

SHAREHOLDER VALUE AND EMPLOYEE INTERESTS: INTERSECTIONS BETWEEN CORPORATE GOVERNANCE, CORPORATE LAW AND LABOR LAW*

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I. INTRODUCTION

It has been observed that corporate law and labor (or employment) law are, in essence, separate fields of legal scholarship and regulatory policy.¹ This separation does not mean there has been no interest by company lawyers in labor law or vice versa, nor does it mean that the two fields lack relevance to one another. Clearly, both corporate law and labor law have provided certain fundamental starting points for analysis, each shaping the regulatory scope of the other. For example, corporate law, by bestowing legal personality on business entities, allows such entities to enter bilateral employment contracts with workers. At the same time, the corporation's actions in establishing, conducting, and terminating such employment relationships are subject to labor law. What the separation does mean, however, is that, generally speaking, the concerns and problems associated with corporate governance are regarded as separate from those problems associated with employment regulation.

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¹ Steven Anderman, *Termination of Employment: Whose Property Rights?*, in *THE FUTURE OF LABOUR LAW* 101, 126 (Catherine Barnard et al. eds., 2004); Simon Deakin, *Workers, Finance and Democracy*, in *THE FUTURE OF LABOUR LAW* 79, 79 (Catherine Barnard et al. eds., 2004); Henry Hansmann, *Worker Participation and Corporate Governance*, 43 *U. TORONTO L.J.* 589, 589 (1993).

Events over the past ten to fifteen years have done much to suggest that this “radical”² separation of corporate governance concerns and labor law is no longer sustainable or desirable. Indeed, it has been argued that “the question of who exercises power and control in corporations, and the implications of the growing ‘financialisation’ of the economy for notions of democratic participation and accountability” constitute a “set of issues . . . of direct and central concern to labour lawyers,”³ resulting in the relationship between labor law and corporate governance becoming “both complex and paradoxical.”⁴

Such revised analysis is partly owed to a stream of high-profile corporate collapses that have left employees out of pocket with regard to wages and other entitlements. This has directed labor lawyers’ attention to the corporate form itself and how its manipulation through, for example, deliberate asset stripping and the use of group structures might be used to achieve certain industrial relations ends, and thence to the question of how employees’ claims can be strengthened against the rights conferred by corporate law on shareholders and secured creditors in such circumstances.⁵ This revised analysis is also related to debates about issues such as employee representation on company boards of directors, employee share ownership, and whether employees should be consulted in relation to planned corporate restructuring.

More broadly, some industrial relations scholars have pointed to a coincidence between the growing dominance of a corporate law system intent on delivering “shareholder value”

² Hansmann, *supra* note 1, at 589.

³ Deakin, *supra* note 1, at 99.

⁴ *Id.* at 79.

⁵ High profile corporate collapses in Australia in which these issues have arisen include Patrick Stevedores, Ansett Airlines, National Textiles and Coogi. See Paula Darvas, *Employees’ Rights and Entitlements and Insolvency: Regulatory Rationale, Legal Issues and Proposed Solutions*, 17 *COMPANY & SEC. L.J.* 103 *passim* (1999); Anthony Forsyth, *Corporate Collapses and Employees’ Right to Know: An Issue for Corporate Law or Labour Law?*, 31 *AUSTL. BUS. L. REV.* 81 *passim* (2003); David Noakes, *Dogs on the Wharves: Corporate Groups and the Waterfront Dispute*, 11 *AUSTL. J. CORP. L.* 27 *passim* (1999); Joellen Riley, *Lessons from Ansett: Locating the Employee’s Voice in Corporate Enterprise*, 27 *ALTERNATIVE L.J.* 112 *passim* (2002).

and more fragmented labor markets, especially as regards job security, work intensification, and investment in training and skills.⁶ The extent to which these events and issues are causally related is a matter for debate.⁷ Their interconnectedness and interaction, however, suggest the grounds for an argument that the concerns of corporate law and labor law are now similarly interconnected. Indeed, some theorists have explored the idea that there may be a causal relationship or functional complementarity between models of corporate governance and models of labor management, and that these couplings may be classified according to national “varieties of capitalism”⁸ or “business systems.”⁹ One form, variously called “Rhineland capitalism,” “welfare capitalism,” or “coordinated market economies,” is said to be characteristic of countries such as Germany, Sweden, the Netherlands, and Japan, and entails a corporate governance system characterized by bank-based debt, an intertwining of debt and equity ownership, and inter-corporate shareholdings. This system encourages direct and long-term monitoring of corporate performance by capital providers rather than reliance solely on bottom-line, short-term financial indicators. Given this long-term orientation, it is argued that employers and employees are more able to pursue cooperative relations and industrial relations strategies that have a long-term payoff: credible commitments on job security,

⁶ See, e.g., PETER CAPELLI, *THE NEW DEAL AT WORK* (1999); BENNETT HARRISON & BARRY BLUESTONE, *THE GREAT U-TURN: CORPORATE RESTRUCTURING AND THE POLARIZING OF AMERICA* (1988); MICHAEL PORTER, *CAPITAL CHOICES: CHANGING THE WAY AMERICA INVESTS IN INDUSTRY* (1992); IAN WATSON ET AL., *FRAGMENTED FUTURES: NEW CHALLENGES IN WORKING LIFE* (2003); Julie Froud et al., *Restructuring for Shareholder Value and Its Implications for Labour*, 24 *CAMBRIDGE J. ECON.* 771 (2000); William Lazonick & Mary O’Sullivan, *Corporate Governance and Corporate Employment: Is Prosperity Sustainable?* (Levy Econ. Inst., Working Paper No. 183, 1997), available at <http://econwpa.wustl.edu/eps/mac/papers/9802/9802022.pdf>.

⁷ See *CORPORATE GOVERNANCE AND LABOUR MANAGEMENT: AN INTERNATIONAL COMPARISON* (Howard Gospel & Andrew Pendleton eds., 2005); Shelley Marshall, *Hedging Around the Question of the Relationship Between Corporate Governance and Labour Regulation*, 18 *AUSTL. J. LAB. L.* 97 *passim* (2005) (reviewing *CORPORATE GOVERNANCE AND LABOUR MANAGEMENT: AN INTERNATIONAL COMPARISON* (Howard Gospel & Andrew Pendleton eds., 2004)).

⁸ *VARIETIES OF CAPITALISM* (Peter Hall & David Soskice eds., 2001).

⁹ RICHARD WHITLEY, *DIVERGENT CAPITALISMS: THE SOCIAL STRUCTURING AND CHANGE OF BUSINESS SYSTEMS* (1999).

investment in training and skill formation, and a commitment to employee participation.

In contrast, liberal market economies, such as the United States and the United Kingdom, are characterized by highly liquid capital markets, dispersed share ownership, companies' greater vulnerability to hostile takeover bids, and the presence of large institutional investors anxious for quarterly improvements in share price, all of which entrench a narrow understanding of shareholder value as the dominant objective of corporate management. This, in turn, demands flexible employment arrangements, which allow for short-term adjustments in labor costs. Even if managers do not believe their primary duty is to shareholders, they may still feel constrained from making long-term commitments to employees in these areas because their decision-making horizon is shaped by short-term financial indicators. In such economies, mechanisms of employee participation, consultation, or collective bargaining are liable to be discounted because they may restrict management's freedom to maneuver to meet shareholder imperatives. By contrast, remuneration schemes that use employee share ownership to link pay to share performance will be favored as a way to align worker and shareholder interests. Further, there is a sense that the growth in shareholding in the wake of privatizations and demutualizations has further entrenched the pursuit of shareholder value within liberal market economies, as has an aging population concerned with saving for retirement, where retirement savings depend upon market performance.

This posited link between the increasing pursuit of shareholder value and deteriorating outcomes for labor has become the subject of an increasingly sophisticated international scholarship.¹⁰ At the same time, some commentators have questioned the extent to which broad, national ideal types of corporate governance and ownership structure can usefully explain labor

¹⁰ See, e.g., Gospel & Pendleton, *supra* note 7 (the country studies); Gregory Jackson, *Toward a Comparative Perspective on Corporate Governance and Labour Management* (Research Inst. of Econ., Trade and Indus. (RIETI), Discussion Paper Series 04-E-023, 2004), available at http://www.sase.org/conf2004/papers/jackson_gregory.pdf.

management practices at the individual company level.¹¹ Others, writing in the British context, have argued that new labor law rights, especially those surrounding statutory employee representation, mean that the shareholder value norm must be seen as unstable and less institutionally fixed than is often thought.¹²

In this paper, we commence an examination of some of these issues, with a particular focus on Australia. Our attention is explicitly focused on the regulatory framework provided by Australian corporate and labor law. Within corporate law, shareholders have at their disposal a range of potential strategies by which they may influence management business strategy, structure the time frame of managerial decision making, and/or elevate financial factors in decision making. The key corporate law doctrines in this area concern shareholders' powers to vote on important corporate matters (including the appointment and removal of directors) and the affirmative duty of loyalty owed by directors.

Beyond these traditional concerns of corporate law, there is a range of other potential strategies by which shareholders might either enhance their control over management or structure management decision making. These include shareholders' capacity to express dissatisfaction with management performance through exiting a company by selling shares. Further strategies may involve moderating any underlying conflicts of interest between management and shareholders in the following ways: by giving decision-making rights to independent directors with no self-interest; by aligning management self-interest with shareholder self-interest; and most obviously, by linking managers' remuneration to the successful delivery of shareholder wealth maximization.¹³ As will become apparent in the following discussion of developments in Australian corporate governance, it is in fact these latter types of strategies that are increasingly the focus of

¹¹ See Howard Gospel & Andrew Pendleton, *Finance, Corporate Governance and the Management of Labour: A Conceptual and Comparative Analysis*, 41 BRIT. J. INDUS. REL. 557 *passim* (2003).

¹² John Armour et al., *Shareholder Primacy and the Trajectory of UK Corporate Governance*, 41 BRIT. J. INDUS. REL. 531 *passim* (2003).

¹³ R.P. AUSTIN ET AL., *COMPANY DIRECTORS: PRINCIPLES OF LAW AND CORPORATE GOVERNANCE* 9-12 (2005) (outlining these as well as other strategies).

regulatory reform: the fostering of a market for corporate control, the promotion of independent directors, and performance-based pay for senior executives. We suggest that, whereas the traditional strategies favored by corporate law give only modest support for shareholder primacy, these recently favored strategies are more closely allied to facilitating the pursuit of shareholder value over and above the interests of labor. Yet, as we also suggest, the impact of these strategies on corporate governance remains ambiguous.

Our consideration of the regulatory framework cannot be divorced from a discussion of patterns of share ownership and corporate control. This is because we would expect certain shareholder strategies to be favored over others according to the structure of the securities market. Whereas concentrated ownership of shares facilitates direct control by shareholders, such control is more difficult to wield amongst dispersed shareholders. Dispersed ownership instead may facilitate “market-based” governance through trading of securities and takeovers or by reliance on incentive remuneration strategies aimed at senior management. Regulation also structures the flow of information within securities markets. Adequate disclosure of accurate and up-to-date information on corporate performance is essential to all strategies,¹⁴ but access to apparently reliable, current information about company performance may also make small investors, in particular, feel comfortable about participating in share trading and so encourage dispersed, liquid markets (which, in turn, offer ease of exit to shareholders). Conversely, information asymmetries between corporate “insiders” and “outsiders” may embed closed, concentrated patterns of shareholdings.¹⁵

Importantly, as noted above,¹⁶ in some contexts labor law will influence governance structures whereby employees can pursue strategies which constrain or structure management decision-making and thus modify the pursuit of shareholder value and/or its negative impacts on labor. Accordingly, we test this proposition by tracing the trajectory of Australian labor law.

¹⁴ PAUL DAVIES, INTRODUCTION TO COMPANY LAW 122 (2002).

¹⁵ Bernard Black, *The Legal and Institutional Preconditions for Strong Securities Markets*, 48 UCLA L. REV. 781, 786-89 (2001).

¹⁶ See Armour et al., *supra* note 12, at 532.

The paper proceeds, then, as follows. In Part II, we begin with the rise of the shareholder value model of corporate governance, and examine in detail the implications that it might have for labor. In Part III, we then examine the extent to which such a model of the corporation finds support in the key doctrines of corporate law concerning shareholder decision-rights and directors' duties. Part IV examines recent aspects of corporate governance reform in Australia and their relationship to the shareholder value or shareholder primacy model. This is followed, in Part V, by an examination of some aspects of the structure of share ownership in Australia, with attention given to the rise of institutional investors in particular, again with the objective of identifying potential links with the shareholder value agenda. In Part VI, the argument moves to a consideration of the role of labor law in corporate governance. Part VII is the concluding section.

II. THE RISE OF SHAREHOLDER VALUE AND THE CORPORATE GOVERNANCE 'PROBLEM'

We use the term "corporate governance" to refer to both descriptions and prescriptions about the exercise of power in large, publicly listed companies: who controls (or should control) the company, in whose interest the company is (or should be) controlled, and the ways in which control is (or should be) exercised.¹⁷ At its broadest, then, "corporate governance" would refer to all the forces that bear, or should bear, on decision making within the company. From a regulatory perspective, this would include not merely the legal rights of shareholders; but the contractual covenants of debtors; the commitments entered into with employees, suppliers, and customers; the regulations imposed by various government agencies; and the regulatory structuring of the various markets in which the company operates. Such a perspective is consistent with a "stakeholder" theory of corporate governance, in which the interests and welfare of employees, creditors, suppliers, customers and the local community are all seen as restricting the freedom of management to maximize

¹⁷ See Gospel & Pendleton, *supra* note 11, at 560; Steve Letza et al., *Shareholding versus Stakeholding: A Critical Review of Corporate Governance*, 12 CORP. GOVERNANCE 242, 242, 254-55 (2004).

wealth for shareholders. Such a view can be based on economic efficiency¹⁸ and/or social justice.¹⁹

In contrast, a narrower, more traditional legal understanding of corporate governance considers the corporation as a legal instrument whereby shareholders are able to maximize their wealth. Delivering shareholder value, measured according to increasing returns on capital employed and rising share prices, is adopted as an index of management success. This entails the financialization of management goals and the logic of public, market valuation of management performance.²⁰ The focus on shareholder value reinforces the controlling rights of shareholders in the corporation; the focus of regulatory intervention is on the three-tiered hierarchical relationship among shareholders, the board of directors, and senior managers.

The shareholder and stakeholder perspectives give rise to differing diagnoses of the “problem” of corporate governance, and suggest different solutions.²¹ For stakeholder theorists, the major problem is the lack of involvement in company decision making by stakeholders other than shareholders. From this perspective, corporate governance recommendations should support the coalition of interests that embody and perpetuate the company’s core capabilities. Corporate boards should be a deliberative forum, representing not solely shareholder interests, but also those interest groups among the company’s stakeholders that add

¹⁸ See, e.g., MARGARET BLAIR, *OWNERSHIP AND CONTROL: RETHINKING CORPORATE GOVERNANCE FOR THE TWENTY-FIRST CENTURY* (1995).

¹⁹ See, e.g., *STAKEHOLDER CAPITALISM* (Gavin Kelly et al. eds., 1997).

²⁰ See Julie Froud et al., *Shareholder Value and Financialization: Consultancy Promises, Management Moves*, 29 *ECON. & SOC’Y* 80, 85 (2000) (explaining that advocates of shareholder value may debate the exact metric to use in evaluating performance, and various consultancy firms and their principals have developed proprietary concepts to measure management performance, such as ‘Economic Value Added’ and ‘Market Value Added’ (Stern Stewart); ‘Shareholder Value Added’ (LEK/Alcar Consulting Group); ‘Total Shareholder Return’ (Boston Consulting Group); ‘Economic Profit’ (McKinsey) and so on).

²¹ See, e.g., MARY O’SULLIVAN, *CONTESTS FOR CORPORATE CONTROL: CORPORATE GOVERNANCE AND ECONOMIC PERFORMANCE IN THE UNITED STATES AND GERMANY* 289-290 (2000) (drawing a simple distinction between ‘shareholder’ and ‘stakeholder’ models); Kevin Keasey et al., *Introduction: The Corporate Governance Problem—Competing Diagnoses and Solutions*, in *CORPORATE GOVERNANCE: ECONOMIC AND FINANCIAL ISSUES* 1 (1997) (containing a more nuanced taxonomy); Letza et al., *supra* note 17, at 254-55.

value and assume unique risk.²² In contrast, advocates of shareholder primacy focus on the delegation of corporate control to directors and managers to run a company on behalf of all shareholders. The major problem arising here is a risk that managers and directors will look after their own interests at the expense of shareholders. Given this risk, the key issue becomes one of determining which set of regulatory or institutional arrangements can ensure that shareholders' interests are adequately protected and managers rendered accountable.

We suggest that the problem/solution couplet generated by the shareholder model, particularly in its modern variant known as "agency theory," currently dominates regulatory discourse and reform in Australia. The diagnosis of the corporate governance problem in these terms goes back to Adam Smith, who observed that directors in the joint stock company could not be expected to be as vigilant and careful with other people's money as with their own.²³ Much of the subsequent debate and doctrinal development in corporate law around issues of governance has been driven by an image of shareholders as a dispersed and marginalized group, separated from their investment as a result of the division between "ownership" and "control."²⁴ This approach was given impetus by empirical work undertaken by Adolf Berle and Gardiner Means in the United States in the late 1920s, which suggested that the dispersed nature of shareholdings left few large blocks of shareholders capable of using their legal powers to select and control management. Instead, management had become a self-selecting oligarchy in effective control of most corporations, thus giving them ample scope for opportunism, shirking, or self-dealing.²⁵

²² See, e.g., Allen Kaufman et al., *A Team Production Model of Corporate Governance Revisited* (George Washington Univ., Dep't Strategic Mgmt & Pub. Pol'y, Working Paper 03-03, 2003), available at http://ssrn.com/sol3/abstract_id=410080.

²³ See ADAM SMITH, *Of the Expence of Public Works and Public Institutions*, in WEALTH OF NATIONS 244, 260 (Edwin Cannan ed., Univ. Chi. Press 1976) (1776).

²⁴ Jennifer Hill, *Visions and Revisions of the Shareholder*, 48 AM. J. COMP. L. 39, 39 (2000).

²⁵ ADOLPH A. BERLE, JR. & GARDINER C. MEANS, THE MODERN CORPORATION AND PRIVATE PROPERTY 94 (1932), found effective management control in 44 percent of the 200 largest US corporations, and a further 21 percent on the brink of such control. By the 1960s, one study classified 84 percent as "management

There were, over time, a number of different responses to the corporate governance problem as outlined by Berle and Means. Berle, around the time of writing his book with Means, had emphasized the fiduciary character of management's relationship to shareholders and stressed the need to strengthen the equitable standards that constrain managers.²⁶ Others saw potential in activating shareholder democracy and fostering more participation by investors in corporate affairs.²⁷ Some scholars, however, insisted that the dispersed, uncommitted nature of shareholders was a virtue rather than a vice, in that shareholders' readiness to "exit" corporations underpinned the liquidity necessary for a functioning "market in corporate control." Henry Manne argued that managers were not as unaccountable as they seemed, and were in fact subject to quite strong market disciplines or, ideally, were subject to such disciplines provided managerialists did not have their way in "abandon[ing] the ideal of competition as a resource allocator within the economy."²⁸ Product market competition and the labor market for managers each play a part in ensuring that managers act diligently and efficiently in pursuit of profits, but central is the "market for corporate control":²⁹ if a company underperforms due to management incompetence or dishonesty, its share price will drop, providing the opportunity for outsiders to purchase shares at a lower price, oust the incumbent management, and run the company more efficiently so as to obtain greater reward. Managers will want to keep their jobs, so the mere possibility of takeover compels them to run their companies in a way that keeps share prices high.

Manne's analysis represented a rebuttal of Berle and Means' description of the corporation as one in which shareholders had lost effective control to managers. In arguing that the impact of

controlled." Robert J. Larner, *Ownership and Control in the 200 Largest Non-Financial Corporations, 1929 and 1963*, 56 AM. ECON. REV. 777, 781 (1966).

²⁶ See generally A. A. Berle, Jr., *Corporate Powers as Powers in Trust*, 44 HARV. L. REV. 1049 (1931).

²⁷ See, e.g., FRANK D. EMERSON & FRANKLIN C. LATCHAM, *SHAREHOLDER DEMOCRACY* (1954); J.A. LIVINGSTONE, *THE AMERICAN STOCKHOLDER* (rev. ed. 1963).

²⁸ Henry G. Manne, *The "Higher" Criticism of the Modern Corporation*, 62 COLUM. L. REV. 399, 414 (1962).

²⁹ Henry G. Manne, *Mergers and the Market for Corporate Control*, 73 J. POL. ECON. 110, 113 (1965).

market mechanisms had been underestimated, Manne paved the way for law-and-economics scholars to further develop a model of corporate governance, both descriptive and prescriptive, that drew on notions of efficiency, agency costs, and incomplete contracting to explain why shareholder wealth maximization both is, and should be, at the heart of corporate governance. This model views the corporation as a series of bargains or contracts among all those involved in the business enterprise. Within this “nexus of contracts,” shareholders are viewed as the only participants who make investments in the corporation that are open-ended and without any contractual guarantee of a specific return. As solely residual claimants whose return is almost wholly dependent on the company’s economic success, they have an interest in making the residual or surplus as large as possible and thus have the most powerful incentive to ensure that management operates in the most efficient and productive manner. Accordingly, running corporations to maximize shareholder value will result in superior economic performance.

Accepting that managers *should* be running the company to maximize shareholder wealth, and accepting the contract as the preferred metaphor by which economists understand human relationships, there emerges a view of shareholders as “principals” and managers as their “agents.” Albeit using a more systematic theoretical language, finance theorists largely returned to the Adam Smith/Berle and Means problematic: managers and shareholders have divergent interests, yet shareholders, or, at least, dispersed shareholders, find it difficult and expensive to monitor management. This is the problem of “agency costs.”³⁰

However, the nexus-of-contracts, or agency, theory of the corporation (we will use the terms interchangeably) also differs from the Berle and Means approach in at least two ways. First, it displaces shareholders from any formal centrality as “members”

³⁰ For classic statements of the ‘nexus of contracts’ and ‘agency’ theories of the firms, see Armen A. Alchian & Harold Demsetz, *Production, Information Costs, and Economic Organization*, 62 AM. ECON. REV. 777 (1972); Eugene F. Fama, *Agency Problems and the Theory of the Firm*, 88 J. POL. ECON. 288 (1980); Michael C. Jensen & William H. Meckling, *Theory of the Firm: Managerial Behavior, Agency Costs and Ownership Structure*, 3 J. FIN. ECON. 305, 308 (1976). For applications to corporate law, see FRANK H. EASTERBROOK & DANIEL R. FISCHER, *THE ECONOMIC STRUCTURE OF CORPORATE LAW* (1991); Symposium, *Contractual Freedom in Corporate Law*, 89 COLUM. L. REV. 1395 (1989).

or “owners” of the corporation, making them one of merely several groups that have contractual claims on the corporation.³¹ At the same time, however, for efficiency reasons, it reinstates the maximization of shareholder value as the appropriate goal of management.³² Second, following Manne, it tends to see the solution to the agency problem not in terms of the traditional core doctrines of corporate law, such as shareholders’ powers of direct intervention or directors’ fiduciary duties, but in market-based mechanisms of governance. These include, first, adjusting the remuneration packages of senior management so as to produce optimal incentives for management to pursue shareholder wealth maximization. This is done through an outcome-based contract for management pay, based on share options, which tie pay to share price increases. Second, because managers may manipulate the flow of information with regard to company performance, or otherwise dominate board decision making, a strong disclosure regime and a board of independent directors is also needed to monitor management behavior, ensure external auditing of the company’s financial statements, set appropriate performance hurdles, and so on. Third, in situations where both

³¹ See, e.g., Fama, *supra* note 30, at 290 (discussing “the irrelevance of the concept of ownership of the firm”). Outside of ownership, agency theorists tend to base shareholders’ contractual claims on their role as “investors.” See Andrei Shleifer & Robert W. Vishny, *A Survey of Corporate Governance*, 52 J. FIN. 737, 738 (1997), who proclaim, “our perspective on corporate governance is a straightforward agency perspective, sometimes referred to as separation of ownership and control. We want to know how investors get the managers to give them their money back.” Yet the stock market does not serve as an important source of funds for long-term business investment in any advanced industrial economy. In Australia, the importance of equity financing has waxed and waned across the twentieth century and varied by sector. For most of the twentieth century, listed companies tended to use equity opportunistically to fund mergers and acquisitions, but it was not the dominant source of net finance. See GRANT FLEMING ET AL., *THE BIG END OF TOWN* 140-41 (2004). Even initial public offerings of shares usually represent the original owners of enterprises which have become successful on the basis of investments that have already been made cashing out their interest. The most common source of corporate finance is retained earnings, followed by debt.

³² Technically, agency theory can posit an agent-principal relationship between management and any investor of critical firm-specific assets. Typically, agency theorists put the shareholder in that position, but dissenting arguments can be made utilizing agency theory that other corporate actors might occupy the position of principal and pursue interests other than share value maximization. See, e.g., BLAIR, *supra* note 18, at 276.

these mechanisms fail, Manne's market for corporate control acts as a backstop.

Neither agency theories of the corporation nor consultancy metrics around shareholder value provide a clear operating guide as to what management must or can do to deliver results in specific circumstances.³³ There is no indication, for example, of the extent to which the delivery of shareholder value might involve enhancing the welfare of other corporate stakeholders such as employees, suppliers, or creditors. As we saw in the postwar period, many commentators shared the view that, given the dispersed nature of contemporary shareholdings, management indeed had the potential to dominate the corporate hierarchy. Yet unlike more recent agency theorists, many presumed management would exercise its powers responsibly rather than opportunistically, with potentially good results for labor: it meant the supersession of the profit maximization motive in favor of a neutral technocracy that was able to balance "a variety of claims by various groups in the community and [assign] to each a portion of the income stream on the basis of public policy rather than private cupidity."³⁴ "Functionless" shareholders were incapable of exercising the control rights which the law vested in them, and in any event did not desire to do so. In consequence, "the psychology and motivation of the top management class itself" had fundamentally changed as a result of its newfound independence from the company's shareholders. Fragmented shareholders were incapable of exercising the control rights which the law had vested in them, and did not desire to do so. "The psychology and motivation of the top management class itself" had changed as a result of its newfound independence from

³³ Julie Froud et al., *Financialisation and the Coupon Pool*, 78 *CAPITAL & CLASS* 119, 122 (2002). They argue that as a management strategy, "shareholder value" ignores the fact that most companies cannot easily deliver shareholder value because of structural constraints related to product markets, with gains made for capital at the expense of labor often needing to be passed on to consumers in the form of lower prices.

³⁴ ADOLPH A. BERLE & GARDINER C. MEANS, *The Modern Corporation and Private Property* 312-13 (rev. ed. 1967).

shareholders.³⁵ In this new world, “the shareholders have little power, and the government and the unions have much.”³⁶

In contrast, the gist of many agency perspectives on the corporation tend to presume a zero-sum game between shareholders and other stakeholders, whereby any regard by management to constituencies other than shareholders is seen as equivalent to a form of self-dealing. Berle and Means, for example, noted that managerial opportunism might include managers “out of professional pride . . . maintain[ing] labour standards above those required by competitive conditions.”³⁷ Similarly, for Jensen and Fama, management pursuit of perks might include not just spending shareholders’ money on air conditioned offices and plush carpets, but also pursuing “friendly employee relations.”³⁸

More generally, market and/or regulatory pressures on managers to enhance shareholder value might, in some circumstances, be expected to result in deteriorating outcomes for labor.³⁹ Where companies’ capacity to achieve increases in returns is limited by highly competitive product markets, moves to enhance shareholder value in the short-term will tend to focus on the reduction of labor costs, to the extent that employment protection legislation allows this, through redundancies, a shift to atypical hiring and decreased job security, the marginalization of trade unions, work intensification, and an underinvestment in employee skill development. The valorization of the takeover

³⁵ C. A. R. CROSLAND, *THE FUTURE OF SOCIALISM* 34 (1956).

³⁶ *Id.* at 362. For other positive interpretations of managerialism, see JOHN KENNETH GALBRAITH, *THE NEW INDUSTRIAL STATE passim* (1967); ROBIN MARRIS, *THE ECONOMIC THEORY OF ‘MANAGERIAL’ CAPITALISM passim* (1964). For Australian views that the reality of modern corporate management effectively displaced shareholder primacy, see R. KEITH YORSTON, *LIMITED LIABILITY COMPANIES IN AUSTRALIA: SOME ASPECTS OF CONTROL* 60-61 (1956); F.J. Willett, *Conflict Between Modern Managerial Practice and Company Law*, 5 MELB. UNIV. LAW REV. 481 *passim* (1967).

³⁷ BERLE & MEANS, *supra* note 34, at 116.

³⁸ Jensen & Meckling, *supra* note 30, at 314, do not actually use the word “perks” but go for what Doug Henwood calls the “mathematical prestige of a vector,” formalizing the problem as “ $X = \{x_1, x_2, \dots, x_n\}$ = quantities of all factors and activities within the firm from which the manager derives non-pecuniary benefits, such as office space, air conditioning, thickness of carpets, friendliness of employee relations, etc.” DOUG HENWOOD, *WALL STREET: HOW IT WORKS AND FOR WHOM* 267 (updated ed. 1998).

³⁹ HARRISON & BLUESTONE, *supra* note 6, *passim*.

mechanism in particular might also be seen as inimical to labor interests, in that corporate raiders often recoup the cost of high takeover premiums through subsequent downsizing.⁴⁰

Of course, the exact impact of corporate restructures and takeovers on employees will vary on a case-by-case basis, and is further complicated by the fact that cost reductions brought about by labor shedding may allow for real wage increases for remaining employees, and that other employees may benefit, at the point of redundancy or early retirement, from savings or pension schemes themselves based on stock market investment.⁴¹ In addition, flexible labor markets that allow shedding of labor relatively easily can promote product innovation by allowing companies to expand or contract quickly in terms of numbers of employees.

III. SHAREHOLDER VALUE AND THE LEGAL MODEL OF THE COMPANY

To sum up the progress of our argument so far, we have argued that a “shareholder value” model of the corporation dominates current discussion of the corporate governance “problem”; that such a model tends to suggest a particular regulatory

⁴⁰ Simon Deakin et al., *Implicit Contracts, Takeovers and Corporate Governance: In the Shadow of the City Code*, in *IMPLICIT DIMENSIONS OF CONTRACT: DISCRETE, RELATIONAL AND NETWORK CONTRACTS* 289, 291 (David Campbell et al. eds., 2003); Andrei Shleifer & Larry Summers, *Breach of Trust in Hostile Takeovers*, in *CORPORATE TAKEOVERS: CAUSES AND CONSEQUENCES* 33, 33-34 (Alan J. Auerbach ed., 1988).

⁴¹ Froud et al., *supra* note 6, at 792-94. Empirical studies of the relationship between redundancies and share price indicate much depends on the context of the company restructure: financial markets often respond negatively to announcements of redundancies where these are seen as arising from a need to deal with financial crisis or difficulty, compared with a positive response where the decision is framed as part of an overall restructure to improve efficiency, suggesting redundancies themselves are not an explicit signal to increase shareholder value. See Dan L. Worrell et al., *Layoff Announcements and Shareholder Wealth*, 34 *ACAD. OF MGMT. J.* 662, 664 (1991); Henry S. Farber & Kevin F. Hallock, *Have Employment Reductions Become Good News for Shareholders?* (Nat'l Bureau of Econ. Research, Working Paper No. 7291, 1991), available at <http://www.nber.org/papers/w7295>. On the negative impact of hostile takeovers on employment levels, see M. Conyon et al., *The Impact of Mergers and Acquisitions on Company Employment in the United Kingdom* (Ctr. for Research on Globalization and Labour Mkt., Paper 2000/5, 2000), available at http://www.nottingham.ac.uk/economics/leverhulme/research_papers/00_5.html.

agenda; and that such a model and regulatory agenda could be expected, in some circumstances, to operate to the detriment of the interests of labor. In this section we examine the extent to which this model does accurately reflect key features of Australian corporate law.

We suggest that agency theory does not accord particularly well, either descriptively or prescriptively, with what we term the legal model of the company or with some of the core doctrines of Anglo-Australian corporate law. It is true that the idea that a corporation represents a nexus of voluntarily bargained contracts resonates with some aspects of corporate law. For example, the law does view the corporation as a private association of “members” joined by mutual agreement.⁴² The “members” or shareholders of a company in turn delegate, through the constitution, decision-making power to the board of directors. The directors are beholden to the shareholders for the formal grant of their functions and the shareholders retain control over the constitution and its amendment and have the right to approve irregular transactions⁴³ and, in the case of shareholders of public companies, to remove directors at any time without cause by ordinary vote.⁴⁴ Directors, in turn, are required to exercise the powers conferred on them in good faith in the best interests of the company and for a proper purpose,⁴⁵ and to act with reasonable care and diligence.⁴⁶

⁴² See Corporations Act, 2001, c. 2B, § 140(1) (Austl.), whereby the constitution of a company creates contractual relations between members *inter se* and between members and the company and the directors and the company. See also *Automatic Self-Cleansing Filter Syndicate Co. v. Cunningham*, (1906) 2 Ch. 34 (Eng.).

⁴³ Corporations Act, 2001, c. 2E.

⁴⁴ Corporations Act, 2001, c. 2D, § 203D.

⁴⁵ Corporations Act, 2001, c. 2D, § 181(1).

⁴⁶ Corporations Act, 2001, c. 2D, § 180(1). Shareholders also have a claim on company income, by way of dividend, and on its capital on winding up. Although these are, in practical terms, among the most important rights, they are substantively not much different from the rights held by creditors. It is the participative rights and fiduciary duties owed them that distinguishes shareholders. See Ross Grantham, *The Doctrinal Basis of the Rights of Company Shareholders*, 57 CAMBRIDGE L.J. 554, 582 (1998).

Yet while the rights attached to a share are defined, like contractual rights, by the terms of the issue, the company's constitution, and the general and statutory law, many of these rights cannot be abridged by agreement. Those that can be abridged (for example, a company's constitution) are, in the case of large, publicly listed companies, rarely the product of anything resembling a contractual negotiation,⁴⁷ and can be amended without the agreement of all members, by special resolutions requiring only a three-quarters majority vote.⁴⁸ Today, this bundle of rights is rarely regarded in terms of obligation, contract, or personal rights of action, "largely because commercial practice demands that those rights be generally transferable, assignable, and enforceable against third parties."⁴⁹

This analysis suggests that notions of a contractual, agency relationship between shareholders and directors are primarily a remnant of the law as it operated until the early nineteenth century, when joint stock companies were seen at law as partnerships, with shareholders having equitable ownership of the partnership assets and relying on managers as their agents. This was true of both incorporated and unincorporated companies. Whereas incorporation created a separate legal entity, that entity was still conceptualized as composed of members merged into one body.⁵⁰ Shareholders stood in a contractual relation *inter se* and, before the widespread emergence of the fully paid-up share, had contractual connections to third parties by virtue of residual liability.⁵¹ Across the middle decades of the nineteenth century,

⁴⁷ Paddy Ireland, *Recontractualising the Corporation: Implicit Contract as Ideology*, in *IMPLICIT DIMENSIONS OF CONTRACT* 255, 265 (David Campbell et al. eds 2003). EASTERBROOK & FISCHER, *supra* note 30, at 93 also concede that it is "almost impossible" in practice for shareholders in public companies to amend their rights.

⁴⁸ Corporations Act, 2001, c. 2B, § 136(2) provides that a company may amend its constitution by special resolution. See *Bailey v. N.S.W. Med. Def. Union Ltd.* (1995) 184 C.L.R. 399 *passim* (discussing the status of the corporate constitution).

⁴⁹ Sarah Worthington, *Shares and Shareholders: Property, Power and Entitlement (Part I)*, 22 *COMPANY L.* 258, 260 (2001).

⁵⁰ See Paddy Ireland, *Capitalism Without the Capitalist: The Joint Stock Company Share and the Emergence of the Doctrine of Separate Corporate Personality*, 17 *J. OF LEGAL HIST.* 41, 45 (1996).

⁵¹ Paddy Ireland, *Property and Contract in Contemporary Corporate Theory*, 23 *LEGAL STUD.* 453, 459 (2003).

this understanding changed. Industrialization in Britain, particularly the advent of the railway companies, led to a dramatic increase in the number of joint stock shares and a significant fall in their denominations. A sophisticated market for their purchase and sale emerged as they became readily marketable commodities or liquid assets. Also, the emergence of the fully paid-up share freed shareholders from any residual liabilities or responsibilities. These developments, in turn, led to a notable reconceptualization of the joint stock company, both in law and in everyday consciousness. Shares were now seen as rights to profit, with a value of their own rather than as an equitable interest in the assets of the company. Those assets were now owned by the company alone.⁵²

One outcome of the reified notion of the company is that it creates the “conceptual space” for a movement away from shareholder exclusivity and grants management increased autonomy from day-to-day shareholder pressure.⁵³ This can be seen in two aspects. First, the company emerged with a constitutional character. Reflecting changing economic reality, the law has shifted power from shareholders and general meetings to the board of directors.⁵⁴ Directors now have exclusive right to manage the day-to-day activities of the company rather than being beholden to shareholders.⁵⁵ The general meeting of shareholders retains the right to make decisions only in specific, limited, key areas, such as altering the constitution, some alterations of share capital, winding up, or approving (retrospectively or prospectively) certain directors’ transactions where directors’ acts are in excess of their powers.⁵⁶ The other principal shareholder powers are

⁵² *Bligh v. Brent*, (1837) 2 Y&C Ex. 268, 295-97 (Eng.).

⁵³ John Parkinson, *Models of the Company and the Employment Relationship*, 41 BRIT. J. INDUS. REL. 481, 492 (2003).

⁵⁴ Other legal developments, such as the standardization of the incorporation process and articles of association (the company’s constitution), reflected the inability of mostly passive shareholders to protect themselves, contractually or otherwise. See Ireland, *supra* note 47, at 272.

⁵⁵ *Automatic Self-Cleansing Filter Syndicate Co.*, 2 Ch. 34, 34; *Nat’l Roads and Motorists Ass’n v. Parker* (1986) 11 A.C.L.R. 1.

⁵⁶ Furthermore, in the case of companies adopting the Corporations Act’s replaceable rules as their constitution, the general meeting of shareholders retains the right to set the directors’ remuneration. See, e.g., Corporations Act, 2001, c. 2D, § 202A. For a listed company, the effect of the ASX Listing Rules is that there

those of appointment (the selection and removal of directors). A company, through its constitution, decides on the details of the appointment process, and thus there is scope for considerable diversity in arrangements. However, shareholders' participation in the process is, in practice, limited in that it is generally difficult for them to appoint their own nominees rather than merely approve or reject nominees of the existing board.⁵⁷ With regard to the removal of directors, shareholders of a public company can remove a director at any time (subject to notice provisions) by ordinary resolution of the general meeting.⁵⁸ Yet even this power to dismiss is limited by the practical difficulties in convening extraordinary meetings. The conduct of meetings is further constrained by statutory provisions which, although ensuring members have a "reasonable opportunity" to question and convey comments to the board, impose no duty on directors to answer those questions. Nor can members requisition a meeting to pass resolutions relating to matters within the power of the board.⁵⁹

Second, to the extent that the law imposes rules or duties which structure the board's decision-making, such duties are owed not directly to shareholders but rather require directors to act in good faith, in the interests of the company, and to exercise corporate powers only for the purposes for which such powers

are a number of transactions which, under the constitution of a listed company, can only be entered into if approved in general meeting. *See generally* R.P. AUSTIN & I.M. RAMSAY, *FORD'S PRINCIPLES OF CORPORATIONS LAW* ch. 7 (12th ed., 2005).

⁵⁷ PAUL REDMOND, *COMPANIES AND SECURITIES LAW: COMMENTARY AND MATERIALS* 255 (3rd ed. 2000).

⁵⁸ This is a mandatory rule in the case of public companies, overriding any agreement between the company and the director or any other terms in the company's constitution. *See* Corporations Act, 2001, c.2D, § 203D.

⁵⁹ Corporations Act, 2001, c. 2G, §§ 250S, 250T. For discussion, see AUSTIN & RAMSAY, *supra* note 56, at 219.

are granted to the directors.⁶⁰ It is the company, not its shareholders, that is generally in a position to bring an action against a director for a breach of duties.⁶¹

At a practical level, any distinction between the interests of the company and the interests of shareholders may be viewed as negligible because, as Parkinson observes, generally what is good for the survival and growth of the company-as-entity will be good for the shareholders. However, as he notes, the continuity and growth of the company-as-entity is only of instrumental value as far as the shareholders are concerned, and in certain situations the fate of the company and the welfare of shareholders can diverge,⁶² such as in cases in which shareholders vote for compulsory winding up and distribution of the surplus amongst members or, as we shall see below, in takeover situations.

Even if we accept that the interests of the company are largely coextensive with the interests of shareholders, the formulation of directors' duties is still vague enough to allow considerable discretion to directors. It can be in the interests of existing shareholders for directors to take a long-term view of shareholder welfare, having regard to their future as well as existing interests.⁶³ Similarly, although the *end* of shareholder benefit is paramount, discretion as to the *means* to best achieve these ends

⁶⁰ Corporations Act, 2001, c. 2D, § 181(1). There may be an express purpose limitation of some corporate powers, but many powers are general and can only be read by reference to a general "corporate purpose" or the director's intention to benefit the company. For this reason, the 'proper purposes' duty has not always been treated as independent to the duty of good faith. The distinction, however, becomes more important where the power in question is capable of different characterizations, as in takeover situations. See REDMOND, *supra* note 57, at 420-21.

⁶¹ Because in practical terms it would be rare for directors to direct a company to sue themselves for breach of duty, the law has recognized a derivative suit whereby a shareholder can stand in the place of the company to bring a suit against the directors on the company's behalf, with any damages recovered being payable to the company. There is now a statutory derivative action that permits individual shareholders and officers of the company to bring legal proceedings on behalf of the company, subject to a series of limitations. See Corporations Act, 2001, c. 2F, §§ 236-242.

⁶² J. E. PARKINSON, CORPORATE POWER AND RESPONSIBILITY: ISSUES IN THE THEORY OF COMPANY LAW 77 (1993).

⁶³ As J.D. Heydon has observed, "to consider only the short-term interests of present shareholders would mean that every dollar available for dividend should be paid out; that no attempt to re-invest funds or expand the company's market by

remains with the directors. That is, long-term maximization of shareholder wealth may not be served by short-term profit maximization if the latter results in dissatisfied suppliers, antagonistic employees, and angry community groups. Rather, shareholder benefit might require a degree of largesse to other stakeholder groups.⁶⁴ Finally, the duty is largely based on a director's motivation and opinion as to what is in the best interests of the company, and not directed to any assessment of actual outcome. This grants considerable leeway to directors, as courts rarely interfere with the decision making of corporate boards or find conclusive proof that a director did not think the decision was in the best interests of the company.

These three factors — the absence of a time frame, the distinction between ends and means, and the focus on motivation and purpose rather than outcome — mean that directors retain considerable discretion and autonomy in exercising their powers. It is up to them to identify the interests of shareholders, the period over which these can be appropriately achieved, and the extent to which they require bestowing benefits on other stakeholder groups.⁶⁵ Thus the formulation “in the best interests of the company” remains compatible with directors striking a balance between the competing interests of different stakeholders in order to benefit the interests of shareholders in the long run. The main legal restriction on directors' discretion in this regard is that there be the possibility of *some* eventual return to shareholders which justifies a departure from short-term profit maximization. Bestowing benefits on other stakeholders has purely instrumental value, and such value will be difficult to justify where companies have ceased to trade (even where bestowing benefits reflects the declared wishes of the majority of shareholders).⁶⁶

price cutting should be allowed.” J.D. Heydon, *Directors' Duties and the Company's Interests*, in *EQUITY AND COMMERCIAL RELATIONSHIPS* 120, 135 (P.D. Finn ed., 1987).

⁶⁴ See *Hutton v. W. Cork Ry. Co.*, (1883) 23 Ch.D. 654, 673 (“The law does not say that there are to be no cakes and ale [for employees], but there are to be no cakes and ale except as required for the benefit of the company.”)

⁶⁵ L.C.B. GOWER, *GOWER AND DAVIES: THE PRINCIPLES OF MODERN COMPANY LAW* 604, 605 (7th ed., 2003).

⁶⁶ See, e.g., *Parke v. Daily News Ltd.*, (1962) 1 Ch. 927 (ceased to trade); *Hutton*, 23 Ch.D. 654 (winding up); cf. *Hampson v. Price's Patent Candle Co.*, (1876) 34 L.T.

Even where the fate of the company and the short-term welfare of shareholders diverge, the law does not compel the pursuit of shareholder wealth maximization but often continues to grant considerable latitude to directors to make discretionary judgments as to the best interests of the company.⁶⁷ In some takeover situations, for example, a bidder may be prepared to bid substantially above recent market prices, with the stated or suspected aim of taking control and selling off the company's assets. The offer may therefore be in the immediate interests of shareholders but contrary to the continuation of the company as an entity, and consequently to the interests of the management, employees, and third parties who are accustomed to dealing with the company. In such a situation, directors, managing the day-to-day business of the company, could enter into transactions or otherwise conduct the affairs of the company in a way which may defeat the bid but otherwise provide long-term benefits to shareholders. At the same time, acting in such a way would also entrench directors' own positions or benefit other stakeholders (such as employees) whose interests depend on the continued existence of the company. Australian courts have generally taken the view that as long as it is not, for example, the primary purpose of directors to perpetuate their own control, such actions by directors which result in the defeat of a hostile takeover are not a breach of duty.⁶⁸

To sum up, and draw out the implications for labor, the law grants shareholders explicit — although limited and residual — control rights in corporate affairs, yet an obligation on directors to maximize shareholder wealth cannot be implied from such control rights. Instead, managers retain considerable discretion

711 (Ch.) (gratuities to employees lawful as they would indirectly benefit the company in terms of increased worker morale and loyalty).

⁶⁷ Michael J. Whincop & Mary E. Keyes, *Corporation, Contract and Community: An Analysis of Governance in the Privatisation of Public Enterprise and the Publicisation of Private Corporate Law*, 25 *FED. L. REV.* 51, 80-82 (1997).

⁶⁸ See *Pine Vale Inv's. Ltd. v. McDonnell & East Ltd.*, (1983) 8 A.C.L.R. 199; *Winthrop Inv's. Ltd. v. Winns Ltd.*, (1979) 4 A.C.L.R. 1; *Harlowe's Nominees Pty. v. Woodside (Lakes Entrance) Oil Co.*, (1968) 121 C.L.R. 483. The legal position has been altered more recently by adjudications of the Takeovers Panel. These decisions, however, do not so much redefine the constituency of directors' fiduciary duties for the purposes of takeovers, but redefine the relative roles of directors and shareholders during takeover bids. See *infra* Part IV.

and autonomy, with which courts do not readily interfere, to mediate between stakeholder claims in pursuing the “best interests of the company.”⁶⁹ While this gives scope for management to pursue high wage, high skill, and high trust industrial relations strategies, it by no means mandates it. That is, whereas corporate law might be characterized as pro-managerialist, it would be an overstatement to say this necessarily entails positive support for labor or other non-shareholder groups.⁷⁰

In fact, the core of corporate law remains fairly explicitly preoccupied with the rights of shareholders. The interests of non-shareholder stakeholders do not figure prominently, but directors do owe a duty to give consideration to the interests of creditors when a corporation becomes insolvent or approaches insolvency.⁷¹ This could be interpreted as an example of the law

⁶⁹ The idea that corporate law entails a view of management operating as a “mediating hierarchy” balancing and adjudicating claims from different stakeholders is also explored in the United States context. *See, e.g.*, Margaret Blair & Lynne Stout, *A Team Production Theory of Corporate Law*, 85 VA. L. REV. 247 (1999). Arguably, Australian courts have recently been more willing to open the “black box” of management decision-making and to review corporate decisions. This is most apparent as regards directors’ duty of care, but largely focuses on procedure and propriety rather than the substantive effects of the decision in question on shareholders. *See* Whincop & Keyes, *supra* note 67, at 76-77.

⁷⁰ The main dissenting voices within the postwar “managerialist” perspective, BERLE & MEANS, *supra* note 34; CROSLAND, *supra* note 35; GALBRAITH, *supra* note 36; MARRIS, *supra* note 36; YORSTON, *supra* note 36; Willett, *supra* note 36, did not so much question the common belief that managers were in a position to operate free of effective shareholder control, but rather argued that this freedom made little difference to the goals pursued by large corporations, given managers tended to share the same background, social formation and values of the share-owning class. *See, e.g.*, C. WRIGHT MILLS, *THE POWER ELITE* (1956) (in the United States); EDWARD S HERMAN, *CORPORATE CONTROL, CORPORATE POWER* (1981) (in the United States); THEO NICHOLS, *OWNERSHIP, CONTROL AND IDEOLOGY* (1969) (in Britain).

⁷¹ There has not been imposed a direct fiduciary duty to act in the best interests of creditors but, rather, an understanding that fulfilling the fiduciary duty to ‘the company’ will mean, in the case of insolvency or near-insolvency, giving priority to the interests of the creditors over those of the shareholders. *Walker v. Wimborne* (1976) 137 C.L.R. 1, 6 (*per* Mason J.). One implication of this is that where directors breach their duty to the company in an insolvency context such that it directly prejudices the creditors of the company, the shareholders cannot ratify that breach. *Kinsella v. Russell Kinsella Pty.* (1986) 4 N.S.W.L.R. 722. Outside of this development of the common law duties of directors, a more powerful development is to be found within the insolvent trading provisions of the Corporations Act. Corporations Act, 2001, c. 5, §§ 588J-U. This imposes personal liability on directors who incur a debt on behalf of the company when, at

positively protecting a wider range of interests than those of shareholders.⁷² However, in the case of insolvency, creditors merely supplant shareholders and, through processes of receivership,⁷³ voluntary administration,⁷⁴ or liquidation,⁷⁵ succeed to many of their rights. Within corporate law, there appears to be no comparable capacity for employees to supplant and succeed shareholders in defined situations.⁷⁶ Employees now figure in the Corporations Act, but only as a species of creditor for the purposes of any unpaid wages and other entitlements on insolvency. Recent legislative amendments rank employees ahead of other unsecured creditors,⁷⁷ and directors can face a statutory liability

the time, there were reasonable grounds for suspecting the company's insolvency. On the policy background to these provisions and an evaluation of their effects, see Paul James et al., *Insolvent Trading: An Empirical Study*, 12 *INSOLVENCY L. J.* 210, 215-19 (2004).

⁷² Jennifer Hill, *At the Frontier of Labour Law and Corporate Law: Enterprise Bargaining, Corporations and Employees*, 23 *FED. L. REV.* 204, 215-16 (1995).

⁷³ Corporations Act, 2001, c. 5, §§ 416-434C. Receivership is usually triggered when a company fails to fulfill its contractual obligations to a secured creditor — usually repayments on a loan — who will institute the receivership by appointing a receiver to enforce their security. A receiver may work to manage the company and improve its financial situation, or merely sell the assets so as to pay the appointing creditors, leaving the balance for other creditors and shareholders.

⁷⁴ *See id.* §§ 435A-451D. Voluntary administration, first instituted in 1993 as an alternative to pure liquidation with a view to maximizing the chances of a business continuing in existence, activates a statutory moratorium on claims against a company from creditors. An administrator convenes a meeting of creditors which determines the appropriate course of action: liquidation, a deed of company arrangement, or ending the administration and handing the company back to the directors. A deed of company arrangement may involve creditors agreeing to defer or reduce debts or exchange their debt for equity, allowing the company to continue to trade.

⁷⁵ *See id.* §§ 459A-558. When a company cannot be saved, appointment of a liquidator and subsequent dissolution of the company is the most likely outcome. The primary duty of the liquidator is to ascertain company liabilities, realize its assets and distribute the proceeds amongst creditors in the statutory order of priority. Security interests created prior to the insolvency proceedings are not company assets for the purpose of distribution. Whereas a receiver owes primary duties to his or her appointer (the secured creditor), voluntary administrators and liquidators owe duties to the company.

⁷⁶ This is not to say such mechanisms might not be found in aspects of labor law. *See*, Armour et al., *supra* note 12, at 541-43. We will return to this argument in our discussion of Australian labor law. *See infra* Part VI.

⁷⁷ Corporations Act, 2001, c. 5, §§ 433, 556. Priority is given first to unpaid wages and superannuation contributions, followed by injury compensation payments,

for taking action designed to avoid payment of employee entitlements.⁷⁸ While it is true that through entitlement accrual, employees are, in effect, lending funds or working capital to their employer (in aggregate, employer entitlements in Australian companies currently probably exceed A\$50 billion⁷⁹), employees are involuntary creditors at zero finance, unlike other suppliers of finance.⁸⁰ Furthermore, this lending involves neither the capital market discipline nor the monitoring associated with external creditors. Construing employees as “creditors” in such circumstances can efface their real interests as employees as articulated through labor law. This was apparent in the 1998 waterfront disputes, where the Australian High Court held that an administrator’s duty to creditors under corporate law meant four stevedoring companies could not continue to trade so as to give effect to the Federal Court injunction, made under the Workplace Relations Act 1996, that the employees be re-hired.⁸¹ Yet in this case, the bulk of the “creditors” *were* the employees, who had clearly made their preference for continued work—at zero pay, if necessary—apparent by taking action through their union under the legislation.⁸²

IV. CORPORATE GOVERNANCE REFORM IN AUSTRALIA

We have noted that agency theorists emphasize the role of market mechanisms in compelling management to deliver shareholder value. Favored strategies include linking managerial pay to company performance, using boards of independent directors

then leave entitlements arising from an industrial instrument and finally retrenchment payments arising from an industrial instrument.

⁷⁸ Corporations Law Amendment (Employee Entitlements) Act, 2000, c. 5, §§ 596AA-596AI.

⁷⁹ Kevin Davis & Geoff Burrows, *Protecting Employee Entitlements*, 36 AUSTL. ECON. REV. 173, 173 (2003).

⁸⁰ Except for the effects of nominal wage growth. *Id.*

⁸¹ See *Patrick Stevedore Ops. (No 2) Pty. v. Maritime Union of Austl.* (1998) 195 C.L.R. 1, 25-26.

⁸² *Id.* at 23-24. The other major creditors had their debts secured through charges on the whole Patricks group, and so also did not stand to lose if the insolvent companies continued to trade. See, Graeme Orr, *Conspiracy on the Waterfront*, 11 AUSTL. J. LAB. L. 159, 160 (1998).

to monitor managerial action, and allowing a market for corporate control to sanction managers who fail to promote shareholder value. Each of these three areas has been the focus of regulatory reform in Australia in recent years. This recent reform agenda may go some way to explaining the rise in the shareholder value norm. Accordingly, we will examine regulation and impacts on practice in each of these areas in turn. First, however, we look briefly at laws relating to disclosure of corporate information, as such laws provide a vital prerequisite for other shareholder strategies.

A. DISCLOSURE

Because of their nature as an intangible income right, shares represent an unusually vulnerable form of property: prices are determined largely by expectations of future profits, which in themselves are susceptible to manipulation. Thus, a great deal of regulatory intervention is required to ensure that market values reflect, with some degree of accuracy, shares' income-generating potential.⁸³ Prior to the enactment of uniform companies legislation by the Australian States in 1961, directors enjoyed wide discretion as to what information they disclosed to the market beyond the annual balance sheet and profit and loss account. Up until the late 1960s, company affairs in Australia were still often inaccurately and misleadingly reported; and company failures due to fraud were not uncommon. Investors remained cautious and tended to stay with market leaders.⁸⁴ Stock exchange listing rules tended to impose greater disclosure obligations than existing companies' legislation. Unsurprisingly, then, "corporate governance" reform has increasingly focused on an array of regulation intended to bolster investor confidence and so facilitate a liquid securities market, focusing on issues of disclosure,⁸⁵ and

⁸³ Paddy Ireland, *Property, Private Government and the Myth of Deregulation*, in *COMMERCIAL LAW AND COMMERCIAL PRACTICE* 85, 99-101 (2003).

⁸⁴ G DE Q WALKER, *AUSTRALIAN MONOPOLY LAW* 16 (1967). FLEMING ET AL., *supra* note 31, at 149-50, make a similar point about the difficulty of non-market leaders in raising equity finance for much of the twentieth century owing to low investor confidence.

⁸⁵ See especially, the rules relating to 'continuous disclosure.' Australian Stock Exchange, Ltd., Listing Rule 3.1 (2004), *available at* <http://www.asx.com.au/supervision/rules/listing/chapters.htm>; Corporations Act, 2001, c. 7, § 1001A.

the role of “gate keepers” (those reputational intermediaries, such as auditors and securities analysts, who provide information verification services to those participating in the share market).⁸⁶

B. MANAGERIAL REMUNERATION

Empirical data indicates dramatic changes in the composition of the remuneration packages of CEOs, with stock options and share plans becoming an increasingly common feature of executive remuneration in Australian businesses. This has made the amount and growth of executive remuneration a matter of controversy in Australia as it is elsewhere. Surveys of Australia’s largest corporations show that fixed pay as a percentage of the average CEO remuneration package declined from 90 to 43 percent between 1987 and 2002, whereas short-term incentive payments increase to 23 percent and long-term incentive payments to 34 percent.⁸⁷

Long-term incentive payments are linked to market and/or accounting data, and short-term incentive payments often to qualitative measures. Short-term incentives (such as the annual bonus) are usually paid as cash; long-term incentives are usually the “option” to purchase shares in the future (typically several years hence) at the price equal to the market price of the shares at the time the option is granted or at a price indexed to the market return or industry return (in effect a performance hurdle). If the share price at the vesting date is greater than the exercise price (that is, the market price of, say, three years earlier, or the indexed price) then the executive stands to gain. If the share price at vesting is below the exercise price, the executive stands to make nothing, but he or she also loses nothing.

⁸⁶ On recent audit and financial reporting reforms see the Corporate Law Economic Reform Program (Audit Reform and Corporate Disclosure) Act, 2004, which is based to some degree on the recommendations contained in Ian Ramsay, Independence of Australian Company Auditors: Review of Current Australian Requirements and Proposals for Reform (2001) (Report to the Minister for Financial Services and Regulation), available at <http://www.treasury.gov.au> (follow “Business Law & Regulation” hyperlink; then follow “Independence of Australian Company Auditors Report (as printed March 2002)” hyperlink).

⁸⁷ Graham O’Neill & Mark Iob, *Determinants of Executive Remuneration in Australian Organisations: An Exploratory Study*, 37 ASIA PAC. J. OF HUM. RESOURCES 65, 69-71 (1999); G.P. Stapledon, *The Pay For Performance Dilemma*, 13 GRIF-FITH L. REV. 57, 64 (2004).

Thus, whereas short-term bonuses emphasize increases in accounting profit, share option rewards are designed to encourage managerial decisions that result in maximizing shareholder returns via share price appreciation.⁸⁸

This has given rise to concerns that incentives put in place by options plans may lead to accounting and auditing fraud or to the opportunistic manipulation of timing of earnings forecasts and information disclosure so as to maximize performance-based remuneration, rather than to an alignment of shareholder/management interests and enhanced company performance.⁸⁹ Payments to executives and directors of large corporations have risen significantly faster than average earnings over the past fifteen years. By 2003, the average annual total remuneration for the CEOs of Australia's top one hundred companies was A\$3.16 million, the median A\$2.33 million.⁹⁰ Subsequent disquiet over the rising level of executive remuneration has tended to focus not on the logic of a performance-based pay approach, nor on high rewards to managers *per se*, but on *undeserved* high rewards to managers who appear to fail at delivering increases in shareholder value.⁹¹ Thus, the corporate governance response has been focused on proceduralization of the remuneration-setting mechanisms — the use of non-executive directors on remuneration committees, disclosure, adequate audit to ensure accounting-based performance measures are not subject to manipulation, and so on — rather than any retreat from the general principle of performance-based

⁸⁸ See generally, Keryn Chalmers et al., *The Determinants of CEO Compensation: Rent Extraction or Labour Demand?* (2004) (unpublished paper presented at the Corporate Governance Conference, Centre for Corporate Law and Securities Regulation, University of Melbourne, 2004, on file with the author), available at http://ssrn.com/sol3/abstract_id=460040.

⁸⁹ Lucian Arye Bebchuk & Jesse M. Fried, *Executive Compensation as an Agency Problem*, 17 J. ECON. PERSP. 71, 89 (2003); Charles M. Yablon & Jennifer Hill, *Timing Corporate Disclosures to Maximize Performance-Based Remuneration: A Case of Misaligned Incentives?*, 35 WAKE FOREST L. REV. 83, 87 (2000).

⁹⁰ AUSTL. COUNCIL OF SUPERANNUATION INVESTORS, CEO PAY IN THE TOP 100 COMPANIES: 2003 2 (2004), available at http://www.acsi.org.au/dsp_research.cfm.

⁹¹ See DEP'T OF TRADE AND INDUS., LONDON, "REWARDS FOR FAILURE": DIRECTORS' REMUNERATION — CONTRACTS, PERFORMANCE AND SEVERANCE (2003); Press Release, Austl. Council of Superannuation Investors, Time for an Informed Debate on Termination Payments for Executives (March 17, 2005), available at <http://www.dti.gov.uk/cld/4864rewards.pdf>.

pay.⁹² Most contemporary codes of corporate governance now suggest that the level and form of remuneration be approved by independent directors acting in the interests of shareholders. This points to the desirability both of independent directors and the establishment of independent remuneration committees at board level, which we explore in the next subsection.

A further regulatory response has been the requirement since 1998 that listed companies in Australia include in their annual reports a “Remuneration Report” detailing the remuneration of all directors, the top five remunerated executives, and the board’s policy for determining remuneration.⁹³ Since July 2004, more detailed disclosure with regard to share options and executives within corporate groups has been required, and shareholders of listed companies must now collectively express their opinion on the remuneration paid to directors and senior managers and on the board’s policy on remuneration through a non-binding resolution to adopt the remuneration report.⁹⁴

C. INDEPENDENT DIRECTORS

The notion that boards of stock-exchange-listed companies should comprise a majority of independent directors and be chaired by an independent director has become a dominant theme in recent corporate governance recommendations.⁹⁵ The

⁹² Allan Greenspan, Chairman, Fed. Reserve Bd., ‘Corporate Governance’ Lecture at the Stern School of Business, New York University (March 26, 2002), available at <http://www.federalreserve.gov/boarddocs/speeches/2002> (stating that whereas the wrong kind of stock options can have “perverse effects” on managers, the right kind can “in principle. . . be highly effective in aligning corporate officers’ incentives with those of shareholders”); Ian Ramsay et al., *Corporate Governance: The Perspective of Australian Institutional Shareholders*, 18 CO. & SEC. L. J. 110, 134 (2000) (finding that a survey of institutional investors also suggests their prime concern is not with the level of executive remuneration, but with the performance hurdles that accompany contingent pay.).

⁹³ Corporations Act, 2001, c. 2M, § 300A.

⁹⁴ Shareholder approval is required for an agreement to pay an executive or director a retirement benefit greater than his or her final average salary multiplied by the number of years of service (with an upper limit of 7 years). Corporate Law Economic Reform Program Act, 2004, § 9 sched. 5. This applies to any retirement benefit contracts entered into on or after 1 July 2004. *Id.*

⁹⁵ See, e.g., A.L.I., PRINCIPLES OF CORPORATE GOVERNANCE: ANALYSIS AND RECOMMENDATIONS (1992); ASX Corporate Governance Council, Principles of Good Corporate Governance and Best Practice Recommendations (2003), available at <http://www.asx.com.au/about/pdf/ASXRecommendations.pdf>; BOSCH

board, no longer involved in the day-to-day management of the company, is now seen as choosing and monitoring the performance of the CEO who, along with other senior executives, actually runs the company. This monitoring and review role can best be fulfilled, it is argued, if carried out by a board independent of the executives over whom they exercise this supervisory role.⁹⁶ Theory suggests that independent directors can play an important role in situations involving conflicts of interest between management and shareholders, and some U.S. empirical studies (for example, examining independent directors and takeovers) find support for this theory.⁹⁷

The term “independent directors” generally refers to directors who are not members of management, with no substantial shareholdings in the company, no recent (if any) employment by the company, and no other significant contractual relationship with the company. An emerging focus on audit and accounting practices, as well as the requirement that companies have independent audit committees, requires companies to increase the number of independent directors.

A recent study of 494 Australian listed public companies indicates company boards have, on average, seven directors. 70 percent of directors are non-executive directors and 30 percent executive directors (the study did not examine the independence of directors). For the largest fifty companies, 76 percent of the directors are non-executive directors.⁹⁸ A study of the independence of directors in the top one hundred Australian companies

COMMITTEE, CORPORATE PRACTICES AND CONDUCT 11-15 (3rd ed, 1995); THE COMM. ON THE FIN. ASPECTS OF CORP. GOVERNANCE, REPORT OF THE COMMISSION ON THE FINANCIAL ASPECTS OF CORPORATE GOVERNANCE (1992), available at <http://tru.worldbank.org/Documents/PapersLinks/1253.pdf>; Helen Bird, *The Rise and Fall of the Independent Director*, 5 AUSTRALIAN JOURNAL OF CORPORATE LAW 235 (1995).

⁹⁶ Eugene F. Fama & Michael C. Jensen, *Separation of Ownership and Control*, 26 JOURNAL OF LAW & ECONOMY 301, 308 (1983).

⁹⁷ See G.P. Stapledon & Jeffery Lawrence, *Board Composition, Structure and Independence in Australia's Largest Listed Companies*, 21 MELBOURNE UNIVERSITY LAW REVIEW 150, 155-56 (1997) (literature survey).

⁹⁸ KORN/FERRY INT'L, 2003 BOARDS OF DIRECTORS STUDY IN AUSTRALIA AND NEW ZEALAND 11 (2003). Also, 90 percent of the companies studied have an audit committee (100 percent for the largest 50 companies) and 64 percent have a remuneration committee (90 percent for the largest 50 companies). *Id.* at 16.

found nearly 51 percent of all board seats are held by independent directors.⁹⁹ In Australia, for most of the twentieth century, there was greater use of executive directors, but most large listed companies had a majority of non-executive directors by century's end.¹⁰⁰ Another noteworthy change is that, in the postwar period, the board chairman of many major companies was often the CEO or previously had held executive positions with the company, but by 2000 most boards of major companies were chaired by non-executive directors.¹⁰¹

D. TAKEOVERS

We have noted that, following Henry Manne's pioneering work in the 1960s, agency theorists have stressed managers' strong incentive to maximize profits for shareholders where the failure to do so would result in the loss of their jobs through a hostile takeover. For a market for corporate control to operate effectively, however, it must allow hostile bids to be made and succeed. Shareholders must be informed of any bid to acquire the company. Before the mid-1950s, takeovers in Australia were few, and, under the law as it was then, directors were allowed wide discretion as to what information they made available to shareholders regarding takeover offers. The convention of the day was that bidders would not make a direct approach to shareholders without the consent of the target board. This meant that managers could, in practice, easily reject bids outright or defeat or modify the bid by insisting on terms to protect the interests of management or employees.¹⁰²

Despite the lack of priority accorded to shareholder interests in this context, mergers and acquisitions were frequent occurrences throughout the 1950s and 1960s, although these were mostly friendly affairs where shareholders were invited to rubber-stamp a decision previously negotiated between the two

⁹⁹ INST. ANALYSIS, AUSTL. COUNCIL OF SUPERANNUATION INVESTORS, CEO PAY IN THE TOP 100 COMPANIES: 2003 3 (2004). According to this study the average number of directors per board in 2003 was 8.3, with board sizes ranging from 4 to 15. *Id.* at 2.

¹⁰⁰ See FLEMING ET AL., *supra* note 31, at 225.

¹⁰¹ *Id.*

¹⁰² David T. Merrett & Keith A. Houghton, *Takeovers and Corporate Governance: Whose Interests Do Directors Serve?*, 35 ABACUS 223, 225 (1999).

boards of directors. Acquisition of smaller, often unlisted, companies by larger listed ones was commonplace. Hostile mergers were still few and far between before the 1970s.¹⁰³

It was not until the Eggleston Committee's "takeover code" was incorporated in the Uniform Companies Act in 1970 that companies were compelled to inform their shareholders of the identity of a bidder, tell them the terms of the bid, and give them reasonable time in which to make a decision.¹⁰⁴ The legal position has been altered more recently by adjudications of the Takeovers Panel, which, while not redefining the constituency of directors' fiduciary duties for the purposes of takeovers, redefines the directors' role during takeover bids. In short, the board's authority and scope for the exercise of normal managerial power are reduced in the face of a takeover bid by requiring shareholder consent for management conduct wherever such conduct breaches bid conditions imposed by the bidder¹⁰⁵ or where the breach of conditions has the effect of substantially frustrating the bidder.¹⁰⁶ The imposition of such conditions is substantially in the control of the bidder, with some limitations,¹⁰⁷ and the litany of conditions attached to bids has increased in recent years. This suggests the bidder now has considerable scope in setting the boundaries for legitimate managerial action and thereby reduces the scope for defensive tactics by incumbent management. This represents a potentially significant shift from the parameters of the fiduciary duties of directors.¹⁰⁸ The latter,

¹⁰³ David Merrett, *Corporate Governance, Incentives and the Internationalization of Australian Business* 10 (Apr. 19-21, 2002) (Paper Presented at the Business History Conference, Hagley Museum and Library, Wilmington, DE), available at http://www.ecom.unimelb.edu.au/acib/workpap/Corporate_governance.pdf.

¹⁰⁴ Chris Maxwell, *The New Takeover Code and the NCSC: Policy Objectives and Legislative Strategies for Business Regulation*, 5 U.N.S.W. L.J. 93, 97 (1982).

¹⁰⁵ *In re Pinnacle VRB Ltd.* (No. 8) (2001) 39 A.C.S.R. 55, 58-59.

¹⁰⁶ *In re Bigshop.com.au Ltd.* (No. 2) (2001) 39 A.C.S.R. 525.

¹⁰⁷ The fulfilment or otherwise of conditions has to be capable of objective determination and not depend on the judgment of the bidder or be in the bidder's control. Further, shareholder consent is not necessary where the bidder's conditions are 'so far reaching and constraining' as to be commercially unreasonable. See *In re Pinnacle VRB Ltd.* (No. 8) 39 A.C.S.R. at 58.

¹⁰⁸ Emma Armson, *The Frustrating Action Policy: Shifting Power in the Takeover Context*, 21 Co. & Sec. L. J. 487, 506 (2003).

as we noted in Part III, above, focused on purposes or motivation, while the new policy focuses on effects: that is, is the bid frustrated? Thus, while not modifying the directors' fiduciary duties *per se*, the practical effect of the new position is that, for the duration of the bid, shareholders are placed in the "driver's seat," mandating greater managerial passivity in the face of takeovers and prioritizing short-term shareholder wealth maximization for current shareholders over the interests of other stakeholders.

The actual effect of reforms of takeover regulation over the past two decades is difficult to judge. A key change in the operation of the market for corporate control in Australia may have been the willingness of financial institutions to provide funds to the "raider" and taking the assets of the target as collateral, a shift that was in turn influenced by deregulation of the financial system during the 1980s rather than changes to takeover laws.¹⁰⁹ Furthermore, there are several factors that may work to limit the emergence of an effective market for corporate control in Australia. Stapledon estimated that in 1995, on the basis of their concentrated ownership patterns, 40 to 50 percent of listed companies were immune to hostile takeover.¹¹⁰ Also, the Foreign Investment Review Board may operate to suppress successful hostile bids from foreign entities. One survey, drawing on media reports of takeovers, indicated only 9 percent of merger and acquisition activity from 1992–2001 comprised successful hostile bids, compared with just over 20 percent in the U.S. and U.K.¹¹¹ However, a difficulty remains in identifying successful "hostile" bids, as a hostile target board can recommend acceptance late in the bid period once it becomes obvious that effective control has passed or will pass under the takeover offer. A survey of 136 takeovers for the period 1990–98 suggests around 20 percent fall into this category of "reject, then accept" and so can therefore

¹⁰⁹ See Merrett, *supra* note 103, at 10.

¹¹⁰ G.P. Stapledon, *The Structure of Share Ownership and Control: The Potential for Institutional Investor Activism*, 18 U.N.S.W.L.J. 250, 270 (1995).

¹¹¹ Alan Dignam & Michael Galanis, *Australia Inside/Out: The Corporate Governance System of the Australian Market*, 28 MELBOURNE U. L. REV. 623, 641 (2004).

arguably be classed as hostile; 75 percent of bids in this category were successful.¹¹²

E. CORPORATE GOVERNANCE REFORM AND THE ROLE OF LAW

We have suggested that the corporate governance reform strategies just outlined are more closely linked to the pursuit of shareholder value than the traditional corporate law strategies based on shareholders' participative rights and the fiduciary duties owed them. There has been a change in the composition of boards of directors to have more non-executive directors and more independent directors. As we saw, these directors are supposed to better protect the interests of shareholders than executive directors. Takeover reforms have strengthened the position of target company shareholders. Perhaps the most significant change has occurred in managerial remuneration, where performance pay linking remuneration to share options has fundamentally transformed executive remuneration over the past decade or so. This would appear to provide a strong incentive for management to focus on share price maximization.

Yet the impact of each of these reforms on corporate performance, and hence on the delivery of shareholder value, remains uncertain. Despite the emphasis on independent directors, U.S. studies have found that boards with a high percentage of independent directors may not improve corporate performance and that, in fact, such boards may have a negative impact.¹¹³ Nor do Australian studies show a clear link between levels of executive pay and improved corporate performance.¹¹⁴ Finally, as a disciplinary measure, takeovers will only tend to discipline certain types of major managerial inefficiency¹¹⁵ and, compared with

¹¹² Jonathan Farrar, *Acquiring Control of Australian Companies: Takeover or Scheme of Arrangement?* (2000) (unpublished Master of Laws Thesis, University of Melbourne) (on file with author).

¹¹³ Sanjat Bhagat & Bernard Black, *The Uncertain Relationship Between Board Composition and Firm Performance*, 54 *BUS. LAW.* 921, 949 (1999).

¹¹⁴ See Chalmers et al., *supra* note 88.

¹¹⁵ John C. Coffee, *Regulating the Market for Corporate Control: A Critical Assessment of the Tender Offer's Role in Corporate Governance*, 84 *COLUM. L. REV.* 1145, 1203-04 (1984).

shareholders' participative rights and duties owed them, only operate in relation to public companies.

We could suggest, following Davies, that the fact that these strategies have yet to prove themselves may explain the tentativeness of the law towards them. Although we have identified these strategies as most supportive of shareholder value, corporate law has not formulated strong rules that promote them, in contrast to the strongly formulated rules around participative rights and fiduciary duties. The push for independent directors, for example, has not been mandated by law but has come through "self-regulation" or "soft law" provisions such as codes of governance.¹¹⁶ Nor has the law insisted on particular types of executive remuneration in order to enhance the delivery of shareholder value. In fact, a main role of the law as regards remuneration strategies has been to *reassert* shareholders' participative rights, by compulsorily involving shareholders in the decision-making process over managerial pay. Similarly, the rulings by the Takeovers Panel, rather than explicitly promoting takeovers *per se*, have also operated to reduce management discretion in favor of shareholders. That is, rather than deal substantively with these issues, the law insists on a procedure whereby shareholders have a good chance of protecting themselves.¹¹⁷ This suggests that a principal role of the law is to subject the actions of management to procedural constraints in circumstances where governance structures, or the pursuit of shareholder value (for example, linking management remuneration to share prices), can create incentives on the part of management to manipulate financial information or act opportunistically.

V. CORPORATE OWNERSHIP AND CONTROL IN AUSTRALIA

In the previous two sections we have examined some of the strategies whereby shareholders might structure corporate decision-making and the links between such strategies and the pursuit of shareholder value. We also noted in our introduction that

¹¹⁶ Generally, companies formally comply with such codes simply by explaining why they have not adopted the recommendations.

¹¹⁷ See DAVIES, *supra* note 14, at 211.

certain strategies might be more successful than others, given the structure of the share market. This is seen most clearly in the case of shareholders' participative rights. The Corporations Act 2001 gives shareholders quite strong rights with regard to convening general meetings,¹¹⁸ removing directors by ordinary resolution,¹¹⁹ and altering a company's constitution by special resolution.¹²⁰ Yet, we have also noted that such rights may be of little practical use in terms of enhancing shareholder power. This is often referred to as a collective action problem. Where shareholdings are widely dispersed, with each shareholder having only very small holdings, shareholders will find it both practically difficult and lacking in incentive to expend resources in formulating a coalition of shareholders able to effect change at a general meeting. Instead, shareholders are more liable to simply sell their shares if dissatisfied with managerial performance, or rely on passive monitoring strategies, such as linking executive remuneration to share price appreciation.

However, commentators have pointed to the reconcentration of shareholdings in the hands of institutional shareholders—superannuation funds, unit trusts, insurance companies, and a range of other managed investment funds—as indicating this collective action problem may be on the wane.¹²¹ A coalition of relatively few institutional shareholders or of fund managers acting on their behalf may be able to exercise effective control in any given company. Furthermore, the size of their holdings in any one company can make them illiquid, as the sale of large holdings tends to depress the price of the very shares a fund might wish to sell, creating an incentive to retain holdings. Indexed funds, by definition, are limited in their capacity to sell shareholdings, as they are required to keep their portfolios weighted in accordance with the market.¹²² Coffee refers to the trade off

¹¹⁸ Corporations Act, 2001, c. 2G, § 249D.

¹¹⁹ *Id.* at c. 2D, § 203D.

¹²⁰ *Id.* at c. 2B, § 136.

¹²¹ *See, e.g.*, GEOFF STAPLEDON, INSTITUTIONAL INVESTORS AND CORPORATE GOVERNANCE (1996); MICHAEL USEEM, INVESTOR CAPITALISM (1996); Paul Davies, *Institutional Investors in the United Kingdom*, in CONTEMPORARY ISSUES IN CORPORATE GOVERNANCE (D.D. Prentice & P.R.J. Holland eds., 1993).

¹²² John W. Cioffi, *Governing Globalization? The State, Law, and Structural Change in Corporate Governance*, 27 J.L. SOC'Y 572, 584 (2000).

between liquidity and control, whereby the reduced liquidity of large holdings raises the incentive for governance activism as the preferred strategy for improving companies' financial performance.¹²³ Thus, the rise of institutional shareholdings suggests the emergence of shareholdings with both an enhanced capacity and an increased incentive to intervene in the management of listed companies.

Accordingly, in seeking to pinpoint possible institutional and regulatory supports for the shareholder value model of the corporation, we need to shift our inquiry from the traditional doctrines of company law, which focus on the regulatory balance-of-power among management, the board and shareholders, and consider the changing market balance-of-power between shareholders and management. In the Australian context, we need to consider the extent to which shareholdings are dispersed or concentrated. If concentrated, we need to identify who the significant blockholders are, as different types of blockholders may have different objectives. For example, a corporate controlling shareholder may be interested in extracting financial benefits through, say, related party transactions, at the expense of minority shareholders. An individual or family controlling shareholder might also value certain private benefits of control, such as social standing. An institutional investor, by contrast, may be primarily interested in purely financial returns to its beneficiaries, and so value capital growth and dividend payments.

We would expect the growing importance of pension funds as a repository of household wealth in Australia to drive a reconcentration of shareholdings in the hands of institutional investors. In the 1990s, Australia had a tax-funded, flat-rate, pay-as-you-go system of pension provision (which entailed no significant asset accumulation) supplemented by mandatory private retirement savings in the form of the superannuation guarantee charge (SGC). Prior to this, superannuation funds tended to be the preserve of high-income professionals and government employees. The new SGC required employers to make contributions on behalf of their employees into fully funded individual accounts maintained by either private or industry-based funds, which

¹²³ John C. Coffee, *Liquidity Versus Control: The Institutional Investor as Corporate Monitor*, 91 COLUM. L. REV. 1277 *passim* (1991).

faced few investment restrictions. Voluntary private retirement provisions also make use of similar savings vehicles such as mutual funds and unit trusts. Between 1987 and 1994 the proportion of all employers involved in providing superannuation rose from 42 to 92 percent.¹²⁴ By January 2005, Australian superannuation funds held A\$649 billion.¹²⁵ Further, the privatization of government-owned assets and the demutualization of financial institutions have also led to a greater direct ownership of shares by households.¹²⁶ Superannuation now forms 22 percent of the wealth of the average family (a rise from 14 percent in 1986), and direct ownership of shares a further 8 percent (a rise from 3 percent in 1986).¹²⁷

Thus, we have seen an important shift in the way households save, particularly a growing reliance on returns from investments in publicly traded shares. Increasing numbers of households thereby have a stake in maintaining high returns on corporate shares, and institutional investors in delivering shareholder value. Yet, in the Australian context, we need to ask: Do these institutions actively monitor companies in which they hold shares? If so, how? And what for?

The first point to be made is that patterns of share ownership in Australia differ from those in the United States and U.K. in important ways. First, according to Brian Cheffins, publicly listed companies play a less important role in the Australian

¹²⁴ ASSOCIATION OF SUPERANNUATION FUNDS OF AUSTRALIA, SUPERANNUATION STATISTICS – JANUARY 2005 (2005).

¹²⁵ *Id.*

¹²⁶ MARIANNE GIZYCKI & PHILIP LOWE, THE AUSTRALIAN FINANCIAL SYSTEM IN THE 1990s' 188 (2000), available at <http://www.rba.gov.au/PublicationsAndResearch/Conferences/2000/GizyckiLowe.pdf>.

¹²⁷ Simon Kelly, Trends in Australian Wealth: New Estimates for the 1990s, 30th Annual Conference of Economists 11-12 (Sept. 24, 2001) (unpublished paper, on file with author). These averages hide an uneven distribution across the population. Whereas the wealthiest households have considerable money in superannuation, it represents only a small proportion of their wealth portfolio, which is spread across interest-bearing deposits, shares, business assets and the family home. See *id.* Low asset households, by contrast, do not have much in superannuation but it is often the only wealth they own. *Id.* at 12. Thus *all* households, including the poorest ones, have become more dependent on the stock market in recent decades.

economy than in the United States or Britain.¹²⁸ Cheffins draws upon data to show that while the vast majority of large companies in the United States are listed on the stock market, and as of 1994, 63 percent of the U.K.'s largest five hundred non-financial companies were publicly quoted, in contrast, again as of 1994, only 35 percent of Australia's top five hundred companies had shares traded on a stock exchange.¹²⁹ Hence, although Australia has more publicly traded companies per capita than the United States or the U.K., companies that are privately held (or government-owned) are of comparatively greater economic significance.¹³⁰

In addition, according to Cheffins, Australian companies traded on the stock market, possess an ownership structure more concentrated than that of publicly traded U.S. and U.K. corporations.¹³¹ Cheffins refers to a study published in 1999, showing that in Australia eleven out of the twenty largest publicly quoted companies could be classified as "widely-held" in the sense that they did not have a shareholder that owned 10 percent or more of the equity.¹³² In the United States and in Britain the figures were, respectively, sixteen out of twenty and eighteen out of twenty according to Cheffins.¹³³ A similar pattern is evident when smaller companies are taken into account.¹³⁴ As of 1996, approximately 45 percent of the companies that make up Australia's ASX All Ordinaries Index had a shareholder other than an institutional investor that owned 20 percent or more of the shares.¹³⁵ In contrast, just over 20 percent of the companies listed on the London Stock Exchange were in the same position.¹³⁶

¹²⁸ Brian Cheffins, *Comparative Corporate Governance and the Australian Experience*, in *KEY DEVELOPMENTS IN CORPORATE LAW AND TRUSTS LAW: ESSAYS IN HONOUR OF PROFESSOR HAROLD FORD* 13, 18 (Ian Ramsay, ed., 2002).

¹²⁹ *Id.*; Geof Stapledon, *Australian Sharemarket Ownership*, in *SECURITIES REGULATION IN AUSTRALIA AND NEW ZEALAND* 242, 243 (Gordon Walker et al. eds., 1998).

¹³⁰ Cheffins, *supra* note 128, at 18.

¹³¹ *Id.* at 19.

¹³² *Id.*

¹³³ *Id.*

¹³⁴ *Id.*

¹³⁵ *Id.*

¹³⁶ *Id.*

By 1997, Australian institutional investors owned around 35 percent of the Australian listed share market, and overseas institutional investors controlled a further 10 to 15 percent, but these institutional ownership patterns are smaller than those prevailing in the United States and U.K.¹³⁷ Thus, while there has been a growth in institutional investors, and a decline in individual shareholding as a percentage of the market, non-institutional block holders still play an important role in the structure of share ownership.

What institutional activism there is in Australia generally goes on behind closed doors, in the form of regular one-to-one meetings with senior management (usually CEO and finance director) of portfolio companies.¹³⁸ Company-initiated meetings with institutional shareholders also occur as regards restructurings and large transactions, and some shareholder-initiated meetings do occur where there is dissatisfaction with aspects of the management of a portfolio company. Institutions are usually given the right to exercise voting rights attached to shares in their portfolio, but there is no legal obligation to exercise the right, and institutions appear divided between those who will generally vote on all matters, while consciously abstaining on some, and many who will routinely abstain, unless the issue is one they strongly object to.¹³⁹ Voting *against* management is particularly rare, and in the case of disagreements with management, institutions' preference is often for behind-the-scenes discussion that attempts to change management stances.¹⁴⁰ Such hands-off or discrete approaches may also be a consequence of conflicts of interest that can arise where large institutional investors also provide financial services to the companies in which they invest, and hence be doing lucrative business with the current management.

Furthermore, as we have seen, a major structural impediment to formal intervention is that although institutional investors may have substantial stakes in many listed companies, in many cases these stakes are counterbalanced by even larger *non-*

¹³⁷ See Stapledon, *supra* note 129, at 244-245.

¹³⁸ GEOFF STAPLEDON, INSTITUTIONAL SHAREHOLDERS AND CORPORATE GOVERNANCE 184-85 (1996).

¹³⁹ Ramsay et al., *supra* note 92, at 120-21

¹⁴⁰ *Id.*, at 121-22.

institutional substantial shareholders (mainly shareholdings of founding families, entrepreneurs or overseas companies), making the chances of a successful institutional intervention very slight indeed.¹⁴¹ Coordinated interventions by two or more institutions also appear rare.¹⁴²

We would expect, then, patterns of institutional activism to vary, depending on the size of the holding, the size of other non-institutional holdings in the company, the size of the company itself, the resources devoted to monitoring, the nature of the institution's portfolio, and whether the institution is managing index funds.¹⁴³ Importantly, information asymmetries between management and institutional investors may contribute to institutional reluctance to intervene. Many institutional investors wish to assess non-financial aspects of management, such as business strategy and innovation.¹⁴⁴ But this move away from bottom-line data can shift the balance of initiative in management's favor.¹⁴⁵ The fact that managers may be spending greater time and resources "managing" their relationship with institutional investors does not necessarily indicate that institutional investors are unilaterally imposing constraints on management, but could instead suggest management are actively "manag[ing] investor expectations to accord with their favored strategies and practices, including labor management."¹⁴⁶

This leads, importantly for our discussion, to the question of *what* institutional investors monitor. Are their interventions directed primarily at shareholder value, or do they have a wider agenda that may also be favorable to labor's interests? Even apart from the difficulties of selling where holdings are large, and the restrictions imposed by indexing, there are indications that

¹⁴¹ STAPLEDON, *supra* note 138, at 186-87.

¹⁴² Ramsay et al., *supra* note 92, at 125-26.

¹⁴³ *See id. passim.*

¹⁴⁴ Mark Lawson, *Business is About More than Just the Bottom Line*, AUSTL. FIN. REV., Dec. 23, 1997, at 8.

¹⁴⁵ As one Australian funds manager put it, "[y]ou hope the board knows more about the company than you do; you'd be disappointed if they did not": Ramsay et al., *supra* note 92, at 134.

¹⁴⁶ Gospel & Pendleton, *supra* note 11, at 573-74.

Australian institutions favor longer-term or “relational” investing.¹⁴⁷ However, a key legal constraint on institutions’ interventions is the duty to act in the best *financial* interests of fund beneficiaries.¹⁴⁸ Room may remain for institutional investors to link these financial interests, articulated in terms of “long-term economic well-being of the firm,” to the promotion of progressive labor management practices.¹⁴⁹ Yet, while the precise nature of institutional intervention in any given company will vary on a case-by-case basis, we can suggest that institutional “activism” at the level of the securities market as a whole takes a particular form. That is, peak representative bodies of institutional investors *have* increasingly pressed for corporate governance “reform,” especially as regards the use of independent directors and managerial remuneration.¹⁵⁰ Again, this macro-level activism may or may not advance labor’s interests: most of these areas of reform are, as we noted in the previous section, promoted as a way of delivering shareholder value.

VI. THE ROLE OF LABOR LAW

Our argument so far has suggested an association of factors, in corporate law and in corporate governance regulation and strategy, which has tended to support a shareholder-centered focus of corporate governance. One major potential consequence of this, we have noted, has been increased opportunities for business strategies that shift risk and insecurity onto workers, resulting in a decline in the terms and conditions of employment. It remains the case, however, that no matter how far management may be committed to the pursuit of shareholder value at the expense of labor, such a strategy will necessarily be constrained by labor law. That is, the capacity of corporate managers to extract

¹⁴⁷ Ramsay et al., *supra* note 92, at 115.

¹⁴⁸ *Cowan v. Scargill*, (1985) 1 Ch. 270 (U.K.); Superannuation Industry (Supervision) Act, 1993, § 62(1) (Austl.).

¹⁴⁹ See the discussion of institutional shareholders’ role in various trade union interventions in corporate governance in KIRSTEN ANDERSON & IAN RAMSAY, *FROM THE PICKET LINE TO THE BOARDROOM: UNION SHAREHOLDER ACTIVISM IN AUSTRALIA* 76-79 (2005).

¹⁵⁰ See, e.g., INVESTMENT AND FINANCIAL SERVICES ASSOCIATION (IFSA), *BLUE BOOK, CORPORATE GOVERNANCE: A GUIDE FOR FUND MANAGERS AND CORPORATIONS* (5th ed. 2004). The IFSA is an organization that represents many Australian institutional investors.

shareholder gains from the direct or incidental lowering of overall labor costs will be limited by the extent to which labor law determines the relative flexibility or rigidity of wage costs; the ability to pursue flexibility through short-term, temporary, or otherwise “cheap” engagements of labor; the capacity of management to direct unilaterally workers to different tasks; the capacity to fragment or sub-divide production through changes to the work process or through outsourcing; and ultimately, the ease with which the size of the workforce can be altered through redundancy.

Arguably, Australian labor regulation has historically provided for a more comprehensive and generalized set of labor standards than comparable systems of labor market regulation. This suggests that, at one level, the employment contract, underpinned by collective agreements and legislated standards, gives employees a *prima facie* degree of certainty as to their rights and entitlements which shareholders do not have. It is this view, as we saw in Part II, above, that underpins the nexus-of-contracts, or agency, theories of the corporation. That is, employees are able to protect themselves against managerial opportunism through appropriate contractual safeguards, underpinned by legislative standards, in much the same way as other stakeholders such as creditors or suppliers. This view reinforces the essentially *sui generis* position of shareholders as uniquely in need of protection by means of governance mechanisms (that allow them, for example, to exert control over the composition of the board) and doctrines that allow *ex post* scrutiny of management decisions (such as fiduciary duties).

Superficially, at least, if we regard the employment relationship as essentially a wages-for-work bargain, employment contracts *do* appear to offer certainty and predictability as regards entitlements. An employee is given a job or set of tasks to undertake, often within prescribed time periods, and in return is paid a wage stipulated in the contract or relevant industrial instrument. The allocation of responsibility for certain risks, such as workplace injury or absence due to sickness, is also often clearly delineated. Yet, from a labor law perspective, to conceive of employment contracts as basically the same as other commercial contracts is a fundamental misunderstanding. They are not “spot” contracts whereby particular tasks are performed for a

particular reward. Employers are usually uncertain at the time of the formation of an open-ended employment contract about the precise nature, quantity, intensity, and timing of particular types of work required by the business. As a result, employment contracts are largely incomplete or open-ended in their specifications of the work to be performed, with management retaining considerable discretion to direct labor as it sees fit: employment contracts are incomplete by design.¹⁵¹ Thus, the employment relationship goes beyond a simple wages-for-work bargain. Inherent in the employment relationship is a power of command by the employer or the idea of “managerial prerogative.” The common law sees this power of command as an implied term: the duty of the employee to obey all lawful and reasonable orders.¹⁵² Based on this authority, employers create governance structures comprising managerial discretion, hierarchies of decision making, internal organizational rules that allocate power and responsibility, and techniques to police and discipline behavior.¹⁵³

Not only are actual contours of the performance of the wages-for-work bargain thereby unclear, and open to opportunism, but the open-ended employment contract is also temporally uncertain. Workers’ long-term entitlement to wages depends on the relationship being kept on foot, but the bargain itself may be terminable at relatively short notice. Further, many workers, especially those working within internal labor markets

¹⁵¹ HUGH COLLINS, *EMPLOYMENT LAW* 10 (2003); SIMON DEAKIN & GILLIAN S. MORRIS, *LABOUR LAW* 238 (3rd ed. 2001).

¹⁵² This reflects the fact that many of the terms and incidents of the employment relationship in Anglo-Australian law grew not out of the private law of contract but from penal masters and servants’ legislation of the nineteenth century. See Simon Deakin, *The Contract of Employment: A Study in Legal Evolution* 7 (ESRC Ctr. for Bus. Research, Working Paper No. 203, 2001); See generally ROBERT J. STEINFELD, *COERCION, CONTRACT, AND FREE LABOR IN THE NINETEENTH CENTURY* (2001). A pioneer of economic theories of the firm, Ronald Coase, writing in the 1930s, used the employment relationship to indicate why firms are *not* contractual but represent hierarchies rather than markets. As Doug Henwood points out, Coase’s citing of Batt’s *The Law of Master and Servant* made the power relationship clearer than more contemporary talk of the “employment contract.” See Ronald H. Coase, *The Nature of the Firm*, 4 *ECONOMICA* 386 *passim* (1937); HENWOOD, *supra* note 38, at 298 n.4.

¹⁵³ COLLINS, *supra* note 151, at 10-11; Hugh Collins, *Market Power, Bureaucratic Power and the Contract of Employment*, 15 *INDUS. L.J.* 1, 1-4 (1986).

or clearly defined “career” occupations, often make “investments” in a job in expectation of long-term return. For example, workers are often paid less than their marginal productivity in the early stages of their career, and more in later stages. For employers, this represents a useful human resource strategy. By deferring remuneration, internal labor markets provide an incentive for employees to remain with the company. This system of job ladders encourages cooperation by rewarding dedicated, long-term employees with seniority benefits in the form of promotions, higher wages, and job security.¹⁵⁴ Employees, in turn, are usually only willing to accept low commencement wages and to make investments in company-specific training in return for this implicit promise of job security that gives them a return on their investment. Overall, then, workers’ ongoing entitlements and expectations are directly affected by the success or otherwise of strategic decisions made by management over time, and hence workers, like shareholders, have an interest, which, arguably, cannot adequately be protected by contract.¹⁵⁵

Thus, we could say that the effort and tasks demanded of workers, their job security, and the protection of any job-specific “investments” exhibit a distinct lack of certainty as management makes business decisions over the life of the employment relationship in response to the changing external environment of the company. It is clear that the terms of the relationship are not fully articulated or spelled out at the individual level at, and

¹⁵⁴ Marleen O’Connor, *Restructuring the Corporation’s Nexus of Contracts: Recognising a Fiduciary Duty to Protect Displaced Workers*, 69 N.C. L. REV. 1189, 1205-07 (1991); Katherine Van Wezel Stone, *Labour Markets, Employment Contracts, and Corporate Change*, in CORPORATE CONTROL AND ACCOUNTABILITY: CHANGING STRUCTURES AND THE DYNAMICS OF REGULATION 71, 71-73 (J. McCahery et al. eds., 1993).

¹⁵⁵ Not only is there a range of practical problems in drafting long-term contracts in the face of the many contingencies that affect a company’s future demand for labor, but workers will typically lack the bargaining power to extract enforceable promises of long-term job security. John Parkinson, *The Contractual Theory of the Company and the Protection of Non-Shareholders Interests*, in CORPORATE AND COMMERCIAL LAW: MODERN DEVELOPMENTS 137, 137-39 (D. Feldman & F. Meisel eds., 1996). Cf. Jonathan R. Macey & Geoffrey P. Miller, *Corporate Stakeholders: A Contractual Perspective*, 43 U. TORONTO L.J. 401, 402-03 (1993) (stating that both employers and employees benefit from their relationship).

from, the moment of its formation.¹⁵⁶ Many of the terms of the employment relationship are in fact specified and transformed only in the course of that relationship. A key question is to what extent that ongoing process of specification and transformation — including distribution of the corporate surplus — is subject to forms of collective regulation, or to what extent it represents the relatively unfettered working of managerial prerogative. What is important in this discussion of the nature of the employment relationship is that shareholders are clearly not the only corporate stakeholder whose contractual relations with the company are so incomplete as to require a supplemental governance structure or other regulatory safeguards which grant them a means of protecting their claims on the company across the life of their relationship with the company.

Much of labor law is, therefore, best understood as a response to the employment relationship being not a continually renegotiated contract between equal parties¹⁵⁷ but, rather, a relationship of authority and subordination between unequal parties.¹⁵⁸ Faced with a system of disciplinary power, employees are concerned that management exercises its authority and discretion fairly. Because contract law traditionally offered employees few grounds on which to challenge or limit employers' contractual power to command,¹⁵⁹ a range of institutional arrangements have arisen to monitor and control an employer's exercise of discretion. These include, on the one hand, mandatory, non-derogable standards, set through legislation and, in the Australian case, through the determinations of industrial tribunals. On the other hand, they also include support for governance structures, such

¹⁵⁶ Paul Davies & Mark Freedland, *Changing Perspectives upon the Employment Relationship in British Labour Law*, in *THE FUTURE OF LABOUR LAW*, *supra* note 1, at 132-33.

¹⁵⁷ See, e.g., Alchian & Demsetz, *supra* note 30.

¹⁵⁸ See *KAHN-FREUND'S LABOUR AND THE LAW* 18 (Paul Davies & Mark Freedland, eds., 3rd ed. 1983). This inequality may be market-based or bureaucratically-based. See Collins, *supra* note 153, at 1-2.

¹⁵⁹ Some limits on employer opportunism might now be found in equitable duties of good faith or "mutual trust and confidence" now emerging in Anglo-Australian law. See Joellen Riley, *Mutual Trust and Good Faith: Can Private Contract Law Guarantee Fair Dealing in the Workplace?*, 16 *AUSTL. J. LAB. L.* 28 *passim* (2003). One justification for the development of such duties has been that "it is no longer right to equate a contract of employment with commercial contracts." *Johnson v. Unisys Ltd.*, (2001) 1 A.C. 518, 532 (U.K.).

as the recognition and regulation of trade unions, support for collective bargaining and, in some European jurisdictions, mandatory consultation with worker representatives.

The key feature of Australian labor law for most of the twentieth century — compulsory arbitration — has worked to perform, albeit imperfectly, two functions: the imposition of protective standards and the support of collective governance structures.¹⁶⁰ Each has limited, to some extent, employer opportunism within the employment relationship and hence management's capacity to extract shareholder value at labor's expense, although we will suggest that this regulatory balance between management and labor is undergoing significant change.

The system of compulsory conciliation and arbitration consisted of independent, quasi-judicial tribunals that arbitrated or certified legally binding awards. Awards defined a range of minimum standards, most importantly wage rates, but also overtime rates, allowances, standard hours, leave entitlements, and a range of other matters. Awards were usually multi-employer in kind, and so the fixation of wages and conditions was overwhelmingly centralized and uniform across industries and occupations. In practice, the application of award standards did not depend on whether an employee was a trade union member.¹⁶¹ In this way, the system operated to extend advances in collective bargaining or award regulation to the majority of employees, regardless of the extent of union representation or power in individual enterprises. This meant reduced scope for companies to make cost savings through, for example, unilateral wage cuts.

Further, through deciding wage margins for skill, the award system mandated a wage structure whereby minimum wage rates were set for whole classes of employees doing particular work. In many instances, this classification system limited employers' abilities to redirect workers to tasks or to fragment and subdivide production tasks through, for example, mechanization aimed at

¹⁶⁰ See *generally* FOUNDATIONS OF ARBITRATION: THE ORIGINS AND EFFECTS OF STATE COMPULSORY ARBITRATION 1890-1914 (Stuart Macintyre & Richard Mitchell eds., 1989); BREEN CREIGHTON & ANDREW STEWART, LABOUR LAW (4th ed. 2005).

¹⁶¹ See *Metal Trades Employers Ass'n v. Amalgamated Eng'g Union* (1935) 54 C.L.R. 387, 387 (Austl.); *Burwood Cinema Ltd. v. Austl. Theatrical & Amusement Employers Ass'n* (1925) 35 C.L.R. 528, 543, 546 (Austl.).

de-skilling. The latter limitation came not through forbidding alternative classifications, but by making them uneconomic; that is, employers could divide craft work but, without obtaining a new classification, would still have to pay the award rates that pertained to the undivided, “skilled” work.¹⁶²

Finally, the arbitral tribunals tended to formalize hiring arrangements around full-time, open-ended contracts of employment, placing limits on the use of cheap, temporary, casual, or subcontracted labor.¹⁶³ Apart from the requirement of a week’s notice, however, prior to the 1980s there were rarely other restrictions or costs involved with termination of an employee. From 1984 on, awards did contain national standards as to redundancy and unfair dismissal, including provisions that required an employer to notify the related employees and their union(s) when it made a definite decision to introduce major changes in production, program, organization, structure or technology that were likely to have a significant effect on employees (such as dismissals, transfers or restructuring of jobs). The employer was required to consult with them over the implementation of the proposed changes.¹⁶⁴ It would be error, however, to overstate the case to which employee co-decision rights were thereby institutionalized so as to limit the capacity of management to make labor force reductions that enhanced shareholder value. The

¹⁶² Laura Bennett, *Job Classification and Women Workers: Institutional Practices, Technological Change and the Conciliation and Arbitration System 1907-72*, 51 LAB. HIST. 11, 20-21 (1986). Where awards were extended to new industry sectors, the tribunals undertook an in-depth inquiry into the value of the different types of work performed, tempered by matters such as industry capacity to pay and the public interest. The tribunals adopted a conservative approach, in that they generally accepted the classifications recognized by the parties to the award. In the building, printing, boot-making and metal industries, this meant awards tended to preserve craft control and enhance workers’ autonomy; whereas in newer industries such as steel, automobile and armaments manufacture, the tribunals tended to rubber stamp the job classification and wage scales proposed by management. See generally CHRISTOPHER WRIGHT, *THE MANAGEMENT OF LABOUR: A HISTORY OF AUSTRALIAN EMPLOYERS* (1995).

¹⁶³ On the regulation of sub-contracting, see Esther Stern, “‘Industrial Disputes’” and the Jurisdiction of the Federal Industrial Tribunal 115-116 (July, 1993) (unpublished Master of Laws thesis, University of Melbourne) (on file with author); on the development of regulation of various “non-standard” work statutes, see generally Anthony O’Donnell, “*Non-Standard*” Workers in Australia: Counts and Controversies, 17 AUSTR. J. LAB. L. 89 (2004).

¹⁶⁴ Termination, Change and Redundancy Case (1984) 8 IR 34; 9 IR 115 (Austl.).

regulation did not confer absolute protection against job loss, but imposed a *procedural* obligation on employers. Consultation was only to occur at the implementation stage, once a definite decision had been made, so discussion would generally involve the level of severance compensation. As one commentator put it, employers still retained

the clear authority to decide upon the methods of production and determine the appropriate size and skills of the workforce that will be employed. . . . The fact that unions are generally precluded from involvement in strategic management decisions on such matters as investment plans, the choice of new technology, product development and the like means that they are unable to exercise any influence over the key variables which ultimately shape employment security.¹⁶⁵

Accordingly, the basic effect of these standards was to increase the costs of restructuring through isolated dismissals or collective redundancies, rather than limiting restructuring *per se*.

What is also important about the arbitral process in Australia is that it can be understood as a system of “three-sided bargaining between management, union, and court.”¹⁶⁶ Aside from the power of the tribunals, trade unions had extensive rights and protections under the system, and were consequently largely integrated, along with employers, into the regulatory process. Such bargaining enabled employees, through the conciliation and arbitration process, “to play a qualified and indirect role” in industry decision making.¹⁶⁷ They were able to have some input on the production process and the structuring of business operations, but no substantial involvement in management’s ability to determine the size of the workforce through termination and redundancy.

Ultimately, any conflict between the governance structure put in place by arbitration and the broad contractual discretions

¹⁶⁵ Stephen Deery, *Redundancy, Employment Protection and the Law*, in AUSTRALIAN LABOUR RELATIONS READINGS 318, 339 (GW Ford et al. eds., 4th ed. 1987).

¹⁶⁶ E.I. Sykes, *Labor Arbitration in Australia*, in AUSTRALIAN LABOUR RELATIONS READINGS 300, 303 (G.W. Ford et al. eds., 3rd ed. 1980).

¹⁶⁷ W.B. CREIGHTON ET AL., *LABOUR LAW: TEXT AND MATERIALS* 490 (2nd ed. 1993).

vested in management under the common law to direct the workforce and make strategic decisions concerning business operations was resolved both through the constitutional and legislative requirement that the tribunal only had jurisdiction over disputes “industrial” in character or that involved “industrial matters” and through a doctrine which cordoned off areas of supposed “managerial prerogative.”¹⁶⁸ This resulted, over time, in a broad range of issues considered to be beyond the reach of the arbitration process. These included shop trading hours, staffing levels of public transport, the use of outworkers, the reinstatement of dismissed employees, occupational superannuation, compulsory unionism, and the direct deduction of union dues.¹⁶⁹ Thus, while awards did regulate many aspects of the wage-effort bargain in a fairly comprehensive manner, the restricted ambit of such matters represented what one commentator referred to as “the essentially marginal nature of the area in which the representatives of labor and management negotiate.”¹⁷⁰

Since the second half of the 1980s, the Australian labor law system has undergone a process of fundamental reform. This has entailed the gradual replacement of the centralized fixation of wages and conditions with enterprise-based employment systems which, it was felt, would be inherently more flexible, more productive, and hence offer greater opportunity for profitability, economic growth, and employment creation.¹⁷¹

¹⁶⁸ The latter is not found within legislation but was given early expression by the High Court in *Clancy v. Butchers’ Shop Employees Union* (1904) 1 C.L.R. 181, 183 (Austl.).

¹⁶⁹ See Michael Kirby & Breen Creighton, *The Law of Conciliation and Arbitration*, in *THE NEW PROVINCE FOR LAW AND ORDER: 100 YEARS OF AUSTRALIAN INDUSTRIAL CONCILIATION AND ARBITRATION* 98, 117 (J. Isaac & S. Macintyre eds., 2004). Across the 1980s, an increasing number of matters were brought within the jurisdiction of the tribunal, and in 1987 the High Court dismissed the idea that “managerial prerogative” could constitute an inherent restriction on jurisdiction, pointing to a “growing recognition that management and labour have a mutual interest in many aspects of the operation of a business enterprise. Many management decisions, once viewed as the sole prerogative of management, are now correctly seen as directly affecting the relationship of employer and employee. . . .” *Re Cram* (1987) 163 C.L.R. 117, 135 (Austl.).

¹⁷⁰ G.H. SORRELL, *LAW IN LABOUR RELATIONS: AN AUSTRALIAN ESSAY* 116 (1979).

¹⁷¹ See generally Braham Dabscheck, *The Slow and Agonising Death of the Australian Experiment with Conciliation and Arbitration*, 43 *J. INDUS. REL.* 277 (2001);

This process was commenced by the Australian Labor government in the latter half of the 1980s and went through three somewhat hesitant phases. First, a period of “award restructuring” saw the Australian Industrial Relations Commission (AIRC) use its national wage decisions to induce employers and unions to review awards and work practices with a view toward greater functional and numerical flexibility, consultation, training and career-path progression.¹⁷² Important in this process was the removal from awards of limitations on the use of part-time and casual workers, contract and agency labor, and removal of restrictions on working time. Second, the AIRC reluctantly accepted an “enterprise bargaining” principle, which was closely followed by the statutory introduction of enterprise-level bargaining in the Labor Government’s amendments to the Industrial Relations Act in 1992. Third, the Labor Government’s concept of enterprise bargaining was extended to include the endorsement of non-union based collective agreements made at enterprise level (known as enterprise flexibility agreements).¹⁷³

The most substantial systemic revision in Australian labor law, however, followed the election to office of the Liberal/National Party coalition government in 1996. The Workplace Relations Act 1996 brought about a paradigm shift in the nature of employment regulation.¹⁷⁴ The principal objects of the federal legislative scheme shifted focus to a concern with international competitiveness, productivity and flexibility in labor markets. Whereas awards had historically been the main instruments regulating employment conditions, these were now reduced in influence, restricted to the status of “safety-net” regulation, and limited to only twenty allowable industrial matters.¹⁷⁵ Thus, for employees to improve their pay or supplement their award conditions, further negotiation was required at the workplace level,

Duncan Macdonald et al., *Ten Years of Enterprise Bargaining in Australia: An Introduction*, in 12 LAB. & INDUS. 1 (2001).

¹⁷² National Wage Case, Review (1989) 27 I.R. 196 (Austl.); National Wage Case (1987) 17 I.R. 65 (Austl.).

¹⁷³ Dabscheck, *supra* note 171, at 281-84. Several Australian State systems also commenced the move to a greater enterprise focus in labor law regulation at around the same time.

¹⁷⁴ See generally Margaret Lee & David Peetz, *Trade Unions and the Workplace Relations Act*, 9 LAB. & INDUS. 5 *passim* (1998).

¹⁷⁵ Workplace Relations Act, 1996, § 89A.

and for this purpose several new forms of enterprise-based agreements were introduced in the Act.¹⁷⁶ These included union-based collective agreements, non-union-based collective agreements, and non-union individualized agreements (hereinafter “Australian Workplace Agreements” or “AWAs”).¹⁷⁷ Any of these forms of agreement could be used to supplement award conditions or to derogate from award minimum standards, provided they did not “disadvantage” employees in a total “money-value” sense.¹⁷⁸

Other major changes melded with the central pre-occupation with enterprise-based bargaining. First, the role of the principal regulatory body, the AIRC, was substantially downgraded.¹⁷⁹ As we have noted, its arbitral powers in settling disputes were reduced with the stripping back of awards, and although it retained powers to process and certify or approve the various forms of agreements introduced in the 1996 Act, its powers to intervene and arbitrate in the making of such agreements were tightly circumscribed.¹⁸⁰ While it continues to exercise many other powers of importance, the AIRC has largely been eliminated as a regulator setting employment standards across industries and occupations.

¹⁷⁶ As noted, some of these had been introduced in a somewhat moderated form in the legislation of the preceding Labor government. For discussion, see generally Laura Bennett, *Bargaining Away the Rights of the Weak: Non-Union Agreements in the Federal Jurisdiction*, in ENTERPRISE BARGAINING, TRADE UNIONS AND THE LAW 129 (Paul Ronfeldt & Ron McCallum eds., 1995); Amanda Coulthard, *Non-Union Bargaining: Enterprise Flexibility Agreements*, 38 J. INDUS. REL. 339 (1996).

¹⁷⁷ The individualized agreements are preferred over the collective forms through subtle legal measures. See Richard Mitchell, *Juridification and Labour Law: A Legal Response to the Flexibility Debate in Australia*, 14 INT'L J. COMP. LAB. L. & INDUS. REL. 113, 126 (1998).

¹⁷⁸ This is the “no-disadvantage test,” a core commitment of the government made as a precondition to the introduction of labor market deregulation. Workplace Relations Act, 1996, §§ 170X-170XF. In addition to these forms of enterprise agreements, the common law of employment could also be used as an instrument of enterprise-based regulation, although unlike the other forms of agreement mentioned it was not possible to use it to undercut award conditions.

¹⁷⁹ Dabscheck, *supra* note 171, at 288.

¹⁸⁰ *Id.* at 285.

Trade unions were also seriously affected by the introduction of the Workplace Relations Act 1996. The Act virtually severed the longstanding symbiotic relationship between the labor law system and the union movement. While unions may still seek awards in the course of industrial disputes, these are now of diminished value to most members. When it comes to seeking improvements through enterprise, negotiation unions face opposition in the form of individual agreements and non-union collective agreements. It is obvious that this has had an impact upon union bargaining strategies.¹⁸¹ The maintenance of union organizational strength was also removed as an object of the workplace relations system and replaced by the philosophy of “freedom of association,” meaning, in this context, particularly the right of workers not to be obliged to join unions by coercive labor market practices.¹⁸²

Further legislative change removed union security devices from awards and agreements, and facilitated further union fragmentation by eliminating the monopoly rights which unions had over particular trades, industries, and occupations.¹⁸³ At the same time the restrictions on industrial action were tightened considerably, making coordinated national or industry campaigns difficult to organize.¹⁸⁴ Like the AIRC, therefore, Australian trade unions have lost their legally guaranteed central role in the regulation of workplace conditions. What they have available to them depends upon their bargaining power in particular industries and workplaces, which is necessarily fragmented and conditional. Largely as a result of these developments, union membership has declined from 50 percent of all Australian workers twenty years ago to only 23 percent today.¹⁸⁵

¹⁸¹ See, e.g., Bill Ford, *Changing the Dynamics of Bargaining: Individualisation and Employment Agreements in Western Australia*, in EMPLOYMENT RELATIONS: INDIVIDUALISATION AND UNION EXCLUSION 88 (Stephen Deery & Robert Mitchell eds., 1999).

¹⁸² Lee & Peetz, *supra* note 174, at 8-9; Mitchell, *supra* note 177, at 123.

¹⁸³ Lee & Peetz, *supra* note 174, at 10-11.

¹⁸⁴ *Id.* at 15.

¹⁸⁵ Andrew Leigh, *The Decline of an Institution*, AUSTL. FIN. REV., Mar. 7, 2005, at 21.

As we have noted, there are objects of the Workplace Relations Act 1996 directed towards the encouragement of employment regulation, which sustains productivity, flexibility and international competitiveness. At the same time, the requirement that the shift to enterprise-based regulation must take place without “disadvantage” to employees perhaps indicates the illegitimacy of a simple cost-cutting agenda. On one reading, then, the Workplace Relations Act 1996 might be doing no more than providing the parties to employment relationships with choices on how to conduct their affairs—choice over the form of regulation, choice over individual or collective forms of activity, choice on whether to join in industrial action, and so on. It is clear, however, that it is necessary to look beyond the legislation, towards the outcomes and effects of the system in order to understand what labor law is doing. Most important here is the general recognition that the shift to enterprise-based arrangements, coupled with the weakening of the authority of the AIRC and trade unions, has considerably strengthened managerial prerogative.¹⁸⁶

That labor regulation now appears to grant management greater latitude to realize gains for shareholder value through cutting labor costs, restructuring the production process, and excluding workers from enterprise-level regulation seems borne out by much of the evidence. Pay, increasingly in the form of performance-based pay, is now, for a substantial proportion of the workforce, a matter for unilateral managerial determination.¹⁸⁷ Second, management has gained greater power over the

¹⁸⁶ See, e.g., Cameron Allan et al., *More Tasks, Less Secure, Working Harder: Three Dimensions of Labour Utilisation*, 41 J. INDUS. REL. 519 *passim* (1999); John Buchanan et al., *Wages and Wage Determination in 1999*, 42 J. INDUS. REL. 109 *passim* (2000); John Buchanan et al., *Wages and Wage Determination in 1998*, 41 J. INDUS. REL. 102 *passim* (1999); John Buchanan et al., *Wages Policy and Wage Determination in 1997*, 40 J. INDUS. REL. 88 *passim* (1998); Richard Mitchell & Joel Fetter, *Human Resource Management and Individualisation in Australian Labour Law*, 45 J. INDUS. REL. 292 *passim* (2003); Richard Mitchell et al., *What's Going On With The 'No Disadvantage Test'? An Analysis of Outcomes and Processes Under the Workplace Relations Act 1996 (Cth)* (Ctr. for Employment & Labour Relations Law, Univ. of Melbourne, Working Paper No. 33, 2005), available at <http://www.hotkey.net.au/~jimcd/papers.htm> (follow “What's Going On With the 'No Disadvantage Test'? an Analysis of Outcomes and Processes Under the Workplace Relations Act 1996 (Cth)” hyperlink).

¹⁸⁷ Awards continue to lose ground as they are reduced from “real” rates to “safety-net” status, and so the level of comparison for the operation of the “no-disadvantage” test moves to an increasingly unrealistic standard. Over-award standards

scheduling of production and the organizing of business operations. This is most clearly seen in the expansion of casual, fixed-term, contract, and agency labor.¹⁸⁸ The engagement of such labor can also absolve employers of some of the indirect costs associated with hiring permanent, full-time workers, such as holiday and sick leave, penalty rates, redundancy and notice provisions, and so on. The removal of restrictions on “non-standard” labor began, as noted above, with the award restructuring process in the late 1980s, but was consolidated with express legislative provisions in the Workplace Relations Act 1996.¹⁸⁹ While it is true that the rapid growth in non-standard employment is due to many factors, Australian labor law in the 1990s has allowed this shift to occur without serious legal obstruction.¹⁹⁰

A third outcome has been work intensification. Enterprise-based agreements, whether in the form of the common law contract of employment, AWAs, or non-union collective agreements are, in many sectors of industry, providing great scope for the utilization of labor by management fiat. Consistent with our earlier argument about the effects of expanded managerial power, studies of non-union-based agreements formalized under the Workplace Relations Act 1996 reveal a higher level of provisions pressuring working time obligations than is the case with union-based formalized agreements.¹⁹¹

expressed in other forms of agreements are not taken into account in the “no disadvantage” calculation. Research carried out on the process of agreements and the application of the “no disadvantage” test reveals grave doubts over the validity of the mechanism as a means of preventing “under award” deals. *See, e.g.,* Omar Merlo, *Flexibility and Stretching Rights: The No Disadvantage Test in Enterprise Bargaining*, 13 AUSTL. J. LAB. L. 207 *passim* (2000); Peter Waring & John Lewer, *The No Disadvantage Test: Failing Workers*, 12 LAB. & INDUS. 65 *passim* (2001); Mitchell et al., *supra* note 186. On the spread of performance-based pay, see Mitchell & Fetter, *supra* note 186.

¹⁸⁸ *See* AUSTL. BUREAU OF STATS., FORMS OF EMPLOYMENT, AUSTRALIA 3 (2005); AUSTL. BUREAU OF STATS., AUSTRALIAN SOCIAL TRENDS 2000 115 (2000). *See* also the discussion in O'Donnell, *supra* note 163, *passim*.

¹⁸⁹ The Workplace Relations Act, 1996, § 89A(4)(a), now expressly forbids any such provision from inclusion in an award unless exceptional circumstances apply.

¹⁹⁰ At the same time there is nothing to stop unions from bargaining and entering agreements over these matters where there is sufficient union power to do so. There has been a tendency for unions to use such agreements to seek restriction of casual employment by accepting more “permanent part time” employment.

¹⁹¹ *See* authorities cited *supra* note 186.

Finally, whereas awards are still expressly permitted to regulate notice of termination and redundancy pay, most of the consultation requirements introduced into awards in the 1980s cannot be regarded as “allowable matters” under the Workplace Relations Act 1996, representing in one view, “a definite attempt to achieve a return to former managerial prerogatives and to limit the area for union involvement and input.”¹⁹² Again, it would appear that the removal of award provisions for information disclosure to employees over restructuring has only partly been compensated for with agreement-making at the enterprise level, with less than one-third of enterprise agreements making provision for discussion between management and employees/unions about redundancies or other forms of workplace change.¹⁹³ Obligations for employers to consult with employees are not only rare in such agreements, but often appear only as an obligation to “advise” rather than engage in deliberative discussions. Formal joint consultative committee structures are more common, especially in union agreements, but usually only exist for dealing with matters that are the subject of the collective agreement, rather than any broader issues of workplace regulation.¹⁹⁴

To conclude, our discussion suggests that the recent changes to labor law increasingly allow for an approach to delivering shareholder value based on the cutting of overall labor costs and allowing management considerable latitude to restructure business operations relatively unfettered by external controls. The evidence demonstrates an approach generally focused on the enterprise level—on wage reductions, greater intensification of

¹⁹² Marilyn Pittard, *Collective Employment Relationships: Reforms to Arbitrated Awards and Certified Agreements*, 10 AUSTL. J. LAB. L. 62, 72 (1997).

¹⁹³ The exclusion of consultation provisions from awards was partly redressed by the AIRC in a March 2004 decision, which held that employer obligations to inform and consult about redundancies were an allowable award matter relating to “dispute settlement procedures.” The outcome might be an improvement on old award standards in that consultation must commence once redundancies are “contemplated,” but narrower in that consultation is limited to redundancies rather than broader workplace change. Redundancy Test Case Decision, PR032004 (A.I.R.C. Full Bench, Mar. 26, 2004), available at http://www.airc.gov.au/documents/full_bench/full_bench_decisions.html.

¹⁹⁴ See Mitchell & Fetter, *supra* note 186 *passim*; Mitchell et al., *supra* note 186 *passim*.

work, greater resort to cheap and flexible forms of employment, and less reliance on management-employee consultation.

Australian labor law exhibits few of the offsetting mechanisms identified in some other (mostly European) jurisdictions that give employees an effective voice in business restructuring. Mandatory consultation over redundancies survives,¹⁹⁵ and the sharing of “information” under such provisions may include information about the selection criteria for redundancy and redeployment plans, but labor law does not require the production of information going to the necessity of the employer’s decision to implement redundancies. In essence, management’s commercial decision-making rights about business strategy remain intact. Indeed, the procedural regulation and formalization of redundancy may enhance managerial efficiency by sidestepping grievance strikes at plant level while ensuring that employees in declining industries are given incentives to abandon resistance to technological change.

There have also been important developments with regard to business restructuring through outsourcing. There is no formal recognition that employees of a business which is transmitted to another entity should have any claim to employment with that new entity (in comparison to the European Union Acquired Rights Directive), but the Workplace Relations Act 1996 does contain a provision which provides for the continued application of awards and certified agreements in the event that there is a transmission of all or part of an employer’s business.¹⁹⁶ These transmissions of business provisions have been in the federal industrial relations legislation since the early decades of the twentieth century, but have more recently been found to have

¹⁹⁵ Now imposed where an employer has decided to terminate the employment of 15 or more workers for economic or structural reasons. Workplace Relations Act, 1996, § 170CK-170EF. Such consultations must cover possible measures to avert or minimize dismissals and to mitigate the adverse affects if they cannot be avoided, and should commence at an early stage in the management decision-making process, well before specific employees are identified for redundancy. See Anthony Forsyth, *Giving Teeth to the Statutory Obligation to Consult Over Redundancies*, 15 AUSTL. J. LAB. L. 177 *passim* (2002).

¹⁹⁶ Workplace Relations Act, 1996, §§ 149(1)(d), 170MB. For a discussion of the Australian provisions in the light of the European Union Transfer of Undertakings Directive, see Martin Vranken, *Transfer of Undertakings in Australia and New Zealand: How Suitable is the European Regulatory Approach for Exportation*, 21 INT’L J. COMP. LAB. L. & INDUS. REL. 227 (2005).

application in the context of business restructuring, especially concerning outsourcing and privatization. Thus, there can be a “transmission of business” in situations where all or part of an employer’s business is outsourced to an outside provider.¹⁹⁷ These decisions do provide some protection for the terms and conditions of employment of employees whose jobs are outsourced by their employer, and so limit the power of employers to unilaterally arrange their commercial and corporate affairs in such a way so as to minimize their employment law liabilities.¹⁹⁸

VII. CONCLUSION

The focus of this paper has been on three core issues. We first examined the extent to which shareholder value has come to dominate debates around corporate governance and theories of the company. Second, we explored the extent to which the Australian corporate law framework offers clear support for shareholder value as a corporate governance norm or imperative. Third, we examined the degree to which labor law provides a constraint on, or compels a modification of, the idea of shareholder primacy.

In relation to the first two of these issues, because we can clearly identify the consolidation of the shareholder value norm in contemporary corporate governance debates, our analysis leads us to conclude that some longstanding parts of corporate law provide only modest support for shareholder primacy. However, recent corporate governance reform strategies, such as those linking senior executive remuneration to share prices, and increasing reliance upon independent directors, are more closely linked to the pursuit of shareholder value than to some of the more longstanding corporate law doctrines. Yet, the impact of each of these reforms on corporate performance, and thus on the

¹⁹⁷ These provisions would appear not to apply, however, where an employer outsources a significant but entirely incidental part of its activities. See *PP Consultants Pty Ltd. v. Fin. Sector Union* (2000) 201 C.L.R. 648 (Austl.); *N. W. Health Care Network v. Health Services Union of Austl.* (1999) 164 A.L.R. 147, 157 (Austl.). See also Kelly Godfrey, *The Evolution of Transmission of Business: Where Have We Been? Where Are We Going?*, 31 AUSTL. BUS. L. REV. 344, 366 (2003).

¹⁹⁸ See Trent Sebbens, “Wake, O Wake”: *Transmission of Business Provisions in Outsourcing and Privatisation*, 16 AUSTL. J. LAB. L. 133 *passim* (2003).

delivery of shareholder value, remains uncertain based on the results of empirical studies designed to test the outcomes of these reform strategies.

We also examined changes in corporate ownership, where, in the Australian context, the increasing ownership by institutional investors (that provides an incentive for active monitoring of the governance of the companies in which they invest) is, in many cases, counter-balanced by even larger non-institutional substantial shareholders (such as shareholdings of founding families or overseas companies), thereby reducing the prospects of successful institutional intervention. Patterns of institutional activism vary, depending on the size of the shareholding, the size of other non-institutional holdings in the company, the size of the company itself, the resources devoted to monitoring, the nature of the institution's portfolio, and whether the institution is managing index funds. We note that institutional investors have, in recent years, increasingly argued for the types of corporate governance reforms which involve the pursuit of shareholder value.

In relation to the third issue, we argue that labor law, although not often a key focus of the research of corporate governance scholars, has always been in view as part of corporate governance to the extent to which it structures and limits what management can do in its relations with employees. However, current developments in Australian labor law are moving to a position whereby management's power to restructure the enterprise for shareholder value is being subjected to fewer constraints, with a corresponding shift of risk to employees.

Our survey has thus been able to raise certain questions and issues, and to advance partial and tentative explanations. Further research, based upon case study and survey methods, is being undertaken by the authors.¹⁹⁹ This work will enable us to explore the intersections of corporate governance, corporate law and labor law in specific contexts. Rather than presume uniform

¹⁹⁹ This is the objective of the "Partnerships at Work" project currently being undertaken at the University of Melbourne by the Centre for Employment and Labour Relations Law and the Centre for Corporate Law and Securities Regulation. The project is funded by the Australian Research Council.

outcomes or impacts derived from system-wide influences of finance or governance structures, this research may provide further evidence of the diversity we find within and between national systems.