The Berle−Means theory

The Berle-Means Thesis is a theory named after A. Berle and G. Means. It has to do with governance of public corporations in which the board of directors is put in charge of governance. The owners of the public depend on the board of directors to run the operations of the corporation. According to this theory, the interests of the owners of the public corporations are represented by the board of directors. The Berle-Means Thesis describes a structure of governance where there is a separation between the ownership and control of a public corporation.

In 1932, Adolphe Berle and Gardiner Means published a book that would have a huge impact in the vision of corporate ownership. In 'The Modern Corporation and Private Property', it has been argued that US modern public corporations are subject to a separation between ownership and control. Accordingly, shareholders have only a passive role in the direction of the corporation due to their very little influence in the decision-making. Therefore, control is left to the managers giving them the free charge of running the corporation.

In Berle and Means' view, the separation of ownership and control can be explained by two main factors. Accordingly, the higher and higher rise of public corporations and dispersed ownership has contributed to the fact that no one shareholder has enough shares to be able to control the company. Further, shareholders have only few opportunities in the case of a board's election. He can refrain from voting, he can attend the annual meeting and vote his stock, or he can sign a proxy transferring his voting power to certain individuals selected by the management of the corporation, the proxy committee. As a matter of fact, Berle and Means have outstandingly demonstrated the large passivity characterising the role of shareholders in modern corporations.

While some authors claim the necessity of having checks and balance on managers' acts, others state that it is incorrect to consider negatively the shareholders' passivity. According to the Berle and Means' thesis, some authors claimed the positive effects of the separation between ownership and control in accordance with efficient corporate governance. Indeed, they argue that the separation is natural and inevitable, because the process of the public modern company itself causes it. Moreover, the separation of ownership and control is well justified by the fact that managers are professionals more trained and qualified than shareholders for such a role.

Additionally, it is doubtful to believe that shareholders will act at any time for the best interests of the company. In this view, it has been argued that shareholders can frequently be motived by suspicious incentives, which may be detrimental for the corporation. Indeed, "investors may prefer liquidity to control, especially when stock markets provide them with an easy way of flowing in and out of a given company”

Furthermore, as soon as the management acts without checks, this will lead to the suppression of the majority abuse towards minority shareholders. An absence of shareholder control leads to the fact that managers are in better place to eliminate any kind of oppression and make greater balance between the different stakeholders.

In addition, in case of mismanagement, opponents of shareholder control argue that the market will control mismanagement effectively, since market forces prevent and limit managerial abuse of misuses of power. Moreover, maladministration from managers would be harmful to their own self-interests “as it will lead eventually to the bankruptcy of the firm and to managers’ future employment prospects becoming spoiled, as a result of competition from better managed rivals”.

Considering the above-mentioned reasons, shareholders’ passivity is not only inevitable, but also a necessary way for the whole bien-être of the company. Based on the Berle and Means’ theory, proponents argue that the most efficient corporate governance cannot run in a system in which shareholders control management.

Berle and Means influenced corporate legal theory in two important ways. First, they identified the central problem of corporate law, namely the separation of ownership and control. The shift in power to management gave managers control over property that was, in fact, owned by someone else, After Berle and Means, the biggest problem faced by corporate law was how to protect shareholders' interests. Second, Berle and Means implicitly claimed that it is economics that drives corporate law. They argued for this in the second part of their book by showing that the concentration of economic power in a corporation conjoined with the separation of ownership and control actually led to a decline in legal control over managers. Economic considerations of the corporation's role in the market influences corporate law. This claim has important normative implications. If it is truly economics that drives corporate law, then large, technological economies should eventually develop similar corporate legal structures. Corporate governance structures should "progress" towards achieving a vibrant stock market and diffuse ownership of large companies, with strong managers and weak financiers. This is how the Berle and Means theory of corporate law is evolutionary. Economics should inevitably create a corporate structure with strong managers, weak shareholders, and few legal controls over the managers. Berle and Means's theory that corporate governing structures would evolve until managers held all the power endured for sixty years. The governance structures of U.S. corporations are the best evidence for the validity of this evolutionary theory.