CHAPTER 2

EVOLUTION OF CORPORATE STRUCTURE AND TRANSNATIONAL EXPANSION

THE BACKGROUND:

Commerce is as old as the human civilisation itself and in my opinion, a basic human instinct. It is one of the building blocks of a society. Infact, one of the earliest interactions between humans was the process of taking and giving, initially through barter and later on, through the monetary system. Commerce tends to bring about a balance in the society resulting from distribution of goods/products/services from those who have it to those who don't have it, which is very essential for progress of any given society.

Even in historical times i.e. starting from the time of four major ancient civilisations\(^{50}\), commercial transactions have existed at the international level. Historians and Archaeologists have found evidence of Harappan pottery seals in Mesopotamia. Infact, such was the level of commercial interaction, that evidence suggests that different traders had their own peculiar seals lending credence to the theory that system of Trademarks is old as the earliest known human civilisation itself. However, for obvious reasons, international trade between different early societies was a limited individual effort by traders\(^ {51}\).

\(^{50}\) Mesopotamia (Tigris and Euphrates), Harappa and Mohenjo-Daro (Indus), Egyptian (Nile) and Chinese (Hwang Ho)

\(^{51}\) The only possibility of co-operation of efforts between traders appears to have been to travel together to places where the distance was too much for any individual trader to traverse alone. Beyond this basic co-operation, there is little evidence to suggest that individual traders pooled their resources for trade beyond their civilizations
2.1 EARLY INTERNATIONAL TRADE

The earliest example of traders coming together in the sense of pooling their resources for a joint commercial venture is during the time when land route to the spice land i.e. India, was blocked by the Ottoman Empire. New routes had to be found from Europe to east in search of spices which resulted in the exploration of sea routes. Once the sea route to east, in particular India, was discovered, the spice trade became profitable once again and thereafter, it was basically a race to secure the royal permission to trade with the east. This was the time when earliest recorded ‘associations of persons’ for commercial ventures finds a mention. Trade with the East through the sea route was not an easy option. The royal permission to trade through the sea route itself was very expensive to receive as it was not permitted for anyone to start trading through the sea route. In addition, the expedition itself was a very expensive proposition and was not possible for a lone merchant to undertake. Both these factors i.e. securing the royal charter to trade and financing the expedition resulted in a number of persons forming Associations to trade with the east.

2.2 BIRTH OF THE COMPANY

This ‘Association’ was the predecessor of the modern day Company, the most popular and organized form of business enterprise today. During the early days it had close affinity with the partnership firm. The registered Company had its origin in the English Law by the middle of the 19th century i.e. by 1844 through the Joint Stock Companies Act 1844. Before that there were only two types of corporations namely: (1) the Chartered Company which came into being on the issuance of a Royal charter, and (2) the statutory corporation which was created by a special enactment. Incorporation
through both these methods was not easy. In addition, the cost of incorporation was also prohibitive.

The Chartered Companies were incorporated mainly for the purpose of overseas trade. The Statutory Corporations on the other hand were functional in the domestic arena, mainly in infrastructure and public utilities sector. Since it was very difficult to obtain incorporation through the above two listed methods, most of the business activities were carried out through large unincorporated business associations popularly known as the ‘deed of settlement company’ or ‘common law companies’ which was the predecessor of the modern day registered company but in legal terms it was a large partnership firm. The capital was divided into shares and was made transferable. The management of the business was entrusted to a committee of directors or governors. The property of the association was vested in another body of trustees. Many of the trustees were also members of the Board which shows that these associations had a lot in common with the modern day company which is based essentially on the twin principles of a separate identity/legal personality and distinction between ownership and management. The Deed of Settlement Company was the main vehicle through which the commercial activities were carried out.

Before tracing any further the growth of the corporate form of organisation, it will be worthwhile to study the formation and subsequent rise of a Company which was incorporated through a Royal charter – the East India Company, an Organisation which can truly be called as probably the First Transnational Corporation.

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52 For example Railways
2.2.1 **East India Company – The First Trans National Corporation**

Governor and Company of Merchants of London trading into the East Indies were granted a charter of incorporation on December 31st 1600 by Queen Elizabeth. The aims of the Company were essentially commercial. Trade with the East was essential in order to obtain those spices necessary to render palatable the limited foodstuffs available under the primitive agricultural conditions of the day and other products prized for their utility or beauty in the West. The traditional route passed through the dominions of the Sultan of Turkey, and Elizabeth in 1581 granted a charter to the Levant Company to trade with these dominions under the terms of the concessions made by the Sultan in 1579, when he granted privileges of trade and residence, with exemption for most purposes from Turkish criminal and civil jurisdiction, to English subjects. The Company sought to extend its trade to India, and in 1592 secured a fresh charter authorizing them to trade to India overland through Ottoman territories. Serious difficulties, however, were placed by the Sultan in the way of the development of overland trade, while the discovery of a practical passage to India by the Cape of Good Hope suggested a new line of approach\(^{53}\). Political conditions favoured action. The Bull\(^{54}\) of May 4, 1493\(^{55}\) of Pope Alexander VI had assigned India to Portugal\(^{56}\) in its

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54 Bull is a formal proclamation issued by the Pope
55 [www.naiveweb.org/pages/legal/indig-inter-caetera.html](http://www.naiveweb.org/pages/legal/indig-inter-caetera.html) accessed on 22.2.2014 - Columbus’ discovery in 1492 of supposedly Asiatic lands in the western seas threatened the unstable relations between the kingdoms of Portugal and Castile, which had been jockeying for position of colonial territories along the African coast for many years. The king of Portugal asserted that the discovery was within the bounds set forth in Papal bulls of 1455, 1456 and 1479. The King and queen of Castile disputed this and sought a new papal bull on the subject. Pope Alexander VI, a native of Valencia and a friend of the Castillian King, responded with three bulls, dated May 3 and 4, which were highly favourable to Castile. The bull ‘Inter
division between that country and Spain of the undiscovered non-Christian world; and subsequent treaties between these countries had recognized with modifications the allocation. Since 1580 the sovereignty of Spain had been extended over Portugal, and the Portuguese rights over Indian territories had passed to the Spanish Crown. But the Reformation\textsuperscript{57} had undermined the validity of Papal dispositions, and the revolt of the Netherlands\textsuperscript{58} involved the decision to strike a determined blow at Spain through depriving her of the monopoly of Eastern trade. The ambition and courage of Dutch merchants in association were displayed to great advantage in the expeditions of 1595-6 and 1598-9 to Java, and, if they were not to find a Dutch monopoly replacing that of Spain, early action by the merchants of London was plainly necessary. At a meeting at Founders’ Hall under the auspices of the Lord Mayor on September 22nd 1599, the vital resolution was arrived at to form an association to trade direct with India\textsuperscript{59}.

\textsuperscript{56} www.answers.yahoo.com/question \ accessed on 22.2.2014 – the 1493 Bull “Inter caetera” granted unlimited rights to Spain and the subsequent Treaty of Tordesillas (inspired by the Bull ‘Inter caetera) divided the world in half; everything 370 leagues west of the Cape Verde islands went to Spain, everything east went to Portugal.

\textsuperscript{57} http://elane.stanford.edu/wilson/html/chap3/chap3-sect3.html \ accessed on 22.2.2014 – the reformation in Europe (1500 – 1700) – in 1517 Martin Luther King, a German catholic priest at the university of Wittenberg, appealed to the Pope to correct abuses in the Roman catholic church about which there was already widespread concern within the church. When reforms were not forthcoming and Luther was excommunicated by the Pope for insubordination, religious dissension and wars erupted in Europe and continued intermittently for the next 200 years. Historians now refer to these events as Reformation. During this period, the Catholic Church was reformed and reorganized and numerous ‘protestant’ sects were separately established.

\textsuperscript{58} Netherlands was under Spain and was known as Spanish Netherlands

\textsuperscript{59} A. Berriedale Keith, \textit{A Constitutional History Of India 1600 – 1935}; Methuen & Co. Ltd London, 1936, p. 2
In securing this end, the Levant Company was clearly much interested. The first governor of the Company of Merchants of London which received the royal charter in 1600 to trade with East Indies, was also governor of the Levant Company. In these circumstances all that was contemplated by the merchants was the creation of an association to carry on trade by dispatching ships to Indian territories and by founding therein trading stations with the permission of the local rulers, on lines similar to those on which trade was conducted with the Ottoman dominions. There could be no question, as in the case of the patent granted to Sir Humphrey Gilbert in respect of Newfoundland, of the assumption of sovereignty over newly discovered lands. But the Crown was entitled in the view of the lawyers of the day to regulate by the prerogative foreign trade and the actions of its subjects beyond the realm, and on the basis of these powers the royal charter was issued. It conferred corporate character and juristic personality on the Earl of Cumberland, and the 217 knights, aldermen, and burgesses with him associated, granted them essential commercial privileges, and provided them with authority to govern themselves and their servants.

2.2.2 Early Years of the East India Company

The Company was authorized freely to traffic and trade 'into and from the East Indies, in the countries and parts of Asia and Africa, and into and from all the islands, ports, havens, cities, creeks, towns, and

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60 A trading company incorporated on 31 December 1600 for 15 yrs with primary purpose of exporting the staple production of English woolen clothes and importing the products of the east Indies – www.iranicaonline.org/articles/east-india-british

places of Asia and Africa, and America, or any of them, beyond the Cape of Bona Esperanza to the Straights of Magellan'. This right was to endure for fifteen years, but might be determined on two years' warning, if the trade did not appear profitable to the realm; otherwise a renewal for a further fifteen years was contemplated. It was to be an exclusive right, but the company might grant licenses to trade. Unauthorized traders, on the other hand, were to be liable to forfeiture of their goods, ships and tackle, and to imprisonment and such other punishment as might seem meet and convenient for so high a contempt of the 'prerogative royal, which we will not in that behalf have argued or brought in question'62. The legality of the grant of such a monopoly was not then seriously in question; and at that date the successful prosecution of trade with the East demanded the concentration of authority in the hands of a single body which could deal with native princes, regulate sailings, and contend against rival European traders.

The constitution of the Company was simple, falling within the type of 'regulated companies' as opposed to 'joint-stock companies'. In such companies members were subjected to certain regulations and enjoyed certain privileges, but traded on their own capital. In practice the Company in its early days functioned as a syndicate with a concession for the Indian trade, which it worked by forming minor groups from among its members who found the capital for each separate voyage, and whose liability was normally limited to the voyage for which they had subscribed, though they might be forced to contribute to a further venture if fresh capital could not be raised from a new group of subscribers. After 1612 the subscribers threw their contributions into a joint stock, though not yet on a permanent basis, the joint stock

62 Supra Note 59 at p. 3
being formed for a series of voyages only. Membership of the Company was accorded in the charter to those who had purchased a share in the first voyage, and was granted subsequently to such persons as took up shares in later voyages, the amount contributed varying from time to time. Membership could also be claimed by the sons of members on reaching the age of twenty-one. Further, membership could be secured through service or apprenticeship and the payment of a small sum on admission. Or members might be admitted in return for a fixed cash payment, usually of a hundred pounds, and membership was from time to time conferred on distinguished individuals who were deemed likely to be able to aid the Company.

2.2.3 **Growth of Company Powers**

The control of the Company’s business was democratic in principle. The Company was authorized to elect annually a governor and twenty-four committees, the precursors of later directors, who were to have the direction of the Company’s voyages, the provision of shipping and merchandises, the sale of merchandise brought to England, and the managing of all other things belonging to the Company. Other officers were soon added, including a deputy governor, secretary, and treasurer. In general the governor and committees managed the general detail of the voyages, but they called together a general meeting of the members when they deemed it necessary. To the Company were conceded certain limited powers of a legislative character, based on those recognized at the time as appropriate for municipal and commercial corporate bodies. The Company might assemble themselves in any convenient place, ‘within our dominions or elsewhere’, and there hold court for the Company and its affairs, and might ‘make, ordain, and constitute such and so many reasonable laws, constitutions, orders, and ordinances, as to them or
the greater part of them being then and there present shall seem necessary and convenient for the good government of the said Company, and of all factors, masters, mariners, and other officers, employed or to be employed in any of their voyages, and for the better advancement and continuance of the said trade and traffic.63

They were further authorized to impose such pains, punishments, and penalties by imprisonment of body or by fines as might seem necessary or convenient for the observation of such laws and ordinances. Both laws and punishments must be reasonable and not contrary or repugnant to the laws, statutes or customs of the realm of England. It will be seen that the power given is essentially a power of minor legislation, forbidding any fundamental alteration of the principles of English law, and limited drastically by the character of the punishments which could be inflicted in respect of contraventions. The limited character of the Company’s authority is clearly marked in the earliest copy of such laws extant that printed in 1621. They assert in accordance with the charter the illegality of private trade and order factors to seize goods so shipped and to send them home, and require that all presents made by foreign princes, rulers, or commanders to members of the Company shall be brought into the general account of the Company.

It is important to contrast the terms of this grant with those made to the companies or individuals who contemporaneously were seeking to establish themselves in the newly discovered Western lands. The charter of Charles I to the governor and company of the Massachusetts Bay in New England confers on the general meeting of that company the right to elect officers and admit members, but the legislative power is in wider terms, ‘to make Laws and Ordinances for

63 Supra Note 59 at p. 5
the Good and Welfare of the said Company and for the Government and Ordering of the said Lands and Plantations and the People inhabiting and to inhabit the same'. There is here unmistakably a definite power to legislate for and govern territory, which is not contemplated in the case of the London Company64.

The powers of the London Company were manifestly unequal to the situation unless supplemented, but the Crown made good this defect by a further exercise of prerogative. For each voyage the Crown granted to the 'General' in command of the vessel the right to inflict punishment for capital offences, such as murder or mutiny, and to put in execution martial law. This was followed up by a royal grant of December 14th 1615, authorizing the Company itself to issue commissions to their captains with the important proviso that in capital cases a verdict must be found by a jury. The power, it will be seen, was intended to cover the case of the maintenance of discipline on board ships, but as soon as the Company established on the Indian coast trading settlements the question of maintaining discipline inevitably arose. In their transactions with the natives of India the Company's servants were of course subject in the absence of agreement to the contrary to the control of the native ruler, but it was not to be expected that the local authority would concern itself with disputes arising among the members of a foreign settlement. James I, therefore, on February 4th 1623, extended the power of the Company by authorizing it to grant commissions to their presidents and chief officers for the punishment of offences committed by the Company's servants on land, subject to the same provision for trial by jury in capital cases, thus, at last, placing the Company in the position to

64 ibid
provide more or less effectively for the due government of its servants, both on the high seas and in India.

Under the charter the Company was established on a regular permanent joint-stock basis, and voting power at its meetings was accorded to each member on the basis of one vote for every 500 subscribed by him. To the Company thus reorganized, and enjoying the royal favour largely through the influence of the famous economic expert Sir Josiah Child, the King accorded wide powers which recognized the extent to be noted later of the Company's effective authority in India. It was recognized that the Company owned fortresses and not merely trading factories. They were authorized to send ships of war, men, and ammunition for the security of their factories and to erect fortifications and supply them with provisions and ammunition free of export duty, and to transport volunteers to garrison them. They might choose commanders and officers and give them commission under their common seal or otherwise to make peace or war with any non-Christian people in any places of their trade for the advantage and benefit of the Company and their trade. They were to exercise power and command over their fortresses and to appoint governors and other officers. They might govern their employees in a legal and reasonable manner and punish them for misdemeanour and fine them for breach of orders\textsuperscript{65}.

The trading monopoly of the Company was reaffirmed; they might seize unlicensed persons and send them to England, where they might suffer such punishment as the laws would allow. In addition to the authority over their servants a general judicial authority was given to the governor and council of each factory 'to judge all persons belonging to the said governor and Company or that shall live under

\textsuperscript{65} Supra Note 59 at p. 7
them, in all causes, whether civil or criminal, according to the laws of this kingdom, and to execute judgment accordingly’. In any place where there was no governor the chief factor and council were empowered to send offenders for punishment, either to a place where there was a governor and council or to England. The same power to send persons as prisoners to England was accorded by the charter in the case of appeal being made against their sentence by persons in the employment of the Company, when punished by ICS officers.

The chief advantage of this provision lay in effect in the recognition which it accorded to the expulsion from India of unruly servants. The extended authority, both political and judicial, accorded to the Company by the charter of Charles II was further reinforced on the occasion of the transfer to the control of the Company of the island of Bombay, which was ceded by Portugal by the marriage treaty of 1661. The prerogative of the Crown to govern a ceded colony was absolute, and the King accordingly was in the position to confer on the Company full sovereign rights over the territory and the inhabitants of the island as well as over the servants of the Company. The Company, therefore, was authorized through their general court or court of committees to make laws, orders, ordinances, and constitutions for the good government of the port and island and of the inhabitants thereof. They were authorized by their governors and other officers to exercise judicial authority. Moreover, they were to have power and authority of government and command in the island with power to repel any force which should attempt to inhabit precincts without license or to annoy the inhabitants.
2.3 CORPORATE CRIME

The relevancy of studying the growth of East India Company must be briefly highlighted before going further. The study shows how the Company structure gradually developed in response to needs and requirements, and how the concept of Joint Stock took shape. In addition and more importantly, the manner in which East India Company was authorised to do trade with the East including Asia and Africa and the gradual vesting of powers in the Company officials, initially to enforce English law on their subjects outside the English territory and thereafter, even to fight a legitimate war with the native rulers, shows that the seeds of corporate imperialism were sown right from the beginning when the East India Company was granted the right to carry on overseas trade. Besides, many of the activities of British East India Company went beyond the royal authorisation to do legitimate trade with the permission of the native rulers. Most of such acts can be classified as crimes even by the standard prevailing in those times which buttresses the fact that Company form of organisation has always been prone to the ill effects of divorce between ownership and management, and the lure to secure more and more profits. Just to give an example, by the 1830's, the English had become the major drug-trafficking criminal organization in the world; very few drug cartels of the twentieth century can even touch the England of the early nineteenth century in sheer size of criminality. Growing opium in India, the East India Company shipped *tons* of opium into Canton which it traded for Chinese manufactured goods and for tea. This trade had produced, quite literally, a country filled with drug addicts, as opium parlours proliferated all throughout China in the early part of the nineteenth century. This trafficking, it should be stressed, was a criminal activity after 1836, but the British
traders generously bribed Canton officials in order to keep the opium traffic flowing. The effects on Chinese society were devastating. In fact, there are few periods in Chinese history that approach the early nineteenth century in terms of pure human misery and tragedy. In an effort to stem the tragedy, the imperial government made opium illegal in 1836 and began to aggressively close down the opium dens66.

We tend to think of the "drug problem" as a modern phenomenon. But a century ago, illegal drugs brought an end an empire that had lasted for thousands of years. In 1793, China was the home of a sophisticated culture and a rich history. Among other remarkable achievements, China invented movable type, kites, and gunpowder. They perfected porcelain, silk and tea production. Great Britain and other European nations, desiring her silk, tea and porcelain, wanted badly to trade with China. China, however, wanted nothing to do with Europe, and even refused to see European diplomats. Finally in 1793, a British diplomat was successful in reaching the Chinese court. He told the Chinese of the wonderful products of his country, convinced that once they really knew what Europe had to offer, they would quickly agree to engage in trade. China, however, was unmoved. In a letter to King George, the emperor said,

. . . As your Ambassador can see for himself, we possess all things. I set no value on objects strange or ingenious, and have no use for your country's manufactures. . . Our Celestial Empire possesses all things in prolific abundance and lacks no product within its own borders. There was therefore no need to import the manufactures of outside barbarians in exchange for our own produce. But as the tea, silk and porcelain which the Celestial Empire produces, are absolute necessities to European nations and to yourselves, we have permitted, as a signal mark of favour, that foreign hongs [merchant firms] should be established at

66 http://richard-hooker.com/sites/worldcultures/CHING/OPIUM.HTM accessed on 3.4.2010
Canton, so that your wants might be supplied and your country thus participate in our beneficence.

They would sell Europe their silk, tea and porcelain, but would buy nothing in return. Because Chinese goods were so sought-after in Europe, an imbalance of trade developed. European gold and silver went to China to import goods, but none returned because there was no possibility of export. This was unacceptable to the British and they desperately looked for a solution. The solution to Britain’s problem was opium. Although opium had been used in China for medicinal purposes for a long time, it had not been used as a recreational drug. The British introduced opium to China in 1825, and soon, not surprisingly, Chinese began to be addicted to the drug. The emperor outlawed the possession, use, and trade in opium, but the profits were so immense, that an illegal trade quickly developed. The East India Company in India supplied all the opium the Chinese wanted and the Chinese government was unable to stop the smuggling. The balance of trade gradually reversed.

In 1839 the Emperor ordered Commissioner Lin Tse-Hsu to put a stop to the opium trade. Lin wrote to Queen Victoria, appealing to the British sense of justice and compassion:

We have heard that in your own country opium is prohibited with the utmost strictness and severity; this is a strong proof that you know full well how hurtful it is to mankind. Since then you do not permit it to injure your own country, you ought not to have the injurious drug transferred to another country, and above all others, how much less to the Inner Land! Of the products which China exports to your foreign countries, there is not one which is not beneficial to mankind in some shape or other. There are those which serve for food, those which are useful, and those which are calculated for re-sale; but all are beneficial. Has China (we should like to ask) ever yet sent forth a noxious article from its soil?
He received no reply. Left on his own to solve the problem, Lin ordered the destruction of a large supply of opium stored on Chinese soil. (The Chinese had allowed the British one port in which they could trade with China). The British were outraged, and the first Opium War began. Faced with British industrial weaponry, it was no contest, and Britain easily defeated the Chinese. As part of the settlement of the war, China was forced to agree to open up new ports for trade, and to surrender the island of Hong Kong. A second Opium War was launched by Britain in 1856, forcing more concessions on the Chinese. Among other humiliations, the Chinese government was no longer able to hold foreigners accountable under Chinese law for crimes committed in China. The proud Central Kingdom had lost the ability to control trade and foreign nationals within its own borders. It is thus apparent that how crimes committed by British East India Company resulted in the downfall of a hugely successful Chinese empire.

We would now revert to the study the development of corporate structure which will reveal the slow but steady march of the Company form of organisation as the dominant form of commercial organisation and the freedoms granted to it for carrying on its operations/ activities which eventually transformed the corporate structure into a tool of exploitation.

### 2.4 CONSOLIDATION OF COMPANY FORM OF ORGANISATION

By the beginning of 18th century, speculative activities reached a high point which in turn paved way for malpractices. There was a danger of misrepresentation and involves considerable risk taking. As the name itself suggests, speculative trade is generally in relation to unpredictable markets. Speculative trade
frantic boom in company floatation. Large unincorporated companies with transferable stock appeared almost overnight but most of them had a short life span and burst like water bubbles i.e. giving high hopes to the investors, especially small shareholders and then vanishing from the market place either due to business failure or by committing deliberate fraud. In this regard, the story of South Sea bubble is a clear illustration of the gambling mania of the period. The Company South Sea was set up in 1710 with the object of exploring the trade with South Africa. It launched a scheme to acquire all the national debt in exchange for the company shares. The scheme turned out to be a failure. In 1720 the South Sea Company Directors were summoned before the Parliament and fined for fraud.

To control the speculative fever, the British Parliament enacted a statute which is popularly known as the *Bubbles Act 1720*. The Statute which was clearly negative in its approach was the first attempt by the British law makers to frame a Company Act. For example, Section 18 of the Act provided that ‘all those undertakings as were therein described, tending to the common grievance, prejudice and inconvenience of His Majesty’s subjects should be illegal and void’. The corollary was that Associations purporting to act as corporate bodies but without legal authority and the raising of transferable stock by such bodies were manifestly to the prejudice of the public trade and commerce of the Kingdom. Broker dealings in illegal companies were also prohibited. The effect of Bubbles Act is beautifully summed up by Holdsworth who commented – “what was needed was an Act which made it easy for joint stock societies to adopt a corporate form and at the same time, safeguard both the shareholders

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69 However, companies and partnerships established before 1718 were exempted from the purview of the act
in such societies and the public against fraud. What was passed was an Act which deliberately made it difficult for joint stock societies to assume a corporate form and contained no rules at all for the conduct of such societies”.

Repeal Of Bubble Act – The Bubble Act had a restraining influence on the commercial activities of the period following it. Since the Bubble Act made it a criminal offence to form any company presuming to be a corporate body, the commercial community was forced to operate within the limits of the unincorporated partnership. However, towards the end of the century, Parliament showed willingness to incorporate by special Acts. It was limited to activities such as Banking, Insurance and canal works. The only alternative thus available for ventures requiring large capital was the unincorporated partnership. This resulted in the re-birth of the ‘deed of settlement companies’ which the Bubble Act attempted to suppress.70

In the latter half the 18th century, the unincorporated joint stock company with a large number of shareholders emerged as the dominant type of trading association. In course of time, many of them operated with transferable shares. The Bubble Act was conveniently forgotten. At the turn of the century, speculative activities again touched a new high. In many cases, the company promoters defrauded the public. State intervention to regulate the trading activities became inevitable. The first step taken by the government was to initiate prosecution against a few unincorporated associations with transferable stock for violation of the Bubble Act though the same was forgotten almost but was revived due to the fact that unincorporated partnerships were again defrauding public

70 Bubble Act expressly exempted genuine partnerships from its ambit. It was thought that large unincorporated bodies with joint stock were not hit by it provided that some restrictions were imposed on the transferability of shares.
investment. In two of such prosecutions, the Court took the view that unincorporated joint stock companies were illegal. But some other judges refused to hold that all unincorporated bodies with transferable shares were illegal. The conflicting decisions also contributed to the confusion prevailing regarding the status of joint stock companies. It was increasingly felt that active governmental intervention was essential to bring law in tune with the commercial urge of the period. The first step in this regard was the repeal of the Bubble Act in 1825.

The repeal of Bubble Act was also followed by a slump. This was followed soon by the appearance of Joint Stock Companies which again began to dominate the commercial scene. It was thus clear that it was inevitable to have trading associations through which capital could be easily raised for commercial projects. Consequently, the Trading Companies Act 1834 was enacted. It empowered the Crown to confer by letters patent all or any of the privileges of incorporation without actually granting a royal charter. The Chartered Companies Act 1837 re-enacted the provisions of the Trading Companies Act 1834 by specifically providing that the liability of the members could be limited by the letters patent.

In 1841, a Parliamentary Committee was appointed to study and report the functioning of joint stock companies. Based on the report of the Committee, the Joint Stock Companies Act 1844 was passed which is popularly known as The Gladstone's Act. This Statute formed the basis of modern day Company law by introducing three cardinal principles:

1) **Incorporation by mere registration** - The Joint Stock Companies Act provided an easy and cheap method for the

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71 Gladstone, the then President of the Board of Trade became the Chairman of the Committee.
incorporation of commercial associations which otherwise could only be granted through a royal charter or an Act of the Parliament. This new Act provided that every association satisfying the stipulated requirements was entitled to the incorporated status.

2) **Compulsory Registration** – The Act also provided that companies with membership above 25 or with shares transferable without the consent of all the members could function only as incorporated bodies.

3) **Publicity** – The Act incorporated the principle of disclosure to provide effective guarantee against fraud and other malpractices. It insisted that various information regarding the company and its affairs should be periodically supplied to the Registrar of Companies.

The biggest advantage of this Act was that incorporation was no more a privilege which could be afforded only by those who could influence the Crown or the Parliament. It transformed into a legal right subject to the fulfillment of the stipulations of the Act. Although the Joint Stock Companies Act 1844 was landmark legislation, yet it suffered from a major defect which was the absence of limited liability and which essentially distinguishes a Company from a Partnership Firm. Even under the new Act the members continued to be fully liable for all the debts and liabilities of the Company, quite much like a partnership firm.

This drawback was removed by the Limited Liability Act 1855 which fulfilled the long pending demand of the business community to have limited liability in large scale commercial ventures. However, stringent conditions were put for a Company to be able to have limited liability for its members – (a) the Company had at least 25 members each holding a minimum of shares of nominal value, paid up to 20 percent;

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72 Liability limited to the value of the shares held by a subscriber or member
(b) not less than three fourth of the authorised capita was subscribed; 
(c) the auditors of the Company were approved by the Board of Trade; 
and (d) the word ‘LIMITED’ was added to the company’s name. 
However soon after, the Joint Stock Companies Act 1856 was passed 
which was more liberal and which repealed the earlier Acts of 1844 
and 1855. Under the new Act, deed of settlement which was the 
constitutional document to be registered with the Registrar for 
incorporation was split up into two documents– (1) Memorandum of 
Association and (2) Articles of Association. 
The next important statute was the Companies Act 1862. 
This was a consolidating Act which 
included a model form of Articles of Association which the Company 
could adopt instead of drafting its own articles. With this enactment, 
the pendulum of corporate enterprise reached the extreme end of 
liberty. Then onwards, it has been a movement in the opposite 
direction as subsequent company/corporate law legislations have 
been trying to impose more and more restrictions on companies and corporate activities.

At this point, it will not be out of place to mention that the distinction 
between ownership and management resulted from the nature of a

73 **Lord Bramwell** commented on the new Act – the statute denotes the triumph of the champions of laissez-faire doctrine who pleaded that if there was a rule established by reason, authority and experience, it is that the interest of the community is best consulted by leaving to its members, as far as possible, the unrestricted and unfettered exercise of their talents and industry. **Prof. Gower** also commented on the effect of the Statute of 1856 – Passed as it was in the heyday of laissez-faire, it allowed incorporation with limited liability to be obtained with freedom amounting almost to license; all that was necessary was for seven or more persons to sign and register a memorandum of association.

74 According to **Sir Francis Palmer**, this statute was the ‘magna carta’ of corporate enterprise.

75 Companies Act 1908, Companies Act 1928, Companies Act 1948, Companies Act 1967, the European Communities Act 1972, the Company Act 1985, the Competition Act.
Company or even a deed of settlement company. One might even put it that the philosophy behind a joint stock company is the reason why the Company form of organisation makes a distinction between ownership and management. The pooling of resources by a large number of people essentially means that technically they all have an equal and individual right in determining the manner in which the pooled resources should be applied. However, not all contributors have the expertise or even knowledge of running a successful business. Going a bit further, many of the contributors might not even be interested in decision making except that they would want to have a share in the profits which is essentially a return on their investment. Proper application of pooled resources with a view to earn profits, which can be distributed amongst investors as also help in the growth of business, is thus of fundamental importance in a Company\textsuperscript{76}. This in turn forces the need to have a specialised body consisting of persons adept in management of finances and in administration so that they take care of the day to day functions as also the crucial decision making, subject of course to the overall will of the investors manifested through the forum of annual general meetings. The advantage of distinction between decision making and ownership is obvious. However, there is little acknowledgment of the fact that corporate crime has its genesis in this distinction which has been briefly mentioned above.

The entrustment of decision making in the hands of specialised management body leads to sheer indifference on the part of the

\textsuperscript{76} It does not mean that prudent application of funds and earning profits is not fundamental to small business ventures but in a Company, the pooled resources are large and those who own the resources are not capable of managing it and hence, the management is in a sense in a fiduciary relationship with the investors owing a far greater degree of care and caution.
investors i.e. shareholders, especially small shareholders who remain solely concerned with the rate of return on their initial investment. In the process, they have little inclination to see as to whether the practices of the company are legal or ethical and hence, justified. This lack of effective supervision gives such a free run to the management that they have little fear of any reprimand from the shareholders. Once the decision making is in their hands and the obvious (and huge) individual gains resulting from malpractices, there is little to stop the management from going astray and indulging in corrupt practices. As will be explained in detail in the next chapter, the bulk of blame of corporate crime or corporate malpractices has to be borne by the management. Of course, management consists of independent Directors but there is adequate representation of the institutional investors alongside the majority shareholder who in both cases, is usually a Company only, being driven with the mad race to achieve as much financial gains as possible, even at the cost of peril to human life and perpetuation of human suffering.

It is most ironical, as will be discussed in subsequent chapters, as to how the drive for efficiency resulting in division between ownership and management ultimately leads to culpable behaviour of the Corporations.