This essay was originally published in Equity & Trusts in its second edition (2001) but was removed from the fourth edition (2005) to make room for the 200 pages of new material in that edition. The purpose of this essay is to trace an often-forgotten part of modern trusts and company law: viz. the roots of company law in trusts law and the continued links between those topics. There is a tendency in company law to dismiss any connection between the two fields since the Saloman case in 1897, whereas in truth the law on directors' duties is still bicameral with the law on trustees' duties in many contexts, also the general equitable principles on e.g. personal liability to account for dishonest assistance in a breach of fiduciary duty are identical. The notion of separate personality is a thin thread – it would take only words to break it because it took only words to make it. This piece is of particular significance to my postgraduate students when considering commercial trusts law.

ESSAY – CORPORATIONS, COMMERCE AND EXPRESS TRUSTS

25.1 THE DEVELOPMENT OF THE ENGLISH COMPANY OUT OF THE LAW OF TRUSTS

It has become voguish to separate out company law from the law of trusts and to treat the two as completely distinct areas of law. The reason for this distinction is that the company has its own legal personality under English law as a result of the House of Lords decision in *Saloman v A Saloman & Co Ltd*.[1] With that has come an ideology as to the distinctness of the company and a separation of the personality of this legal fiction from the personality of its shareholders, employees, creditors and directors. It is now usual to talk of the company as part of the law of persons[2] and as something distinct from the law of trusts or of equity.

The Limited Liability Act *1844* provided for limited liability for investors in a companies, meaning that shareholders in such company could limit their own liability to meet the losses of the company, but it was the common law which gave companies their own legal personality. Before the seismic change effected in *Saloman*[3] the company had been a partnership between the shareholders (or members) of the company and the company's property was held on trust for the members as beneficiaries. What is important to note is that the company is now the owner of its own property and that the members have merely rights against the company but no title in any of the company's property until the company is wound up. The history deserves a little more attention.

The commercial companies which developed as part of the industrial expansion of the 19th century were originally formed as joint stock companies. The joint stock company saw lawyers lash concepts of partnership together with concepts of trust. These evolving legal techniques were developed at a time when ordinary companies had been made illegal because of the losses caused by speculative companies in the South Sea Bubble, an economic crisis of huge proportions in which the South Sea Company collapsed after having raised very large sums of money from the public to invest in the 'south seas' of the British Empire. Two techniques evolved to circumvent these prohibitions. First, the unit trust whereby investors became beneficiaries under a mutual investment fund – considered in chapter 24. Second, the joint stock companies.

1 [1897] AC 22.

2 See eg *Private Law*, ed Birks, 2000.

3 [1897] AC 22.

The Joint Stock Companies Act 1856 and other subsequent legislation permitted limited liability in recognition of the extant commercial practice of limiting the shareholder-capitalists' liability by means of contract and trust. It was the common law which recognised the need for the logic of limited liability to extend to the creation of separate legal personality for companies in the House of Lords decision in the *Saloman* litigation in 1897.[4] This remarkable decision (treated as second nature by English lawyers today) conferred distinct legal personality on companies despite the earlier determination of the courts as late as 1879 that directors should be considered to be trustees holding property attributed to the company on trust for the members of that company as though beneficiaries.[5] Therefore, it is perfectly correct to say that companies are modern expressions of 19th century trusts – although now conceptually distant from trusts according to the case law. The trust itself was being used, in conjunction with contract, to pursue commercial objectives.

The modern company is a very different animal after the decision in *Saloman* precisely because the company was then accepted as being a distinct legal person from its directors, shareholders and so forth. For the capitalist this offers both the opportunity to raise capital from the public and the protection of limited liability. The entrepreneur can hide behind corporate personality and contend that when the company is in difficulties there is no necessary liability owed by the entrepreneur personally for the debts of that company.

Under the joint stock company structure the company was quite literally that: a *company* of people, in the same way that a dinner party guest list may be described as a 'company'. The word derives from the Latin words '*com*' (together) and '*panio*' (bread): literally, a companion is someone with whom you break bread and a company is a group of people breaking bread together. A company was therefore an association of persons who invested in common – they were members (still the technical term for shareholders in company law) of a company. It is only the decision in *Saloman* which accords these companies their own legal personality distinct from the membership.

The fortunes of the members improved with this development in the law in one sense because they bear no liability for the losses of the company; however, they have worsened in another sense because they no longer have the rights of a beneficiary in the property owned by the company. The development of the company involves a distance between the property held by the company and the rights of the shareholders: shareholders are not in the same position as beneficiaries under a trust because the company takes absolute title in its own property. Therefore company law has displaced the equitable principles of good conscience and equality required by the law of trusts in favour of principles built on economic power and pecuniary democracy such that the shareholders with the most shares effectively control the company. The derivative action of minority shareholders remains the only means of protection of the minority shareholder[6] as compared to the power of the beneficiary under the trust to compel equality of treatment by the trustee.[7] The majority shareholders can vote down the minority in company law (a principle built on 'let the devil take the hindmost', or possibly on Darwinian ideas of survival of the fittest) unlike the egalitarian demands of the law of trusts and of equity considered in chapter 9.

Many commentators decry this distance between the company and the people who work in or for the company because it reduces the responsibility which employees and directors owe to those third parties who deal with the company – no stigma attaches to individuals for actions done in the name of the company.[8] What the law has permitted is a form of 'moral gap' between the personal responsibility of the capitalists and the effects they have on the real world outside their office premises.[9]

25.2 HOW COMMERCIAL LAWYERS THINK OF PROPERTY RIGHTS

What has always struck this writer as remarkable is the difference between the manner in which property lawyers consider questions of title in property and the manner in which commercial lawyers consider those same questions. To put the point crudely, commercial lawyers are concerned to give effect to contracts wherever possible without concerning themselves as to the niceties of title.[10] Property lawyers and trusts lawyers can be expected to take a more doctrinaire approach to rights in property. The one exception arises in relation to insolvency.

---

4 *Saloman v A Saloman & Co Ltd* [1897] AC 22.

5 *Smith v Anderson* [1879] 15 Ch D 247.

6 *Foss v. Harbottle …* ; *Prudential Assurance v. Newman …* .

7 Companies Act 1985, s 459.

8 Chomsky, 1999; Cotterell, 1992.

9 Bauman, 2000.

10 An attitude approved by Goode, 1997.

The clearest example of the difference between a property lawyer and a commercial lawyer arises in relation to the discussion of certainty of subject matter in chapter 3. The property lawyers' strict approach is personified by the decision in *Re Goldcorp*[11] that there must be segregation of property before that property can be held on trust. Other concepts, like the floating charge in which property rights of a certain value can attach loosely to a fluctuating pool of property, have grown out of equity and been seized upon by commercial lawyers as providing a different form of security for commercial parties.[12] The commercial lawyer, by contrast, will not want a contract to be invalidated simply because some formality as to the segregation of property has not been complied with. So it is that the Sale of Goods (Amendment) Act 1995 was enacted to provide that even where property has not been segregated, if the claimants have rights to part of a mixed fund of property those claimants can assert rights as tenants in common of the entire fund.

The only context in which commercial lawyers follow as strict a line as the property lawyers is in relation to insolvency. It is a central principle of insolvency law that no unsecured creditor be entitled to take an advantage over any other unsecured creditor: the well-known *pari passu* principle.[13] That explains the decision in *Goldcorp*[14] whereby there were more claims than there was property to go round such that all creditors who could not identify any property which was held separately on trust for them could only receive the rights of unsecured creditors under the *pari passu* principle on the liquidation of the insolvent person's assets.

What emerges from this short discussion is an impression that commercial law is concerned to develop principles which are likely to support the efficacy of commercial contracts. As considered in chapter 22 there is a great suspicion among the commercial community of equitable principles, despite the fact that most of the significant commercial structures were developed by equity: for example the ordinary company, floating charges, and express trusts. What is also significant is the form of fiduciary responsibility which will be imposed by commercial law in future. An outline of that discussion follows.

25.3 NEW FIDUCIARIES IN THE RISK SOCIETY

25.3.1 The argument

Despite the increasing automation of financial markets and the vast anonymity of global banking institutions, the human beings who people them will continue to be particularly significant. No risk weighting model, no automatic trading system, no system of financial regulation, can fully replace the activities of individual human beings who will remain brim-full of their own opinions, frailties and personal mythologies. However, one context in which the law governing investment and companies will have to develop in the coming years is in the development of principles relating to the control of fiduciaries. For it is the fiduciary (the officer, director, trustee or other functionary) who will continue to make day-to-day decisions in relation to the vast panoply of corporate entities and non-corporate investment vehicles which exist under English law.

Company law, trusts law and the law of restitution will be required to develop over the next 20 years to account for the developing nature of fiduciary relationships, not only in the private sector but also in the public and quasi-public sectors. Whereas the growth of English company law from the late 19th century placed the company at the heart of investment policy, a new range of fiduciaries and investment vehicles are becoming ever more important.

11 *Re Goldcorp* [1995] 1 AC 74.

12 *Clough Mill v Martin* [1984] 3 All ER 982.

13 *Stein v Blake* [1996] 1 AC 243.

14 [1995] 1 AC 74.

25.3.2 The new context

Private investment takes place not only through ordinary companies, but also through investment trusts, open-ended investment companies, unit trusts, pension funds and so forth.[15] Trust structures used for investment, such as pension funds and unit trusts, have established themselves as some of the most powerful investment institutions in the United Kingdom. Fund managers hold very significant proportions of the FTSE-100 and the bond markets. The range (and power) of investment vehicles is a feature of the modern financial markets. However, a more recent phenomenon has been the growth of public sector pools of investment capital in private sector models of entity, such as NHS trusts[16] and the proposals for re-vamped credit unions.[17] Social investment through quasi-private sector models, and the concomitant need for fiduciary principles to regulate their management, will be a feature of this new quasi-corporate sector.

The main area for debate will be the manner in which fiduciary responsibility appears to be demonstrating a trend towards strict liability. Aside from the rigour of rules like that in *Keech v Sandford*,[18] providing that fiduciaries must not allow conflicts of interest, other areas of fiduciary responsibility are hardening into almost strict liability (for example, in relation to personal liability to account for accessories to breaches of trust[19]).

In the context of the public sector, though, applying principles as to responsibility for investment will require different principles from those applied to fund managers in the private sector. Regulation and substantive law's control of fiduciaries in this new context will become critical as the financial markets take the place of much of the state-controlled social security system. As the public comes to rely ever more on these private sector bodies for their pensions and their healthcare, it can be expected that there will be increased legal scrutiny of those people who administer them.

25.3.3 Private sector investment vehicles – the roles of the fiduciary

It is not clear in many private sector investment vehicles which of the many fiduciaries involved with the entity are competent to exercise all of those fiduciary duties. The fiduciary responsibilities currently divide between 'management duties' (e.g. the duty to prepare accounts, the duty to supervise delegates, the duty to provide information to shareholders (or beneficiaries)); 'stewardship of property' (for example the duty to oversee maintenance of the entity's property (or trust fund)); 'personal propriety in office' (for example the duty not to permit conflicts of interest, the duty not to make unauthorised personal profits); and 'investment' (for example the duty to obtain a maximum return, the duty to act in relation to the beneficiary as though acting for someone for who one is morally bound to provide) – all considered in chapter 9 above.

These fiduciary duties will clearly differ in application to different commercial contexts. Thus, the small family maintenance trust will require a different rate of investment return from a pension fund. Similarly, it can be expected that different principles will apply in relation to public sector entities where the forms of investment undertaken are frequently infrastructural but where the duties of maintenance of property, the avoidance of conflicts and observance of the terms of the fiduciary duties are broadly similar. In short, what emerges is a difference in the detail of those fiduciary responsibilities, born out of overly vague expressions of the underlying nature of the fiduciary obligations in the core legislation which is then applied by different regulators in each context. It can be expected that this will lead to uneven application of these principles in many contexts.

25.3.4 Traditional fiduciary responsibilities in the new context

The development of public policy in relation to the use of private sector investment initiatives, and also the use of public-private partnerships to deliver welfare state services, offer up a new arena for the application of fiduciary responsibilities. What is at issue is the manner in which private law fiduciary norms will be applied to these new contexts. Two problems arise. First, will the permissive context of some part of the law of fiduciaries which is suitable for arm's length investment contexts need to adapt to protect ordinary citizens who are dependent on their investment for their sole income in their old age or otherwise? Second, do those norms work effectively in dealing with public sector bodies and their officers; or in other words, how is the interaction between public law and private law to be managed in this area?

---

15 Hudson, 2000.

16 Chapter 29.

17 Chapter 28.

18 (1726) Sel Cas Ch 61.

19 *Royal Brunei Airlines v. Tan* [1995] 2 AC 378.

In short it seems that there may need to be a retreat by equity into the 19th century rules which sought to protect family incomes in the form of trust funds by interpreting powers of investment and the role of trustees very strictly. That morality may see its return in the increasingly strict liability imposed on fiduciaries for conflicts in their office with other commercial goals. These are new fiduciary contexts but probably requiring flexible, ancient approaches asserting ethical standards of behaviour to be applied contextually.

25.3.5 Dissonance in the treatment of professional and non-professional trustees

One startling theme to have emerged from this book is that with the expansion of the importance of investment in the social life of the United Kingdom, the liabilities of market professionals are expressly limited by contract. The result is that market professionals, from whom we may expect a higher standard of investment competence, are subject to a lesser standard of obligation than non-professional trustees who take on the office of trustee. There is an important schism here. Market professionals are categorised by the law as owing duties in contract to the beneficiaries, whereas the non-professional owes duties under the law of fiduciaries and trusts. That means that the market professional is able to rely on her bargaining power to generate favourably slight contractual liabilities. Properly put, this is the result of favourably broad limitations on liability. The non-professional is subject to the hawkish expectations of the judiciary applying equitable principle as a result of the trustee's own lack of bargaining power or ignorance of the possibility of limitations being placed on their liabilities by contract.

What is suitable fiduciary behaviour in relation to a bond transaction may not be suitable behaviour in relation to our personal pensions. What is suitable in the management of a FTSE-100 company may not be suitable in relation to the provision of healthcare services. An equitable approach moulded to assess suitability in this way would recognise the place of chaos, social complexity and the multifaceted nature of risk within its remit – a debate which is pursued in the final chapter of this book.

25.4 GLOBALISATION – A MEANS OF UNDERSTANDING THE FRAGMENTATION BETWEEN COMMERCIAL AND NON-COMMERCIAL TRUSTS

Globalisation is one of the more elusive buzz-words of the late 20th and early 21st centuries: the post-postmodern era.[20] Globalisation possibly indicates two subtly different trends. The first is a literal tendency for the entire world (or, globe) to share ideas, aspirations and transactions. The suggestion is that the world is transforming from being a collection of distinct nation-states into a 'global village'. At that level, perhaps this is to notice that communications and transport technology have made it possible for people to interact with one another across huge distances in ways that had previously been impossible; perhaps it is to observe that (predominantly American) capitalist brands like McDonalds, Coca-Cola and Microsoft have added to that lexicon of internationally understood words like 'taxi'. At the time of writing, however, it is not clear whether or not this analysis is satisfactory. It appears, instead, that the eighteenth and nineteenth century development of nation states, as opposed to the more fluid movement of people and ideas around the Mediterranean with smaller principalities, tribal areas and geographic units up to that time, is being replaced in part by a form of imperialism through which American capitalism is establishing itself as the governing creed in much of the world. This is a form of imperialism, it has been suggested,[21] which is very different from the British and similar empires through history because the Americans have no apparent ambitions to govern other states nor to colonise them with their own bureaucrats, soldiers and so forth. Rather it is a combination of American ideology (free markets, democracy and codes of law built on human rights) and their status as the only world, military superpower which constitutes this novel form of imperialism. What has resulted is level of cultural homogeneity around the world but one which has produced evident antagonism in the Middle East and a wave of dissent in Western Europe.

---

20 Beck, 1992, 2.

21 Hardt and Negri, … .

The second trend is subsumed within the first, that is the globalisation of a range of norms and values across most of the disparate nation states of the world, with at least a token acceptance of them even by those which have not sold into them completely in practice. So it is that the post-Cold War era has seen a blithe acceptance of the need for democracy and human rights, together with a slightly more contentious dissemination of the benefits of free market capitalism. The acceptance of the need for human rights and democracy perhaps masks more profound issues as to the content of those rights. There are also other questions as to the intellectual foundations of those same ideas,[22] whether it is socially useful to have 'rights' without clear, countervailing responsibilities (as communitarians like Etzioni would prefer[23]), and how we can differentiate between 'rights' (in the sense of enforceable entitlements) and mere 'claims to benefits'.[24] Behind this debate is the questioning of the role of capitalism – free market capitalism prefers human rights to extend as far as democratic rights to vote but is less keen on an institutionalised right to strike or to tax corporations. Consequently, the process of globalisation remains a contested notion.

For the purposes of this chapter it is important to understand the role of globalisation. Commercial law is now an international phenomenon which frequently overlaps with international trade law and aspects of private international law, as well containing subjects like carriage of goods by sea between jurisdictions, international banking transactions and so forth. Commercial law has itself become a commodity – the primacy of English law and New York law in this context mean that lawyers based in London generate tremendous incomes from advising both national and international clients on the norms of that system of law, English law, which is so commonly chosen to govern their contracts. With increasing frequency neither party to a commercial dispute will be resident in the English jurisdiction, nor will their transaction have had any connection with England or Wales, nor will there have been any interaction with England at all other than a selection of English law as the governing law of a contract. Often English law is chosen simply to provide neutral ground between contracting parties from different jurisdictions or to comply with the prevailing norms in many banking or other commercial markets.

Given the international character of commercial law, many commercial lawyers prefer to ignore the ethical norms which inform much English law. Instead of busying themselves with rules created in the 19th century to cater for the needs of people seeking to allocate rights to family property, commercial lawyers look to this new global context in which commercial people wish to be left free to reach their own decisions and to form their own contractual norms. But does that mean that the ordinary principles of English common law and equity ought to be relegated to background?

The late modern world has changed the way we might think about the structure of many of our core legal concepts. The French sociologist Durkheim long stressed the positive connotations of contract law on the basis, in his view, that it enables citizens to organise their own relationships on a voluntary and self-regulating basis.[25] The problem with this analysis in relation to commercial law is that modern contract law enables commercial people to create their own self-contained worlds in which contracts provide all the rules and broader society is not necessarily able to regulate the ways in which these contracts are performed. Particularly the use of arbitration between commercial parties does mean that the courts are not able to impose the ethical basis of contract law and equity on multinational enterprises in the same way as it is imposed on private citizens. Therefore, we can identify this context as a process of closing some activity off from the rest of society: a problem which Durkheim used to identify with property law. Whereas property law was once considered to be socially divisive, in that ownership of property necessarily means that people other than the owner are not entitled to use it, that same property law also offers models for communal action through co-operatives[26] and charitable trusts. It is a near cousin of the co-operative and of the trust which has since become the most significant model for holding private wealth and for carrying the message of Western capitalism around the world: the company. The company is itself a combination of contract and property law. The contract is expressed in the articles and memorandum of association which stand for the constitutional basis of the company akin to the rules of an unincorporated association;[27] the property element, as considered above,[28] is expressed by the roots of the modern company in trusts law and now in the rights of shareholders.

---

22 Para 17.2.1.

23 Etzioni, 1993.

24 Raz, 1986, 165.

25 See generally Durkheim, 1894; Cotterrell, 1999.

26 Para 28.2.1.

27 Para 4.3.2.

28 Para 25.1.

By allowing companies to behave as though they were tangible people we enable the real people who support those companies, either by means of their investment capital or by directing the company's day-to-day decisions, to hide from direct responsibility for the actions of those entities. If we were to remember that a company is in truth an expression of those people who came together to form it, then we would be able to attribute the liability of the corporation to those who support it and to those who constitute its controlling mind. To achieve a more humane lifeworld for our fellow citizens it is important that fiduciary law attributes liability to those human beings who ought to bear it. As an engine of enhanced social solidarity it is important that corporations are not permitted to conceal the truth of their operations behind brand names, logos, and the reflective glass of their corporate headquarters. The development of modern company law through the *Saloman* principle has meant that the moral control of trustees which was at the root of the early companies has now been lost. Instead, commercial activity in the global marketplace operates, for the most part, beyond the effective control of the courts of conscience and has consequently developed its own, closed norms as to the contract law and the use of property.