

The Impact of Economic Theories in comparison with the UK Company Law and Kuwait Company Law:

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There are significant impacts on company's laws by economic theories in the UK and in Kuwait. Professor Andrew Griffiths pointed out that there was a political affect on the UK law to have neo-liberal of free markets and deregulation specially during the 1980's.ⁱ Those impacts were seen in two economic theories which are contract theory and agency theory. Economists were interested to have a better legislation based on sound economic theories, which is why their theories are applied to many branches of the law as shown below. Also economists have interesting points on what makes investing in shares attractive.

Another subject matter which arises in this discussion is a key economic argument of the proponents of corporate social responsibility which lays down a question when legislating whether only to consider maximizing the wealth of the company or also consider the morality and public policy of the state and their relation to Corporations. Furthermore while discussing the economic impact on the corporate law, limited liability pros and cons is a fundamental subject to discuss in an economical conception.

Firstly, in an economic sense; directors are seen as agents of shareholders. That means shareholders are managing the company through the directors. According to section 160 of the UK Companies Act 2006 and Article 141 of Kuwait companies Act 15-1960 shareholders appoint the members of the board of directors by exercising their voting rights which is why directors should represent shareholders interests while managing the company, while in reality, directors are pursuing their own interests. Practically shareholders do not give much attention to the company management which should be a primary concern in corporate governance. Moreover, in large companies many shareholders do not even attend the company annual general meetings, which exhibits they do not act like owners.

It is recommended that shareholders should participate in controlling the company because that shall provide efficient and effective corporate governance. Economic scholars like Ferran strongly defend shareholder control and regard voting as a way by which shareholders of the corporate community exercise control over the decisions and conduct of their management.ⁱⁱ

Nevertheless, managers still continue to not act like agents of shareholders and the corporate governance still regards this as a major issue.

Another issue with agency theory is that, if directors are agents of shareholders then they cannot act freely while managing the affairs of the company, and would have to act according to shareholders orientation. But in contrast they have the freedom to act and to carry on their job according to section 173 of the UK Company's law which gives directors the right to exercise independent judgment in management but within the limits of their duties in accordance to sections 170 to 177 of the UK Companies Act 2006. Similarly article 146 of Kuwait Companies law empowers directors the right to practice all relevant activities on behalf of the management but within the limits of the scope of their duties which is in accordance with article 133 of Kuwait Companies law that sets restrictions on their acts and some liabilities on them as well according to article 148.

Arguably it is more accurate to say that shareholders are electing directors and they are not appointing them which, is why directors are not their agents even though shareholders have the right to dismiss any director in accordance with section 168 of UK Companies Act and article 152 of Kuwait Companies Act.

Secondly, Manne in (1967) pointed out that a key feature of the economic analysis in relation to public companies is that the relationship between a company and its shareholders is construed as a complex and open-ended contractual arrangement concerning the provision of equity capital to the company and the securing of a return on that input of capital.ⁱⁱⁱ In other words the company is analyzed as a network of contracts as Boyle pointed out.^{iv}

In a detailed explanation, the contract between the company and shareholders creates obligations and rights for both parties. Shareholders are committed on contributing or paying up company's capital in return for two general rights. First, being the financial rights which are to share company's profits over time & other financial characteristics and second, constitutional rights which are the right to participate in management through voting and other rights which are mentioned in Article 131 of Kuwait Companies Act and also in different sections on UK Companies Act.

Thirdly, it is important to discuss what makes investing in shares attractive to people. There are certain reasons which encourage investors to invest their money in stock markets. For instance, firstly, in some countries investors have the right to request last five years financials in order to ascertain whether to invest or not in the share market. Second reason, is the ability to sell shares in order to exit the company and the ability to trade them on a share market make people feel safe to enter stock market because if the management did not perform well then minority shareholders can exit the company since they do not have the power to vote for change of directors. Third reason, is in order to maximize a company's capital, promoters have positive motivation to increase the attractiveness of shares in their company. Fourth reason being the high standards of companies laws also help to improve the attractiveness of shares by providing safe market with a high level of protection for investors for example; the law should provide more protection for investors.

The economic theory also encourages market efficiency by allowing acquisitions and that is by letting the offeree company to act in the interests of the company as a whole and not to deny the shareholders opportunity to decide on the merits of the bid. This will lead to minimizing the defense tactics which poor management may use to resist as Griffiths stated.^v

Another aspect for making the market more attractive is to invest in is formulating some rules that protect shareholders. For example, Kuwait Stock Exchange or SIX Swiss Exchange can provide high level of protection for investors in order to encourage them to invest their money in the markets.

Fourth, some economic scholars are asking for re-regulation in order to have a free market and all parties such as creditors, consumers and employees set their own limits on their powers so that they can limit the powers of corporate management. Moreover creditors can limit the risks they face in the terms of their own contracts with the company. That will eliminate all constraints and will make the goal of management to maximize the financial return for shareholders. As Friedman's 1970 article in the New York Times magazine stated that the social responsibility of business is to increase its profits.^{vi}

It appears that those reasons are weak. Parties can make all the necessary arrangements in the company's constitution or can make several contracts between each other to reach their goals without breaching the law which shall be within the limits of the law.

Fifth, various economic markets are involved in increasing market efficiency. For example, product markets and ranking markets which rates manager's performances and also the market in which the company's shares are traded. Movement of shares seems like a verdict on management's performance as Andrew pointed out.^{vii}

Sixth, another subject which arises in a key economic argument of the proponents of corporate social responsibility and which lays down a question when legislating whether only to consider maximizing the wealth of the company or also consider the morality and public policy of the state and their relation to Corporations. If it is proposed only to consider economic wealth then economy wealth would be increased if women could sell their babies as E M Landes states in his legal study 1978.^{viii}

Some countries like Kuwait give a consideration on public policy. For example article 131 sub section five (5) allows shareholders to precede an action against the board of directors if they violate the law or the public policy. However it is important not to expand in that matter in order to have growing economy.

Seventh, the economics of limited liability which appeared first in Salmon Case is a fundamental subject in economic prospective which has its pros and cons.

Firstly, separation of equity capital and management encourages investors to invest in the market. On the other hand it reduces the need for shareholders to be concerned with management providing the ability to exit the company easily by selling their shares in the stock market or in the secondary market as another choice which is a main concern in Corporate Governance.^{ix}

Secondly, it eliminates the risks of unlimited liability which contributes to the growth of economy by inspiring investors to enter the market confidently while it changes the risk of loss from the shareholders to the creditors.

Thirdly, the personal wealth of the investors is not relevant which means shareholders have the same rights and obligations but it is considered a disadvantage for creditors as a risk if the company went into insolvency which is why creditors can seek compensation for the increased risk in the overall terms.

Fourthly, the risks associated with particular shares are governed only by factors relating to the company itself (i.e. the nature of its business, the quality of its management, management's attitude towards risk etc) which assure having an objective price as Carney pointed out.^x Nevertheless, it is necessary to invest in a stable place where there are no risks that can have effect on the market.

In conclusion, the economic theories does have an impact on laws in the history but it is very important to have a well regulated market with strict rules in some of it branches like providing high standard protection to investors and at the same time provide flexible laws to

encourage investments as professor Andrew G. pointed out that the last credit crunch and subsequent economic and financial crises have raised doubts as to how far markets do constrain corporate management.^{xi}

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ⁱ Andrew Griffiths, 2011. The Corporation and its Economic Role. University of Manchester – Lecture Hand out 2011, topic 1 LL.M Programmes 2011-2012, Code: LAWS 70081, page: 16.

ⁱⁱ Ferran, 2000. Visions and Revisions of the Shareholder. Company Law and Corporate Finance, 1999, p.246.

ⁱⁱⁱ Manne, 1967. Our Two Corporation Systems: Law and Economics. 53 Virginia Law Review (1967) p. 259.

^{iv} Boyle & Birds, 2011. Company Law. 8th Edition. Jordan Publishing Limited 21 St Thomas Street Bristol BS1 6J. Page 15.

^v Andrew Griffiths, 2011. The Corporation and its Economic Role. University of Manchester – Lecture Hand out 2011, topic 1 LL.M Programmes 2011-2012, Code: LAWS 70081, page: 19.

^{vi} Milton Friedman, 1970. The Social Responsibility of Business is to Increase its Profits. The New York Times Magazine, September 13, 1970. By The New York Times Company.

^{vii} Andrew Griffiths, 2011. The Corporation and its Economic Role. University of Manchester – Lecture Hand out 2011, topic 1 LL.M Programmes 2011-2012, Code: LAWS 70081, page: 18.

^{viii} E M Landes and R A Posner, 1978. The economics of the baby shortage (1978) 7 J Legal Stud 323.

^{ix} P Halpern, Trebilcock, 1980. An Economic Analysis of Limited Liability in Corporation Law 1980. 30 University of Toronto Law Journal 117.

^x William J. Carney, 1999. "Limited Liability" (1999), in ENCYCLOPEDIA OF LAW & ECONOMICS 5620 Volume III (B. Bouckaert & G De Geest, eds).

^{xi} Andrew Griffiths, 2011. The Corporation and its Economic Role. University of Manchester – Lecture Hand out 2011, topic 1 LL.M Programmes 2011-2012, Code: LAWS 70081, page: 20.