



The Functions of Corporate Law in the 21st Century

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Two Periods

- 1. 1970s to GFC
 - Dominance of law-and-economics approach
 - Focus on internal relations of the company
- 2. Since GFC
 - Focus on impact of corporate behaviour on those outside it

First Period Function

- The role of company law is to reduce the costs of carrying on business through the corporate form
 - Operational efficiency
 - Social welfare claim
- Centrality of agency theory

Jensen & Meckling

William Meckling & Michael Jensen



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THEORY OF THE FIRM: MANAGERIAL BEHAVIOR, AGENCY COSTS AND OWNERSHIP STRUCTURE

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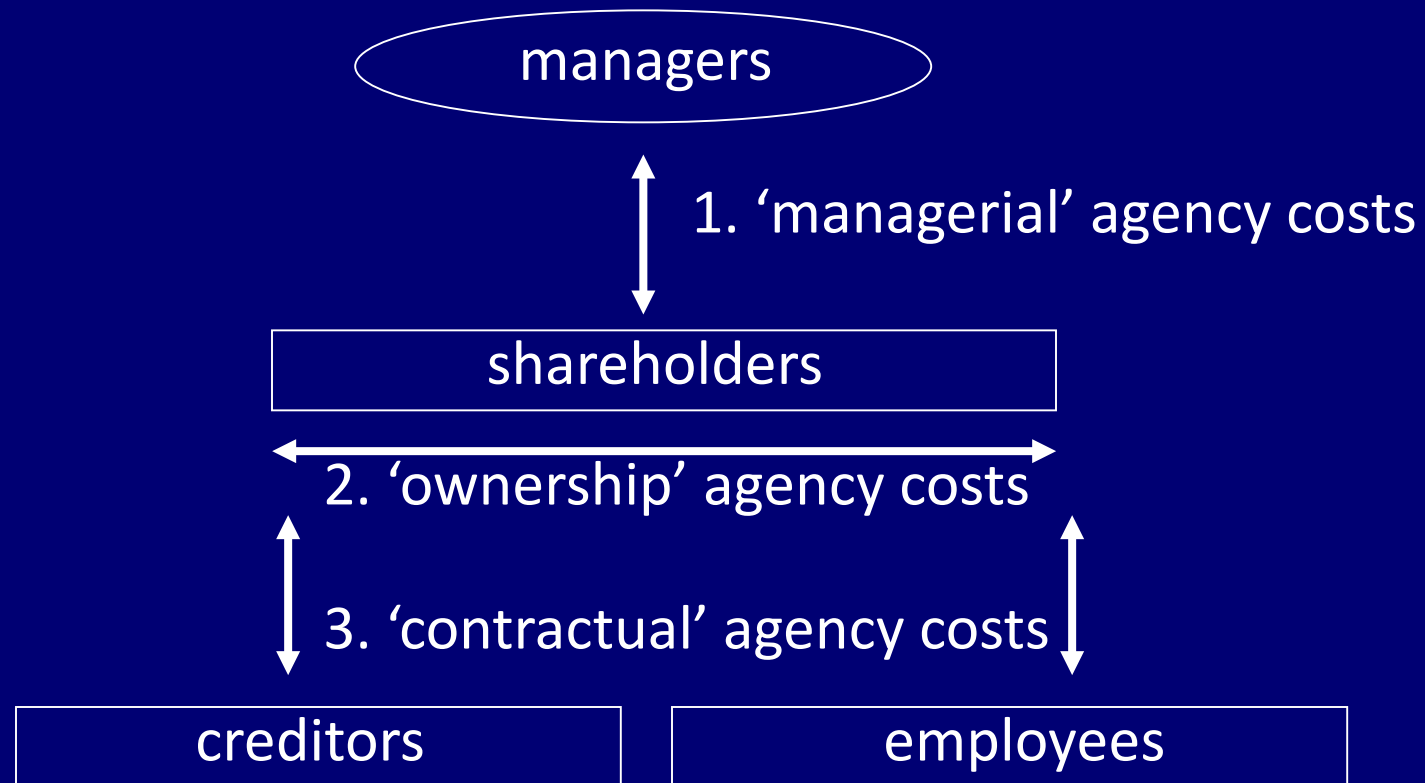
“We define an agency relationship as a contract under which one or more persons (the principal[s]) engage another person (the agent) to perform some service on their behalf which involves delegating some decision-making authority to the agent.”

The Anatomy of Corporate Law

(1st ed 2004, 3rd ed 2017)

- “[A]n ‘agency problem’—in the most general sense of the term—arises whenever one party, termed the ‘principal’, relies upon actions taken by another party, termed the ‘agent’, which will affect the principal’s welfare.”
- Escapes dispersed shareholder focus of early US agency analysis.
- Applies to all voluntary relations with the company

Three dimensions of agency problems



What is an “externality”?

- “Externality”: A’s activity imposes an uncompensated cost on B
 - More fully, a “negative externality”, to distinguish from “positive externality” where actions confer unpaid-for benefit on B.
 - With negative externalities, the problem is that A has an incentive to overinvest in the activity in question.

Regulation

- Is regulation by the state "broken"?
- Can companies do better?
 - 85% of greenhouse gases from the use of oil occur, not when oil is extracted or refined, but when it is used by customers (Scope 3 emissions)

(Proposed) EU Corporate Sustainability Due Diligence Directive, Art 15

1. Member States shall ensure that companies . . . shall adopt a plan, including implementing actions and related financial and investments plans, to ensure that the business model and strategy of the company are compatible with the transition to a sustainable economy and with the limiting of global warming to 1.5 °C in line with the Paris Agreement . . . This plan shall, in particular, identify . . . the extent to which climate change is a risk for, or an impact of, the company's operations. 2. Member States shall ensure that, in case climate change is or should have been identified as a principal risk for, or a principal impact of, the company's operations, the company includes greenhouse gas emission reduction objectives in its plan.

Milieudefensie v Royal Dutch Shell

Hague District Court 2021

- Shell group world-wide required to reduce its CO2 emissions by 45%, as compared with 2019, by 2030
- Legal basis of ruling: “unwritten standard of care laid down in Book 6 Section 162 Dutch Civil Code, which means that acting in conflict with what is generally accepted according to unwritten law is unlawful.”
- The problem of the read-across from a prescription for the global economy to a particular company



Saudi Aramco bets on being the last oil major standing (Financial Times, 12/1/2023)

"While some western energy companies prepare for a future less reliant on fossil fuels, the world's biggest supplier is doubling down. Ultimately, the world's biggest crude producer is betting that it can continue to do what it does best: pump oil for decades to come and gain even more market power as other producers cut back."

Supervision of Delegated Tasks

- Starting points: *Re City Equitable* [1925] Ch 407; *Graham v Allis-Chalmers* 188 A2d 125 (Del 1963)
- Recent developments: *Re Caremark, Inc, Derivative Litigation* 698 A 2d 959 (Del. 1996); *Marchand v. Barnhill*, 212 A.3d 805, 822 (Del. 2019); *In re Boeing Co. Derivative Litig* (Del. Ch. 2021); *Re Barings plc (No. 5)* [2000] 1 BCLC 523
- R Masulis and S Mobbs, *Reputation Incentives of Independent Directors: Impacts on Board Monitoring and Adverse Corporate Actions* (ECGI Working Paper 353/2013)
- *Sharp v Blank* [2019] EWHC 3078 (Ch)
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Proposed EU Directive (Again)

EU's Core Objective

To impose a duty on companies to monitor the discharge by subsidiaries (and other companies in the value chain) of activities which carry risks of breaches of human rights and environment standards laid down in international conventions.

And to impose administrative and civil liability on them if the duty is not properly discharged.

Expected Extra-EU Impact

- “By including European companies’ global supply chains into their scope, and by recognising that the most salient adverse impacts on human rights and on the environment occur mainly outside the EU, the policy options have a strong external dimension through their impacts on supply chain actors and stakeholders in third and developing countries.” (Commission Staff Working Document, *Impact Assessment Report*, (SWD(2022) 42 final) para 6.1.5)
- Does this encourage divestment?
 - *Unilever* – sale of the business to a private equity company; *Okpabi* – Shell exits on-shore drilling in Nigeria, probably in favour of a Chinese purchaser; *Vedanta* – UK plc taken private; capital raising shifted to Mumbai.