



POLITICAL THEORY OF CORPORATIONS: ENTITY SHIELDING AND GOVERNANCE IN CORPORATIONS

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Abstract

The corporation is a business model allowing certain individuals to run a business in a state-like fashion. Since the inception of the concept, liberalism has understood the dangers of such institutions, as evident in the growth of the East India Company, a corporation with its own army and legislative powers. This prompted liberals to strip certain powers away from these corporations, while allowing for some privilege to remain. One such privilege was the concept of private contracts, which ultimately led to corporations being deemed as liberal private entities. From here, we seek to understand the political theory of the corporation. This private ownership or individuality through contract is paradoxical, as it requires civil government to grant it its governing authority. The theory suggests that the corporation should not be placed in the category of private or public, but rather have its own category of corporate or a category of franchise authority.

Introduction

A corporation acts as a private legal entity, with legal recognition similar to that of a citizen. Meaning the corporation, under its legal name, acts as a buyer and seller of assets. The actual owners or shareholders do not bear importance, as it is the corporation that is deemed a legal owner of the bought assets. The entity in itself is separate from the owners and shareholders. The investors have a stake in the assets, but do not directly own them. Rather, a corporate fund consisting of capital from all involved parties is used to purchase assets, usually through the stock exchange. Land, a legal framework, a board of managers, and a corporate collective fund are all necessary prerequisites for a private entity to become a corporation. Toyota Motors and Coca-Cola are examples of business corporations.

The Relation between Corporations and Government

To understand why corporations ought to be understood in different dimensions, other than liberal private ownership, we develop an understanding of two major premises that distinguish



corporations from private entities.

1. Corporations function and run as governments do
2. Corporations require property, and an individual governing authority, both of which are given by the government. I.e., corporations are an offshoot of governments rather than a sole private entity.

Corporations cannot be solely understood in business terms, as many legal frameworks are needed to make privately owned entities into corporations. These include a managerial hierarchy, ownership of property, the right to be treated as a legal entity (one that can sue and be sued), and the right to enforce certain bylaws and rules. These rights make corporations individual entities, with governing powers over the property they own and the people they employ.

Here, we understand why corporations cannot be understood as liberal entities, as these rights make collective governing possible rather than individualism.

Corporations become governing entities in two dimensions, including governing the deployment of labor and capital, and the actual legal frameworks giving them the right to govern.

Corporations strike similarities to constitutional republics. The world's First Corporation, the Dutch East India Company, was set in line with the Dutch Republic. Similarly, the East India Company was organized in line with the parliamentary system of Britain, with powers to elect its own legislative body, mint coins, and even engage in military roles. Previously, such corporations would govern themselves but fulfill a mandate of the ruling crown or government. Whereas in modern times, corporations have become democratized by making use of self-management.

The theory further argues that Corporations are governmental in origin as well. Meaning the government charters their authority to self-govern. But it must be noted that corporations essentially refer to a collection of contracts between different investing parties. The involvement of the government, therefore, is only a way of legitimizing these contracts.

Strong Entity shielding and limited liability

Corporations need to be chartered by the government, but are also able to use liberal ideals, such as individual liability, to protect themselves. This essentially means corporations can separate their property and liabilities from investors. This has the added benefit of evading costs that would be incurred if the entity were an actual partnership. Business Corporations, in particular, use joint stock mechanisms to raise capital from different contracting individuals. However, this raised capital is accumulated into one single fund. This very idea of keeping the governing power in the hands of the corporation, whilst accumulating wealth in terms of shareholders, is not legal in essence. As the owners are separate entities from the corporation, they are not fully liable for the corporation's actions, losses, etc. To collect all raised capital into



one cumulative fund is allowed as a matter of privilege.

In contrast, a partnership is based on shared decision-making between partners or shareholders. Importantly, when a shareholder decides to leave a partnership, they liquidate the shares by selling off to other investors, usually existing shareholders. Whereas the amount invested in a corporation is usually not the same amount investors get if they decide to transfer or sell off their investment. This is mainly because the assets bought with the investor's money are locked in as property or ownership of the corporation, citing the concept of corporate fund mentioned previously. This leads to security in assets, as even if some investors decide to pull out their initial investment, the assets procurement remains unchanged. This leads to assets becoming specialized. This protection from liability works in favor of the shareholders as well, mainly due to the concept of limited liability. This so-called investor shield makes investing in corporations relatively easy for small shareholders as well. These two make corporations tradable, I.E, the stable nature of locked assets, tempts investors. Had it not been for these two concepts of investor shield and limited liability, the actual worth of stocks would fluctuate with the changing financial conditions of shareholders.

However, shareholders do have the right to tort claims or claims of compensation in case of wrongdoing. Similarly, entity shielding does not apply to all members of the corporation. These concepts of asset lock, limited liability, and entity shielding are what distinguish corporate assets from personal assets. It can be argued that these are not natural or even neutral concepts, but ones that are safeguarded and guaranteed by the government. These same ideas give personhood to corporations. This does not mean that corporations need government to exist, but it should be noted that other business entities, such as partnerships and proprietorships, are identified with certain individuals who own them, whereas corporations enjoy a sort of anonymity due to government-given privileges. Corporations are private entities, but need the state's hand to flourish. This is because the ideals of limited liability and entity shielding are allowed to exist due to the government's permission. Partnerships and proprietorships raise capital by selling shares, similar to corporations, but the above-mentioned concepts create a specific parameter only for corporations. The major difference is not the self-autonomy in terms of day-to-day business dealings, but in the security of assets, corporations enjoy.

Corporations do not react to market forces the same way other private entities do. This is because governments have different rules for property and liabilities. Therefore, to treat corporations as liberal entities is purely theoretical. The major negligence by governments, in terms of corporations, is treating and viewing shareholders as owners of the corporation. The true owners enjoy different privileges as compared to the shareholders; at the same time, to improve the performance of these corporations, the shareholders are expected to perform. In our understanding of ownership, we presuppose that every time an individual is referred to as an investor or shareholder, they are owners of or at least have some stake in the ownership of said enterprise. While this is the case in partnerships, it is not in the case of corporations. To assume



that shareholders of corporations are owners causes us to believe that corporations are, in fact, liberal economic entities. But to own, in economic terms, certain prerequisites must be met, such as the option to lend, borrow based on, use, and profit from the “ownership.” Partnerships can be deemed ownership stakes, as a partner can decide to pull out capital and, in turn, reduce the assets of the firm. As discussed earlier, asset lock does not allow for this to happen. The shares in corporations represent stocks of assets that cannot be transferred or liquidated. Instead, the so-called governing body of corporations or the hierarchical management, in simple words, decides the fate of assets. Meaning the complete profits are dispersed to the shareholders as dividends on investment rather than profits from ownership. The true owners of the corporation are the creditors who sell the shares and the management that looks after the assets. This relation of actual owner and shareholder is similar to that of the government and the voter. The voter can influence the individuals in charge, but ultimately, the individuals governing have the power. A shareholder has the same power in corporations about asset management as the citizen does on the fiscal budget parliament passes, i.e., close to none.

Implications

Owners of property are usually the bearers of taxes and the maintainers of that property. An economy based on ownership of private property is primarily a series of different land economies under a collective system (usually through legislation and regulations implemented by governments) However, land owned by corporations, described as socialized property, has different sets of rules. Corporations separate the owners and control, the owners being actual investors and the controllers being asset managers.

Internal Style of Governance in Corporations

It was understood before that corporate managers, being part of a board of directors or executives, would lead their corporations and decide certain important aspects, such as investment time, turnover, hiring of employees, etc. However, it is now assumed that shareholders, having some power, decide on who will be part of this board of management. Previous sections have helped us understand, but this is not the case. Shareholders do not own the corporation, nor do they own shares in leadership, rather shares of assets, which are decided upon by corporate asset managers. It is further argued that even the corporate owners do not have a direct link to leadership; rather, it is the charter of corporations, mandated by the government that acts as the ultimate blueprint for internal governance within the corporations.

Corporate Charter

This is a legal document registering certain private entities as corporations. Whether the firm is for-profit or non-profit, how many shares can be sold, the actual name of the corporation, and the location are some of the basic requisites of such charters. Again proving that while private entities, of corporations, are seen as liberal institutions, they have an almost paternal relation to the government.



Dual Governing Authority – Management

The managing authority acts as internal governance, deciding on two major key issues. Firstly, decisions regarding employees and, secondly, decisions regarding assets. The first is made possible through extensive labor contracts with non-negotiable aspects. This basically means that unless the firm makes the employees do illegal work or directly harms them, they might have no space for tort claims. Other than this, the employees sign off their freedoms to the management, as it decides when and how the labor force will be used. This, in turn, diminishes ideals such as individual decision-making power. The second is the power management has over corporate assets. Ownership of assets is usually understood as ownership over the status and placement of those assets. However, corporations enjoy the privilege of including or excluding shareholders from deciding upon asset status. This is usually done either through references in contracts, which are signed upon, even though they reduce shareholders' power, or through the grounds that management is the best suited for making decisions regarding assets, in line with market values and situations.

Conclusion

The main purpose of the paper was to understand why corporations ought to be understood outside of the domain of private and public, but in the category of their own, known as corporate. The two major premises, i.e., that corporations act as governments and need the aid of governments to exist, were proven in the arguments above. This ultimately leads us to understand that while the actual government running a country is two-tier, with a federal ruling power and sovereignty over its land and territory, there is a third tier of semi-autonomous government, like private entities. Corporations are financed by private entities, yet the government gives them their contractual individuality. The shareholders decide the leadership, but based on a state-given charter. This is precisely why corporations cannot be placed in the category of public or private, but rather have their own category. The major purpose of this category or theory of corporation is to make clear why corporations ought to be understood in different dimensions, other than those of privately owned entities or even state-mandated enterprises.



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