The third problem is as yet unsolved.

The defects are not only of theoretical importance. The failure of the law to separate executive and review functions has tended to make directors into creatures of the executives. Many of the recent company failures have highlighted the fact that directors are barely aware of their review and trusteeship functions and are powerless to exercise them in the face of a strong chief executive. The initial statement of this paper, that company law was often irrelevant to managerial practice has a disturbing reality.