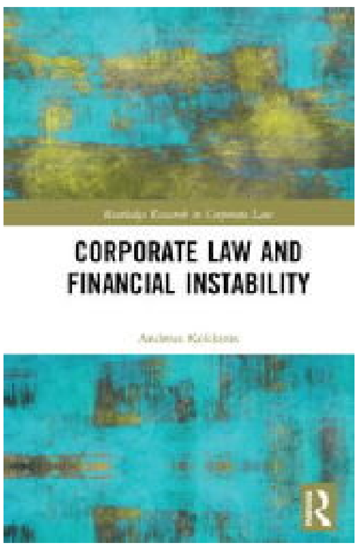
Research explores how corporate law undermines financial stability

December 4 2017, by Sheila Kiggins



Credit: University of Warwick

With the effects of the 2007 credit crunch still being felt around the world, a new book by Dr Andreas Kokkinis, Assistant Professor in the University of Warwick's School of Law, explores whether traditional models of corporate governance fail to promote financial stability.

Corporate Law and Financial Instability (Routledge, 2018) explores the tension between corporate governance systems focused around shareholders who want to maximise their returns, and prudential regulation where risk-taking must be controlled in order to safeguard financial stability.

Virtually all large banks and other financial institutions in the UK and internationally are public limited liability companies whose shares are listed on one or several stock exchanges. As such, their corporate governance and, in particular, the incentives faced by their directors and senior managers are to a significant extent determined by corporate and securities law rules.

But, as Dr Kokkinis explains: "The corporate law regime, which focuses on shareholder empowerment and profit maximisation, encourages risky behaviour that may be in the best interests of individual shareholders, but is not in the broader public interest when it comes to the banking sector."

Dr Kokkinis' analysis suggests that: "Radical legal reform of financial institution directors' and senior managers' civil liability is necessary. This should take the form of a statutory provision making directors and senior managers liable to contribute to the assets of a financial institution that has failed up to a maximum amount."

Banks and other financial institutions are very different to typical corporations. In his book, Dr Kokkinis explains how the business of banking, its assets, its capital structure and its regulatory framework are very different to generic companies, and how these differences limit the ability of shareholder and creditor governance to curb excessive risk-taking by banks.

He said: "The limited ability of shareholders and creditors to restrain risk taking by financial institution managers, combined with the incentives the latter face to take excessive risk, means that financial institutions are likely to take even more risk than fully informed investors would accept. This has a knock-on effect on other financial institutions due to systemic risk, and can undermine the stability of the financial system as a whole."

Although the book's main focus is on UK law, much of the policy argumentation is relevant globally. Appropriate international comparisons are drawn, and analysis of EU law and regulation is included.

Dr Kokkinis added: "This book brings together most of my research over the best part of the last decade. Of course, it is not up to me to say if it is good or not, but I can definitely say that I have put all my mind and all my heart to it. I hope that colleagues and students will enjoy reading it."

More information: Corporate Law and Financial Instability (ISBN 9781138289130) is part of the Routledge Research in Corporate Law series: www.routledge.com/Corporate-La … p/book/9781138289130

Provided by University of Warwick

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