THE MONISTIC ORGANISATION MODEL OF THE ENGLISH PUBLIC COMPANY

Arne Heller, Alexander Schuhr
University of Library Studies and Information Technologies

Abstract: In the context of the corporate governance debate, major corporate scandals and corporate collapses have repeatedly highlighted grievances and errors in control and risk management, reigniting the question of the "right" organisational structure. The authors present the dualistic management model of the German public limited company and the monistic management structure of the English public company and evaluate the advantages and disadvantages of both organisational models within the framework of comparative legal analysis. Ultimately, the aim of both systems is to close the existing gaps between poorly informed shareholders as principals and comprehensively informed company managers as agents and to ensure that corporate control functions comprehensively and efficiently in the interests of the company.

Keywords: Corporate Governance, Organisational structure, Board of Directors, Company Secretary, Information deficits.

Introduction

English legal practice has been concerned with the discussion of corporate governance since the early 90s. This was immediately triggered by the insolvencies of important large companies [1] which had published annual reports only shortly before going "bust" which had not given rise to any negative expectations [2]. The result was the formation of a commission whose final report was published in 1992 as the *Cadbury Report*, the recommendations of which were recorded in a *Code of Best Practice* to improve company management [3]. The *Cadbury Report* was followed by the *Greenbury Report* [4] the subject of which was *directors' remuneration*, and the *Hampel Report* [5]. The *Hampel* commission re-worked the suggestions of the *Cadbury* and *Greenbury* commissions and summarised them in a *Combined Code* [6], to which the stock exchange *Listing Rules* were attached as an annex [7]. At the same time it was stressed though, that all companies and not only those listed on the stock exchange should make efforts to meet the behavioural requirements. The provisional crux of the discussion is formed by the *Higgs Report* [8], which concerns the function and effectiveness of *non-executive directors* and the *Tyson Report* [9], which investigated the possibility of recruiting and further training *non-executive directors*. The suggestions of both the *Higgs Reports*

and the *Tyson Report* were overwhelmingly worked into the revised *Combined Code* ç. The *Combined Code* is today called the UK Corporate Governance Code and is continually edited and adapted to current developments.

Company management of the English public company

The monistic organisation model of the English public company

Unlike a German share company, an English public company is based on the monistic board-system. The public company has only two company committees in the *general meeting* and the *board of directors*. There is no further intermediate committee with the primary legally assigned task of monitoring company management. Therefore, there is basically no supervision of the management of an English public company by way of an institutional exercise of function, or at least one that is separated from personnel. The task of management is rather assigned together with the task of monitoring company management to the *board of directors* [11]. This represents the most striking difference to German company law which is based on the incompatibility of company management and governance functions [12].

The management structure of an English public company

Directors

The Board of Directors

The term "*director*" is not defined as such in the Companies Act 2006. However, it can be seen in the Companies Act that any person holding the post of a *director* is assumed to be a *director*, even if he or she is not described as such [13]. Thus it can happen that designations such as *members of the council*, *governor* or *trustees* should be interpreted as *director*. A public company must have at least two *directors* (section 154 (2) CA 2006). By contrast, no maximum number of *directors* is legally defined. Collectively, the *directors* form the *board of directors*, which is led by the presiding *chairman of the board* [14]. Surprisingly, neither the unification of several *directors* to a *board of directors* nor the position of the *chairman* is explicitly regulated in the Companies Act 2006 [15]. There is also no basic standard in the Companies Act 2006 which generally encompasses the tasks of the *board of directors* within the company structure [16]. From now, the area of tasks of the *board of directors* is more closely delineated in the *Combined Code*.

According to that, the *board of directors* adopts a double function with the effective management of the business and the governance of the *public company*. In particular, the *board* should:

- offer business leadership in a network of effective controls which allow evaluation of risk,
- define the strategic aims of the company, ensure the necessary financial and personnel resources for achieving the aims and check the performance of management,
- define the business standards and moral values and
- ensures that obligations to the shareholders are met.

To carry out these tasks, a division into executive and non-executive directors has crystallised for reasons of practicability [17]. The executive directors are linked to the der public company via an employment contract and dedicate their full attention to day-to-day business and management of the public company and are entitles to make decisions and close contracts on behalf of the public company [18]. Only these executive directors are comparable with German board members.

Non-executive directors

Unlike the *executive directors,* the *non-executive directors* only dedicate a part of their work to the *public company* and are not linked to it by an employment contract [19]. Accordingly, non-*executive directors* regularly receive no salary, just expense *fees*. The level of the expenses is set by the *board of directors*, unless the *articles* empower the shareholders to do so. The *non-executive directors* do not undertake day to day activities at all and only take management decisions to the extent that they contribute to *setting the company's strategy* and in important decisions [20]. They should contribute to strategy development and thus to the long-term establishment in the market by constructive criticism in the context of company positioning [21]. Otherwise, the main tasks of the *non-executive directors* are in participation in meetings of the *board of directors* and in the monitoring of the *executive directors* [22]. Additionally, they also carry out a central role in the appointment and removal of management and in succession planning and in setting appropriate remuneration levels for the *executive directors*. Finally, the *non-executive directors* also have the task of representing the interests of the *shareholders*, especially if there is a worsening of the commercial situation of the *public company* [23].

Despite the different tasks, the English company law does not recognise *non-executive directors* as a special category of *directors*. All *directors* have the same legal obligations and are equally responsible for decisions of the whole *board of directors* [24].

The Company secretary

Preliminary note

Every public company must have a *secretary* (section 271 CA 2006). In the absence of a legal definition of *secretary*, every public company can define the remit of the *secretary* according to their own requirements. This means that the position of *secretary* can be filled by either a natural person or by a partnership or share company (section 278 CA 2006), but not by a person who has been debarred by a court from holding the position of a *directors* (section 3 CDDA 1986) [25]. In the event that the position is temporarily vacant or the *secretary* is prevented for other reasons from carrying out the role, the tasks can also be undertaken by the *assistant secretary*, *deputy secretary* or any *director* who has been authorised by the *board of directors* to carry out the tasks of the *secretary* (section 274 CA 2006) [26]. The chronologically first *secretary* of a public company must be named in the declaration of the *directors* and *secretary* (section 9 CA 2006). The *secretary* of a public company must have recognised professional qualifications as either a professionally qualified lawyer, accountancy professional or business manager or have professional experience to enable him or her to fulfil the duties of the *secretary* of a public company (section 273 (2) CA 2006).

The remit of the secretary

Processing of administrative tasks

The *secretary* is the *chief administrative officer* of the public company who holds considerable powers [27]. The *secretary* is not, though, involved in company management and accordingly has no authority to make decisions about the management. However, he or she has authority to a limited degree to act on behalf of the public company in negotiations with third parties, and sign binding contracts for the public company that are necessary for fulfilment of his or her administrative roles [28]. Thus, he or she can make employment contracts with employees, purchase office materials and enter into rental contracts for premises. He or she does not, however, have any power of representation in the area of company management [29]. This restricted commercial authority show that the *secretary* is in every respect subordinate to the *board of directors* [30]. The *secretary* is indeed nominated by the *board of directors* for a period and under conditions that the *board of directors* considers appropriate. The *secretary* must agree to this nomination by filling in and signing form 288a and returning it within 14 days to Companies House (section 276 (1) (a) CA

2006). He or she must then update the list of secretaries kept by the public company with the corresponding dates (section 277 (1) CA 2006). Together with the nomination, a separate contract of employment is usually agreed with the *secretary* which must be approved and signed by the *board of directors* to be valid [31].

Administrative and implementation tasks

The *secretary* is primarily concerned with administrative tasks and the implementation of decisions taken by the *board of directors* [32]. The main administrative tasks of the *secretary* include [33]:

- signing off the annual report;
- calling meetings of the *board of directors* and the *general meeting* on the instructions of the *board of directors* and creating the agendas [34];
- activities that concern the issue of shares;
- Obligations to cooperate in the formation;
- Management of filing of all business documentation and the register kept by the public company;
- Minuting of general *meetings* and procurement of the required signatures.

Reporting obligations to Companies House

The *secretary* must submit the following documents and forms to *Companies House*:

- the appointment and recall of *directors* (Forms 288a and 288b), which must be submitted within 14 days (section 276 CA 2006);
- security rights *charges* including all details (Form 395);
- *annual accounts* and audits;
- *annual return* (Form 363) and
- all *special* and *extraordinary resolutions*, where the *resolutions* must be presented within 15 days following the *general meeting*.

If the *secretary* fails to submit certain documents or forms to *Companies House*, he or she can be held accountable and criminally prosecuted [35].

Consultancy tasks

In public companies, the *secretary* has the additional remit along with the administrative tasks of advising the *board of directors*. This consultancy can extend to advising in particular on the agreement of actions of the *board*

of directors with the *memorandum* and *articles* and the law. Consultancy in respect of company management and financial reporting is also possible.

A legal analysis of monism versus dualism

The executive board is the management and representative body of the company in the German share company. It leads the company autonomously, i.e., independently of the general meeting and supervisory board. The general meeting then decides only on questions of company management if the board requires that, which only happens in the rarest of cases in public companies, and management tasks cannot be transferred to the supervisory board.

The *general meeting* does fundamentally have this authority under English law and could exercise it, but it is regularly transferred for practical reasons by the *articles* themselves or by the model *articles* to the *board of directors*, that is, to a body that is independent of the shareholders' meeting [36]. In this case, instructions to the *directors* by the *general meeting* are only permissible according to the model statutes if they are made by a *special resolution*. Consequently, the actual administration, business management and representation of the company are not exercised in legal reality either in Germany or England by the shareholders' meeting. A system of separation of the roles and interlocking of powers has prevailed in both legal systems that are characterised by the administrative members not having to follow instructions of the shareholders but is endowed with their own management responsibility [37]. In both countries, this expansion of management competence raises the question of counter-forces internal to the organisation that is suitable for strengthening the proven system of *checks and balances*. With certain differences in the detail, both German and English company law strive for a much more strongly pronounced law of liability for the members of management as a counter-force [38]. There are commonalities in the fundamental concepts insofar as a common awareness of the problem has in respect, of the modern fundamental decisions of shareholders [39]. Whilst the competences of the shareholders are expanded in England with the categorisation under capital market law as *Class 1 transactions*, Germany falls back on the judicially-developed Holzmüller doctrine [40].

In German company law, together with the board, which is concerned with management and representation tasks, the supervisory board is also entrusted with tasks of company management. The primary task of the supervisory board consists in monitoring the board, through which the supervisory board is involved in the company management organisation of the share company. German company law is thus characterised by a strict separation of business management and representation on the one hand and

control on the other, so that no one has the risk of supervising themselves. In theory, this provides the solid fundamental condition for independent and neutral control of business leaders [41], which is, however, overshadowed in legal practice by considerable knowledge deficits in the supervisory board members, as no one can monitor without actually being there [42]. This is compounded by the widespread tendency to selective passing of information by the separation of the two bodies: good news is passed on quickly, bad news is delayed or not reported at all [43]. Ultimately, the institutional dichotomy leads to supervisory board members only being able to exert a limited effect on strategic business decisions [44] and being hopelessly too far behind to take effective counter measures especially in crisis situations for reasons of time [45].

But contrast, management and supervision tasks are typically unified in an English public company in the *board of directors*. Even if there is increasingly a separation of business management and control in the *board of directors* of public company by the division of tasks between *executive* and *non-executive directors* and thereby an approximation to the dualistic system, the monistically constituted public company still has no body comparable to the German supervisory board. Whilst the main task of the supervisory board of a German share company consists of the continuous monitoring of the business management, the authorities of the *non-executive directors* are not limited to control activities but extend to them being involved in crucial company decisions [46]. This lack of an institutionalised supervisory body is a consequence of the prevailing understanding of democracy in England. In that respect the organisational constitution of a public company represents the relationship of parliament to the government, the English state philosophy [47]. Building on this concept, it is consistent that there is no place for an "intermediate" supervisory body and that unrestricted competence and general responsibility rests with the organised shareholders in the *general meeting* [48]. The *general meeting* is thus the seat of control in the public company.

A better supply of information is achieved by separating the *executive* and *non-executive directors* within the *board* system than in the dualistic system, as the *non-executive directors* participate in the meetings of the management body and are thereby stronger and immediately involved in the company's affairs [49]. The *non-executive directors* are, however, subject to the difficulty that they do not receive neutral information, as the selection of data is crucially decided by the Management and agenda items are also set by the *executive directors*. This illustrates the susceptibility of the monistic system to group-dynamic processes which make it more difficult for the outside *directors* to switch between participation in

decisions and monitoring tasks. This applies even more so if the *Chairman of the Board* and the *Chief Executive Officer* are the same person thus further intensifying the internal imbalances of committee power.

Finally, there is a further structural difference in that every *public company* must have a secretary along with the *board of directors*. The *secretary* of the *public company*, who must have recognised professional qualifications, is a kind of "clerk to the court" and "keeper of the seals", unfamiliar to German company law, with important rights and obligations. In particular, the secretary is responsible for keeping the specified accounts and directories of the *public company*, taking the minutes of the *general meeting* and the *board meetings* and submission of the documents required for publication to the company register.

Conclusion

The discussion of advantages and disadvantages of the monistic and dualistic systems of organisation of companies and thus ultimately the question of the superiority of one system over the other is ongoing and both legal and economic literature has been occupied by both for decades – no end is in sight, especially as through the legal form of the SE, the European share company can choose between the two systems. Ultimately, both systems are concerned with closing the existing gaps between poorly informed shareholders as "principal") and the comprehensively informed business leaders as "agent" for the purpose of good Corporate Governance. Big business scandals both here and there have shown that neither system is free from faults and errors in individual cases, and both have failed in control and risk management. The two organisation models are moving closer to each other to contain these control deficits: whilst the monistic system copies a separation of roles by *executive* and *non-executive directors* and attempts to separate the persons of *Chief Executive Officer* and *Chairman of the Board*, the dualistic system tries to improve the information exchange between the executive board and the supervisory board.

It can be seen that each organisation model has advantages and disadvantages compared with the other that carry the same weighting such that neither organisational model is fundamentally superior to the other.

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About the authors

Arne Heller was a partner in the law firm Wirtschaftsrat Recht Bremer Heller and now works as a management consultant for medium-sized companies and as a lecturer on international corporate law.

To contact the author: arne.heller@gmx.de

Alexander Schuhr is a lawyer and notary at the law firm Schuhr Richter Hartwich Glevitzky in Nordenham.