COLLECTIVE BARGAINS FOR CORPORATE CHANGE

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Abstract

What changes in corporate structure are possible through collective agreement? Traditionally unions have sought to negotiate better terms and conditions at work through collective contracts. Their sustainability varied with the power of unions and the approach of the courts. Less attention has been given to changing enterprises from within, by seeking amendment of corporate constitutions. This article presents the theoretical and historical background to collective bargains for corporate change, and explains the general mechanics of company membership and enforcement of the company constitution, as it would be seen from the viewpoint of employees and unions. After explaining the importance of membership and voting power in the general meeting, it analyses five further specific topics: representation on a company boards of directors, the administration of insolvent companies, control of dismissals by elected worker representatives, other social functions, particularly wage distribution, and corporate social responsibility. It is argued that corporate change mitigates the risks of collective agreements expiring, and the support of courts or governments dropping away. Based in United Kingdom law, it draws on comparative examples from the Commonwealth, European Union member states and the United States. Its chief aim is to start a debate about a further set of objectives for trade unions, to create sustainable, just and productive business.

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Introduction

Since governments stopped promoting membership in trade unions, there has been a decline in union membership.[2] This temporal trend affects most countries, but especially in the English speaking world it has entailed a decline of the voice people have in their workplaces. Judicial temperament on union matters has always fluctuated, but particularly on unions' most important bargaining lever: the right to strike. The better side of the law recognises the right to strike is necessary and just to balance to an employer's power to dismiss workers. It is an integral part of the common law,[3] and even in England it 'is today recognised as encompassing a fundamental human right.'[4] But the latest indications from the European Court of Justice suggest an entrenched misunderstanding is hard to expel.[5] Unions have also faced more obstacles

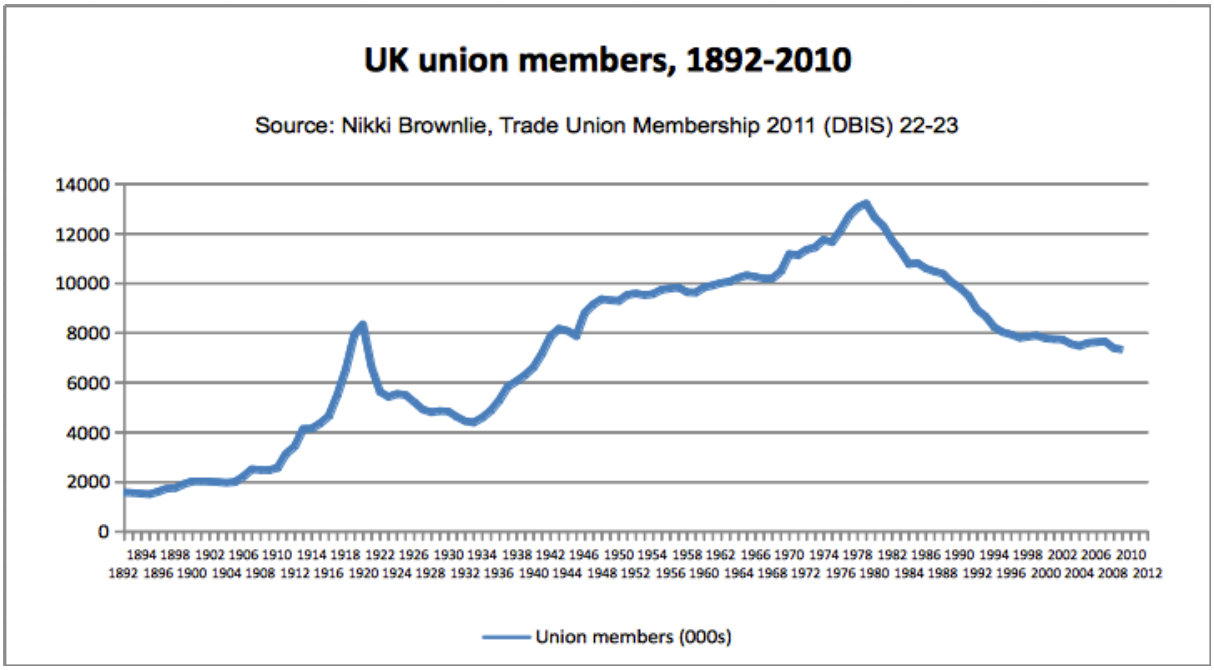
[2] See KD Ewing, 'The State and Industrial Relations: 'Collective Laissez-Faire' Revisited' (1998) 5 Historical Studies in Industrial Relations 1

[3] *Mogul Steamship Co Ltd v McGregor, Gow & Co* [1892] AC 25, Lord Bramwell, 'I have always said that a combination of workmen, an agreement among them to cease work except for higher wages, and a strike in consequence, was lawful at common law...' *Morgan v Fry* [1968] 2 QB 710, 725, Lord Denning MR, 'It has been held for over 60 years that workmen have a right to strike (including therein a right to say that they will not work with non-unionists) provided that they give sufficient notice beforehand: and a notice is sufficient if it is at least as long as the notice required to terminate the contract.' In the US, see generally *Vegelahn v. Guntner*, 167 Mass. 92 (1896) per Holmes J.

[4] *London Underground Ltd v RMT* [1996] ICR 170, 181, per Millett LJ. It may be recalled however in *Metrobus Ltd v Unite* [2009] EWCA Civ 2009, [118] Maurice Kay LJ stated 'In this country, the right to strike has never been much more than a slogan or a legal metaphor.' This courageous opinion contrasts heavily with the more influential views of Lord Bramwell, Lord Denning MR and Millett LJ, as quoted above.

[5] *The Rosella* or *International Transport Workers Federation v Viking Line ABP* (2008) C-438/05, [2008] IRLR 143 and *Laval Un Partneri Ltd v Svenska Byggnadsarbetareforbundet* (2008) C-319/05, and C-319/06, [2008] IRLR 160

in recruiting members on their own account, which is plain from the statistical chart below. The European Convention on Human Rights makes the closed shop unlawful,[6] and there have as yet been no collective agreements or legislation to automatically enrol workers in a trade union, as people are now being automatically enrolled in pensions.[7] A union's influence can still be great with a comparatively small number of people,[8] but only if the form of influence does not depend on mass participation. Even if there is a solid membership, people frequently perceive all kinds of personal costs to participation in collective action. Despite strong views on a workplace issue, for whatever reason, a smaller number of people participate in strikes than become union members. If the goals that people have in joining a union are to be achieved,[9] it is desirable that voice in the workplace does not oscillate with factors irrelevant to the principle of having a voice. It therefore seems desirable that a voice at work is more independent from (1) government support, (2) judicial attitude, and (3) the number of union members who are active.



[6] *Young, James and Webster v United Kingdom* (1981) 4 EHRR 38. In the US, the Taft-Hartley Act 1947 prohibited the closed shop, although continued to allow unions to collect fees from non-members, in 'fair share' agreements, to contribute to the costs of collective bargains from which all employees would benefit. See *Railway Employees Department v Hanson*, 351 US 225 (1956). However, §14(b) allows state legislation to prohibit this practice as well. Such states are misleadingly called 'right to work' states by their political proponents. The principle of freedom to disassociate from any organisation's membership, when one takes a job with an employer, is informed by the experience of the Nazi dictatorship and its *de facto* compulsory nationalised union, the Deutsche Arbeitsfront. See FL Neumann, *Behemoth: The Structure and Practice of National Socialism* (2nd edn 1944) 337-341.

[7] The Pensions Act 2008 s 1 requires that employers automatically enrol every UK 'jobholder' (essentially, any worker) in a basic pension scheme. Behavioural research has demonstrated that if a pension is available, far fewer people actively 'opt in' than will opt out. We tend to have a bias toward inertia, even if something is very much in our interests (like a pension, or union membership). There seems to be no reason why a collective agreement, or legislation, could not require automatic enrolment of every new worker in a union, subject to an opt out right. This would represent no problem for the European Convention on Human Rights, article 11, since freedom would always be retained to opt-out.

[8] See VL Allen, *Power in Trade Unions. A Study of their Organisation in Great Britain* (Longman 1954)

[9] Talking about the 'goals' or 'ideas' of labour law in an objective abstract can become quite a complicated exercise, because different people have different goals, and they cannot always be pinned down. It is therefore preferable that one sticks with the goals that people set for themselves, or have the goal (as explained below) of expanding people's collective capacity to choose their own goals.

Can collective bargaining achieve change in corporate structures to overcome these problems? This question of the enterprise, which lies in the social space between the private law of individual bargaining and the exercise of public law power and discretion,[10] has not yet been systematically examined. Collective agreements, as they seek to settle terms and conditions at work, are usually expected to last for a certain amount of time. They are expected to be amended or novated by negotiation in future. However, if the collective agreement disappears because negotiation in future becomes impossible, only individual employment contracts remain. Why should collective agreements not seek to embed and entrench what they do in the enterprise itself? In the public sector, the target in which to embed such norms could be an Act of Parliament, or secondary legislation, or perhaps a corporate structure of some kind.[11] Most of the time in the private sector, the legal form of enterprise will be a company limited by shares.[12] This will mean that the target for entrenchment, and the focus of this article, is a company constitution.

Part one will start by outlining a theory of voice in enterprise, with the ultimate goal of human development. To this end, it is argued that a voice at work is necessary, and corporate change is the means. Directors in control of companies have the power to appropriate the benefits of labour and direct the distribution of a company's combined product. This creates the risk that they will use their power to unjustly enrich themselves. If the law subsidises the unjust enrichment of a few at the expense of the many who contribute, it reduces the motivation to work. This damages productive efficiency, and with it society's capacity for human development is reduced. Individual contracting cannot disperse power. Power cannot be bought. Collective agreements, which are not built to last, have so far been vulnerable. While legislation is not forthcoming, this leaves room for collective agreements for corporate change. Part two gives a short historical account of the idea and practice, drawing on theory and examples from the UK, Germany and the US.

Part three shifts to substantive legal analysis. It explains the relevant mechanics of company constitutions: how collective agreements can be used to acquire membership of the company, how constitutions can be amended when necessary, and how their provisions can be enforced. Part four moves to explore five more specific topics where change is most desirable: (1) representation on the company board (2) participation in appointing the administrator of an insolvent company, (3) control over dismissals for performance and redundancy (4) delegation of general social functions, particularly wage distribution, and lastly (5) the possibility of making the company socially responsible. The article's purpose is to show what is possible, to describe how it can be done, to give a different perspective on the traditional issues of labour law, and

[10] On the field of social law, between the 19th century binary division of private law and public law, see O Gierke, *Die Soziale Aufgabe des Privatrechts* (Berlin 1889). Please contact me for an English translation.

[11] To give examples from some of the author's own and previous workplaces, the London School of Economics is a company limited by guarantee, which has articles of association like any other company. King's College, London, is established by an Act of Parliament, and bylaws are issued underneath these. The rules of a local council, such as Lambeth Council, operate through Statutory Instrument. A quango, like the Prison Ombudsman, operates under legislation. Sections of the civil service, such as that appended to the Asylum and Immigration Tribunal, are similarly constituted by legislation.

[12] In the UK, this is typically either a public or a private company. Other private sector legal forms (including the charitable sector) would include a partnership agreement, a trust document, or the constitution of a company limited by guarantee (which operates in a very similar fashion to a company limited by shares).

to start a debate about the role of labour law in the future. Its argument is that, until analogous legislation is enacted, collective bargains for corporate change are both achievable and desirable.

1. A theory of voice in enterprise

To say it is desirable that "collective agreements should seek corporate change" requires some sense of a goal. Contemporary theories, between corporate law and labour law, are numerous in their exploration of the concepts of 'participation' and 'voice'. Among labour lawyers, a starting point is often the concept of voice being a human, social or economic right. Among corporate lawyers, economic analysis is increasingly popular and generally speaking it discloses a deep ambivalence about the merits of participation. Here the natural goal is usually said to be greater economic, productive or social efficiency: the idea that the law should maximise wealth or welfare.[13] The global bestselling text, *The Anatomy of Corporate Law* represents the view that worker participation in corporations, especially on the board of directors, is highly problematic because the conflicts of interest among shareholder and worker representatives would impede efficient decision making.[14] This accords with a general view that in free market economies the most efficient structures of enterprise will naturally evolve.[15] Similarly in mainstream economics Oliver Williamson, ever more influential since he won half of the 2009 Nobel Prize,[16] has argued that 'not by history, but by logic' is shareholder control of companies the ordinary result. You can only get worker participation by enacting coercive legislation. In the heady days before the millennium it was boldly argued that enterprise structures around developed economies, with shareholder ownership at the centre, represented the end of history for corporate law.[17]

This overall narrative has been convincingly challenged on the ground that efficient structures do not naturally result because the institutional cultures prevailing among economic actors can prevent the evolution of 'optimal' arrangements.[18] People's capacity for rational choice is constrained by prevailing practice: we often do things because we do them, not because they are always smart.[19] Shareholder dominance may well just be an interim phase. Another counter-argument to the narrative is that because the economic institutions adjust to one another there can be a 'variety' of efficient social equilibria.[20] A shareholder dominant model of corporate governance, as in the UK and the Commonwealth, is not

[13] Often 'welfare economics' appears to conflate welfare with wealth, and utility with money. The two are plainly distinct.
[14] R Kraakman, J Armour, P Davies, H Hansmann, K Hopt, H Kanda and EB Rock, *The Anatomy of Corporate Law* (2nd edn OUP 2009) 110-113
[15] H Hansmann, *The Ownership of Enterprise* (1996) 92 and 112-115
[16] The other recipient in 2009, from a different economic tradition, was Elinor Ostrom. The Nobel Prize in Economics is in fact the 'Bank of Sweden Prize in Memorial of Alfred Nobel'. A prize for economics, as opposed to peace, physics, chemistry, mathematics and literature, was no part of Nobel's will or wishes, but was rather funded at the bank's initiative from 1970 onwards.
[17] This appears to fall into the tradition of the Washington "Consensus". For a recent critique of this, and a broad summary of economic views of labour law, see S Deakin, 'The Contribution of Labour Law to Economic and Human Development' in G Davidov and B Langille (ed), *The Idea of Labour Law* (2011) ch 10
[18] D Kershaw, 'No End in Sight for the History of Corporate Law: the Case of Employee Participation in Corporate Governance' (2002) 2 Journal of Corporate Law Studies 34
[19] cf OW Holmes, *The Common Law* (1881) ch 1
[20] PA Hall and DW Soskice (eds), *Varieties of Capitalism: the institutional foundations of comparative advantage* (2001)

necessarily better than the systems seen across the EU, and neither are codetermination systems better than the UK.[21] Both have advantages and disadvantages.[22] The basic problem with this stance is that in supplying counter-arguments against a unitary convergence model, a positive case for anything particular is neglected. Moreover the role of power in shaping institutions has become puzzlingly absent.[23] Other theories of participation, which do present a positive case and expressly deal with corporate structures, have frequently worked by analogy. It has been said that more participation is desirable as a method of democratising the economy, in a similar fashion to democracy in the political sphere.[24] Or there could be an analogy to property rights: shareholders have property, and they have voice, and because workers make property-like contributions to companies, they too ought have similar entitlements.[25] While enlightening, such arguments by analogy depend on easily contestable comparisons, and tend to assume that once the analogy is established, the job is done. Why should there be political democracy anyway? What is so special about the *numerus clausus* of property rights that it (and only it?) should carry the right to a voice? So it seems that to make an argument complete, a clear and ultimate goal ought to be kept in mind, and reasons should be given for pursuit of that goal on its own merits.

The goal: human development

While every normative theory depends on the goal in view, different people may legitimately have different goals. However, human development, which has been roughly measured by the United Nations' inequality adjusted Human Development Index since 2010,[26] is probably the most defensible goal in any democratic society which is concerned with the welfare of its citizens. Human development means people developing their personalities to the fullest. It is reasonable to see this as the highest aim, to which all law (not just labour law) should aspire, in a world where everything else may be good or bad, depending on the relative position one occupies. Wealth, fame, and hedonic pleasure, jointly or severally, may all represent a virtue, but given the wrong circumstances they can all be a vice.[27] The same can be said for concepts like democracy, liberty, and equality. None are inherently good, just as none can be unqualified. The same cannot be said for human development, in a community where as many people are brought

[21] PL Davies, *Company Law* (Clarendon 2010) ch 9, 'Shareholder Control'

[22] nb, making a positive case for the model of corporate governance or labour law in the United States at the moment is a more difficult task.

[23] cf PL Davies and M Freedland, *Labour Law: Text and Materials* (1984) 1

[24] R Dahl, *A preface to economic democracy* (1985) 134

[25] W Njoya, *Property in work: The employment relationship in the Anglo-American firm* (2007)

[26] This human development index measures gross national income, with a deduction for inequality, life expectancy and years in education. See United Nations Development Programme, *Human Development Report 2010, 20th Anniversary Edition. The Real Wealth of Nations: Pathways to Human Development* (2010). As an accurate measure of 'human development' the HDI is itself still developing. For example, social expenditure on security cameras, prisons, or nuclear weapons all still count as contributing gross national income, and the years spent in education have no manner for measuring the quality of thinking those years produce.

[27] B Spinoza, *On the Improvement of the Understanding* (1677) translated by RHM Ewles (1887) §§1-6, 'After experience had taught me that all the usual surroundings of social life are vain and futile; ; seeing that none of the objects of my fears contained in themselves anything either good or bad, except in so far as the mind is affected by them, I finally resolved to inquire whether there might be some real good having power to communicate itself, which would affect the mind singly, to the exclusion of all else...'

along as possible.[28] It was at the foundations of democratic theory,[29] and in the roots of our modern notions of economic fairness.[30] In theory, and more importantly in practice, it is where philosophies of utility and rights meet.[31] On the one hand, there can be no objective measure of utility, or welfare, without some conception of the rights one desires to maximise (whether money, happiness, liberty, or some other good). You cannot say utility is maximised, unless you have broken down which components of aggregate pleasure matter most: you need a theory of rights. On the other hand, there can be no way to objectively value the rights one seeks without some method to compare rights where they conflict (whether property and equality, free expression and privacy, safety and guns). The only way to perform such an exercise is to have a purpose in mind.[32] It is true, again, that people have different purposes, and it would be futile to argue one has any objective superiority over another.[33] But being human myself, I happen to think that human development is the most agreeable, persuasive purpose, and one under which all other purposes may be subsumed.

The sub-goal: productive efficiency

In the economic sphere one of the most important contributors to human development is the assurance of productive efficiency, in the sense widely understood in economics.[34] Productive efficiency matters because more wealth means more access to personal property.[35] Property is one of the most important vehicles for expressing our personalities.[36] This means more property, production and growth is one of

[28] B Spinoza, *On the Improvement of the Understanding* (1677) §§13-14, 'man conceives a human character much more stable than his own, and sees that there is no reason why he should not himself acquire such a character... This, then, is the end for which I strive, to attain to such a character myself, and to endeavor that many should attain to it with me. In other words, it is part of my happiness to lend a helping hand...'

[29] T Paine, *The Rights of Man* (1792) Part II, ch 3, 'There is existing in man, a mass of sense lying in a dormant state, and which, unless something excites it to action, will descend with him, in that condition, to the grave. As it is to the advantage of society that the whole of its faculties should be employed, the construction of government ought to be such as to bring forward, by a quiet and regular operation, all that extent of capacity which never fails to appear in revolutions.'

[30] S Webb and B Webb, *Industrial Democracy* (9th edn 1926) Part IV, ch 4, 847-849, 'We ourselves understand by the words "Liberty" or "Freedom," not any quantum of natural or inalienable rights, but such conditions of existence in the community as do, in practice, result in the utmost possible development of faculty in the individual human being.... When the conditions of employment are deliberately regulated so as to secure adequate food, education, and leisure to every capable citizen, the great mass of the population will, for the first time, have any real chance of expanding in friendship and family affection, and of satisfying the instinct for knowledge or beauty. It is an even more unique attribute of democracy that it is always taking the mind of the individual off his own narrow interests and immediate concerns, and forcing him to give his thought and leisure, not to satisfying his own desires, but to considering the needs and desires of his fellows.'

[31] On utilitarian theory, see JS Mill, *Utilitarianism* (1863) and on their late 20th century critique, see HLA Hart, 'Between Rights and Utility' (1979) 79 Columbia Law Review 828. More recently theories of utility have become closely associated with professional economics, while rights based rhetoric has been the domain of lawyers. This is, naturally, a large oversimplification, since the law led field of 'law and economics' pins its colours to the mast of utility, eg RA Posner, *Economic Analysis of Law* (2010) ch 1. Within economics, some of the most important thinkers of the 20th century plainly disavow what would usually be associated with utilitarian thinking, eg JE Stiglitz, 'Employment, social justice and societal well-being' (2002) 141 International Labour Review 9.

[32] eg L Wittgenstein, *Philosophical Investigations* (1953) §69 ff and Q Skinner, *Visions of Politics* (2002) vol 1, ch 1

[33] cf A Hyde, 'The Idea of the Idea of Labour Law: A Parable' in G Davidov and B Langille, *The Idea of Labour Law* (2011) which outlines history of 23 different ideas of labour law that have emerged.

[34] See N Kaldor, 'Welfare Propositions in Economics and Interpersonal Comparisons of Utility' (1939) 49 Economic Journal 549, and J Hicks, 'The Foundations of Welfare Economics' (1939) 49 Economic Journal 696.

[35] Personal property ought to be distinguished from productive property. See AA Berle, 'Property, Production and Revolution' (1965) 65(1) Columbia Law Review 1-20 and AA Berle, 'Modern Functions of the Corporate System' (1962) 62(3) Columbia Law Review 433. There is probably no clear dividing line between the two (for instance, a car could be 'consumed' or used by the same person in the course of business) rather than a continuum, where property is squarely of the personal or productive kind at different poles. All property rights should be subject to the maxim that its use should not harm others (*Sic utere tuo ut alienum non laedas*) and that the ownership of property carries responsibility. See, for example, the German Constitution, *Grundgesetz* (1949) art 14(2) and the Brazilian Constitution (1988) art 5(23).

[36] See GWF Hegel, *Elements of the Philosophy of Right* (1820) §41. Hegel was writing at a time when the importance of responsibility

the most important routes to human development, so long as the 'invisible hand' of the market is simultaneously oriented toward equity in distribution (or at any rate greater equality than is presently seen).[37] To achieve human development to the fullest, the 'economic' may have to concede to the 'social'. And because the purpose of productive efficiency is human development, in this sense the social must never concede to the economic. But on the whole, any credible theory of labour rights will come up against the issue of how it promotes productive efficiency, precisely because it is one of the most important contributors to human development.

With these goals in mind – productive efficiency insofar as it contributes to human development – it is possible to build the case for having a collective voice in the workplace. This must begin with a positive analysis of two of the most important implicit terms in virtually all employment relations: the right to appropriate, and the right to direct.[38]

Right to appropriate

The right of an employer to appropriate the benefits of labour is so fundamental that often it goes unnoticed. It means the benefits of labour accrue to the property of the employer, not the employee. The employee simply receives a payment according to the construction of his or her contract, which is usually (though not inevitably) less. It is the oldest incident of employment. It was one of the first justifications for the employer's responsibility for the torts commissioned by its workers.[39] It matches the reasonable expectations of the parties, because virtually all employment relations involve the combined production of two or more people's labour and capital.[40] Property over the fruits of production must similarly combine. Direction of its division and distribution is a separate question. Illustrations of this implied right are innumerable. To take just one, in *Stevenson, Jordan & Harrison v MacDonald & Evans*, an engineering firm claimed a copyright over its former employee's lectures, the text of which could be turned into a

attaching to property, particularly in its distribution, was fully accepted, remarking at §49 that to say people were equal was 'an empty tautological proposition since a person abstractly considered is not yet separate from others, and has no distinguishing attribute.'

[37] See A Smith, *The Theory of Moral Sentiments* (1759) Part IV, ch 1, §10. Smith hypothesised that because 18th century employers had a limited propensity to consume, they would have to spend their income by employing others with the consequence of a tendency toward equal distribution of wealth. 'They are led by an invisible hand to make nearly the same distribution of the necessaries of life, which would have been made, had the earth been divided into equal portions among all its inhabitants, and thus without intending it, without knowing it, advance the interest of the society...' However see his remarks in *The Wealth of Nations*, on employment and companies quoted below.

[38] The other most important implied terms, which tend to benefit workers from the arbitrary exercise of discretion are the duties of good faith, or 'mutual trust and confidence' and the implication of the relevant collective agreement (even if it is not incorporated through reasonable notice). Terms are implied into contracts, firstly as a standardised incident to contracts of specific types, and secondly on individual circumstances to reflect the reasonable expectations of the parties: see *Malik and Mahmud v Bank of Credit and Commerce International SA* [1997] UKHL 23 and *Attorney General of Belize v Belize Telecom Ltd* [2009] UKPC 10. They are default rules out of which parties with sufficient bargaining strength may contract. Individual employees may not contract out of the protective terms of employment contracts. This will be viewed as a sham: see *Autoclenz Ltd v Belcher* [2011] UKSC 41, [35].

[39] See *Turberville v Stampe* (1697) 91 ER 1072, Holt CJ, 'if the defendant's servant kindled the fire in the way of husbandry and proper for his employment, though he had no express command of his master, yet his master shall be liable to an action for damage done to another by the fire; for it shall be intended, that the servant had authority from his master, it being for the master's benefit.'

[40] Terms are implied in English contract law to reflect the parties' reasonable expectations, either as a standardised incident of different contract types (sales of goods, insurance, companies, employment and so on) or on an individual basis as the fact specific circumstances require. See *Equitable Life Assurance Society v Hyman* [2000] UKHL 39.

publication. The Copyright Act 1911 section 5(1), which codified the common law position, stated that the author of a work would be its owner, unless it was done in the course of employment. Denning LJ held the lectures were composed from knowledge the engineer held, which was not subject to any trade secrets, so the book's copyright belonged to the engineer's estate.[41] This exception illustrates the rule: all the benefits of labour, within the course of employment, accrue to the property of the employer.[42] The limit is that if a person acquires skills or knowledge within a profession, and uses those skills outside the profession, those benefits of labour will belong to the person, and not the employer.[43] More generally it was put in the following way by Bowen LJ in *Falcke v Scottish Imperial Insurance.*

> The general principle is, beyond all question, that work and labour done or money expended by one man to preserve or benefit the property of another do not according to English law create any lien upon the property saved or benefited, nor, even if standing alone, create any obligation to repay the expenditure. Liabilities are not to be forced upon people behind their backs any more than you can confer a benefit upon a man against his will.[44]

While this fails to mention that property owners have obligations to those who contribute, Bowen LJ captured the most fundamental element of employment: the right to appropriate is the implied term in private law that the benefits of labour accrue to the property of the employer.

Right to direct

The second fundamental implied term is the right of an employer to direct employees, within the scope of discretion set by an employment contract. This is invariably necessary to reflect the parties' reasonable expectations that people can do their work, and resources can be managed, in response to a business' needs. The desire to have a flexible employment relation is usually a rational response to underlying economic demands, which potentially benefits all parties, rather than being just a pro-employer element of contract law. Indeed, the fact that employees are subject to the direction of employers has come to be one of the defining indicators of the employment relation itself.[45] It is also one of the first, and central, elements of a company constitution.[46] But the right to direct brings with it a powerful discretion: one that entitles the employer to unilaterally vary the contract's consideration.[47] The employer's right to direct will mean that he can require an employee to work harder than before within the contract's terms, but not pay a higher wage. It also means that a greater share of the combined product (which the employer has the

[41] [1952] 1 TLR 101
[42] See also *British Reinforced Concrete Engineering Co Ltd v Lind* (1917) 34 RPC 101 (colliery invention belonged to the employer) and *LIFFE Administration and Management v Pinkava* [2007] EWCA Civ 217 (employee's invention of a swaps trading innovation, patented in the US, belonged to the employer).
[43] See generally, regarding the problems encountered in Silicon Valley, O Lobel, 'Intellectual property and restrictive covenants' in KG Dau-Schmidt et al, *Labor and Employment Law and Economics* (Elgar 2009) vol 2, ch 18, 526-532
[44] (1886) 34 Ch 234, this case itself concerned the right to a life insurance policy.
[45] eg *Lawrie-Blum v Land Baden-Wurttenberg* (1986) Case 66/85, [17]
[46] eg Companies (Model Articles) Regulations 2008, SI 2008/3229, art 3, 'Subject to the articles, the directors are responsible for the management of the company's business, for which purpose they may exercise all the powers of the company.'
[47] Consideration means all the things that amount to the *quid pro quo* of the contract, but mostly the mutual obligations of work in exchange for wages.

right to appropriate) may be retained than an employee, or the workforce as a whole, could reasonably expect. If at the end of a year of production a greater than anticipated turnover is realised, which will be due to the combined contributions of everyone in an organisation, a company's directors will have a discretion about how to share these gains of growth.[48] They could raise wages for the following year, declare and distribute dividends to shareholders, raise their own salaries, invest back in the business, or some combination of all four. The initiative and discretion to do this, so far as it is not bounded by a company's constitution or contract, comes from the right to direct.

Risk of unproductive enterprise: capital

When organisations appropriate the benefits of labour, and when the directors of an organisation have the power to direct the distribution of the product, productivity is at risk because directors may use their office to unjustly enrich themselves.[49] In a company, the shareholders of an organisation (and especially the beneficiaries of institutional shareholders, like anyone with an occupational pension) bear analogous risks to employees. When they contract for shares, the benefits created by the deployment of their capital accrues to the property of the company as well. The capital they contribute may also be directed to a use determined by the directors. Without any mechanism of accountability, this separation of the original owner of property from control, means the directors could profit purely from the occupation of their office, and not from productive effort.[50] The capacity for unjust enrichment will reduce directors' motivation to work in a useful manner, and thus reduce overall wealth creation.

UK law gives shareholders compulsory rights to restrain directors from unjustly profitly at their expense. However symbolic for the ultimate beneficiaries of institutional shareholders,[51] the registered shareholders have an equal vote among one another.[52] And however imperfect in practice,[53] with this vote shareholders may dismiss the directors for a reason they collectively determine, subject only to giving reasonable notice and a fair hearing.[54] The position of employees is not so good.

Risks of unproductive enterprise: labour

Between the workforce and directors,[55] the problem of management under-motivation arises once more.

[48] See generally F Rodriguez and A Jayadev, *Human Development Research Paper 2010/36: The Declining Labor Share of Income* (2010)

[49] cf A Smith, *The Wealth of Nations* (1776) Book V, ch 1, part III, §107, 'The directors of such companies, however, being the managers rather of other people's money than of their own, it cannot well be expected, that they should watch over it with the same anxious vigilance with which the partners in a private copartnery frequently watch over their own.... Negligence and profusion, therefore, must always prevail, more or less, in the management of the affairs of such a company.' (Profusion means a tendency to unjustly enrich one's self.)

[50] See AA Berle and GC Means, *The Modern Corporation and Private Property* (1932) 5 and 65, drawing an analogy between shareholders in the 'corporate revolution' of the early 20th century and workers in the industrial revolution.

[51] See E McGaughey, 'Piercing the institutional veil' (2013) forthcoming.

[52] This task is performed by the default expectations set by the Companies Act 2006 s 284, which has always been actively policed by the courts: *Pender v Lushington* (1877) 6 Ch D 70. In addition, the London Stock Exchange had the policy of bringing pressure for a one share, one vote principle since the Jenkins Report, *Report of the Company Law Committee* (1962) Cmnd 1749, 49, [140]. This has been bolstered by the indefeasible right of shareholders to dismiss directors.

[53] For example, shareholders have no specific say in the appointment of directors, or formally binding vote for the pay that company executives receive.

[54] Companies Act 2006 ss 168-169.

[55] One may include the interests of shareholders under management if management is effectively accountable to its shareholders.

If a company's directors may appropriate a share of the combined product, which is disproportionate to their effort at the expense of the labour force, then directors will be under-motivated to work productively. But there are also a second and third problem. The second is that there is the risk of under-motivation of the workers. Underpaid people do not work as productively.[56] A human is not a resource. People have characters, not 'capital'. It is true that someone who feels devalued, not treated with dignity through the pay they receive, can be motivated to work hard anyway. They can be monitored and sanctioned, generating all the 'agency costs' that a rational, self interested principal might face.[57] But costs which bring gains to an employer can inflict a greater loss on an employee, and so reduce social welfare. Reasonable pay, in a workplace where mutual trust and confidence prevails over prescient suspicion and surveillance, can often produce positive effects on motivation at a far lower price.

Third, if directors are capable of unjustly enriching themselves at the expense of their workforce, the resulting inequality in income is a source of demotivation in itself. A behavioural study carried out by Alain Cohn, Ernst Fehr Benedikt Herrmann and Frederic Schneider gives exemplary proof.[58] They created an experiment with groups of workers who distributed cards for nightclub entry in teams of two. Then their pay was varied in different ways. In the first group pay remained the same, and worker A and B's productivity remained at a certain level. In the second group, worker A and B's pay was unilaterally cut from €12 to €9 per hour. Their productivity dropped by 15 per cent. In the third group, where worker A's pay was cut and worker B's pay remained constant, worker A's productivity dropped by 34 per cent. The fact that worker A's productivity drop was so great, more than if the pay of both workers had been cut, reflects the innate behavioural requirement we have for fairness. Not only does excessive executive pay demotivate the executive, not only does low pay demotivate the worker, unfair pay for people relative to one another degrades the whole enterprise. If the law permits unjust enrichment in enterprise, it damages productive efficiency, and with it goes human development.

Remote chance of voice through individual contracting

Any individual employment contract can be drafted to infuse the private law rights to appropriate and direct with accountability, fairness and reason. It can give the employee a voice. However, the chance of this happening through individual bargaining is remote, because the bargaining power of organisations is routinely superior to the power of the individual.[59] The same problem would be presented to small, individual shareholders were it not for a set of compulsory legal rights entitling them to a voice in

[56] eg A Marshall, *Principles of Economics* (3rd edn 1895) Book VI, ch 4, 649

[57] See MC Jensen and WH Meckling, 'Theory of the Firm: Managerial Behavior, Agency Costs and Ownership Structure' (1976) 3(4) Journal of Financial Economics 305, 308-309.

[58] A Cohn, E Fehr, B Herrmann and F Schneider, 'Social Comparison in the Workplace: Evidence from a Field Experiment' (2011) IZA Discussion Paper No 5550

[59] The concept of unequal bargaining power is an old one in the common law, see *Vernon v Bethell* (1762) 28 ER 838, Lord Henley LC, 'necessitous men are not, truly speaking, free men, but, to answer a present exigency, will submit to any terms that the crafty may impose upon them.' See also M Weber, *Economy and Society* (Roth and Wittich 1979) vol 2, ch 8, 'The formal right of a worker to enter into any contract whatsoever with any employer whatsoever does not in practice represent for the employment seeker even the slightest freedom in the determination of his own conditions of work, and does not guarantee him any influence on this process.'

companies. The same problem is encountered by beneficiaries of shareholding institutions who lack effective rights.[60] Inequality of bargaining power exists because an individual employee has fewer alternatives than his employer, especially when the employer is a corporation. The corporate employer will often have numerous job applicants who seek work, while each applicant has relatively few positions to try for. Particularly in times of unemployment, every worker (even if acting in unison) needs wages to support their standard of living with greater urgency than employers usually need to hire workers.[61] So, without the ability to contract on an equal footing, it is foreseeable that a company's directors will be able to appropriate the gains of growth in an organisation. Employers often face substantial objection and protest if they actively cut wages. But the intensity of protest employers face against gradually growing their relative share of wealth, and economic power with it, is less.[62] This is true even though director pay, or shareholders' portion of income, becomes more and more unjust with every financial year. At a similar rate, the social capacity for workplace cohesion, motivation, efficiency and development will peter away. For all these reasons, in the law of enterprises, inequality of bargaining power is the most basic market failure.[63]

To some extent the institutional culture of workplaces restrains the market power that employers hold. People no longer think in the way we once did. We do not just defer to the boss, we recoil at being scientifically managed, and people laugh at the notion there is a "right to manage": we see macho business celebrities barking "you're fired" as TV entertainment.[64] The modern labour force does not accept to be treated like a commodity, and human beings know that they are not just another resource (even if that unfortunate term has not yet been changed). Culturally, in a democratic society, people do not accept a hierarchical ethic to prevail in their workplace nearly as much as the law would allow it to happen. Business theory reflects this in the negative sense. For some time, some strands have focused on how to give orders without sounding like orders are being given,[65] on driving through a leader's will under the guise of 'team' work, and on instilling in employees an identity with, and belonging in, a firm which is only interested in possessing. The positive strands of business theory emphasise all these things, but for ends in which everyone may share, not just the employer. Cultural constraints are not enough for an outdated legal structure, but they do give a sign that the law has gotten out of touch.

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[60] Some rights are available for beneficiaries of collective pension funds in the UK, in the Pensions Act 2004 ss 241-243, however in individual pensions, for policyholders of insurance companies, and effectively for mutual fund investors there is no occasion for exercising a voice.

[61] eg A Smith, *The Wealth of Nations* (1776) Book I, ch 8; *Eleventh and Final Report of the Royal Commissioners appointed to Inquire into the Organization and Rules of Trades Unions and Other Associations* (1868-1869) Parliamentary Papers vol xxxi, §61; S Webb and B Webb, *Industrial Democracy* (1920) Part III, ch 2

[62] JM Keynes, *The General Theory of Employment, Interest and Money* (1935) ch 2, II, 'Whilst workers will usually resist a reduction of money-wages, it is not their practice to withdraw their labour whenever there is a rise in the price of wage-goods. It is sometimes said that it would be illogical for labour to resist a reduction of money-wages but not to resist a reduction of real wages.... But, whether logical or illogical, experience shows that this is how labour in fact behaves.'

[63] E McGaughey, 'Inequality of bargaining power as a market failure' (2013) forthcoming

[64] It should be noted that, at least in the UK, Alan Sugar on the BBC show *The Apprentice* appears to be in full compliance with the Employment Rights Act 1996 s 94, which creates the right to a fair dismissal. This is because despite the tag-line that "you're fired", the show actually makes clear that it is an extended TV interview: the "apprentices" are not actually apprentices at all, and they do not yet have employment from which they could be "fired". I am grateful to my students at King's College, London for explaining this important cultural point.

[65] eg P Pigors, 'How can a boss obtain favorable responses to his orders?' (1961) 1(1) Human Resource Management 15

The Catch 22 of voice through property

Another option to get a voice is that the employee could become a shareholder in his or her company. This would, of course, be paying for participation twice: first through the investment of labour,[66] and second through purchase of a capital stake.[67] A practical obstacle is that in a world where employees lack a voice, they will probably not possess significant funds to purchase a voice. A voice through property is a Catch 22. To participate in enterprise governance, employees need to have money, but employees are not getting enough money because they have no right to participate. Even if employees do acquire enough money, and there are many examples,[68] to buy a voice in their own firm, employees need a significant financial stake to have achieve any substantial participation. This would break the most basic principle of prudent investment: to diversify your share portfolio in order to spread the risk of insolvency. On any widespread basis, promotion of this kind of employee ownership would produce an Enron-economy. A voice for labour must be completely independent from monetary investment.

Voice through collective bargaining: solutions and problems

If workers can build the bargaining power they have by forming a trade union, bargaining collectively and taking collective action in support of their interests, then it is possible to participate, and so counteract the risk of unproductive enterprises and market failure. In the view of some strands of economics, trade unions are productivity damaging cartels of labour.[69] No text taking this view explains, by parity of reason, why a corporation is not a 'cartel of capital'. As such it discloses both an intellectually indefensible position and an aversion to history.[70] Still, it is said that unions can only raise the market price for labour at the inevitable cost of creating unemployment. It would follow that unions merely redistribute wealth from one group of employees to another. This strict view of trade union activity does not give full (or perhaps any) weight to the pre-existing inequality of bargaining power which trade unions correct.[71] If employers

[66] The phrase 'investment of labour' is gratefully adopted from R Goode, *Principles of Corporate Insolvency Law* (2005) 44.

[67] cf OW Williamson, *The The Mechanisms of Governance* (1984) 314, 'in effect broad participation on the board invites two bites at the apple (get your full entitlement at the contractual interface; get more in the distribution of the residual).' Also in the 19th century, common law judges would have agreed with Williamson, albeit that the following remarks were made about a shareholder's investment: *In re Wragg Ltd* [1897] 1 Ch 796, Lindley LJ, 'We must not allow ourselves to be misled by talking of value. The value paid to the company is measured by the price at which the company agrees to buy what it thinks it worth its while to acquire. Whilst the transaction is unimpeached, this is the only value to be considered.' However, Williamson and Lindley LJ both thought that unequal bargaining power is irrelevant. This is wrong, and there is a difference between the price of an exchange where parties have equal bargaining power, and a price where their positions are very unequal. This is why, today, the law routinely disregards many market prices, which are so unfair that they create no binding obligation. Williamson also fails to grasp the importance of dismissals, in his distinctions between employees and shareholders.

[68] eg JN Gordon, 'Employee Stock Ownership in Economic Transitions: The Case of United and the Airline Industry' in M Blair and M Roe, *Employees & Corporate Governance* (1999) ch 10

[69] eg RA Posner, *Economic Analysis of Law* (Aspen 2011) 425, 'The main purpose of a union, most economists have long believed, is to limit the supply of labor so that the employer cannot use competition among workers to control the price of labor (wages).' Note that the 'most economists' is an unsupported assertion, and in any case does little to explain why those economists were correct when the views of sociologists, philosophers, or even lawyers, may have differed.

[70] In the US, the Sherman Antitrust Act 1890 was first used against trade unions, rather than business combinations. When it was used against business cartels, it triggered the greatest merger wave in US history as business realised they could acquire the same market power by merging into larger corporations. This was stopped by the Clayton Act 1914, which both removed labour from the ambit of antitrust law and introduced controls on mergers that substantially lessened competition. Many commentators have simply refused to accept this century old law, and have refused to acknowledge that bargaining power justifies the distinction.

[71] This is why in the US the National Labor Relations Act 1935 §1 pointed to the 'inequality of bargaining power between employees who do not possess full freedom of association or actual liberty of contract, and employers who are organized in the

exercise market power, unions' counter-veiling power will eliminate the capacity for managerial unjust enrichment, and thus optimise productive efficiency. It will only be if unions begin to make unreasonable demands, which are in excess of the realities of enterprise, that they would damage productive efficiency.[72] But in the vast majority of cases, bringing equality to an unequal world is what unions do best.

However, collective agreements have a central weakness: they become outdated. They require periodic renegotiation. Many envisage joint negotiation machinery for the future, but the source is the collective agreement itself. Even if the agreement is built to last, the employer may not view it this way in the future. Attitudes and legal circumstances change. Collective agreement rests on the fragile basis that members can take collective action, including a strike. Every time collective action becomes harder, every time collective bargaining fails, the residual norms in the positive law of employment will return: the unrestricted private law power to appropriate and direct.

Solution of legislation, and waiting for it

Legislation can solve many, if not all problems of collective agreement. When labour law creates a sensible minimum standard it solves two issues. First, even collective action is vulnerable to the fact that some people may, pursuing an individual interest,[73] break the coalition or simply ride for free on the efforts of others. This increases the costs for everyone else.[74] Second, collective action is frequently unable to deliver complete protective coverage: but effectively enforced legislation can approximate a minimum floor of rights for everyone. It follows that an effective solution to counter the risks of unproductive enterprise would be to say that the private law powers to appropriate and direct come with the requirement that those in control are accountable through the vote. There is no justification for the law to subsidise the unjust enrichment of the few at the expense of the many. There is no reason that public money should fund courts which enforce contracts and associational structures of enterprise that are unjust. The consent to individual contracts of employment is fictive. In a world where property buys participation, equality of opportunity is a dream. Legislation is the remedy, but the problem with that is it may not have happened. Sometimes Parliaments act too late.

Solution of collective agreements for corporate change

If individual agreement cannot work, if a voice through property is a Catch-22, if collective agreements

corporate or other forms of ownership association'.

[72] eg JS Mill, *Principles of Political Economy* (1848) Book V, ch 10, 'It is a great error to condemn, per se and absolutely, either trade unions or the collective action of strikes.... The market rate is not fixed for him by some self-acting instrument, but is the result of bargaining between human beings... those who do not "higgle" will long continue to pay, even over a counter, more than the market price for their purchases.'

[73] This is not to suggest for a moment that everybody, or even any more than a small minority of people actually conform to the model of rational self interest that is frequently reified in some strands of economic theory. On the contrary: 'How soever selfish man may be supposed, there are evidently some principles in his nature, which interest him in the fortune of others, and render their happiness necessary to him, though he derives nothing from it except the pleasure of seeing it.' A Smith, *The Theory of Moral Sentiments* (1759) 1.

[74] JS Mill, *Principles of Political Economy* (1848) Book V, ch XI, §12, explaining collective action problems as what he regarded as the fourth (very broad) exception to the rule that *laissez faire* was the best policy. This theory was elaborated, without much credit given, at length by M Olson, *The Logic of Collective Action : Public Goods and the Theory of Groups* (1965).

tend to run out, and if legislation to entrench a voice for workers in enterprise is not given, a second best solution can be found in changing a company's constitution. Collective agreements may require management to amend the internal rules of the company. This would lend permanence to the terms and conditions that collective agreements sought to introduce, even if the environment a union faces changed. A voice within companies would not change or replace the necessity of ongoing collective bargaining: the two are not mutually exclusive.[75] Shareholders are expected by law to engage with company boards,[76] and can create shareholder agreements to regulate the functioning of the business. The external and internal voice of shareholders is complementary, and so it is with employee relations.

If mechanisms exist within a company to represent the voice of the workforce, then it will be largely self-enforcing. In many systems, particularly the United Kingdom, collective agreements are not usually legally binding.[77] The merits of this policy in the 21st century can be debated, but it came from the enduring view that if collective agreements were legally enforceable, they would be interpreted by the judiciary, and the judiciary might use their powers of interpretation to the detriment of workers' interests.[78] Where collective agreements could embed machinery for the ongoing change of workplace terms through representative institutions, provisions that are sufficiently simple need never see a court. Embedding participation in the enterprise will create a culture that becomes increasingly self-enforcing as people internalise a new way of listening to one another. It would replace contract with a new constitutionalisation of the employment relation.[79] This would fulfil the central objective for company and labour lawyers alike: autonomy.[80] Just as labour law will become the new frontier for company law, company law is the new labour law.

2. A brief, notable history

The idea of bringing company law and labour law together, and that the workforce can play a role in enterprise, has a long history,[81] but its modern foundations lie in the late industrial revolution. At first, among those who cared, labour law's problem was how to infuse law into a relationship of subordination. Its second phase was one dealing with the resolution of collective conflict. The 21st century challenge is different: it is about the shape that fusion of interests between capital and labour will take. This is the domain of corporate change. Two formative examples in English theory are John Stuart Mill and Sidney

[75] There is sometimes an assumption, wrongly, that in countries with codetermination, collective agreement is reserved for 'contentious' issues such as wage policy, while codetermination focuses on areas where there can be mutual agreement. This is a mischaracterisation, because collective agreements set wages in negotiation with a management which is itself codetermined.
[76] Stewardship Code (2012) Principle 1. Guidance: 'Engagement is purposeful dialogue with companies on those matters as well as on issues that are the immediate subject of votes at general meetings.'
[77] Trade Union and Labour Relations (Consolidation) Act 1992 s 179
[78] Otto Kahn-Freund was a key proponent of this view. It has a great deal to do with his experience in the Weimar Republic in his early career as a Berlin Labour Court judge. See O Kahn Freund, 'The Social Ideal of the Reich Labour Court - A Critical Examination of the Practice of the Reich Labour Court' (1931) in O Kahn-Freund, R Lewis and J Clark (ed) *Labour Law and Politics in the Weimar Republic* (Social Science Research Council 1981) ch 3, 108-161.
[79] A contract would of course still exist to enter into the relationship with a company.
[80] See Lord Eldon in *Carlen v Drury* (1812) 1 Ves & B 154 and Lord Wedderburn, *The Worker and the Law* (1965) 1, 'Most workers want nothing more of the law than that it should leave them alone.'
[81] eg in Germany, HJ Teuteberg, *Geschichte der Industriellen Mitbestimmung in Deutschland* (1961)

and Beatrice Webb, with whom this brief, but notable history of corporate change can begin.

John Stuart Mill

In *Principles of Political Economy*, Mill argued that a divided society could not advance, and that society remained divided while the people who worked for a living were totally separate from those who owned capital. His solution envisaged an extension of the 'principle of partnership', where workers would become part owners and controllers of business.[82] Mill exemplified the idea that the 'futurity of the labouring classes' lay in assimilating people's social positions into the existing system of individual property holding. Mill avidly favoured the right of unionisation, collective bargaining and the right to strike. However he also believed it was not a permanent state. He wrote ominously that once employees were capable of becoming partners, and particularly sharing in profits of an enterprise, 'such a transformation would be the true euthanasia of Trades' Unionism'.[83]

Sidney and Beatrice Webb

If advocating partnership would be the euthanasia of trade unions, then proponents of unions had a real cause to be suspicious. The first great theorists of labour law, Sidney and Beatrice Webb, were initially keen in *Industrial Democracy* to stress that the structure of enterprise ought to be based on a strict separation of powers. They argued there were three functional decisions in enterprise: what to produce, how to produce, and the conditions of production. These were absolutely exclusive. Consumers exercising market choices determined the first, management (and by extension shareholders) determined the second, and workers, through their unions and by creating collective agreements should determine the third.[84] They argued the conflicts of interest 'permanently disqualified' consumers and management or shareholders from controlling conditions of production, because these groups would only want cheaper goods. Similarly workers were to be excluded from the spheres of what was produced and how by their less specialised knowledge, and lack of concern for consumer demand.[85] As such, the idea that unions would not share in management solidified. On the essential question of who determined the distribution of an enterprise's product, there had only to be joint settlement through collective bargaining. But the role of union was not, initially, in management.[86]

[82] JS Mill, *Principles of Political Economy* (1848) Book V, ch IX, §5 'the industrial economy which divides society absolutely into two portions, the payers of wages and the receivers of them, the first counted by thousands and the last by millions, is neither fit for, nor capable of, indefinite duration: and the possibility of changing this system for one of combination without dependence, and unity of interest instead of organized hostility, depends altogether upon the future developments of the Partnership principle.'

[83] JS Mill, *Thornton on Labour and Its Claims* (1869) 'The identification of the interest of the workmen with the efficiency, instead of the inefficiency of the work, is a happy result as yet only attained by co-operative industry in some of its forms. And if it should prove, in the end, not to be attainable otherwise; if the claims of the workmen to share the benefit of whatever was beneficial to the general interest of the business, became an embarrassment to the masters from which no system of arbitration could sufficiently relieve them, and growing inconvenience to them from the opposition of interest between themselves and the workmen should stimulate the conversion of existing businesses into Industrial Partnerships, in which the whole body of workpeople have a direct interest in the profits of the enterprise; such a transformation would be the true euthanasia of Trades' Unionism, while it would train and prepare at least the superior portion of the working classes for a form of co-operation still more equal and complete.'

[84] S Webb and B Webb, *Industrial Democracy* (1926) 822

[85] S Webb and B Webb, *Industrial Democracy* (1926) 818-820

[86] See also, S Webb and B Webb, *The History of Trade Unionism* (1920) 17, 'direction and control... are the special functions of the entrepreneur.'

Let's 'put this differently'

While the Webbs' theory of enterprise had a conceptual neatness, World War One changed their minds. Out of necessity to secure maximum production and minimum disruption, governments everywhere had to ensure some voice for labour at work. In an appendix to *The History of Trade Unionism*, in 1920, the Webbs said that circumstances had changed in a way that made them prefer to 'put this differently.'[87] They approved of the seating of worker or union representatives on boards of companies, and highlighted this as a particularly important goal for nationalised industry.[88] 'The need for final decisions,' they wrote, 'will remain,' but they said they had previously 'confined [them]selves unduly to a separation of spheres of authority'. Increased consultation through multiple levels of work councils, and consensus based decision making, informed by extended financial and social reporting, was apt to replace 'a great deal of the old autocracy'.[89] At this stage, however, the Webbs did not explain a clear view about the models for participation in private enterprise, there seemed to be little distinction between the private enterprises and specific enterprises coloured by a public interest, and there was little notion of how financial risks could be divided.

Codetermination by law

Also after World War One, the most important collective agreement in history was signed, in the midst of the German Revolution. On 15 November 1918, the *Stinnes-Legien Abkommen*, between Hugo Stinnes, a steel magnate on behalf of German employers, and Carl Legien, the chairman of the free trade unions, agreed to joint management and control in the future industry. This principle was put into the Weimar Constitution of 11 August 1919, where article 153 stated that 'property carries responsibility' and article 165 gave workers the promise of participation in the 'entire field of economic development'. The collective agreement finally resulted in legislation, when the *Betriebsrätegesetz 1920* (Work Councils Act 1920) codified the right of workers to send two representatives to company supervisory boards, along with the right of worker representatives to affect decisions on dismissals and a fixed list of workplace issues. These developments had been foreshadowed in the German legal tradition by the post-Bismarck *Arbeiterschutzgesetz 1891* (Worker Protection Act 1891), that had expressly empowered companies to voluntarily establish work councils; the Prussian Mining Act 1905, which after strike action had required work councils in the mining sector business; and the wartime *Hilfsdienstgesetz 1916* (Auxillary Service Act 1916), which had required work councils with limited powers in service industries. Nevertheless the

[87] S Webb and B Webb, *The History of Trade Unionism* (1920) 760, Appendix VIII, The Relationship of Trade Unionism to the Government of Industry. 'In 1920, after nearly a quarter of a century of further experience and consideration, we should, in some respects, put this differently. The growth, among all classes, and especially among the manual workers and the technicians, of what we may call corporate self -consciousness and public spirit, and the diffusion of education coupled with further discoveries in the technique of democratic institutions would lead us to- day to include, and even to put in the forefront, certain additional suggestions...'

[88] S Webb and B Webb, *The History of Trade Unionism* (1920) 760, 'It is a real social gain that the General Secretary of the Swiss Railwaymen's Trade Union should sit as one of the five members of the supreme governing board of the Swiss railway administration. We ourselves look for the admission of nominees of the manual workers, as well as of the technicians, upon the executive boards and committees, on terms of complete equality with the other members, in all publicly owned industries and services...'

[89] S Webb and B Webb, *The History of Trade Unionism* (1920) 761

foundational Weimar developments represented the first comprehensive retraction of the right to manage. The fact that the laws were the product of a collective agreement indicated how weakened the militarist industrialists of the German Empire had become, how far the functions of government had broken down, and how much the objectives of the German union leadership had shifted, given the total social and economic failure up till then.

The bureaucratic path

In both the United Kingdom and the United States there had also been a fundamental shift in the theory about the role of labour. The leading labour lawyers in the UK, Germany and the US were all on the same page.[90] However the practical measures, between Germany on the one hand and the UK and US on the other, differed in one crucial way. In the US, the National War Labor Board, established in April 1918 had the objective of bringing together employers and unions to codetermine the management of industry through a system of collective agreements and work councils. Business was firmly opposed to this incursion on their right to manage. The main employer association, the National Industrial Conference Board, made it clear that they viewed work councils as acceptable so long as this did nothing to impede the right of management to determine dismissals and control the distribution of the company product.[91] With insuperable opposition after the war, it was disbanded in May 1919. In the UK, the Whitley Reports aimed at securing joint management over the whole scope of industry, via a system of collective agreements in Joint Standing Industrial Councils. The system was, however, underwritten by the influence of the Ministry of Labour. It was empowered under the Trade Boards Act 1918 to fix wages in sectors where an acceptable system of collective agreements was not forthcoming. The willingness of the Ministry of Labour to act was dependent on the Ministry's political control by the Secretary of State, and in turn the sympathy of government to the project. The system was almost as short lived as the US War Labor Board. It fell victim to the first round of cuts, which took place under the Conservative led coalition with the Liberal party in 1922.[92]

Thus, the crucial difference was that in the US and UK, new structures for corporate change were underpinned by a bureaucracy. German policy was underpinned by law. While the strength German system was arguably eroded by judicial interpretation toward the end of the 1920s, it was only once the Nazis took power in 1933 that the system finally ended.[93] After the Second World War, re-establishing and entrenching codetermination was the foremost and non-negotiable goal of the German union

[90] In the UK, see S Webb and B Webb, *Industrial Democracy* (1897); in Germany see H Sinzheimer 'The Development of Labor Legislation in Germany' (1920) 92 Annals of the American Academy of Political and Social Science 35; in the US see JR Commons, *Principles of Labor Legislation* (2nd edn 1920) ch 1.

[91] National Industrial Conference Board, *Works Council Manual* (1920) Supplemental to Research Report No 21, Appendix, 'The right to employ and discharge, the direction of the working forces, and the management of the business, except as above stated, is reserved exclusively to the company...'

[92] Cave Committee, *Report to the Ministry of Labour of the Committee Appointed to Enquire into the Working and Effects of the Trade Board Acts* (1922) Cmd 1645

[93] Arbeitsordnungsgesetz 1934 §6, and FL Neumann, *Behemoth: The Structure and Practice of National Socialism* (2nd edn 1944). In practice, the freedom of work councils ended the moment that Hitler took the Chancellorship, and control of police through the Ministry of the Interior.

movement.[94] By that point, the total moral bankruptcy of German business leaders, after their staunch support for Hitler's policies of abolishing unions and democracy, meant that reform was possible.[95] Whatever debates there are today, economic democracy is entrenched in German law, and it has spread through most of the EU. The same cannot yet be said in the US and the Commonwealth. The post war developments in the German law of codetermination are relatively well known and discussed elsewhere.[96] For the purpose of this article, it is most fruitful to understand the initiatives to change corporations that occurred in systems without compulsory legal enactment.

UK codetermination: sectoral and issue specific

In the UK, collective agreements cannot be said to have changed corporate structures on any scale yet, but it is useful to mention the analogous initiatives for codetermination. There have been two main kinds. First, codetermination has existed on a sectoral basis in a number of public industries from at least 1896 up to today. This was usually underpinned by legislation, which in the later years resulted from the industry union indicating its willingness to participate to an agreeable government. Voluntary experimentation was advocated by the Donovan Commission in 1968,[97] before the Bullock Report's failed attempt at promoting legislation in 1977.[98] At various times, codetermination was seen in gas,[99] iron and steel,[100] the docks,[101] postal services,[102] and finally the railways in their first days as a privatised structure.[103] Today, though talked about little, it operates in universities, where staff and students sit on governing boards. A number of private companies did in fact experiment with worker directors through the 1970s, although their effective power in cases where there was no legislation was limited.[104]

The second kind of UK codetermination has existed on an issue specific basis. Certain defined fields of the common law right to direct have been carved out and shared with elected worker representatives. The Health and Safety at Work, etc Act 1974, section 2 has required joint management of workplace health and safety committees. More recently, the Pensions Act 2004, sections 241 to 243 require that at least one

[94] eg WH McPherson, 'Codetermination: Germany's Move Toward a New Economy' (1951) 5(1) Industrial and Labor Relations Review 20

[95] This might be said to have resulted from the other "collective agreement" of that tragic era in European history: at the Cologne residence of the banker, Baron Kurt von Schröder, Hitler met with the incumbent chancellor of the minority Conservative Party, Franz von Papen on 4 January 1933 and agreed to a coalition. Big business magnates like Krupp agreed to fund the next election, on the promise of abolishing unions and democracy. In the election socialists and communists were arrested and imprisoned, and opponent campaigners were intimidated or beaten up by Nazi thugs. See A Schweitzer, *Big Business in the Third Reich* (Indiana University Press 1964) 104-105.

[96] eg M Schneider, *A Brief History of the German Trade Unions* (1989). An excellent discussion of union goals post-war is found in C Kerr, 'The trade union movement and the redistribution of power in postwar Germany' (1954) 68(4) The Quarterly Journal of Economics 535.

[97] Lord Donovan, *Report of the Royal Commission on Trade Unions and Employers' Associations* (1968) Cmnd 3623, §§1000-1006

[98] *Report of the committee of inquiry on industrial democracy* (1977) Cmnd 6706

[99] South Metropolitan Gas Act 1896 until the Gas Act 1948 abolished it during the nationalisation programme.

[100] Iron and Steel Act 1967 Sch 4

[101] Mersey Docks and Harbour Act 1971

[102] Post Office Act 1977

[103] Transport Act 1968 s 38

[104] See the very important article by E Chell, 'Worker Directors on the Board: Four Case Studies' (1980) 2(6) Employee Relations 1. Chell examines the plans that operated in Berry Wiggins, the Mersey Docks and Harbour Company, the Bristol Channel Ship Repairers and the Computer Machinery Company.

third of pension trustees are representative of the employees and pension beneficiaries.[105] What is notable about pensions is that trade unions had negotiated representation on trustee boards, which would be entrenched and codified in the pension trust instrument, since the Trade Boards Act 1918.[106] It had become a common practice among larger unions to seek parity representation on pension boards with employers. All experience appears to suggest the normal conduct of business on trustee boards was consensual, rather than conflictual, delivering multiple benefits to all sides.[107]

US codetermination: union nominated directors

In the US there has also been, first, widespread codetermination on an issue specific basis, again in health and safety and pensions. The developments in pensions were spurred by the Taft-Hartley Act 1947, which required (in the opposite direction to UK legislation) that at least half of the seats of any fund to which an employer contributed would be representatives of the employer. The Taft-Hartley Act 1947 aimed to roll back union power, and the goal of this provision was to ensure that workers' savings could not be used as a private fund by a union for its own purposes.[108] After the law was passed however, unions took it as a cue to push for parity-codetermination in every collective, multi-employer pension plan.[109]

Second, the US has not seen significant legislation on a sectoral basis for worker representation on boards.[110] However, during the 1970s, a number of US trade unions bargained for board representation. In 1972 and 1973, pilots at United Airlines and workers at the General Tyre and Rubber Company had their proposals for representation rebuffed. In 1974, AT&T won a decision of the Securities and Exchange Commission (controlled at the time by the Republican government) that it was lawful for management to prevent a shareholder vote on having employee board representation.[111] The United Auto Workers declared that they sought representation on the board of Chrysler in 1976. The proposal was rejected,[112] but then in 1980 as Chrysler drifted into severe financial problems, the board conceded.[113] Another significant instance, in 1993 the United Steel Workers agreed to have representation on five company

[105] PA 2004 ss 241-243 was preceded by the Pensions Act 1995, which contained the same right for beneficiaries, but with an opt out. This followed from the Goode Report's recommendations in 1994.
[106] See Bournville Works, *A Works Council in Being* (1922) HD5 118, LSE archives
[107] eg T Schuller and J Hyman, 'Pensions: The Voluntary Growth of Participation' (1983) 14(1) Industrial Relations Journal 70
[108] Taft-Hartley Act 1947 §302(c)(5). Republican Party Senator Robert Taft wanted no union voice in their pensions at all, see Senate, *Congressional Record*, 80th Congress 1st Sess (1947) 4892-94.
[109] The threat to the survival of these pensions is significant, as is their general importance for pension 'reform' proponents.
[110] There are remarkable exceptions in the company laws of Massachusetts and New Jersey, which expressly allow some companies to put employees on the board, eg Massachusetts Laws, General Laws, ch 156, §23. This was introduced under the governorship of Calvin Coolidge: An Act to enable manufacturing corporations to provide for the representation of their employees on the board of directors (3 April 1919) Chap. 0070.
[111] *American Tel. & Tel. Company*, CCH Fed. Sec. L. Rep. 79,658 (1974). This decision concerns what US corporate lawyers call the 'no action' letter. Under the Securities and Exchange Act 1934, SEC Rule 14a-8 allows shareholders to put proposals on proxy forms, which are circulated to all a company's shareholders for a vote. They have this right unless it falls within 'day to day business' that is considered within the legitimate sphere of management's control. It follows that if directors choose to take 'no action' to put a proposal to a vote, the only remedy of shareholders lies in removing the board and replacing it. The ability to do this depends on the state's law, but it is notoriously difficult in the most important state, Delaware.
[112] 'Auto Union Seeks Directors' Seats (13 May 1976) NY Times, 51, col 8
[113] JD Blackburn, 'Worker Participation on Corporate Directorates: Is America Ready for Industrial Democracy?' (1980-1981) 18 Houston Law Review 349

boards for a period of six years.[114] By 1999 there had been around 35 major representation plans.[115] This seems even more remarkable given the environment that US unions face. It was frequently urged, somewhat desperately, by opponents and sceptics that such developments would violate the provisions of the National Labor Relations Act 1935, which required unions to not be dominated by management, or the antitrust laws, or something else.[116] However the real problem was instead that management sought to link representation to share ownership plans. Most share ownership plans into which employees were enticed would have no voting rights, and if they did they would never be enough to afford a significant share of participation. Moreover, the tolerance of American workers for ESOPs was drastically reduced by the collapse of Enron.[117] If the workforce had invested undiversified capital in the business, they stood to lose not just their jobs, but also their pensions and savings if the business environment turned bad.

Contemporary theory

In the modern writing that relates to corporate governance and labour, there is a very significant contrast to the early theory. There is now a recognition that, unlike a century or half a century ago, rigid class divisions have dwindled. Stratification of income and education remains, and is probably becoming worse than twenty or thirty years ago. But there is no longer a binary divide between owners of capital and workers. Henry Hansmann and Reiner Kraakman have argued that, because a large portion of capital invested in the stock exchanges derives from employees' retirement savings, shareholders and employees no longer constitute clearly divided groups.[118] This point cannot be taken too far, because employees in their capacity as beneficiaries of institutional shareholders are systemically separated in most cases from actual influence in the way their money is used. Nevertheless it is true that the ultimate investors of capital are a largely similar body of people to those who work for a living.

Leo Strine has also argued in favour of an identity of interest between workers and the directors of corporations,[119] in contrast to the kind of shareholder who seeks purely to maximise short term value for itself at the expense of others: the stereotypical hedge fund, private equity firm, or corporate raider. The identity of interest here lies in the idea that the workforce and management alike are the people who have most invested in the business, not because they have money, but because they give the enterprise its culture and essence.[120] Stephen Bainbridge, who has perhaps ungenerously been referred to as the 'Tea Party' caucus of US corporate law academia,[121] has ridiculed this notion. In his view management elites

[114] 'The Unions Step on Board' (27 October 1993) Financial Times
[115] RB McKersie, 'Union-Nominated Directors: A New Voice in Corporate Governance' (1 April 1999) MIT Working Paper
[116] eg 'Labor Unions in the Boardroom: An Antitrust Dilemma' (1982) 92(1) Yale Law Journal 106. cf JB Bonanno, 'Employee Codetermination: Origins in Germany, Present Practice in Europe and Applicability to the United States' (1977) 14 Harvard Journal on Legislation 947
[117] See generally, PJ Purcell, 'The Enron Bankruptcy and Employer Stock in Retirement Plans' (11 March 2002) CRS Report for Congress
[118] H Hansmann and R Kraakman, 'The End of History for Corporate Law' (2000) Working Paper No 00-09, 16.
[119] L Strine, 'Toward Common Sense and Common Ground? Reflections on the Shared Interests of Managers and Labor in a More Rational System of Corporate Governance' (2007) Institute for Law and Economics Research Paper, No. 07-25
[120] eg *Paramount Communications, Inc. v. Time Incorporated*, Fed Sec L Rep (CCH) 94, 514; affd 571 A.2d 1140 (Del. 1989) per Chancellor Allen.
[121] See 'WTF is Jack Coffee's problem?' (20 December 2011) ProfessorBainbridge.com.

inevitably regard the masses with scorn.[122] While it appears obvious that the potential for conflicts of interest among shareholders, directors and workers may always arise, the value in Hansmann, Kraakman and Strine's work lies in the acknowledgement that laws and institutions may be restructured in a way that reduces conflict. If this is true, then social conflict is largely socially constituted. In particular, if the actions of shareholding institutions can be made accountable to the people who ultimately invest in them, and if directors can be made accountable to the workforce upon whom their power to appropriate and direct depends, then the largest sources of conflict would be resolved. This leads to the substantive part of this article: change is possible and practical through the mechanics of company membership and constitutions.

3. Mechanics of company membership and constitutions

The mechanics of a company constitution are lawful objects of negotiation for a trade union. The power of UK unions to get collective agreements has always depended on their freedom to take collective action 'in contemplation or furtherance of a trade dispute'.[123] The meaning of a 'trade dispute' has varied over time, but if it relates to an employment contract at the minimum it will be lawful.[124] A company constitution that gave rights to employees would be incorporated into every employment contract, but even if it was not it would relate to the employment relationship.[125] Company constitutions are legal structures that lie somewhere in between a commercial contract and the constitution of a nation state.[126] They are based on a general ethic of freedom and flexibility, but are heavily underscored by compulsory norms to protect the weaker parties. In UK law the main constitutional document is called the 'articles of association'. It literally has articles, which set out the terms upon which company members associate with one another. Three main questions matter here. First, how can employees become members of the company, by becoming privy to the 'company contract'? Second, how can the company constitution be amended, for the purpose of entrenching various rights? Third, how can provisions of the company constitution be enforced, by who, and to what ends?

Company membership

Formally acquiring membership of their company is, for employees, a crucial first step in effective corporate change. Membership delivers all the rights articulated in the Companies Act 2006. These include the right to vote on resolutions, to propose resolutions, to call meetings, to dismiss directors, to enforce

[122] S Bainbridge, 'The Shared Interests of Managers and Labor in Corporate Governance: A Comment on Strine' (2007) UCLA School of Law, Public Law & Legal Theory Research Paper Series, Research Paper No. 07-15

[123] Trade Union and Labour Relations (Consolidation) Act 1992 s 219

[124] *BBC v Hearn* [1977] 1 WLR 1004, 1010-1011

[125] *P (A Minor) v National Association of School Masters/Union of Women Teachers* [2003] UKHL 8, [2003] 2 AC 663, [4]

[126] There is a long, and sometimes fruitful, debate among company lawyers about whether companies have more of a 'contractual basis' or are more creatures of state enactment and concession. The basic dividing line is drawn between those who believe in 'freedom of contract' (enforcement of any terms, no matter how notional the quality of consent) and those who advocate more compulsory rules to protect shareholders, creditors, employees and so forth (no matter how bureaucratic and costly such compulsion may prove to be). For a broad spectrum of opinion, at least among US corporate lawyers, see the special edition on 'Contractual Freedom in Corporate Law' in (1989) 89(7) Columbia Law Review 1395 ff. The articles by Frank Easterbrook and Daniel Fischel contrast most with Melvin Eisenberg, with John Coffee and Robert Clark marking intermediate positions.

the company constitution in court with a personal or derivative claim, or to receive financial accounts.[127] UK company law requires only two company organs: the board of directors, which is accountable to the general meeting.[128] Members of a company would invariably exercise their voice in the general meeting. To become a member, someone must simply be entered on the company's register of members.[129] However, the default rule is that in companies with share capital, members have a vote according to the capital they have invested. This nexus between voting and money is subject to any provisions in the company's articles.[130] It has already been stressed that employee participation cannot be dependent on money. Employees should not be forced to pay twice for participation: once through their investment of labour, and a second time through the purchase of a capital stake. Indeed, the desire for participation is wholly distinct from the desire to receive dividends, and the wish to bear any financial liability. With this in mind, the Companies Act 2006 gives three main options to acquire membership, with varying requirements: (1) membership through a simple decision by the board of directors to allot shares at the nominal share price (that is usually far below market value) to employees, (2) by the existing shareholders voting with a simple majority create a new class of employee shares, or (3) by the existing shareholders voting by a three quarter majority to amend the constitution so as to grant membership to employees without shares at all.[131]

Membership by directors' decision: share issue at nominal value

Employees can become company members, without any vote of shareholders, and by a simple decision of directors upon a collective agreement. To get the bare benefits of being able to enforce the company constitution, employees could naturally purchase one share each. This would be cheap, but the voting power would not amount to much. A substantial issue of shares is desirable, and this is possible with the special exemptions that exist for 'employee share schemes'. These are plans for 'encouraging or facilitating the holding of shares' by employees, former employees or their relatives.[132] Usually, if directors wish to allot new shares in the company, this must be approved by an affirmative vote of shareholders, or the directors must be empowered by a provision in the constitution.[133] The purpose is to ensure that the new share allotment will not dilute shareholder power or financial returns, without their say. But the requirement is disapplied for employee share schemes.[134] Also, when new shares are issued, and for the same reasons, existing shareholders are usually entitled to the right to pre-empt the sale, and buy the new

[127] Companies Act 2006 ss 284, 292, 303, 168, 260-263 and 423.
[128] Companies Act 2006 ss 154 and implicitly from 301 ff. Company members need never actually physically meet, yet there is still a right to meet.
[129] CA 2006 s 112(2) 'Every other person [after subscribers to the first company constitution at incorporation] who agrees to become a member of a company, and whose name is entered in its register of members, is a member of the company.'
[130] CA 2006 s 284(1) 'On a vote on a written resolution— (a) in the case of a company having a share capital, every member has one vote in respect of each share or each £10 of stock held by him... (4) The provisions of this section have effect subject to any provision of the company's articles.'
[131] CA 2006 ss 21-22, rarely a company can have a 'provision for entrenchment' requiring a higher threshold, say 80% or 95%. However this can only be introduced at a company's formation or through a unanimous vote subsequently.
[132] CA 2006 s 1166
[133] CA 2006 s 549(1)
[134] CA 2006 s 549(2)(a)

shares first.[135] But once again, for employee share schemes this right is disapplied.[136] The crucial question, then, is whether directors have the power to allot significant numbers of shares without employees having to pay for them.

The Companies Act 2006 presents some hurdles. A basic rule is that shares may not be issued at a discount, below their 'nominal value'.[137] The nominal value of a share is a sum stipulated by the company when they first begin trading,[138] but is routinely far lower than the price they trade at. The market price is the nominal price plus the 'premium'. For instance, on 27 May 2013, ordinary shares in BP were trading at $43.53, while the nominal value is 25 cents (0.57 per cent of the market price). Companies usually set the nominal value of shares at a much lower price than what they expect them to trade at because if they do not, and the share price falls significantly, and they wish to raise more equity capital, they must go through a procedure for issuing more shares (requiring a shareholder vote). The justification for companies being prohibited by law from issuing shares at a discount below their nominal value is allegedly to protect creditors. If a company goes insolvent, shareholders lose the money that they have invested in the shares. But if a shareholder, for example, could get a £1 share for 25 pence, then it can be argued that less capital would be in the company to satisfy the creditors' claims after insolvency.[139] That said, if a company has issued shares with a nominal value of £1, the rise in the market premium could mean the shares are worth £2.70, for example, or far higher. A public company is an under an obligation to ensure that shares are at least one quarter paid up by the new shareholder, but again this requirement is disapplied for employee share schemes.[140] Moreover, supposing that the directors of a company declare they have nominally valued shares at 1 penny, and they trade at £2.70 or £270, it has been judicial policy that 'so long as the company honestly regards the consideration as fairly representing the nominal value of the shares in cash, its estimate ought not to be critically examined.'[141]

All this means that, where company constitutions set the nominal value of ordinary shares at a lower than market price, directors could allot shares to employees at nominal value, but not paid up.[142] A collective agreement could therefore seek management's agreement to allot shares with full voting rights for a price that was the nominal value. Such shares would presumably also carry a right to dividends, but to ensure

[135] CA 2006 s 561
[136] CA 2006 s 566
[137] CA 2006 s 580
[138] CA 2006 s 542
[139] *Ooregum Gold Mining Co of India v Roper* [1892] AC 125, Lord Halsbury LC, 'the Act of 1862… makes [it] one of the conditions of the limitation of liability that the memorandum shall contain the amount of the capital with which the company proposes to be registered, divided into shares of a certain fixed amount. It seems to me that the system thus created by which the shareholder's liability is to be limited by the amount unpaid upon his shares, renders it impossible for the company to depart from that requirement, and by any expedient to arrange with their shareholders that they shall not be liable for the amount unpaid on their shares.'
[140] CA 2006 s 586
[141] *Ooregum Gold Mining Co of India v Roper* [1892] AC 125, Lord Watson
[142] That English courts do not inquire into the fairness of a contractual exchange, where the bargaining power of the parties is equal, or that consideration must generally speaking be sufficient and not adequate, is a familiar principle of contract law: see *Williams v Roffey Bros & Nicholls (Contractors) Ltd* [1989] EWCA Civ 5, [1991] 1 QB 1, 18, and *Chappell & Co Ltd v Nestle Co Ltd* [1960] AC 87, 114.

that existing shareholders suffered no dilution of their financial interest, the collective agreement could easily include a clause for any dividend payments to be automatically returned to the company's accounts.[143] The feasibility of this approach would depend on the nominal value of the company's shares, which is stipulated in the company's 'statement of capital' registered at Companies House, and what could be done to mitigate the risks of insolvency.[144]

Membership by ordinary resolution: new share class

The foregoing approach is less attractive in that it remains technically wedded to the financial investment paradigm of voice in companies. A more agreeable solution is to create a different class of shares altogether, and stipulate that such shares are to be allocated on the basis of holding a contract of employment. The Companies Act 2006 section 585 does state that public companies 'must not accept at any time, in payment up of its shares or any premium on them, an undertaking given by any person that he or another should do work'. The mischief which this section targets is management receiving large bonuses in company shares at their own instance, in return for little. It would not be applicable if the newly created class of shares made clear in its terms that shares were not being allocated in return for 'payment' by employees' labour, but were allocated as an automatic incident of employment, unrelated to the value of work performed, wages or anything else. The matter would be wholly outside the paradigm of remuneration being proportional to performance, because the object would be to grant membership on the basis of equality. The ability to issue new classes of shares is, however, not presently subject to an exemption for employee share schemes. The power to issue different classes of share is determined by each individual company constitution. To give an example, the Model Articles for Public Companies require in article 43 that it can be done by ordinary resolution,[145] that is a majority vote of shareholders.[146] This is a far greater hurdle than the allotment of shares upon payment of a nominal price by directors, although it may not be so great as it initially seems.

Membership by special resolution: constitutional amendment

The neatest option is simply to amend the company constitution to create the right of membership, with whatever desired percentage of voting rights, for everyone with a contract of employment. For example, in the Model Articles of Public Companies, article 1 states that "'member" has the meaning given in section 112 of the Companies Act 2006'. As explained above, this refers in turn to anybody who is entered on the register of members, and it presupposes (though does not require) that each member will have shares. But then, in section 284 the general rule for votes is that they are proportionate to the number of shares possessed, subject to a company's articles. The Model Articles are silent on voting rights, except to say in article 34 that resolutions at meetings are determined by a show of hands unless a

[143] For instance, 'The parties to the collective agreement, and all employee members, agree that all distributions or dividends to which they are formally entitled shall be held on trust for the company, and that they shall irrevocably forgo all rights thereto.'
[144] CA 2006 ss 9 and 10. The Companies House website can be used to search for these.
[145] The Companies (Model Articles) Regulations 2008, Sch 3, art 43
[146] CA 2006 s 282. The newly created class must then be registered at Companies House in the normal way, CA 2006 s 638.

formal poll is demanded. This could easily be amended so that article 1 states a member has the section 112 meaning 'and also includes every person who holds a contract of employment with the company.'[147] Then, a new article 34(2) could be inserted to read, for instance, as follows: 'Members with a contract of employment shall have equal voting rights among themselves. Together these shall constitute one third of the voting rights of the company'. In order to introduce such a provision, or something similar, it would be necessary under the Companies Act 2006 section 21 to procure a three-quarter majority vote of shareholders in favour.[148]

Collective bargaining with directors and shareholders?

Is it feasible for a trade union to seek a collective agreement with a company board, which also depends on shareholder approval by a majority (to issue a new class of shares) or a three quarter majority (to amend the constitution)? There are at least three reasons to believe this is not such an unlikely venture. First, and most fundamentally, the majority of proposals by management, including amendments to a company's constitution pass so long as management recommends it. Both shareholders and management can propose constitutional amendments,[149] but a director led proposal (for instance, which is the result of collective bargaining) is in practice more likely to succeed. In any company meeting, or on any resolution, the requirement for a three quarter majority is simply one among those who actually are voting. Since the 2007-2008 financial catastrophe, there has been a series of initiatives to ensure shareholding institutions actively use their voting power and 'engage' with company boards, culminating in a comply or explain instrument called the Stewardship Code 2010. Most shareholding institutions, however, remain willing to go along with well considered management initiatives. The simple notion of ensuring a voice for people at work can easily be seen as a measure to enhance company productivity for the benefit of everyone.

Second, trade unions and their members can use their influence as shareholders to support amendments to a company constitution, particularly through codetermined pension funds. Pension funds frequently distribute their investments among large numbers of companies, but in some they may be more concentrated than others. Large pensions often manage their own investments, and can therefore use their financial influence to directly support initiatives favoured by their trade union. This would require a union to actively coordinate the message it sought to convey through its negotiators and work with its affiliated pension trustees. However, many smaller pension funds delegate investment management to fund

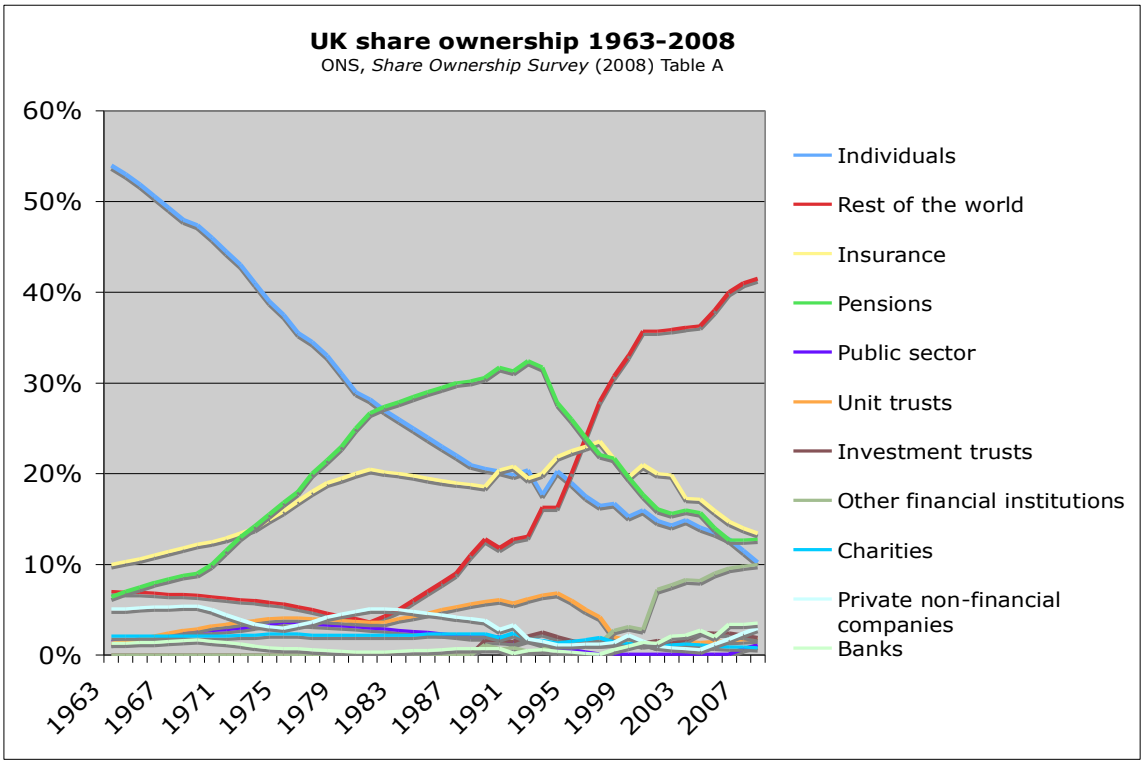
[147] To resolve any difficulties about who is an employee, it would be also a safe route to add two things. First, that it will be company policy to treat any person who provides work, and is in a position of relatively unequal bargaining power, as an employee, including any person hired through an employment agency, or on a casual, part time or temporary basis. This should be consistent with the approach that a company takes to keeping a list of its employees, as required by CA 2006 s 411. This adopts the approach to construction given by the UK Supreme Court in *Autoclenz Ltd v Belcher* [2011] UKSC 41, [35]. Second, it should be stipulated that any employee of a subsidiary company shall be regarded as an employee of the parent company, whether it is the parent through shareholding or other form of decisive influence. This uses an approach to company groups familiar in competition law.

[148] Other English speaking jurisdictions have different requirements. The Delaware General Corporation Law §242(b)(1) requires an ordinary majority of stockholders, but the initiative for amendment lies with directors. Commonwealth countries tend to be similar, eg the Canadian Business Corporations Act 1985 s 173 requires a three quarter majority. The Australian Corporations Act 2001 s 136(2) requires a three quarter majority vote.

[149] CA 2006 ss 292-294

management firms, such as Henderson, Blackrock, Schroder, UBS and so on. It is not yet common practice, but there is a basic right in equity to give instructions on any issue to a fund manager, who counts as a fiduciary.[150]

Third, a trade union can directly engage with shareholding institutions. The world of financial power is indeed a strange one, but can a few basic elements can be generalised. Most company shares are owned by three kinds of institutions: pension funds, insurance companies and various other 'mutual' fund firms.[151] In the UK these institutions are not distinct, so insurance companies offer mutual fund services, and both attempt to sell investment services to pension trust funds. The upshot is that the vast majority of wealth in FTSE 100 companies, although from a variety of sources recorded by the Office of National Statistics in the chart below, is controlled by fund managers.[152]



In each fund management firm, a small group of people (let us say between 3 to 10 men) control all the

[150] See *Kirby v Wilkins* [1929] 2 Ch 444

[151] 'Mutual' fund is less of a technical term than a convenient label for a whole range of collective investments institutions, as defined by the Financial Services and Markets Act 2000 s 235. Mutual funds can be seen to include unit trusts, open-ended investment companies (pronounced 'oik'), hedge funds, funds of funds, and so on. These are all simply different kinds of legal vehicle (trusts, companies, or contracts) to invest money along with other people who are interested in the same 'financial product': a person buying into a unit trust or an 'oik' will choose a certain class of assets with infinite combinations of risk, some of which usually contains company shares. Other asset classes are company bonds, government bonds, commodities, foreign exchange reserves and 'derivatives' (like the option to buy one of the foregoing, or a right to buy it in future). The service provided by the fund manager will be in monitoring or trading with these investments in an attempt to match or perhaps outperform the market standard.

[152] Three notable points about UK share ownership are (1) the terminal decline of individual shareholding and with it the collectivisation of capital (2) the rise and fall in pensions' share of the equity market, which correlates with the power of trade unions (3) the massive upswing of the 'rest of the world's ownership of UK shares: this is globalisation in action.

voting power. A typical top 30 fund manager may have about £50 billion invested in around 300 to 400 companies' shares, out of, let us say, £500 billion 'assets under management'. So if the average UK salary is around £25,000 in each firm a similarly small group of fund managers controls an amount of money equivalent to the combined salaries of about 2 million people. Usually there will be an assistant corporate governance manager, or perhaps a small team, which carries out the fund managers' decisions on the matters in which they take an interest. However, more routinely, the corporate governance departments pay a company called Institutional Shareholder Services, or another, for advice on how to vote. ISS is called a 'proxy advice' company. It employs around 250 staff in London who research the activities of all publicly traded companies. Fund management firms pay ISS for advice on how they want to vote shares (by 'proxy'). Payment for this advice can be likened to payments to a credit ratings agency: they rate the private companies that pay them. Fund managers get the type of advice they want. For a trade union this means that there are two potential actors, beyond company boards, with whom dialogue and engagement could prove useful. First, fund management institutions, and second the proxy advice firms. Both need to be persuaded of the obvious merits that greater employee involvement in companies would bring for long term stability, growth and managerial accountability.

Enforcement of the constitution

While the emphasis so far has been upon securing company membership *per se*, and in addition securing significant voting power, the ability to enforce the terms of a constitution is important in its own right. Without becoming a member of a company, employees would be treated in the same way as any third party to a contract. Suppose that a company constitution purported to confer a benefit upon employees, either individually or as a group. For example, a constitution might state that it would not make any staff redundant without consultation and approval from the trade union, or an agreed social plan. Without membership, the enforceability of such a provision at common law is not entirely clear. The Contracts (Rights of Third Parties) Act 1999 section 1 provides that, in most contract types, someone who is conferred a benefit under a contract may enforce it, unless the parties' intentions are construed to be otherwise. However, section 6 excludes companies from the Act's scope. The better view of the pre-existing common law is that a third party beneficiary can enforce a contract conferring such a benefit,[153] and the 1999 Act was built upon the principle that the common law would develop.[154] But this is not totally clear.

The leading company law authority points in the old direction. In *Eley v Positive Government Security Life Assurance Co Ltd*,[155] a solicitor attempted to sue to enforce a provision in the company's constitution that said he should remain the solicitor. He had in fact drafted the constitution, and surreptitiously insert the provision without true agreement. He later sued for 'breach of contract'. Lord Cairns LC held that the company constitution was only 'a matter between the directors and shareholders, and not between them

[153] The better view of the law is represented by *Beswick v Beswick* [1966] Ch 538, per Lord Denning MR.
[154] Law Commission, *Privity of Contract: Contracts for the Benefit of Third Parties* (1996) Report No 242, para 5.10
[155] (1876) 1 Ex D 88

and the plaintiff'. Mr Eley had himself become a shareholder, and it seems that if the courts had not been so unimpressed with the innate demerits of his claim, they could have said he would be able to enforce the constitution if he had sued in his capacity as a member of the company.[156] On this view every member has a right to sue to enforce compliance with the company constitution. At the very least, every member has the right to bring a derivative claim to enforce the duties of directors,[157] which under the Companies Act 2006 section 171 includes a duty to comply with the constitution. The main threshold requirement is that enforcement of the right would promote the success of the company for the benefit of members, with regard to other stakeholders, including employees.[158]

4. Specific topics for bargaining

So far, the reasons for seeking corporate change through collective bargains have been explored, and some basic mechanics of the company constitution have been outlined: the concept of membership, how to get it, how to get a substantial numbers of votes, how to amend the constitution, and how to enforce it in court. This would create rights for employee members identical to the compulsory or constitutional rights that exist for shareholding members. However there are at least five specific topics where changes could be made to create rights of significant importance to employees. Acquisition does not necessarily depend on membership: substantial corporate change can come through agreement by the board of directors.

4.1 Representation on the board of directors

Collective agreements are easier to conclude when you elect people you bargain with. Under the Companies Act 2006 sections 172 and 173, every director has a duty to act in the way she or 'he considers, in good faith, would be most likely to promote the success of the company', and to exercise independent judgment,[159] for the benefit of members with regard to stakeholders.[160] Contemporary corporate governance standards create the expectation that shareholders engage with boards, while they also exercise heavy influence over appointments. In the same way, trade union engagement with management for the purpose of concluding collective agreements would be substantially assisted if employees also exercised electoral influence.

Is the importance of board representation exaggerated?

The value of being able to elect a specified number or percentage of directors on boards may, however,

[156] cf PL Davies, *Gower and Davies' Principles of Modern Company Law* (2008) 69-70, and *Quin & Axtens, Ltd v Salmon* [1909] AC 442.
[157] CA 2006 ss 260-263
[158] CA 2006 s 172
[159] CA 2006 s 173(2) adds the duty is not infringed by acting 'in accordance with an agreement duly entered into by the company that restricts the future exercise of discretion by its directors'. This plainly includes a collective agreement.
[160] It may be noted that CA 2006 s 173 effectively repeats the s 172 requirement to promote the company's success in the way 'he considers' is best. Under s 172, almost every conceivable 'stakeholder' is listed to which a director must pay regard. The glaring exclusion is that directors cannot pay regard to their own interests: s 172 is the flip side of s 175 on avoidance of any possibility of a conflict of interest.

have been given undue attention, given the results it has produced in countries with codetermination laws. First of all, unless employee representatives constitute a majority of board members, they might be routinely outvoted. In Germany, which is usually referred to as having a system of 'quasi-parity' codetermination, in companies of more than 2000 staff members, employees and trade unions elect half of the seats on the supervisory board (*Aufsichtsrat*).[161] However, the chairperson, who holds a casting vote, is always accountable to the shareholder voting block.[162] The supervisory board's role, sometimes seen as roughly approximating the role of non-executive directors and the chair in the UK,[163] is to monitor the long term progress and strategy of the company, and elect the day to day executive members, who sit on a separate board (the *Vorstand*).[164] The result of shareholders having a slight majority on the supervisory board means that in every vote for every member of the executive, they win. Only one 'staff director' (*Arbeitsdirektor*) is required by law on the executive to be accountable to the workforce.[165]

On the other side, the agenda of shareholder elected directors in German companies is mostly determined by banks. It follows that Commerzbank, Deutsche Bank, UniCredit, Postbank and a few others dominate the executives of all major German companies.[166] This is because, in a not dissimilar fashion from fund managers in the UK, German banks act as custodians for almost all shareholders. Through an historical quirk of the German civil law, shares had to be certificated. Certificates had to be kept safe. Banks kept the shares certificates safe. They also used standard form contracts with their shareholder customers to appropriate the right to cast votes. If they receive instructions the banks must follow them, and since the *Aktiengesetz 1937* (Public Companies Act 1937) the law requires that all such votes cast have to be 'in the interests' of the depositor.[167] But this is just a paper duty. It appears to be wholly unenforceable. What evidence would suffice to show the bank had not acted in your interests? Because of the law's practical inefficacy, a government report in 1979 proposed that the banks' corporate governance departments be required to represent depositors.[168] Recently in Switzerland, where the same system operated, a referendum of March 2013 abolished the analogous right of its banks to appropriate depository votes altogether.[169] Until some similar development happens in Germany, the result for labour is this: while employee representation among the board of directors provides multiple benefits, it does not

[161] Mitbestimmungsgesetz 1976 §§1, 7 and 9
[162] Mitbestimmungsgesetz 1976 §§27-29
[163] Such analogies are fundamentally incorrect in the sense that the German system in effect insulates the executive from direct accountability to the general meeting (*Hauptversammlung*) or the employees.
[164] Aktiengesetz 1965 §§ 84 and 111
[165] Mitbestimmungsgesetz 1976 §33
[166] cf F Kübler, 'Comment: On Mark Roe, German Codetermination and German Securities Markets' (1998-1999) 5 Columbia Journal European Law 213, 'Most shareholders give their proxy to a limited number of nationally operating banks. For the election of shareholders' representatives to the supervisory board of the public corporation, management prepares a list of candidates which, although open to discussion with the banks, are almost certain to be accepted. This list will presumably contain the names of managers of other large publicly owned corporations including financial institutions. Thus, if there are large institutional shareholders (banks, insurance companies or industrial firms), they will be offered proportionate representation; they will delegate managers of exactly the same type which we find on management's list. For this reason there will be very little or even no difference between the board of a purely public corporation and a company with one or several significant shareholders.'
[167] Aktiengesetz 1965 §135
[168] Geßler Commission, Bundesministerium der Finanzen, *Grundsatzfragen der Kreditwirtschaft - Bericht der Studienkommission* (1979) 287.
[169] Swiss referendum "against rip-off salaries" (3 March 2013) inserting a new article 95(3) into the Federal Constitution of 18 April 1999.

necessarily stop domination of corporate priorities by shareholding institutions generally, and banks in particular.

The continuing importance of the general meeting

Because of the role of banks and the two tier board system in Germany,[170] the experience of countries with unitary boards is more enlightening. Swedish corporate law requires that three members of the board of directors, but no more than half the total board, is elected by the workforce.[171] This may well result in substantially greater influence than in Germany in many large companies, especially because the remaining shareholder representatives are strongly influenced by worker-friendly shareholders, particularly pension funds. The essential point is that if managerial accountability is a desirable goal, the law should encourage the possibility of coalitions between shareholder and worker groups, where their interests are identical or overlap. On this approach, and while Sweden too has considerable room for development, direct elections for members of the board take on secondary importance, compared to the importance of voice within the company's general meeting.

Conflicts on the board

Moreover, it is highly desirable that a board of directors is not riven with competing camps of interest group. Such systems of 'consociationalism' can predictably reduce a board's capacity for cohesive collaboration.[172] Germany overcomes the problem of conflict by effectively stultifying the influence that employees appear to have when it comes to the executive. This said, Swedish experience suggests that the potential for actual conflicts between shareholder and worker directors are overstated, when shareholding institutions actually represent the ultimate investors. The problem can be overcome altogether if different interest groups' differences are resolved within the representative voting procedure between the general meeting and the board. One of the very reasons for representative, rather than direct, voting structures is they overcome social conflict.

Appointments by director decision

With the point in mind that membership in the general meeting, while visibly less dramatic, is practically more important, there are at least three ways collective agreements could secure board representation. The appointment process for directors is not in fact a matter of any compulsory rules in the Companies Act

[170] The compulsory nature of the supervisory board, which the general meeting could not sidestep, was solidified by the Aktiengesetz 1937: in the (Nazi government's) Official Reasons it was stated that the changes aimed to stop this: 'that the Board in the course of its administration depends to the extent hitherto known on the mass of irresponsible shareholders who mostly lack the necessary insight into the position of the business.' FA Mann, 'The New German Company Law and Its Background' (1937) 19 Journal of Comparative Legislation and International Law 220, 229. It remains contested that the supervisory board insulates directors on the ground that shareholders, with significant collective action problems, ought to have a permanent representation. On this logic, one would presumably support a law to require that Members of Parliament be elected by local councils, and that citizens can only elect the councillors, on the grounds that it would increase the accountability of MPs to the electorate. If that sounds absurd, so is the German supervisory board.

[171] Board Representation (Private sector employees) Act 1987 §§4-5 (*Lag (1987:1245) om styrelserepresentation för de privatanställda*). For an assessment, see K Levinson, 'Employee representatives on company boards in Sweden' (2001) 32(3) Industrial Relations Journal 264.

[172] R Kraakman et al, *The Anatomy of Corporate Law* (2nd edn OUP 2009) 101 ff. It is unclear whether the authors' concerns would be allayed by compulsory representation for workers as members in a company's general meeting.

2006. The only compulsory rule is that the general meeting may always remove any director on 28 days notice and a fair hearing.[173] It is left for a company's articles to determine, although the UK Corporate Governance Code 2010 does contain standards on board structure, auditing, procedures for setting executive pay, and the committee of the board that is responsible for appointments. Companies must comply, or disclose in the annual report their reasons if they choose not to. Usually it is expected that the chair and non-executive directors perform the appointments. Without any further requirement, a trade union could simply bargain for the appointments committee to appoint, for example, a minimum of two people freely chosen by the workforce. The reason to aim for a minimum of two worker representatives is that one person can become isolated, while two tend to complement each others' work and are less likely to become outspoken.[174]

Constitutional entrenchment

To entrench the right of workers to appoint directors the company constitution could be amended. To use the Model Articles for Public Companies as an example, a new article 20(2) could be inserted as follows: 'A minimum of two directors shall be appointed who have been elected in a secret ballot by members with a contract of employment. The timing of the ballot shall coincide with the annual general meeting.' The benefit of having members of the board who are expressly responsible to a company's workforce, even if in a permanent minority, lie in the improved flow of information between the company's front line and its bottom line. An additional benefit is that the trade union could press for the employee representatives to sit on the remuneration committee.[175] The increased capacity for scrutinising the executives that worker representatives would exercise would plainly benefit the long term profitability for shareholders, and the overall success of any company.

4.2 Security of pay and jobs in insolvency

A voice in insolvency matters because if short term decline cannot be prevented, employee participation will affect two critical matters: whether or not employees receive their wages and whether their jobs survive. Evidence in jurisdictions with codetermined boards suggests that medium and large companies are less likely to fail than in English speaking jurisdictions where direct workforce representation is lacking. However, once a company does go insolvent, jurisdictions with codetermination often cease to give much voice to employees.[176] After insolvency, members of the company lose their rights, and the company's creditors generally take control. This means that employee voice depends on the kinds of credit and security for which they may contract.

[173] CA 2006 ss 168-169. This is a compulsory and effects based standard for large companies, cf *Bushell v Faith* [1970] AC 1099.
[174] Experience from women members on boards of directors, and union nominated directors in the US show this.
[175] At present the UK Corporate Governance Code 2010 D.2.1 states the remuneration committee can be composed of the chair and two independent non-executive directors, while any vote of the general meeting is not binding under CA 2006 s 459. The general meeting could, in such a vote, simply declare that if the result of the vote is not followed every director will be dismissed, effectively coupling it with the general meeting's power under CA 2006 s 168.
[176] See generally, E Geva, 'Convergence and Persistence in Corporate Insolvency Law: Employee Participation in Corporate Insolvency Restructuring' (2011) 12(2) European Business Organization Law Review 315, 348 ff

Security of pay

If a company has not paid employees their wages, reflecting minimum standards across the EU,[177] the UK's National Insurance fund must reimburse employees up to a maximum of £450 a week for 8 weeks.[178] Were it not for this limited sum, employees would be highly unlikely to receive much money at all. Among the host of creditors to whom an insolvent company may owe money, employees rank third in the UK's payment queue.[179] The holders of fixed security interests (mostly banks who have lent money and contracted for a company charge, in much the same manner as banks contract for mortgages in return for home loans) are paid first, and insolvency practitioners (usually from one of KPMG, Ernst & Young, Deloitte or PwC) are paid second.[180] 'Preferential' employee claims are third. Employees' pensions are wholly claimable in priority to other creditors, and in any event are usually protected in advance by statutory funding requirements and the state Pension Protection Fund.[181] However employee wages rank as a preferential claim only up to £800 per person, a figure which has withered in a statutory instrument since 1986.[182] The rest of the money that employees are owed, beyond money that is not covered by National Insurance, will rank along with the claims of the rest of unsecured creditors. The recovery rates in 2000 showed that secured creditors received 77 per cent of the money they were owed on average, preferential creditors received 27 per cent, and unsecured creditors received virtually nothing.[183] After the claims of preferential creditors rank the holders of a 'floating charge'. While a 'fixed charge' must apply to a specific asset, floating charges are characterised by their applicability to any asset, including the fluctuating body of assets which the company possesses, uses and disposes of in the ordinary course of business.[184] They are created, like any charge, simply through a contract expressing the intention that the assets be made available as security.[185] Since 2002, unsecured creditors must have a ring-fenced fund up to £600,000, or 20 per cent of the remaining value, set aside out of the assets subject to a floating charge.[186] Nevertheless, recovery rates for employee wages are unlikely to have become much higher.

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[177] Insolvency Protection Directive 2008/94/EC. See also the ILO Protection of Workers' Claims (Employer's Insolvency) Convention, 1992 (No. 173).

[178] Employment Rights Act 1996 s 182

[179] A great deal of insolvency law theory turns upon what system of distribution is most normatively justifiable. The basic starting point is that losses of creditors be shared *pari passu*, ie proportionally. English law creates so many exceptions that it is best to see the system as one of fixed priorities among different classes of creditor. It has no principled coherence. An interesting, older alternative, was that under the Talmud, Kethuboth, x. 4, 93a, the most vulnerable party, assumed to be the one owed the least, would be paid first: the remaining money would be dealt out among all creditors like a deck of cards. So if creditors A, B and C are owed 10, 30 and 60, but there is only 50 left, then A will get 10, and B and C will each get 20.

[180] Insolvency Act 1986 s 176ZA ensures priority for insolvency practitioners. Assets subject to a fixed security interest are deemed by the common law to lie outside of an insolvent's estate.

[181] Insolvency Act 1986 s 175 and Sch 6; Pensions Act 2004 ss 107 ff

[182] Insolvency Proceedings (Monetary Limits) Order 1986, SI 1986/1996, art 4. The Preferential Payments in Bankruptcy Act 1897 s 2 introduced the preferential status of employees over the holders of a floating charge, after the seminal case of *Salomon v A Salomon & Co Ltd* [1897] AC 22.

[183] Insolvency Service, *A Review of Company Rescue and Business Reconstruction Mechanisms, Report by the Review Group* (2000) para 57

[184] *Re Spectrum Plus Ltd* [2005] UKHL 41

[185] *National Provincial Bank v Charnley* [1924] 1 KB 431, Atkin LJ, 'where in a transaction for value both parties evince an intention that property, existing or future, shall be made available as security for the payment of a debt, and that the creditor shall have a present right to have it made available, there is a charge...'

[186] Insolvency Act 1986 s 176A. This may be disapplied where the amounts owed to creditors, though maybe collectively large, are individually small, eg *Re Hydroserve Ltd* [2007] EWHC 3026 (Ch), [2008] BCC 175.

Job security

Many employees will in practice be more concerned about losing their jobs, even over the prospect of losing some weeks in wage payments. This is the final, undiversifiable, socially critical, and economically systemic risk that employees bear.[187] The likelihood that employees will keep their jobs plainly depends on business circumstances. However there are always a range of possibilities, so jobs also depend on the insolvency practitioner's decisions. Since the Enterprise Act 2002, the main insolvency procedure is called 'administration'. The administrator's core duty is to rescue the company, or if not rescue the business (by selling the insolvent company's assets to a new buyer), or if that is not possible then manage the winding down of the company in a way that reaches the best outcome.[188] If employees are not told otherwise, after two weeks their employment contracts will be adopted by the administrator.[189] This means the full amount of their pay claims achieve priority alongside the expenses of the insolvency practitioner,[190] although the Court of Appeal has excluded compensation for not consulting about redundancies, among other things.[191] What happens after this depends on the plan taken up by the administrator, and the plan of the administrator is heavily influenced by the parties controlling appointment.

Appointment of administrators

Since the Enterprise Act 2002, an administrator is usually appointed out of court under the decisive influence with the holder of a 'qualifying floating charge'. This is a floating charge which covers all of a company's assets, and is usually a bank. Both the floating charge holder and the old directors to appoint an administrator out of court.[192] Other creditors can petition to court for an appointment.[193] However, at any time, the holder of the qualifying floating charge can intervene and demand their preferred administrator be installed.[194] In March 2013, the Government and Insolvency Service announced it would start an independent review into the procedure, because of concerns about opacity, unaccountability, and the resurrection of 'phoenix companies'. The stereotypical narrative of shady practice is that, when a business approaches difficulty, the executive directors visit their bank. They agree that the management will buy the assets of the company for a price sufficient for the bank to be repaid its loan in full. However, this means that the company's shareholders and unsecured creditors are wiped out. The bank consents, and out of

[187] By contrast, shareholders risk losing the (usually diversified) monetary investment they have made. It is frequent to read in corporate law literature that the risk shareholders bear is somehow superior, or more grave, than the risk employees bear in losing their jobs, eg F Easterbrook and D Fischel, 'Voting in Corporate Law' (1983) 26(2) Journal of Law and Economics 395, 403. This strand of literature uses risk as both a positive explanation and a normative justification for exclusive shareholder control of companies. Most of these ideas seem to trace back to a rather different point made by JS Mill, *Principles of Political Economy* (1848) Book II ch 15, §1. It is however, not true that shareholders bear risk, because most shareholders are institutions who pass the financial risk of investment onto beneficiaries or policyholders. These people often have no voice. As such justifications for exclusive shareholder voice, based on risk, are predicated on a fiction. So far as the ultimate investors of capital do bear risk, it cannot be said to be so different that other forms of risk become irrelevant, and it is not wholly clear why risk matters so much anyway (as opposed to contribution).

[188] Insolvency Act 1986 Sch B1, para 3

[189] IA 1986 Sch B1, para 99

[190] IA 1986 s 176ZA

[191] *Krasner v McMath* [2005] EWCA Civ 1072, [2005] BCC 915. See also *Leeds United AFC Ltd* [2008] BCC 11 and *Re Allders Department Stores Ltd* [2005] BCC 289 on dismissals.

[192] IA 1986 Sch B1, paras 14 and 22

[193] IA 1986 Sch B1, para 12

[194] IA 1986 Sch B1, para 36

court they hire a friendly administrator who initiates and closes a 'pre-packaged insolvency' plan. The whole procedure is over in a day. The old management is back in control of the business that it had just run into the ground, free of debt, and perhaps a number of jobs.[195] In the press, and in industry circles the argument has been routinely repeated that the Enterprise Act 2002 regime and pre-packs are good because they tend to save jobs. This assessment, however, does not appear to have any evidential, or statistical foundation.[196] Although there are many examples where insolvencies occur and employees need never actually be concerned, it appears more likely that employees would be protected when they had a voice in the process.

Employee security in insolvency

Trade unions can, with few hurdles, use collective agreements to achieve significantly more security for their members who are threatened by insolvency. The status of employees as members, or in the company constitution, at this point becomes irrelevant. The only thing that matters is who has security, in priority to other creditors, over a company's assets. Fundamentally, English law recognises the creation of a security interest as a product of contractual freedom.[197] This is seen as highly problematic in theory, because it allows powerful creditors to use their bargaining power to divert wealth to themselves at the expense of weaker creditors. In economic language it amounts to a 'negative externality',[198] like a business which buys lead from a factory, when neither pay for the toxic exhaust. But, from employees' perspective, this could be ended if a union contracted with a company, in which its members were employed, for a floating charge over all the assets of a business, plus a fixed charge over one or two expensive pieces of property. This would effective guarantee (1) all future wage claims, should the worst happen, and (2) a decisive say in the choice of an administrator. It would have its wage claims protected by the fixed security and the right to intervene to appoint an administrator by the floating charge. The security that floating charges create is voidable in legal action by an administrator, to the extent that new money is not given in return for the charge, if the charge is created within two years before the onset of insolvency.[199] However, the purpose of seeking a floating charge would be to ensure the long term security of pay and jobs of a union's members, and so this time period would not ordinarily be a practical issue. A union's floating charge would not prejudice a company's ability in any way to seek finance from a bank. The only consequence would be that the relatively small figures of outstanding wage claims could not be ignored by powerful financiers, and employee representatives would have a say in the future their enterprise.

[195] For an anecdotal account, see T Webb, 'Crackdown on 'phoenix' insolvency deals' (19 March 2010) The Guardian

[196] An informative study was conducted by S Frisby, *Report to The Association of Business Recovery Professionals: A preliminary analysis of pre-packaged administrations* (R3 2007), funded by the insolvency practitioner professional group R3. It suggested at page 72 that 'pre-packs appear to save more jobs than business sales'. However, the idea could equally appear entirely fanciful given that (1) pre-packs happen quicker than business sales, meaning the jobs are simply shed later (2) no data is given on the position 3 or 6 months after insolvency, and (3) to the extent that pre-packs defeat the claims of many other business creditors, there will be knock-on job losses, which are not recorded in the immediate data of the insolvent company.

[197] *National Provincial Bank v Charnley* [1924] 1 KB 431

[198] eg LA Bebchuk and JM Fried, 'The Uneasy Case for the Priority of Secured Claims in Bankruptcy' (1996) 105(4) Yale Law Journal 857. Contrast R Mokal, *Corporate Insolvency Law: Theory and Application* (2005) ch 5, who builds a robust case, with empirical support, that security interests can benefit commercial creditors just as much as banks. His argument, notably, is not intended to relate to employees, who he views as being in a different class and deserving of automatic protection, at 121.

[199] IA 1986 s 245. Under s 245(3)(a) employees would be considered as being 'connected' to the company for the purpose of the relevant time in which the floating charge is created.

4.3 Controlling dismissals

While a company is still running, the job security of employees can be just as vulnerable as it is in insolvency. Just as shareholders risk losing the money they invest in a company, employees risk losing their jobs.[200] Shareholders cannot, of course, be 'dismissed' from a company,[201] and neither can they strike. Employees can strike, and one the main reasons this is essential is precisely because they can be dismissed. The loss of a job is frequently associated with severe psychological, social and economic hardship. Psychologically, people may simply be emotionally unprepared for losing their work, and in extreme cases they suffering psychiatric injury whatever procedure is used.[202] Socially, people become detached from relationships they form: people frequently spend more time with their work colleagues than their families or non-work friends. Economically, if another job cannot be found immediately, savings will be depleted. In really bad cases, people are forced to move homes. Compounded economic hardship and unemployment is a causal contributor to divorce, child poverty, crime, riots, and in the worst cases systemic economic and social collapse. Many young people in particular see the concept of the modern 'flexible' worker as loathsome sophistry, because contrary some beliefs they have not suddenly learned to like the precarity of the 19th century worker. The corporate governance problem is that dismissals, and all the consequences, may happen even when they are harmful to the business, the economy and society alike.[203]

Conduct dismissals: management conflicts of interest

When dismissals relate to an employee's conduct, qualifications or performance, both shareholders and often directors have a strong interest in giving employees more control. Personal disputes and favouritism sometimes develop between employees and their supervisors. Shareholders have an interest in ensuring that people higher up in a workplace hierarchy do not abuse their authority, as do directors who are not personally involved. Over the last 40 years, court supervision has proven excessively vulnerable to unfavourable judicial interpretation and government interference. The standard of review adopted by the

[200] This has started to be reflected in some new statutory language: the Pensions Act 2008 s 1 refers to 'jobholders'.

[201] There is an exception in the Companies Act 2006 s 979, where the a takeover bidder who has acquired 90% of a company's shares may apply for compulsory purchase of the remaining minority. This is to prevent the minority exploiting and profiting the investments of a new majority holder without themselves contributing anything.

[202] That said, the procedures for dismissal matter greatly. Juridification and bureaucratisation of the whole affair have probably done little service. The most unfortunate example remains *Johnson v Unisys Ltd* [2001] UKHL 13, [2001] IRLR 279.

[203] Hugh Collins has stated a contrasting position: 'Economic analysis therefore provides indeterminate support for a mandatory law of unfair dismissal, and other kinds of arguments, such as those based upon respect for the dignity and autonomy of workers, are required in order to make the case complete.' H Collins, KD Ewing and A McColgan, *Labour Law: Cases, Text and Materials* (2005) 510. However, this really depends on which economic theories one chooses to select, and what one means by 'economic' in any case. There does not seem to be any good reason to have an 'economic' set of theories that are segregated from more 'social' ones. It is, of course, entirely true that limited support may come from many economic theories historically.

courts wavers between the statutory language of an outright reasonableness test,[204] a perversity test,[205] and (what appears to have become the settling point) a good business standards test,[206] akin to the *Bolam* standard in medical negligence.[207] Because the Employment Tribunal's decision is given great deference by appellate courts, it is easy to find flatly contradictory rulings in similar situations. The fairness of court decisions varies with the temperament of the panel, none of whom work in that workplace. Moreover some courts, albeit beginning with a highly politicised Master of the Rolls in 1983,[208] have manipulated the definition of an employee to remove casual and agency workers from the scope of protection.[209] The Supreme Court in *Autoclenz Ltd v Belcher* ended this line of jurisprudence decisively in 2011,[210] although the practice of the lower courts tends to take time to change. Government interference has also proven an ongoing problem. It has been possible to vary the qualification by Ministerial Order, most recently from one to two years.[211] The government is also capable of cutting funding from the Tribunal system, cutting legal aid, or raising fees to access tribunals. More generally, even if judicial oversight must be the final assurance of justice in dismissal, most people do not want to go anywhere near a court to get justice.

Collective agreements can bring the procedure into the workplace, and make the decision for dismissal lie with elected worker representatives who are independent from management. Since *Edwards v Chesterfield Royal Hospital NHS Trust*, the courts have indicated a preference for awarding injunctions against dismissals in breach of an agreed procedure.[212] Individual disciplinary procedures will always be terms in a collective agreement that are apt for incorporation into every individual employment contract. A collective

[204] Employment Rights Act 1996 s 98(4) states that lawfulness of the dismissal 'depends on whether in the circumstances (including the size and administrative resources of the employer's undertaking) the employer acted reasonably or unreasonably in treating it as a sufficient reason for dismissing the employee'. This appears to require the court substitutes its decision for the decision of the employer, in the same way that a court will exercise such business judgment in allowing or preventing a derivative claim under the Companies Act 2006 ss 263 and 172.

[205] See *HSBC Bank plc v Madden* [2000] EWCA Civ 330, [2000] ICR 1283, and the criticism in *Haddon v Van Den Bergh Foods Ltd* [1999] ICR 1150 (EAT) per Morison J.

[206] This appears obvious from *Bowater v Northwest London Hospitals NHS Trust* [2011] EWCA Civ 63. Here a woman nurse, while restraining a patient by sitting over him with her legs wrapped around said something like 'It's been a few months since I have been in this position with a man underneath me'. The remark was regarded as lewd for a professional patient relationship, while the Tribunal held this was wrong.

[207] *Bolam v Friern Hospital Management Committee* [1957] 1 WLR 582. See S Deakin and G Morris, *Labour Law* (2008) 446.

[208] *O'Kelly v Trusthouse Forte* [1984] QB 90, decided 20 July 1983.

[209] E McGaughey, 'Should agency workers be treated differently?' (2010) LSE Working Paper No. 7/2010, which discusses the history more fully.

[210] [2011] UKSC 41, [35] per Lord Clarke. The court's decision was that (1) the mutual obligations in an employment contract are work for a wage, meaning there is no longer any further requirement, introduced by *O'Kelly*, for an employer to undertake to provide continued employment, (2) that courts must classify employees in a purposive manner, based on the relative bargaining strength of the parties. This means that all casual workers and all agency workers, especially those in the most vulnerable positions, must be regarded as employees. The remaining issue for agency workers is whether they have contracts with the people they actually work for, rather than the employment agency alone. The idea that a contract with the 'end user' could be denied was based on a misunderstanding of the test for implied terms: the test is not 'necessity', it is 'necessary to reflect the reasonable expectations of the parties', see *Equitable Life Assurance Society v Hyman* [2000] UKHL 39. See (2010) LSE Working Paper No. 7/2010, at page 23 ff.

[211] E McGaughey, 'Unfair dismissal reform: political ping-pong with equality?' (2012) 226 Equal Opportunities Review 1. Working Paper available at http://ssrn.com/abstract=2014699.

[212] [2011] UKSC 57, at [44] per Lord Dyson, If 'an employer... starts a disciplinary process in breach of the express terms of the contract of employment is not acting in breach of contract.... it is open to the employee to seek an injunction to stop the process and/or to seek an appropriate declaration... an injunction to prevent a threatened unfair dismissal does not cut across the statutory scheme for compensation for unfair dismissal... The grant of injunctive or declaratory relief for an actual or threatened breach of contract would not jeopardise the coherence of our employment laws and would not be a recipe for chaos in the way that, as presaged by Lord Millett in *Johnson*, the recognition of parallel and inconsistent rights to seek compensation for unfair dismissal in the tribunal and damages in the courts would be.' See also [130] per Lord Kerr.

agreement could require that dismissals do not take effect without the review and consent of, for example, a panel of five workplace representatives. If the representatives determine that the reason given by the employer is unjustified, the dismissal would have no effect. The idea that the employer or supervisor could not force through their will reflects the essential principle of British decency that people are entitled to judgment by their peers.[213] If the representatives approved of the dismissal, the employee would be capable of claiming the dismissal was unfair in court, but the standard of review by the court, which is proper to public bodies, could rather be the proportionality test.[214]

Redundancy dismissals: shareholder conflicts of interest

In the case of redundancies, the conflict of interest between the workforce on the one hand, and shareholders and directors on the other, tends to be far stronger, at least while the law continues to support shareholder controlled enterprise. Both in the run up to corporate insolvencies, and even while a business remains healthy, dismissals can be effected as part of a policy of maintaining or boosting shareholder profits, even while it damages the prosperity of the long term business. Stories of companies dismissing thousands of workers as profits go up prove the simple arithmetical possibility that by shrinking a workforce, distributions to shareholders can be increased.[215] When jobs could be maintained, and with it the long term prosperity of the company, but profits might be temporarily reduced, a shareholder dominated board of directors may make the wrong decision. In an economic crisis, the problem becomes acute: businesses which foresee future reduction in revenue will make dismissals. However, many businesses cutting jobs simultaneously reduces the money people have to buy goods and services (or effective aggregate demand). Because workers cannot consume, businesses lack customers. With business prospects dulled further, shareholder controlled business will have an incentive to cut jobs again. The intervention of work councils in Germany as the financial crisis hit, compared to the actions of UK or US employers, explains some of the difference in severity of unemployment growth between 2008 and 2010 in those countries. Economy wide, unemployment ends up damaging shareholder profits as well, although some time after the lives of thousands of people in and out of work are made substantially harder. Without a different course, through collective action, prolonged recession and unemployment may result.[216]

Some redundancies sometimes will always be necessary to maintain successful business in everyone's interest. Every sensible workforce and trade union recognises this. However, decisions about economic

[213] *Dean v Bennett* (1870) LR 6 Ch 489, 494, per Lord Hatherley LC in a case regarding the dismissal of a minister, 'No one would expect to find that such a course had been adopted in any assembly of English people, who are accustomed in some degree to the ordinary principles of justice...' Magna Carta 1215 XXXIX, and 1297, XXIX, Imprisonment, &c. contrary to Law. Administration of Justice. 'NO Freeman shall be taken or imprisoned, or be disseised of his Freehold, or Liberties, or free Customs, or be outlawed, or exiled, or any other wise destroyed; nor will We not pass upon him, nor condemn him, but by lawful judgment of his Peers, or by the Law of the Land. We will sell to no man, we will not deny or defer to any man either Justice or Right.'

[214] The Employment Rights Act 1996 s 98, because of the imprecision of the word 'reasonable' is easily interpretable as meaning proportionality. I am grateful to my students at King's College, London, class of 2011-2012 for the idea of using the proportionality test, which is familiar from the jurisprudence of the European Court of Justice.

[215] eg B Groom, 'More finance jobs face axe' (21 January 2013) Financial Times, 2, 'Financial services companies are likely to cut a further 18,000 jobs over the next three months despite optimism that business volumes will rebound...'

[216] JM Keynes, *The General Theory of Employment, Interest and Money* (1935)

redundancies cannot be left to shareholder representatives. Collective agreements on the issue have not been enforceable by a combination of custom and statute,[217] and courts have held even the clearest redundancy policies to be inapt for incorporation in individual employees' contracts. If an employee reads an assurance from management that 'THERE WILL BE NO COMPULSORY REDUNDANCIES' it is likely that they will think this means that management will in fact make no compulsory redundancies.[218] It seems unfair something else might happen. The institutional competence of courts is limited in this field. They have tended to favour managerial discretion, regardless of the conflicts of interest that shareholder representatives have.[219] Statutory notice and severance pay has been an important, but limited financial cushion.[220] Notice and consultation about redundancies effectively extends the time that workers have to adjust.[221] However informing and consulting, without participation, is frequently felt by the workforce to be insulting, and a distraction to make employees be conforming.[222] Four Directives and their implementing legislation, with varying focus, require information and consultation when substantial economic changes of one kind or another are pending.[223] Significantly, all require engagement with worker representatives.

A collective agreement could require that elected worker representatives hold a veto on any redundancies. It could be negotiated to operate in a similar fashion to worker representative control of conduct dismissals. The difference is that the collective voice of work colleagues is not the only legitimate ones: long term financial stability remains important. This is represented by the shareholder interest, and ultimately people's pensions. In businesses which rely on capital contributions, worker representatives with unfettered discretion could act in a way that could damage financial stability. The German model allows the employer, if it is determined to push through redundancies, to take the matter to court. The courts are then empowered to create a social plan, effectively a substantial redundancy payment, but one which may often include funding for retraining.[224] The same could be achieved through collective agreement by stipulating a higher schedule of payments, which a court would be able to enforce by injunction. Ultimately, the existence of judicial arbitration, at the end of a long procedure designed to ensure the parties settle, is necessary so long as management is excessively responsive to shareholder interests.

Constitutional entrenchment

Can dismissal protection be entrenched in a company's structure? The existence, at present, of a statutory framework for consultation means that worker representation already constitutes what the company does:

[217] TULRCA 1992 s 179. The idea that there should be no intention to create legal relations with a collective agreement, which is now codified in statute, comes from O Kahn-Freund. Kahn-Freund's views were significantly influenced by the breakdown of labour law, and slide into Fascism that he witnessed while working as a Berlin Labour Court judge.
[218] *Kaur v MG Rover Group Ltd* [2004] EWCA 1507
[219] *Lesney Products & Co v Nolan* [1977] ICR 235
[220] Employment Rights Act 1996 ss 86 and 139
[221] Trade Union and Labour Relations (Consolidation) Act 1992 s 188 ff
[222] In the same way it is said that 'collective bargaining' without the right to strike is 'collective begging'.
[223] European Works Council Directive 2009/38/EC, Transfer of Undertakings Directive 2001/23/EC, Collective Redundancies Directive 98/59/EC, and Information and Consultation of Employees Directive 2002/14/EC, etc, etc.
[224] Betriebsverfassungsgesetz 1972 §§99 and 111-112. Although old, an excellent overview is A Döse-Digenopoulos and A Höland, 'Dismissal of Employees in the Federal Republic of Germany' (1985) 48(5) Modern Law Review 539

whether in the Companies Act 2006, a constitution, or another instrument, worker representation committees literally constitute the company's being. However, it is not entrenched. A structure of permanent work councils, composed of elected representatives, for each company establishment could be introduced by amendment to a company's articles. In effect, recognition given to the legitimate role of employees in dismissal policy would be recognition of the unique vulnerability of employees as a class of company members. The rights of a class of shareholders cannot be varied without approval of 75 per cent of members of that class.[225] Entrenching dismissal protection in a company's constitution would be an analogous step forward.

4.4 Delegating social functions

While this part has so far discussed the essential distributive functions of a company in relation to its workforce (by representation in the general meeting, on the board, in insolvency and in dismissals) a far broader variety of issues are appropriate for delegation to the workforce. There are multiple benefits.

The general efficiency of participation

In 1922, a set of experiments conducted by an Australian scholar, working at Harvard Business School, revealed that participation by workers in job decision making increased their job satisfaction, and this improved their productivity. Elton Mayo had initially wanted to prove a theory he had that workers for General Electric, taken from the Hawthorne Works, would work faster if the lighting intensity was increased.[226] He put a group of workers in a test lab, where his observation staff were encouraged to let the workforce get on with their tasks as much as possible. The intention was to create a 'neutral' test environment, but the unintended consequence was that for the first time the workers found themselves in a collaborative, collegiate atmosphere. The observation staff asked the workers how they wanted to work, when they would like breaks, what kind of food they preferred, and so on. Without realising it, in the interests of science, management was removed. And while Mayo found no connection between lighting and productivity, his results showed a massive improvement in productivity of workers in the test lab, compared to the factory.[227]

Social functions

Elected work councils could be delegated a range of social functions: company budgets for recreation, training, canteens, timing of breaks, patterns of working hours are all areas where improvements in productivity would be likely.[228] This has been the policy in place for health and safety, with outstanding

[225] CA 2006 s 630

[226] See E Mayo, *The human problems of an industrial civilization* (1933)

[227] P Blumberg, *Industrial democracy: the sociology of participation* (1968) chs 1 and 2

[228] The German legislation is indicative. It creates codetermination rights for (1) organising the business and tasks of employees (2) working time and breaks (3) overtime and shortening of working time (4) wage payment methods (5) principles for holidays (6) introduction and use of work technology to 'monitor' employees (7) rules about health and safety, accidents and sick time (8) social facilities and employee accommodation (9) workplace accommodation use (10) principles governing remuneration (11) bonuses, or special payments (12) the workplace suggestion system (13) group work principles. Betriebsverfassungsgesetz 1972

success.[229] If worker representatives hold competence in relation to economic changes and dismissals, they could also take on responsibility for social functions. An entrenched right to do such things can be achieved through company constitutional amendment in the normal way.

Wage sharing decisions

The division wages among workers is one of the most interesting topics, not least because collective agreements routinely seek to set wage scales. As the pay of company executives has become increasingly incompatible with the values of democratic society,[230] and financial sector workers who handle other people's money on its way to company investment followed suit, there have been more and more demands for statutory standards. Common proposals include fixing pay ratios between the top director and the bottom worker,[231] mandating some formula for relating pay to performance,[232] or fixing a maximum ratio of bonuses to salaries.[233]

An option which is flexible, and not prone to failure, is to delegate the wage decision to the workforce. A recent behavioural study by Gary Charness, Ramón Cobo-Reyes, Natalia Jiménez, Juan Lacomba and Francisco Lagos compared the productivity of workers who set their own wages among themselves, compared to workers whose wages were set or dictated by an employer.[234] The experiment gives evidence that the 'agent who bears the responsibility for an outcome will behave in a more 'pro-social' manner', and that workplace effort increases. Studies like this can be repeated an infinite number of times, and because they identify an inherent feature of human behaviour, they will always show the same. Together with the evidence from the study by Cohn, Fehr, Herrmann and Schneider, summarised above, that inequality demotivates the workforce, there is a strong case for allowing all workers direct control over wage issues, from the shop floor to the board. On this analysis, it turns out that the most efficient way for shareholders to exercise a say on pay for company directors,[235] would be to leave the issue to employees.

§87 (Work Constitution Act 1972 §87).

[229] HSWA 1974 s 2

[230] For analysis and opinion polling on income distribution, see L McCall and L Kenworthy, 'Explaining Americans Beliefs About Income Inequality' (2009) University of Arizona Working Paper

[231] Plato, *The Laws* (ca 350BC) was the first proponent of this idea. He viewed the maximum ratio between the highest and lowest paid to be one to four. By contrast, the factory workers in Savar, Bangladesh, where the building collapsed in 24 April 2013 earned around $456 a year. They made clothes for Walmart (as well as Primark, Mango, Benetton, Bonmarché and others), where CEO Mike Duke's pay was set was $20.7m in 2012. The workers of the Savar factory would have to work their whole lives (if we say 50 years for argument's sake) 900 times over to make what Mike made in one year. This is a pay ratio of 1:45,395. Pay ratios laws would need to be carefully drafted to stipulate that employees of subsidiary companies must be included, as well as any outsourced businesses over which the central business has significant influence, by ownership or contract.

[232] eg UK Corporate Governance Code 2010 D.1.1 and Schedule A

[233] Capital Requirements Directive, draft amendments. This proposed law seems to have heeded some of the warnings that bonus incentives make people less productive when they are involved in a task which requires any kind of creative thought (as finance does). See D Ariely, *The Upside of Irrationality* (2011) ch 1. However, by allowing financial sector bonuses to compose up to half a person's pay, apart from being avoidable, does not change the damaging incentives that bonuses have.

[234] G Charness, R Cobo-Reyes, N Jiménez, JA Lacomba and F Lagos, 'The Hidden Advantage of Delegation: Pareto-improvements in a Gift-exchange Game' (2012) 102(5) American Economic Review 2358

[235] CA 2006 s 439 gives shareholders of UK companies a non-binding say on pay. In fact, the original companies legislation forsaw that shareholders would have a binding right to set pay under the Model Articles (known then as Table A). As companies became larger, and management became more removed, this practice whittled away, and it came to be reflected in today's Companies (Model Articles) Regulations 2008 SI 2008/3229, Sch 3, art 23(2) 'Directors are entitled to such remuneration as the directors determine...' It was noted above there is no reason why at each annual general meeting, shareholders could not make their say on pay binding by coupling the resolution with a resolution to remove directors from office who do not comply with

4.5 Directors' duties and socially responsible corporations?

A final area in which collective bargains could aim for corporate change is in the way companies act in society: particularly their impact on workforces abroad, through supply chains, or the environment, on democracy in developing countries, and taxation. At present the Companies Act 2006 section 172 says that, apart from promoting a company's success for the benefit of members, directors must pay regard to all stakeholding groups. The duty is largely unenforceable because the section states the director must act in the way 'he considers' to be best. This probably limits its ambit to cases where evidence is found of directors doing something they subjectively perceive to be damaging, or actively disregarding someone's interests. There is an argument that directors could be found to have breached a duty of care by paying insufficient regard to the relevant stakeholders,[236] or that an irrational exercise of discretion would breach the duty.[237] Whatever might result, legal enforcement might not reach the aspirations of a new 'corporate social responsibility'. In US states there have been 'corporate constituency' statutes which require directors to consider all stakeholding groups, and the duties are often not subjective.[238] Nothing much has happened. Canada's Supreme Court has indicated that it will allow stakeholder led derivative actions.[239] However it seems that directors' duties, enforceable in court, are ill suited to producing actively good behaviour: courts are best suited to the enforcement of minimum standards.[240]

If a collective agreements sought the insertion of specific directors' duties in company constitutions, a similar gulf between the aspiration and the outcome is foreseeable, if the aspiration is to produce the corporate equivalents of Archbishop Desmond Tutu.[241] However, constitutional amendments could achieve a multiplicity of minimum standards, with sufficient flexibility to develop in line with social values. For example, clauses could be inserted that require directors to ensure that suppliers pay their employees wages comparable to those in the parent company. They could prohibit any form of political donation, lobbying, or spending on tax avoidance advice. They could say that operations abroad will act in full compliance with UK health and safety, or environmental standards, even though foreign law is more relaxed. Indeed, in a multinational corporation, a constitutional provision could require that it acts in accordance with standards of the most favourable nation.[242] Constitutional provisions could be enforced

their wishes, using their right under CA 2006 s 168.

[236] Since the duty of care under CA 2006 s 174 must logically apply to the making of decisions regarding stakeholders.

[237] This follows from the pre-Companies Act 2006 case of *Regentcrest plc v Cohen* [2001] 2 BCLC 80.

[238] For general background, if unsympathetic analysis, see SM Bainbridge, 'Interpreting Nonshareholder Constituency Statutes' (1992) 19 Pepperdine Law Review 971

[239] *Peoples Department Stores Inc (Trustee of) v Wide* [2004] 3 SCR 461 held that the duty under the Canada Business Corporations Act 1985 s 122 to act in the best interests of the corporation is not merely owed to the corporation itself, but also to corporate stakeholders, namely 'shareholders, employees, suppliers, creditors, consumers, governments and the environment.' See also, *BCE Inc v 1976 Debenture Holders* [2008] 3 SCR 560.

[240] cf JE Parkinson, *Corporate Power and Responsibility* (1994) 134, 'unlike the market and market-linked devices, [directors' duties cannot] create a more positive motivational environment. They lay down minimum standards, and do not as such provide an incentive… to achieve top-quality performance.'

[241] Archbishop Desmond Tutu received the Nobel Peace Prize in 1984, for his work to end South African apartheid.

[242] There could be an anology here to the 'most favoured nation' rule used in the law of the World Trade Organisation, see the General Agreement on Tariffs and Trade 1947, Article I.

by any member of the company in a derivative claim, and for the avoidance of doubt in any country's legal system, the constitution could create an explicit right for stakeholders, or public interest groups, to bring enforcement actions.[243] The reason that a trade union, and the company as a whole would have an interest in doing such a thing might or might not be for reasons related to business profitability. Enlightened self interest, or long term interest, or some other theory of interests might be a motivation.[244] Change could also be made because it is morally right.

Whatever constitutional standards might be introduced, the aspiration of corporate social responsibility is probably not achievable through one measure, or one theory. Different configurations of public ownership of some industries, public sector competition in others, sector specific regulation, or private ownership appear to be required. A one size fits all model of private enterprise, even with social responsibility, is not enough. Such regulatory choices depend on the state of technology, development, democratic deliberation, and multiple other social and economic circumstances. However, in private sector enterprises, aspirations of better governance are most likely to become reality if the people who hold power in companies are accountable through the vote to those over whom power is exercised. One of the most important groups will always be the workforce. If legislation is not forthcoming, collective agreements can begin to achieve corporate change and it will go significant lengths to improving society.

Conclusion

This article has posited three main ideas. The first was a normative theory of voice in enterprise: that to achieve productively efficient enterprises, as a route to human development, it is necessary that company directors' powers to appropriate the product of shareholder and employee investments, and direct their distribution, are accountable to all contributors. If any group lacks a voice, the controlling parties will use their positions to unjustly enrich themselves. This theory's components were not new: it drew on a consistent line of thought in law and economics for around 250 years. The second main idea was that membership in a company for employees can be achieved through collective agreements. Agreement can procure either a simple decision of management to make a new kind of employee share scheme, or a majority vote of shareholders to create a new class of employee shares, or a 75 per cent majority vote of shareholders to create a completely new non-share based membership. To get shareholder resolutions, unions may well need to engage with shareholding institutions. But procuring such votes is eminently possible given the voice that union members already hold through their pensions, and because their interests will frequently overlap with shareholders.

This led to the third main idea, that representation as members in a company's general meeting would

[243] cf *Sutradhar v Natural Environment Research Council* [2006] UKHL 33

[244] A Smith, *Theory of Moral Sentiments* (1759) 1, 'How soever selfish man may be supposed, there are evidently some principles in his nature, which interest him in the fortune of others, and render their happiness necessary to him, though he derives nothing from it except the pleasure of seeing it.'

bring about fundamental corporate change. Then, five additional specific topics for bargaining were discussed. First, it was argued that while the utility of direct board representation (compared to a voice within company general meetings) is frequently exaggerated, it is easily accomplished through the director appointment procedure. At least two worker representatives can create substantial benefits in terms of information and cohesion in an enterprise. Second, employees could acquire a substantial voice, which is currently non-existent, in corporate insolvencies if unions bargained for a floating charge over a company's assets at the outset, and before banks or other lenders take the leading role. Third, collective agreements can build upon the work councils established for information and consultation to secure specific decision making rights for dismissals concerned with conduct or redundancies. Fourth, there are powerful arguments for more delegation of social functions to the workforce. Particularly on the question of wage distribution, it turns out that shareholders have a strong financial interest to ensure workers control the wage bill. Fifth, it was argued that collective agreements could secure company constitutional amendments to include a range of 'social responsibility' clauses. However, genuine change to match the aspirations of corporate social responsibility seem to depend foremost on changing the accountability structure of companies and who has voice. This makes the case of collective bargains for corporate change even more compelling.

One more question calls out to be answered. What if nothing happens? What if trade unions are currently so weakened, or too reluctant, to bring about the kind of structural developments in corporations that, as it has been argued here, are necessary? Change usually happens when it needs to, and in a world riven by periodic economic crises, growing inequality and social deprivation, that need seems greater than ever. In any case, I hope that this article is nevertheless useful because it highlights the connections and issues that are not as well understood across the company and labour lawyer divide as they might be. It has made a step toward putting labour rights and corporate governance together in their context of the law of enterprises. Its aim is not merely to advocate change, but also to stimulate a broader discussion, of a broader scope, about how to advance human development.