TOWARDS DEMOCRATIC AND SUSTAINABLE BUSINESS

Possibilities for Corporate Governance Reform

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Foreword

I am pleased to welcome the publication of this important report, Towards Democratic and Sustainable Business: Possibilities for Corporate Governance Reform, by Chris Rees and David Offenbach, both members of our Industry & Business Policy Group.

This report is not the policy of the Labour Party or of Labour Business, but both will subscribe to many of the ideas it discusses. As Covid-19 has shown, governments in the future will have to accept a more active role in the economy. In this context, the regulatory framework for corporate governance will need to be adapted to support economic growth and encourage responsible business practices. This report provides a route for how the Labour Party in office might begin to bring this about.

Labour Business hopes that this report will make a valuable contribution to the policy making process of the Labour Party as it develops a radical and reforming programme for government.

Hamish Sandison
Chair, Labour Business

Executive Summary

The Covid-19 pandemic has precipitated a deep and lasting economic crisis, adding to the on-going aftershocks of the 2008 financial crisis. Whilst the challenge is immense, any long-term recovery strategy must be premised upon working towards a more inclusive and sustainable economy, with greater resilience for the future. Within this context, it is widely understood that governments will have to accept a more active role in the economy. Legal and regulatory frameworks will need to adapt in response to rapidly changing expectations. The task for the Labour Party is to begin to develop a transformative agenda for government that will facilitate this new economy.

Over the past decade, unregulated free-market capitalism has been increasingly challenged, and there have been widespread calls for a more 'responsible capitalism'. We argue there is a crucial role here for effective state intervention through company law reform. This will necessitate the corporate governance framework being re-configured to support responsible business, facilitate the delivery of long-term and sustainable economic growth, and provide an overarching regulatory framework within which good businesses can thrive.

This report considers a series of legal changes aimed at improving the monitoring, transparency, accountability, and effectiveness of corporate power. Specifically, we advocate changes to the corporate governance regime to promote workforce voice in company decision-making, together with changes to the rules governing company ownership and purpose to create companies focussed on long-term, sustainable success, shared by all their stakeholders. The democratization of the company must be fundamental to this effort. A democratic and sustainable society requires democratic and sustainable businesses. That is the key message of this report.

The report outlines the rationale and principles behind a series of broad policy areas, drawing from a review of recent academic and policy-oriented literature. We place policy proposals in the context of the wider political economy, explaining the role of financialization and the marketization of the corporate governance regime. Our focus is on the key actors in corporate governance – shareholders, directors, employees – as well as certain aspects of the broader regulatory architecture for business. In summary, we consider the potential for reform across several areas, and we argue for:

- a reformulation of the purpose of the company
- a shift away from shareholder primacy to a more stakeholder-driven governance model
- greater democracy in company governance and decision-making
- revisions to the role of shareholders and investors
- stronger regulatory mechanisms for corporate sustainability
- a recasting of the incentives and duties of company directors
- greater democracy and transparency in executive pay
- more diverse and inclusive company boards
- enhanced employee voice and consultation within company decision-making
- the promotion of new corporate forms and governance structures

- a range of enforcement mechanisms and a coherent regulatory overlay to shift the governance framework in a more pluralistic and stakeholder-oriented direction

The report has sought to establish some of the options for reform, point to those policy areas that will need attention from a progressive Labour government, and help to provide a narrative and vocabulary for taking these arguments forward. The challenge for the Labour Party is to advance a renewed vision of democratic socialist reform, with an active state working in partnership with businesses, workers, and their trade unions. Attitudes towards capitalism and the role of business are shifting rapidly. Labour must show itself to be leading and shaping that argument. This begins with the articulation of a principled and pragmatic agenda for change.

1. Introduction

In March 2020, a rapidly developing public health emergency triggered a sudden, severe, and deliberate contraction of the real economy. We now face a three-way crisis. The current health crisis has precipitated an economic crisis, against the backdrop of an already existing climate crisis. Finding an adequate response to these crises is an immense challenge. As a wide range of voices has argued, any post Covid-19 recovery strategy must be premised upon working towards a more inclusive and sustainable economy, with greater resilience for the future (CommonWealth, 2020; IPPR, 2020; NEF, 2020; TUC, 2020).

Within the coming period, the task for the left will be to develop an agenda for government that will facilitate a new economy, rather than simply continuing the inequalities of the old. If successful, this may presage a potentially transformative juncture – a '1945 moment'. Churchill may have been said to have won the war, but Attlee's Labour government won the peace. Labour's finest government so far created the NHS, established universal education, funded local authority care homes, nationalised the mines and railways, and built 400,000 new council homes per annum. And this was in spite of a national debt to GDP ratio more than twice as high as at present. As then, progress now will depend upon political will married to the democratic consent of the people. In 2020 the Labour Party must begin to generate the same sense of common purpose to win support for a programme of far reaching transformation.

The response to the current crisis must be different to the response to the 2008 financial crisis. Without effective policy interventions, we will likely see a further consolidation in ownership, with distressed firms purchased on the cheap by large corporations and private equity, accelerating the concentration of wealth and power (CommonWealth, 2020; Dobbins, 2020). The objective must be to avoid these negative aspects of unrestrained capitalism whilst still encouraging business competitiveness and a more productive economy. Indeed, it is precisely the need to achieve economic growth that necessitates a focus on the effective regulation of business. Everything proposed by the Labour Party must be 'pro-good business' in the widest sense, but *not* 'business as usual'. There needs to be fresh thinking on how to develop a partnership of government, businesses, workers, and their trade unions, to drive fairness at work and sustainable economic growth. This will require significant reform across many areas, including company law and employment law.

The government has already played a vital role in supporting firms through the immediate Covid-19 period. The Future Fund 2020 has been established for start-up companies, borrowing between £125k and £5m from the government, matched by private investment. By June 2020 the government had lent £16billion to the Bank Of England Covid Corporate Financing Facility scheme. Helping businesses is vital in the present crisis, but it is not clear whether the public interest has been sufficiently protected here. Conditionality is required, not in a punitive way, but in a way that lays the foundations for the kind of economy that we want to see develop over the next decade – namely one that is more inclusive, democratic, and sustainable (Mazzucato, 2020; NEF, 2020). For this to happen, state support must lead to changes in corporate priorities and practices. We must learn from the mistakes of the 2008 crisis, when government bailouts simply allowed firms to reap even higher profits once the crisis abated. This time we need to find ways to embed democracy and sustainability in the way corporations operate. This report considers how far corporate governance reform can contribute to that effort.

If the government is to avoid distributing unconditional subsidies to ailing companies, one option is for taxpayer money to be used to purchase an equity stake. The principle of a public equity stake for public investment is self-evident. If the government provides risk capital then it too must share in the profits of the enterprise, just like any shareholder. Equity taken should be held as a strategic, permanent, public stake to create a powerful form of leverage and grow public wealth in the long term (CommonWealth, 2020). We note with approval the announcement on 3rd July 2020 that the government will take an equity stake of £400m in the satellite firm OneWeb. Government stakes in private business could be used to inaugurate a new UK sovereign wealth fund, as in other countries, with the profits generated used for public purposes. Sovereign wealth funds can be immensely successful, as in Norway, for example. This new form of government revenue from part-ownership would bolster state capacity, mitigating the need for further austerity measures, whilst also giving the state steering powers to influence business practices, such as efforts to advance decarbonisation (Bailey, 2020).

Aside from this level of strategic intervention, in terms of the regulation of business there has been growing recognition of the need for a new and more progressive approach to corporate governance in the UK (Lawrence, 2017; Talbot, 2016; TUC, 2014; Veldman et al., 2016). Following the 2008 financial crisis, unregulated free-market capitalism has been increasingly challenged, and there have been widespread calls for a more 'responsible capitalism' (Hockman, 2012, 2014). Over the past decade there has been continuing evidence of a lack of public trust in business, a culture of rising executive pay, short-termism in corporate decision-making, low re-investment, stagnant wages, and poor productivity (IPPR, 2018; Johnstone et al., 2019). More recently we have witnessed a series of corporate scandals and controversies: examples include BHS, a privately-held chain of clothing stores, which failed in June 2016 with a pension fund deficit of £571m; Sports Direct, a chain of listed sports apparel stores, which admitted using oppressive workplace practices, and agreed in 2017, under intense pressure, to put an employee representative on its board; Carillion, a multinational construction services company, which went into liquidation in 2018 accused, among other things, of prioritising shareholder dividends over the funding of the pension scheme; and GKN, one of Britain's oldest manufacturing companies, subject to a hostile takeover in 2018 by a 'financial engineering' firm known for asset stripping and workforce reductions (in terms of this latter case, we intend that a further report will consider how the law on takeovers can be reformed to promote long-termism in corporate management and the better protection of the public interest).

More is now being asked of the UK corporate governance regime to address and ameliorate some of the problems these cases have highlighted (Haldane, 2016; ICSA, 2017), and there is significant analysis and debate concerning the fundamental purpose of the corporation (British Academy, 2019; NEF, 2017). In this report we argue that businesses can only do so much on a voluntary basis, and the more enlightened employers also face significant constraints in how far they are able to be progressive in this area. As a result, there is a crucial role for effective state intervention through company law reform. We consider a series of legal changes aimed at improving the monitoring, transparency, accountability, and effectiveness of corporate power. Specifically, this will require changes to the corporate governance regime to promote workforce voice in company decision-making, together with changes to the rules governing company ownership and purpose to create companies focussed on long-term, sustainable success, shared by all their stakeholders.

As this agenda gathers pace, an important shift also appears to be under way in corporate America. The largest US business group (the Business Roundtable) has replaced the long-held view that maximising shareholder value is the defining corporate purpose with a more inclusive vision that takes account of other stakeholders. This encapsulates a major change in thinking, explicitly elevating broader interests such as those of employees, the environment, and customers, in an effort to set a new standard for companies across the US. However, whilst this is a most welcome development, it remains only a voluntary statement. In the UK, the task for the next Labour government must be to enshrine these principles in legislation, as recent experience shows us that voluntary codes and industry statements, and the continued tweaking of soft law instruments, have not prevented poor company management.

The democratization of the company must be fundamental to this effort. A democratic and sustainable society requires democratic and sustainable businesses. That is the key message of this report. There is therefore a need to address both the issue of *ownership* (relating to shareholder rights, as well as the ownership claims of employees), and the issue of *decision-making* (to promote more democratic corporate structures incorporating a wider range of voices within the firm, and also to develop legal structures which allow for greater stakeholder engagement with business more broadly). This report focusses on how these issues might be addressed through *company law* reform. We intend that a further report will consider the contribution of *employment law* reform (examining workers rights and the enhancement of democracy at the level of the firm through trade unions and collective bargaining).

We argue that a raft of reforms is necessary to the corporate governance of companies, both private and publicly quoted, to support entrepreneurial activity, encourage new long-term investment, increase investor confidence, and repurpose companies to take account of a wider range of stakeholder interests. In summary, we advance a series of key principles and proposals:

- A new partnership is needed between government, business, and trade unions to drive economic recovery and growth. This should involve a **reformulation of the purpose of the company**, with the rationale for business understood as being to serve stakeholders and the public interest.

- The UK corporate governance regime should be reoriented away from shareholder primacy to support a **long-term and sustainable approach to company success**, and to encourage more democracy in company governance and decision-making.

- Shareholders should only have entitlements commensurate with their commitment and legal responsibilities. This means challenging 'enlightened shareholder value' and encouraging a **more stakeholder-driven governance and ownership model**.

- Within this, a nuanced approach would distinguish between the interests and activities of different investors, tackling those institutions (like hedge funds) that seek aggressive value extraction and short-term gains, whilst encouraging those (like pension funds) that may look for more **stable and long-term investments in emerging sectors of the economy**.

- Voluntary corporate social responsibility (CSR) initiatives are insufficient in addressing the foundational shifts needed to meet the challenge of climate change, hence the need for **regulatory pathways to achieve corporate sustainability** and build a more resilient economy.

- Directors' incentives need to be reformulated. Section 172 of the Companies Act 2006 should be amended to specify that **the primary duty of a director is the long-term success of a company** (to the benefit of all stakeholders, including employees), rather than merely the maximization of the shareholder interest (through dividends and share buybacks).

- There needs to be **more democracy and transparency in executive pay**, involving increased disclosure of pay ratios and broader stakeholder governance of compensation.

- There is a strong case for **company boards to be more diverse and inclusive**, with action needed to achieve a wider and more accurate representation of women and BAME members.

- There is also both a convincing moral and economic rationale for an **enhanced employee voice within governance structures**, as part of the democratization of work. In particular, company law should be reformed to require board-level employee representation.

- Consideration should be given to promoting **new corporate forms and governance structures** which explicitly include positive social impact as a legally defined goal, and are accountable to stakeholders as well as shareholders (either through a new type of statutory corporation with model articles, or as a voluntary company with 'B Corp' certification).

- A range of **new enforcement mechanisms** should be considered. Principal among these would be a new Business Commission to represent the interests of all stakeholders, with powers to intervene at the behest of shareholders, employees, or consumers. Other enforcement mechanisms might include new criminal liabilities for company mis-management.

- As codes of conduct and guidance statements from industry have proved ineffective, a **coherent form of regulatory overlay** will be required to facilitate this reform agenda, with progressive company law reform shifting the governance framework in a more pluralistic and stakeholder-oriented direction.

As the bold type in these bullet points indicates, these are not detailed policy proposals, but rather a series of broad statements and challenges for discussion, from which policy can develop through dialogue, and we stress the importance of moving in a planned and pragmatic way towards a new regulatory architecture for business. A progressive Labour government must work with business, not against it, improving business practices whist simultaneously promoting long-term economic growth. The aim will be to encourage productive, purposeful, and long-term oriented companies, founded on a partnership between government, shareholders, management, and workers. The potential benefits are widespread, and include: better management decision-making, increased employee engagement, improved corporate performance, long-term value creation, and more sustainable economic growth. The task for the Labour Party now is to provide the leadership and vision to take these arguments forward.

We next offer a critique and comment on the current UK corporate governance regime, as a means to establish the rationale for this radical and progressive reform agenda.

2. Financialization, corporate governance, and democracy

Corporate governance essentially concerns the way power is exercised over corporate entities. In large private firms, the nature of firm ownership, and the roles of shareholders and directors, are crucial factors (Moore and Petrin, 2017; Tricker, 2015). In the UK, the corporate governance system is strongly oriented towards a norm of shareholder primacy, and towards the 'maximization of shareholder value' (MSV).

There is now extensive evidence that this model, with its emphasis on using corporate profits for share buybacks and delivering returns to investors, has a systemic bias towards value extraction and transfer rather than value creation, and acts as a barrier to internal, long-term re-investment in human and physical capital, productive capacity, and R&D (CIPD, 2017; Lawrence, 2017; Lazonick, 2016). Strongly embedded incentives for asset holders and corporate executives create powerful tendencies towards short-termism in both finance and industry (Gospel et al., 2014; Jacobs and Mazzucato, 2016). Relatedly, there has developed an active 'market for corporate control' in the UK, with the associated threat of hostile takeovers, which tends to induce asset disposals and job losses in the companies targeted (Johnston and Njoya, 2014; Pendleton, 2016). It is also clear that the MSV model generates and disseminates a language, concepts, and practices that increases its reach and impact beyond large listed corporations into other sectors, sizes, and types of organisation (Cushen and Thompson, 2016).

Analysis of the EU28 shows a strong positive correlation between shareholder-oriented governance systems and poor performance on productivity, lower R&D expenditure, and higher rates of inequality (Lawrence, 2017; Stiglitz, 2016). Clearly this corporate model is broken, with short-term profit maximization leading to value extraction, asset stripping, insecurity, and inequality (Sikka et al., 2019). If we look deeper we can see how this approach to corporate governance, and the problems associated with it, have been facilitated by processes of financialization and marketization over recent decades. Simply put, financialization refers to the generation of income through financial channels rather than productive activities. Whilst *profit*-seeking activity increases wealth through the creation of value and associated economic growth, *rent*-seeking activity generates firm-level profits merely by changes to the structure and financing of the firm. As economic rents are extracted from the production process, income is derived from ownership of existing assets, without creating anything new (Blakeley, 2019).

Recent decades have seen the emergence of financialised corporations in the UK, centred on the growing embrace of these rent-seeking behaviours. Within this framework, investors will tend to see firms as 'bundles of assets' within a wider portfolio, and the stakeholder interests of employees become marginalised (Clark and Macey, 2015). Financialization thus breaks the 'retain and re-invest' circuit of capital associated with managerial capitalism, giving rise to a finance-dominated regime of accumulation. Corporate earnings are re-directed to shareholders in the form of increased dividends and share buybacks, rather than re-invested in the productive capacity of the firm or in rising real wages (Horn, 2017). These trends have also developed further, rather than receded, since the 2008 financial crisis. In 2018, overall total shareholder pay-outs among the 100 largest UK-domiciled companies stood at just over 100% of net profits, compared with 43% in 2011. Comparing corporate behaviour in the first and second halves of the decade following the financial crisis reveals a measurable *increase* in total shareholder pay-outs relative to pre-tax profits (CommonWealth, 2020).

In terms of the impact on business and management, it is clear that financialization drives corporate level practices, and the pursuit of shareholder value in deregulated and globalising markets has intensified constraints on the strategic choices of firms (Thompson, 2003, 2013). There is a direct connection between the pursuit of shareholder value, the behaviour of firm management, and negative impacts on high-performance productivity bargains (Clark, 2009; Cushen and Thompson, 2016). The key feature of these developments is that employers are unable to 'keep their side of the bargain' with employees, given the constraints imposed upon them by capital markets, the operation of which exacerbates a disunity, or 'disconnect', between macro-level structural changes and micro-level workplace outcomes (Dobbins and Dundon, 2017). It is difficult for firms to protect human capital investments based on 'mutual gains' and 'partnership', as these are fragile under threat of takeover (Davis et al., 2013; Deakin et al., 2002), and management attitudes towards implicit contracts with employees are informed by the imperative of returning money to investors (Appelbaum et al., 2013). The process of financialization also undermines the organisational capacity of trade unions (Grady and Simms, 2019), whilst the UK corporate governance regime lacks strong employee voice and representation mechanisms (Gold and Rees, forthcoming).

It is crucial to recognise that these trends are not independent or 'natural' market mechanisms, and their outcomes and effects are not inevitable. Rather, they have been actively stimulated by successive governments, insofar as financialization depends upon *marketization*, in other words the creation of 'regulatory preconditions' for markets to arise and develop (Callaghan, 2015), thereby extending the market mechanism to new areas of social life. Key factors in this process of marketization have been the globalization and deregulation of financial markets, and the encouragement of an autonomous role for financial intermediaries and asset managers, which have in turn facilitated the fragmentation of corporate ownership (Clark, 2016). The removal of regulatory obstacles to international capital movements and foreign takeovers of British firms has been accompanied by a steep decline in the proportion of UK-based *institutional* investors and *individual* shareholders, with a corresponding increase in *foreign* investors (to over 50% of UK equities). Individual ownership has shrunk from around 50% in the 1960s to less than 10% today. UK pension funds and insurance companies' ownership of UK listed companies has also declined, from over 50% in 1990 to less than 15% today, whilst foreign institutions – such as hedge funds, sovereign wealth funds, and overseas pension funds – have taken an ever increasing share (Haldane, 2015).

The combination of this *increasing diversification* of shareholdings, coupled with a marked *reduction in length* of shareholdings, has made shareholder control over management highly problematic (Haldane, 2016; ICSA, 2017; Kay, 2012). With the share registers of UK companies increasingly globalised, investors have limited jurisdictional commitments, and concentrate on direct and speedy financial gains (Johnston and Njoya, 2014). In 1992, when the UK Corporate Governance Code was introduced (the so-called 'Cadbury Code'), over 50% of shares in UK firms were owned by UK-based pension funds and insurance companies, and these were the investors implicitly expected to make the principle of 'comply or explain' work. By 2014, however, that figure had fallen to less than 10% – 'The majority of shares in UK listed companies are now held by institutions based *outside* the UK, which were not a significant presence in the market in 1992 … For many of them the UK market represents only a small percentage of their overall equity portfolio, and they face practical barriers to direct engagement with UK companies' (ICSA, 2017: 7–8).

As the priorities of 'managerial capitalism' have been progressively eclipsed in this way by those of 'financial capitalism', new investor-owners have also emerged, such as hedge funds, private equity (PE) funds, and associated asset management (Mazzucato, 2018). As Clark and Macey (2015) explain, these new financial intermediaries typically seek to generate profits by alterations to the structure of a firm, taking substantial but minority ownership positions in listed firms on an activist basis, either with the aim of launching a hostile takeover or to encourage incumbent management to improve returns to investors via restructuring, divestment, or closure of under-performing units. Hedge funds will often use their cash resources to buy up distressed or bankrupt companies, promising to turn them around. In many cases this involves very substantial downsizing of the business and the disposal of whatever assets can be sold for cash. In some cases, a viable but much smaller business is created, which can eventually be sold on the market to another corporate group or in a management buyout (Hadden et al., 2014). As for private equity, the cases where PE firms provide the investment or management expertise to help turn companies around or grow are the exception, not the rule. The norm is for PE firms to make extensive use of debt and leverage to seek quick capital gains by financial engineering of the balance sheets of companies, forcing through cost-cutting measures which frequently entail job losses, greater precarity, cuts to pay, and poorer working conditions (Appelbaum et al., 2013). Capital markets thus increasingly regulate the behaviour of firms, driving down the labour share, and legitimizing more aggressive management of corporate assets through delayering, downsizing, and divestment (Pendleton and Gospel, 2014).

Alongside liberalisation and deregulation in capital markets, the core institutions and guiding principles of UK corporate governance – takeover regulations, governance and stewardship codes, and directors' fiduciary duties – are also strongly oriented towards a norm of shareholder primacy (Armour et al., 2003). As Deakin (2018) notes, these rules are justified as making it easier for shareholders to hold managers to account (as per agency theory), yet their effect is to tilt the balance of power away from workers and managers, and towards the holders of the capital interest. Over recent decades there has been a growing political acquiescence in, and support for, these market-enabling rules. Public policy has also emphasised accountability to shareholders, rather than regulation, as the means to improve corporate practice (Talbot, 2013, 2020). We argue that the time is now right for a series of rigorous market-restraining counter-measures. Our analysis suggests a requirement for reform across several areas, with policy options relating to all of the key actors in corporate governance. This will necessitate the state providing a coherent form of regulatory overlay, with the aim of democratizing the way businesses are governed and the way decisions are made. Before outlining specific areas for policy development, the justification for reform will be further strengthened if we briefly reflect on the nature of – and distinction between – the corporation and the firm.

The corporation is an entity with a separate legal personhood, distinct from its shareholders and its directors (Hockman, 2012; Kay, 2015). It is not a fixed or given institution, but rather is a social construction, constituted by politics and law. In legal terms, and contrary to widely held 'common sense', shareholders do *not* own corporations, or the assets of corporations. Shareholders only own shares of stock (bundles of intangible rights, most particularly the rights to receive dividends and to vote on limited issues). The corporate form grants shareholders an extraordinary privilege – limited liability – which shields them from liability for the actions the corporation takes on their behalf. This means shareholders have virtually no responsibility for corporate malpractices, and yet they still enjoy controlling rights (CommonWealth, 2020; Ireland, 1999; Robé, 2011). Indeed, economic coordination rights in the corporation are currently assigned exclusively to capital via property, and labour is effectively excluded from the government of the company. Moreover, whilst shareholders can hedge their risks by purchasing a diversified portfolio and, thanks to the liquidity of the market, divesting their stock relatively easily at any time, employees with firm-specific skills are unable to hedge, as they will be most unlikely to hold a portfolio of jobs, and they cannot simply trade one job for another (Brown et al., 2019). Workers bear long-term, firm-specific risks in companies, they have their livelihoods at stake, and they usually have a far longer relationship with the company than the typical shareholder (Sikka, 2008). Workers thus carry disproportionate risk in relation to company decision-making, and yet they have little chance to influence it (Deakin, 2018).

Acknowledging this imbalance is at the heart of the argument for the democratization of the company (Ferreras, 2019; Fraser et al., 2020). Rather than assuming (wrongly) that shareholders own firms, and therefore permitting them sole entitlement to control and governance rights, it is more accurate to recognise that there are *two* classes of investors constituting the firm. One is capital. The other is labour. Their investments are mutually dependent: without one or the other, the firm would cease to function. However, the way firms are currently governed does not reflect this reality, since governance rights are only granted to *one* of these investors. As Ferreras (2017) explains in detail, whilst it is to be expected that the *corporation* (as a vehicle for investing capital) will be governed by people whose principle relationship to the firm (via that corporation) is an instrumental one, reflecting the dominant maxim in capital investment, of profit and return, what is *not* equitable (or inevitable) is that these capital investors alone should have also secured the *political right to govern firms* for themselves. This, in essence, is the case for widening democracy in corporate governance – 'The time has come for firms to take labour investors seriously as key partners not only in the *management* but also the *government* of the firm' (Ferreras, 2017: 61). In reality, the firm is not owned by shareholders. Rather, the firm is a 'political entity', much broader in scope than the corporation, and is more accurately considered as 'an institution of the commons: a social institution with multiple constituencies who share overlapping economic and political claims' (CommonWealth, 2020: 13). As such, a firm's government should represent *all* its constituents, not merely those legally organised via the corporation. All of a firm's investors have the right to a voice in the governance structures that rule them.

3. Shareholders and stewardship

The above analysis would suggest an urgent need to reform and regulate the role of shareholders. There is a convincing argument that shareholders should only have entitlements commensurate with their commitment and legal responsibility, and that a stronger set of social obligations should come with the privilege of limited liability. Principal areas for discussion here would therefore be around *downgrading* shareholder entitlement, and challenging the discourse of so-called 'enlightened shareholder value' (Talbot, 2013). That said, an argument can also be made that the powers and responsibilities of shareholders need to be *increased* – so that they can more effectively control the composition and remuneration of the board of directors, and encourage boards to consider ESG (Environmental, Social, and Governance) issues. This tension reflects the essentially double-edged nature of the capitalist economy, wherein shareholder activity can be both a driver of 'financialised' corporations as well a factor in the emergence of more 'socialised' corporations (Ireland, 2018). Policy proposals in this area will therefore need to strike a careful balance.

If we examine the regulatory response of governments since the 2008 financial crisis, rather than emphasising limits on shareholder rights, the idea that institutional shareholders can in fact act as effective monitors or 'stewards' of the company has been a defining feature of this period (Talbot, 2020), as encapsulated in a new code (the 2010 Stewardship Code). Likewise, proposals for reform arising from the recent government review of corporate governance centre on further revisions to the Corporate Governance Code and the Stewardship Code (BEIS, 2017; Mor, 2019). These are both 'soft law' initiatives, continuing recent principles of code-based reform, with a commitment to addressing perceived weaknesses in corporate governance through greater shareholder engagement (Deakin, 2014; Veldman and Willmott, 2016).

However, whilst the Stewardship Code contains a principle that institutional investors should publicly disclose how they will discharge their stewardship responsibilities, 'it cannot be assumed that the stewardship role is intended to protect anyone other than the particular beneficiaries of the fund for which those investors have responsibility' (Hockman, 2014: 213). Unlike most members of a partnership or a family business, shareholders' interest is comparatively detached and speculative, and they will seek to invest in whatever will produce a strong return. If they are not satisfied, the easiest option is to invest elsewhere. Moreover, we have noted that there has been a marked shift in ownership patterns in favour of foreign investors and hedge funds. As such, 'the fact that the Code is directed towards UK-based asset managers and domestic institutional investors, who own less than one third of the shares in UK quoted companies, means that it is unlikely to have a transformative effect on corporate governance' (Hockman, 2014: 214). We should also note that in order to be 'good stewards', shareholders would need to be both active in corporate governance and guided by social responsibility, but as Talbot (2013: 185) observes, 'many … only seem active when engaged in social irresponsibility and rapaciousness; otherwise they are inactive. Broadly speaking, pension funds fall into the latter (passive) category, and hedge funds into the former (active, rapacious) category'.

This reminds us, then, of the need to distinguish between different types of share ownership and investment activity. As Meadway (2020) argues, whilst some financial activities and institutions (hedge funds, for example) are clearly very much driven by short-term gains, others (like pension funds) often look for longer-term, stable investments that produce steady returns, and these might be the sorts of investment – in renewable power generation, or new public transport, for example – that are urgently needed. Evidently there is a strong case for limiting, or in some instances completely removing, the right to vote of those whose connection to the company is short-term and opportunistic – hedge funds do not operate out of a concern to improve corporate governance, but rather to make short-term gains for the fund – but at the same time, reform proposals must recognise the growth and potential in responsible and long-term shareholder investment.

Various policy options are available that might distinguish between different types of investor. Consideration could be given to imposing a minimum period between the acquisition and disposal of shares. Voting rights in relation to takeovers could be made conditional upon a minimum ownership period, say two years, something the Trades Union Congress has long argued for (TUC, 2014), and voting rights per share could increase with length of ownership. Similarly, takeover decisions could be restricted to shareholders who own shares when the bid is launched, distinguishing between those with a long-term commitment and those without, and rewarding the former with differentiated control of the company. Alternatively, a two-tier share register might be developed, with long-term investors again monopolising voting rights. Revisions to the Stewardship Code could also be considered. For example, funds which engage in 'M&A arbitrage' could be required to make reference in their Code statements to how, if at all, they engage with the management of companies, what the nature of their interest is (i.e. shares or derivatives, long/short combinations etc.), the typical duration of their interest, etc. Indeed, all investors and asset managers should be required to be public about their stewardship and engagement activity (Powdrill, 2018).

There is now an emerging consensus among many investors around the need to move past the sole objective of maximizing firm profits, and recently there has been a more intense focus on ESG criteria in the management of companies. Investment in ESG strategies has grown rapidly, with the Global Impact Investing Network estimating the value of dedicated impact funds at more than $500bn in 2019 (Colback, 2020). Again there is a need for a balanced policy response. Although so-called mainstream investors do pay attention to ethical and other factors that may affect the reputation or performance of the companies in which they invest, importantly, this focus is not their principal concern. It is a beneficial side-effect of their desire to achieve a good return for their clients, not an attempt to fulfil some sort of implicit public duty (Powdrill, 2018). So, whilst the rapid development of 'sustainable asset management' is unquestionably very positive, the ambitious sales pitch on these themes raises questions as to how to inform investors properly and, more particularly, how to prevent the risk of 'greenwashing'.

It has been suggested that, post Covid-19, companies may adopt a more 'authentic' version of social responsibility, and we could see a new wave of investors demanding investment strategies that go beyond ESG risk integration in pursuit of real-world social and environmental impact. For this to happen, it is said that business leaders and institutional investors will need to 'embrace a new era of governance dialogue' (ICGN, 2020). Again, however, many companies have been criticised for continuing 'business as usual' or, worse, taking advantage of the current crisis. We should also note that the much publicised Business Roundtable declaration in the US will not easily change business behaviour. Individual CEOs may sincerely wish to make progress, but the declaration is perhaps best seen as an example of the age-old 'don't regulate us and we will be nice' argument. We would argue that in this area corporate voluntarism is insufficient, and given the nature of the UK corporate governance regime, as outlined above, regulation will be required to ensure companies pursue a long-term approach to sustainable value creation (Sjåfjell, 2018).

The pervasive and well-entrenched discourse of 'corporate social responsibility' (CSR) has consistently advanced a purely voluntary concept of business responsibility, claiming that firms' social objectives can simply be 'integrated' into business decision-making, the so-called win-win, 'business case' scenario, often referred to as a process of 'creating shared value' (Porter and Kramer, 2011). There are various self-regulatory mechanisms and controls which corporate management might initiate to ensure, or be seen to ensure, compliance with ethical standards. But there remains a fundamental ambiguity in CSR's role and intent (Hadden et al., 2014). It may be a means to legitimise and promote genuine modifications in corporate behaviour, but it may also function merely as a form of public relations window-dressing. The problem is that voluntarist CSR ignores the inherent tensions between the legal framing of management discretion under shareholder primacy and social pressures to address wider concerns which may not – and indeed are unlikely to – be embraced by shareholders (Johnston, 2017). Indeed, this failure to acknowledge the tension in firms between economic and social value-creation is a characteristic of much of the stakeholder value and CSR field (Crane et al., 2014).

So, as Johnston (2017) explains, under the current corporate governance regime we cannot assume that shareholders will steer or 'steward' companies towards a long-term and socially responsible approach, and indeed there is evidence that shareholder engagement is actually having the opposite effect, with on-going pressure on managers to maximize quarterly returns further reducing the willingness of firms to voluntarily address the social costs (the externalities) their activities create. The 'business case' argument for CSR – voluntary practices exercised under the purview of corporate discretion – is also a weak form of sustainability that is insufficient in addressing the foundational changes needed to meet the United Nations Sustainable Development Goals and climate targets by 2030 (Sjåfjell, 2018). Hence the increasing recognition of the need for regulatory pathways to achieving corporate sustainability (Cullen et al., 2020; Vitols and Kluge, 2011). Assessing the picture across Europe, Johnston and Sjåfjell (2019) argue that information disclosure alone is insufficient to secure the contribution of business to environmental sustainability, in the face of the 'detrimental social norm' of shareholder primacy, and therefore a fundamental shift towards a firmer and more coherent regulatory approach is needed. In this context the task for governments is to 'dare to mandate that one of the objects of business is to contribute to sustainability, that it must be verified whether and the extent to which this is done, and create a meaningful threat of enforcement in the event of non-compliance' (ibid: 15).

This analysis suggests that, rather than focus on voluntary, management-led CSR, it is more helpful to acknowledge 'the more deeply rooted *institutional foundations* of corporate *ir*responsibility', in other words how 'the potential for irresponsibility … is inscribed in the corporate legal form as currently constituted' (Ireland, 2018: 13). As Ireland (2018) explains, in the context of a corporate legal form which combines no-liability shareholding with increasingly open and global financial markets, we should not be surprised to see the emergence of socially irresponsible forms of governance. As such, appeals to voluntarist CSR, or to pursue shareholder value in a more 'enlightened' manner, rather miss the point: 'in this institutional context, reforms aimed at empowering and enhancing the proprietorial rights of *rentier* shareholders and at making them more active, whether in financial markets or in corporations, are … more likely to exacerbate the problem than to solve it' (ibid: 34). As such, ideas like time-dependant voting rights are a step in the right direction, but they do not go far enough, as the problem is not merely one of shareholder 'commitment'. Rather, as long as no-liability *rentier* shareholding continues to be *combined with control rights*, this will be a recipe for short-termist governance, managerial excess, and corporate irresponsibility. A more rigorous solution lies in acknowledging separate corporate personhood, dispelling the ideological myth of 'shareholder ownership', and institutionalising a stronger role in governance for labour and other stakeholders (ibid: 34–35). A range of reforms can further this agenda and set in train the next stage of development of the corporate legal form.

4. Directors and the boardroom

As we have outlined, shareholder-driven models of corporate governance are heavily predicated on the need to discipline firm leadership, with company directors (the agent) acting in ways that are consistent with the interests of shareholders (the principal). Hence corporate executives see their main duty as maximising short-term shareholder value, which steers them away from internal firm investment and value-creating activities (Brown et al., 2019; Cushen and Thompson, 2016). Although in law directors are *not* simply the 'agents' of shareholders, duty bound to maximise shareholder wealth to the exclusion of other interests (Kay, 2015), directors' skills have nonetheless been honed to increase share prices and dividends in ever more financialised ways, and they will take professional pride in doing so because these are valued achievements which are rewarded in remuneration and promotion (Talbot, 2013). Indeed, modern forms of executive remuneration which align the interests of managers and shareholders have made the ruthless pursuit of shareholder value very lucrative for executives, and since the 1990s their pay has seen exponential growth (Ireland, 2018). We thus need to consider a range of reforms to the incentives, compensation, and composition of the board of directors.

Principal among these reforms is the need to revise the duties of directors, as specified in the Companies Act 2006. Specifically, this would mean re-wording Section 172 to make it explicit that the long-term success of a company is (or should be) the primary concern of its directors, and that shareholders' interests, which are increasingly short-term, do not eclipse those of employees as the principal long-term stakeholder in the firm. Recent government proposals in this area have now been incorporated into the revised Corporate Governance Code (effective from January 2019), with a new requirement on firms to 'explain compliance' with Section 172, and to disclose how boards 'have regard to' non-shareholder interests. This disclosure involves explaining how key stakeholders have been identified, how their views have been sought, why the company's engagement mechanisms were considered appropriate, and how the information obtained from them influenced the board's decision-making. Whilst this is a welcome development, in order to firmly shift corporate governance from its focus on shareholder value and towards a stakeholder model of purposeful enterprise, we would suggest a stronger formulation is needed.

Currently, Section 172 states: 'A director of a company must act in the way he considers, in good faith, would be most likely to promote the success of the company for the benefit of its members as a whole, and in doing so have regard (amongst other matters) to: (a) the likely consequences of any decision in the long term, (b) the interests of the company's employees, (c) the need to foster the company's business relationships with suppliers, customers and others, (d) the impact of the company's operations on the community and the environment, (e) the desirability of the company maintaining a reputation for high standards of business conduct, and (f) the need to act fairly as between members of the company'. This could be re-worded to more strongly assert the long-term success of the company as its central objective ('long-term success' is used in the first paragraph of the Corporate Governance Code but is absent in the legislation). Moreover, the words 'for the benefit of its members as a whole' could be removed, as these suggest the primacy of shareholders over all other interests. Instead of stating that directors must 'have regard to', there could be a clear duty to take account of the interests of a range of stakeholders: employees, pension holders, suppliers, customers, creditors, the environment, the local community, and society as a whole. Again, the firm needs to be understood – and so formally regulated – as a social and political entity constituted by a wide range of investors, and not merely as a vehicle for the interests of capital.

This brings us to a further issue that has contributed significantly to the erosion of public trust in business, namely the widening pay gap between the average worker and senior executives, and the extensive use of long-term incentive plans (LTIPs) and stock options, which gradually reward executives through equity in the company. In the UK, the ratio of executive to average worker pay increased from 47 times in 1998 to a staggering 148 times in 2014 (High Pay Centre, 2015). Pay levels have risen far in excess of returns to shareholders, profits, and employee wages (Big Innovation Centre, 2017; Lazonick, 2016). As of the latest filings, just over 700 executives at 86 of the 100 largest non-financial UK companies held a collective £6 billion in equity at their respective corporations, representing nearly £8.5 million per director (CommonWealth, 2020).

The recent government proposals in this area primarily relate to company responses to significant shareholder opposition to their executive pay, pay ratio reporting, remuneration committee responsibilities, and clearer disclosure with respect to the share-based incentive components of remuneration policies. Again a number of these proposals are now reflected in the newly-revised Corporate Governance Code (CIPD / High Pay Centre, 2019). For instance, from 2020, UK companies are required to list the pay ratios between their CEO and the 75th (upper quartile), median, and 25th percentile (lower quartile) points of the pay distribution of their UK employees (on a full-time equivalent basis). Other potential areas for further reform might include: mandatory employee and consumer votes on executive pay packages and bonuses (with bonuses only paid for extraordinary performance or effort, not as a matter of routine), a set ratio to be applied to the difference between CEO and average pay, a broader stakeholder governance of compensation (with boards having the final say), and effective measures to tackle the gender pay gap. Pay systems which are perceived to be fair are an important factor in good employment relations

(Stern, 2018), and workplace collective disputes frequently involve concern over the relative level of executive pay compared to that in the rest of an organisation (ACAS, 2018).

In terms of the latest developments, a recent High Pay Centre (2020) report analyses the pay ratio disclosures made by 107 FTSE 350 companies between 1st January and 31st April 2020. It found that the median gap between the CEO and the lower quartile threshold of the pay distribution was 78:1 for all companies in the sample, whilst for the larger FTSE 100 companies it was 109:1. As the report makes clear, hypothetical exercises reveal the potential for relatively minor redistributions from upper to lower quartile earners to achieve meaningful pay increases for the latter. For example, across all companies, reducing the pay of employees at the upper quartile by 3% could fund a median pay rise of £2,000 for the lowest earning quartile of employees in the same companies, whilst still leaving the median upper quartile earner with pay of over £60,000. Redistributions from those at the very top could achieve significantly more. Reflecting on the report, the Director of the High Pay Centre concluded: 'After over a decade of pay stagnation, raising wages for low and middle-income workers is a vital political priority … Measures that can turn the hypothetical redistributions identified in our research into reality are integral to hopes that we can 'build back better' in the aftermath of the pandemic. Specific policies could include better workplace access for trade unions; business governance reforms to give workers more say in corporate decision making; and much wider provision of all-employee share ownership or profit-sharing schemes' (Hildyard, 2020).

As well as reforms to the incentives and compensation of directors, there are also strong moral as well as economic reasons for broadening the composition of boards, and for seeking greater gender, ethnic, and social diversity. Improving the diversity of boardrooms so that their composition better reflects the demographics of employees, customers, and the communities within which companies operate can help improve decision-making and therefore performance, as well as ensure that boards have access to a wider range of perspectives, talent, and experience. There has been a steady increase in the number of women on the boards of the UK's top companies in recent years. The final report of the Davies Review in 2015 showed that the proportion of female directors in FTSE 100 companies had more than doubled in the previous four years (BEIS, 2015), albeit from a low base, and progress has continued since. In 2017 there were only six all-male boards across the FTSE 350, down from 152 in 2011. That said, the more recent Hampton-Alexander Review has highlighted a lack of female representation in senior leadership roles on executive committees, which are one level below the board, and this has long been considered one of the main barriers to increasing gender balance in the boardroom, as they are seen as providing the pipeline of future directors (Goodley, 2020).

For the government, the steady progress in this area is proof that a non-interventionist and business-led strategy, rather than legislative quotas and penalties, is the right approach (BEIS, 2017). This view is also reflected in mainstream business circles. For example, the CIPD has always advocated a voluntary approach to increasing boardroom diversity, encouraging companies to develop their own responses to the challenge. There is extensive evidence that certain organisational practices are the most effective in promoting gender diversity in senior roles (principally an open and supportive culture, unbiased recruitment and selection practices, work–life balance policies that support female staff with caring responsibilities, and clear career paths and promotional opportunities in middle and senior management roles). A CIPD (2015) report on gender diversity concludes that female progression to top roles is effectively only possible if companies 'provide a strong and sustainable framework to recruit and develop women at every stage of their career' (ibid: 2).

The implication of this position is that legislating to require that a certain number of women are appointed to board positions will not alter or remove the underlying reasons for a lack of boardroom diversity, and indeed a quota imposition could be counter-productive as it presents an appearance of equality (equality of outcome) without addressing the structural and organisational factors that continue to deny women equality of opportunity. As the CIPD (2015) conclude, it could also lead to a potential backlash towards those appointed as a result of perceived positive discrimination: 'People want to be seen as successful based on their own ability and not as a result of their identity. While voluntary targets … can be helpful … the key criterion for boardroom appointments should be merit' (CIPD, 2015: 4). The newly revised Corporate Governance Code very much reflects this sentiment, with Principle J stating: 'Appointments to the board should be subject to a formal, rigorous and transparent procedure, and an effective succession plan should be maintained for board and senior management. Both appointments and succession plans should be based on merit and objective criteria and, within this context, should promote diversity of gender, social and ethnic backgrounds, cognitive and personal strengths' (FRC, 2018: 8).

Whilst improvements are being made to the gender balance in boardrooms, we feel that progress is too slow, and a legislative quota would indeed accelerate the pace of change. As a comparator, women-only shortlists in the selection of parliamentary candidates have of course helped to increase overall diversity in the Parliamentary Labour Party, and a quota for boardrooms would have the same effect. Clearly, if government is to play a constructive role in the current context, it must also seek to encourage and incentivise businesses, across all sectors and sizes, to provide a supportive framework of effective workplace and human resource policies, in order to promote and facilitate genuine equality of opportunity. At the same time there is a need to push for more ambitious targets for companies to meet with respect to new appointments to senior and executive management positions, and for more stringent and transparent reporting of diversity issues in annual reports. Reporting requirements have now been introduced through the Companies Act 2006 (Strategic Report and Directors' Report) Regulations 2013, and these could be further monitored and strengthened so that shareholders and other stakeholders, including trade unions, have the necessary information to properly hold companies to account.

Whilst there are welcome signs of progress in terms of gender diversity in the boardroom, the situation regarding ethnic diversity is less positive. The Parker Review published draft recommendations in November 2016 proposing a target for the FTSE 100 to appoint at least one board-level director from a Black and Minority Ethnic (BAME) background by 2021. A follow-up review in 2019 found just 84 directors from BAME backgrounds out of 1,048 director positions. That said, Sir John Parker believes there is now much broader support for boardroom diversity than when he launched the review, and that the recent strengthening of the Black Lives Matter movement will help to drive the issue forward (Makortoff, 2020). Together with the Covid-19 pandemic, this has undoubtedly increased public sensitivity to social injustice, and a number of companies have responded to this change in mood, with a range of business leaders making statements in solidarity and vowing to examine their diversity practices (Colback, 2020). Major business groups like the BCC and the CBI are formulating plans in the wake of these developments. The CBI is pledging to establish a 'business-led movement' to boost boardroom diversity, and develop toolkits to help businesses attract, hire, and promote employees from BAME backgrounds. The TUC is stressing the need for employers to monitor recruitment, pay, and progression for BAME workers, and to publish clear targets for improving representation at all levels. Again there is a role for government intervention, and we believe that the Parker Review recommendation for at least one BAME board member in every FTSE 100 company should be legislated for.

Notwithstanding greater gender and ethnic diversity, there remains a prevailing one-dimensionality in the constitution of most boards, with minimal, if any, representation from stakeholders other than investors and executives, and this is clearly a block on progressive corporate governance reform. Boardrooms remain relatively homogenous, and critics suggest they have in general become less open to innovation and more risk-averse, focusing on the short-term benefits of cost cutting rather than the long-term returns of investment (Lawrence, 2017). If corporate diversity policies focus only on the appointment of more female and BAME non-executive directors (NEDs), the prioritisation of shareholder value is likely to persist if these individuals continue to be drawn from the same business elite of executives and advisors, and very rarely from other constituencies. Moreover, robust oversight by NEDs has already proved elusive, and nomination processes remain relatively closed. In this context, corporate diversity policies may have little impact on shifting governance priorities and challenging short-termist 'group think' if directors all come from similar backgrounds and share the same bonds of class and educational privilege. In many large professional firms, there is a pressing need to facilitate the representation of different socio-economic backgrounds and challenge the persistence of exclusionary mechanisms based on class (Ashley and Empson, 2017). The traditional boardroom monoculture needs to be challenged by dissenting voices and a 'diversity of thought', in order to promote more democratic governance and decision-making (Hadden et al., 2014). We expand on these arguments in the next section with reference to worker directors.

5. Employees

As we have outlined, there is extensive evidence that the UK corporate governance regime is tilted too far towards the interests of capital, and away from the interests of employees. Compared to shareholders, workers carry disproportionate risk in relation to company decision-making, yet have little chance to influence it. Shareholders can vote on who sits on the board and make other strategic decisions, and directors have a duty to promote their interests. However, unlike in other European countries, most UK employees have almost no formal rights to information or involvement in corporate decision-making, and are excluded from representation on company boards (TUC, 2016). In terms of formal employee participation rights, the UK ranks sixth from bottom among EU countries – ahead of only Bulgaria, Cyprus, Estonia, Latvia, and Lithuania. We have also noted the potentially negative impact of the UK corporate governance regime on the development of collaborative or 'partnership' employment relations and 'mutual gains' between management and workers (Johnstone, 2015), raising the question of how far it is possible for enlightened employers to 'keep their side of the bargain' under the dominance of shareholder value in capital markets (Thompson, 2003, 2013).

Hence there is a strong case for progressive reform around employee consultation and voice within governance structures, and the benefits of this are widely recognised (Hall and Purcell, 2012; IPA / Tomorrow's Company, 2012). There is evidence that board-level employee representation (BLER) can increase trust and co-ownership, enhance board insight by bringing a different perspective and information set to the board, encourage employees to feel more empowered and engaged, foster longer-term management horizons, and improve the quality of decisions (Gold, 2011; Waddington and Conchon, 2016). Workers bring to the board an in-depth knowledge of the company they work for and the environment in which it operates, making them well-placed to contribute to strategic and operational decisions. Board-level employee representatives are also able to disrupt 'group think', for example of the sort that led to the excessive dividend payments at Carillion. Employee representatives could have questioned this and focused minds on the long-term interests of the firm and on protecting the pension fund.

There is now widespread political support for worker directors in the UK, with all the major political parties having made manifesto commitments in different forms (Labour went the furthest in 2019, arguing that workers in large firms should have a third of board seats). Support for the principle of worker directors is also increasingly mainstream. Andy Haldane, Chief Economist at the Bank of England, has suggested that company law gives too much weight to the interests of shareholders, and that putting workers on boards and making directors consider the 'interests of all stakeholders' could be economically beneficial. The Institute of Chartered Accountants in England and Wales has concluded that employee directors support long-term thinking, help stakeholder engagement, improve board behaviour, and enhance board credibility (ICAEW, 2018). In the final report of its Commission on Economic Justice, the IPPR (2018) proposes that large companies of more than 250 employees should have at least two workers, elected by the workforce, on both their main board and the remuneration committee, as something likely to enhance the quality of strategic decision-making, increase the diversity of opinion and experience on the board, represent employees' interests, and strengthen employee engagement. The TUC has long argued for BLER, and advances a series of core principles: companies should have a minimum of two worker directors on their board to avoid worker directors being a 'lone voice'; worker directors should be elected by the workforce, with candidates nominated by unions where they are present (a worker director appointed by the board or by management is a contradiction in terms); worker directors should be given training and paid for the time needed to undertake their role; importantly, worker directors would bring a *workforce perspective* to the boardroom (as distinct from directly *representing* the interests of the workforce – which remains the role of trade unions through collective bargaining) (TUC, 2018; Williamson, 2018). Finally, recent polling by YouGov also suggests that the principle of workers on boards is supported by about two-thirds of the population in the UK.

The case for worker directors is not only one of natural justice and democracy but also reflects a strong economic rationale (Tomorrow's Company, 2016). The interests of workers are well-correlated with long-term company success, and countries with strong worker participation rights and practices (on board representation, workplace representation, and collective bargaining) score more highly than other countries over a range of important measures – including R&D expenditure, employment rates, and educational participation among young people – as well as having lower rates of poverty and inequality (Williamson, 2018). In much of Continental Europe – including many of the most successful economies such as Germany, the Netherlands, Austria and Denmark –

workers have the right to be represented on company boards. In 14 of these countries, these rights are extensive, in that they apply to the majority of private companies. Significantly, they apply in countries like Sweden that have a unitary board system (i.e. a single board of directors) as in the UK, as well as in countries like Germany that have a two-tier board system (i.e. with an executive management board and a supervisory board which is almost entirely non-executive). In broad terms, worker directors form a significant foundation of 'industrial citizenship' across Europe (TUC, 2016).

The last major debate about worker directors in the UK was in 1977, when the Committee of Inquiry on Industrial Democracy (the Bullock Committee) proposed measures for worker directors in all UK-based companies. The Labour government published a White Paper in 1978 which proposed that companies should negotiate the details of BLER themselves with unions, but that statutory fall-back arrangements should apply in cases of failure to agree. The Conservative government elected in 1979 abolished existing worker director schemes (at British Steel and the Post Office), and there was no further progress in the area for a generation (Gold and Waddington, 2019). Subsequent experience with BLER in the UK has been meagre, with First Group for many years the only UK PLC with a worker director (since 1989). However, after some forty years, BLER has now re-emerged as a significant issue on the UK political agenda. And it has re-emerged from a perhaps unlikely source. Launching her campaign for the Conservative Party leadership in 2016, Theresa May said: 'In practice [non-executive directors] are drawn from the same, narrow social and professional circles as the executive team and – as we have seen time and time again – the scrutiny they provide is just not good enough. So if I'm prime minister, we're going to change that system, and we're going to have not just consumers represented on company boards, but employees as well'. Alas, upon taking office, the reality did not match this lofty ambition. Following a Green Paper consultation and Select Committee enquiry, in August 2017 the government invited the Financial Reporting Council (FRC) to revise the Corporate Governance Code to include a new requirement for companies to adopt, on the Code's 'comply or explain' basis, one of three mechanisms for strengthening employee voice in the boardroom: (i) a designated existing non-executive director, (ii) a formal employee advisory council, or (iii) a director from the workforce (BEIS, 2017).

In advance of these new proposals coming into effect in January 2019, ICSA published a poll in October 2018 indicating that the large majority of companies were opposed to the idea of worker directors – 70% felt that having workers on their board would not be a good idea, 13% thought that it would be a good idea, and 16% were unsure. Of those who had decided on a position, the largest proportion favoured the designated NED option. In response, Peter Swabey (ICSA Policy and Research Director) commented: 'While there is an overall feeling that it is crucial that the board hears and takes note of the views of staff and other stakeholders, respondents believe that there are mechanisms other than a seat at the board table that will allow them to do so …. Some companies have a large number of employees across multiple sites and a diverse workforce in terms of skill base and level of technical or professional expertise – and they might have different needs, interests, and priorities'. A Local Authority Pension Fund Forum (LAPFF, 2019) report confirmed this picture, based on a survey of around 20% of the FTSE 100 and 10% of the FTSE 350. Of those that had decided how to comply with the revised Code requirements, 73% said they would appoint a designated NED, 27% had opted to convene a workforce advisory panel, and only 5% said they would appoint a director from the workforce. The most common reason given for rejecting a worker director was the size of the workforce – some companies said their workforces were too small, whilst larger companies questioned how one person could represent a global workforce. Other objections included the potential for conflicts of interest, distraction, and delayed decision-making.

There has been a widespread critique of corporate responses to the revised Code, with the sense that companies are being too cautious and resisting change. The NED route is seen as the weaker option, and some critics have suggested that, far from embedding effective worker voice at board level, this can amount to little more than a PR exercise. NEDs are part-time, tend to hold multiple appointments, and may spend only one or two days a month on corporate matters. They are not elected by employees and do not receive any mandate from employees (Rees, 2019). Responding to the LAPFF survey, the acting chair Cllr Paul Doughty said: 'Companies are overwhelmingly taking the safe option of giving responsibility to a non-executive director … [which] shows a disappointing lack of innovation and imagination'. Some press commentary has also been scathing. The Independent commented that Theresa May's 'world leading package of corporate reforms' had failed employees and resulted only in 'world leading excuse making' on the part of Britain's biggest companies. Similarly, The Guardian concluded that 'Theresa May's idea was squashed in stages by the corporate lobby, to be replaced by a limp government proposal to give one existing non-executive director the additional role of looking out for workers' interests. The revised formulation is so loose as to be meaningless' (Pratley, 2018). One year on, the FRC is also disappointed with corporate responses to the new options, stating in its annual review of the Code that 'it is not clear from this year's reporting how much thought was given to the effectiveness of the method chosen. There was little analysis of whether the likely method for engagement was the best one for the company to ensure that boards were made aware of key issues raised by the workforce. It was also unclear whether the board were able to feed back their views and decisions once made' (FRC, 2020: 11).

There is some evidence of more progressive thinking in response to the revised Code, with a number of firms appointing worker directors – including Capita, Mears Group, and TUI. Capita appointed two employee directors – Lyndsay Browne (a chartered accountant) and Joseph Murphy (a civil engineer) – following an extensive recruitment process. Capita is therefore the first UK PLC to have multiple employee representatives on its main board, and they will act as full, independent directors. However, the overall picture is again of a voluntarist and code-based system delivering a further round of relatively weak and ineffective proposals, which can all too easily be evaded via the 'comply or explain' principle. We would therefore suggest the need for legislation to mandate board-level employee representation, in order to properly embed worker voice in governance structures across British industry.

Alongside the arguments for greater employee voice in governance structures, there is also a strong case for workers to share more fully in company profits, rather than these being delivered mainly to shareholders through dividends. Evidence suggests that companies with a greater level of worker ownership take a more long-term view of the company's future. It is also morally right that workers share in the ownership of the workplace whose prosperity they help to create, and in which they spend so many of their waking hours (NEF, 2020). Various reforms are possible.

At one end of the spectrum are the traditional share options granted by the company, based on a variety of performance targets. However, many recipients of employee share schemes sell their shareholdings as soon as they can, and the schemes tend to be limited to those with greater disposable income (usually directors and senior staff), and so compound income inequality with equity inequality (Hadden et al., 2014). Some of these schemes have also been rightly criticized for providing excessive rewards and encouraging short-termism. For example, the share option scheme at house builders Persimmon provided over £100m to the Chief Executive and £500m in total to senior executives, and company profits were inflated as a result of the government Help to Buy subsidy scheme for first-time home owners, meaning the taxpayer was indirectly contributing to these extraordinary pay-outs (Evans, 2019). That said, in many cases vesting procedures will ensure that share owners cannot sell their shares before a certain period of time, which curtails this sort of opportunistic behaviour (Sengupta et al., 2007), and there is also evidence that employee share ownership lowers employee turnover rates and enhances labour productivity (Sengupta and Yoon, 2018). At the other end of the spectrum are companies like the John Lewis Partnership, which operates as a trust under which profits, after sensible investment, are shared out proportionally among all staff, known as its partners. It has an impressive record in both commercial and human terms. Surpluses are distributed as an annual bonus (normally around 15% of salary) to the partners, in addition to gold-plated pensions and other benefits. In between these positions are various voluntary share option schemes offering workers shares in their companies, or in the case of Employee Ownership Trusts the opportunity to acquire the company as a whole. This latter process, providing benefits to the selling owner and to the acquiring workforce, was established in 2014, and dozens of companies (including, for example, Richer Sounds) have been sold to the workforce since then. Evidence suggests that employee-owned businesses are likely to deliver greater employment growth as well as increased productivity, and are also more resilient during economic downturns.

Although evidence suggests that companies with greater levels of worker ownership are both more stable and more willing to tolerate long payback horizons on investment, this may only apply to a relatively small number of firms. Hence the need also for measures that apply to large listed firms. The 2019 Labour Party manifesto advanced a 'middle way' to bring about profit sharing, proposing that 10% of the shares of a large company should be transferred to an Inclusive Ownership Fund (IOF), for the benefit of the workers. Employees would receive an annual dividend from the trust (similar to the bonus usually received annually by John Lewis workers). What constitutes a 'large company' for this purpose is a subject for discussion, but perhaps a company with a turnover over £50m per annum or a workforce of 500 people. We believe this proposition should apply to large private companies as well as public limited companies. The trustees should be chosen by the workforce, with one trustee entitled to a seat on the board of directors. The shares owned by the trust would be new shares issued annually, and we suggest 2% per annum, so that a 10% maximum is reached over the lifetime of a parliament. A payment of £500 per annum per employee, indexed for inflation to the RPI, could be the limit, with any surplus paid to the Treasury for use as a 'social dividend', i.e. higher government spending that benefits business and society. Although not implemented, the floating of the Inclusive Ownership Fund idea by Labour has been an important straw in the wind, and whilst a number of technical arguments have been put forward against it, the principle that employees should have a stronger ownership stake in businesses is increasingly accepted. Some version of this policy is likely to remain politically attractive, and so is worthy of further development.

6. Ownership and governance structures

As the discussion above indicates, employees sharing in company profits has implications for the ownership structure of businesses, and so we now consider the corporate governance aspects of alternative corporate forms in more detail. We have stressed that the current institutional configuration reflects a series of historical and contemporary choices, hence there is nothing inevitable about the dominance of the standard for-profit public corporation, indeed its continuing existence is conditional upon on-going political endorsement and public legitimacy. PLCs are without doubt powerful engines of growth and contribute to improved living standards, yet their hegemonic position does not mean that this form of ownership is necessarily the most beneficial method through which to provide economic and social well-being. As we have argued, corporations are in effect under little obligation to recognise or fulfil their stewardship or sustainability obligations, and indeed have every incentive to minimise them (Hadden et al., 2014; Talbot, 2020).

There is a wide diversity of possible business ownership and governance structures. Interest in alternative forms (alternative, that is, to profit-driven and shareholder-governed) has been growing, which is hardly surprising given that the standard for-profit public corporation, as currently constituted, is so heavily implicated in the dysfunctionality of contemporary financialized capitalism. Alternative forms of business enterprise – such as social enterprises, mutuals, and cooperatives – suggest ways to develop a more sustainable 'corporate landscape' (Boeger and Villiers, 2018). Cooperatives are by nature organisations with a purpose, and are very often established to achieve a specific social or environmental goal. Cooperative ownership has the ability to increase employment stability and productivity levels, as well as making firms more democratic. However, the growth of cooperatives in the UK has been rather limited, due to an absence of legislation, institutional support, incentive, and promotion. A recent report from the New Economics Foundation recommends a cohesive programme of law and policy, including: improved access to finance, a re-worked government procurement policy, a 'right to own' for employees, a Cooperative Economy Act, and a new, statutory Cooperatives Development Agency (NEF, 2018).

Although the encouragement of these more 'socialised' organisational forms is vitally important, it is nevertheless the case that a significant proportion of society's productive resources remain under the direct or indirect control of large public corporations, whose activities dominate the economic landscape. Moreover, social enterprises may be considered overly restrictive for those looking to achieve a balance between social outcomes and delivering financial growth and returns. In other words, as Hunter (2018: 257) observes, 'they have been regarded by some as being weighted too much to the social and not enough to the business or enterprise'. So, a central focus must again be on reform of the dominant corporate legal form, in order to encourage and incentivise companies to engage in more democratic and sustainable business practices.

In part to address this, in December 2016 the government published its report of the Advisory Panel to the Mission-led Business Review (Cabinet Office, 2016). The review defined mission-led businesses as 'profit-driven businesses that make a powerful commitment to social impact'. As Boerger and Hunter (2018) explain, such businesses are committed to making and distributing profits for their shareholders, to satisfy their need for capital investment, and it is this freedom to distribute profits that distinguishes them from 'social enterprises' in the wider UK policy context (as social enterprises re-invest most of their profits back into their business for a social purpose). But at the same time as being commercially oriented, these businesses are also committed to social impact, and in this respect are categorically different from traditional corporate businesses that are run for shareholder value. So, being 'mission-led' signifies a shift from the supremacy of shareholder interest, and the quarterly measurement of how this is delivered in financial terms, to a more balanced assessment of the impact of a business' activities across its stakeholders, assessed in the medium to long term.

Boeger and Hunter (2018) consider whether the promotion of the mission-led business signals a genuine movement towards more responsible and sustainable business governance, or is simply a 're-booting' of the well-rehearsed business case for CSR (which, as we have noted above, is of limited value). They remain sceptical, as the focus on business with purpose as a 'competitive advantage' is reminiscent of the CSR agenda that has allowed corporations to present themselves as good corporate citizens whilst continuing to focus on shareholder interests to the detriment of other stakeholders. That said, the important factor here that distinguishes mission-led businesses is that they 'have social impact or value hardwired into their constitution and governance model' (ibid: 8). In other words, such a business will explicitly embed a social and environmental mission *into its governing document*, and is then required to *report performance against this* on a regular basis (in contrast to CSR, which represents an entirely voluntary corporate policy). To that extent, the promotion of the mission-led business does 'seem to be pointing to an appetite for more substantive change … [and] has the potential to have a positive societal impact at a scale beyond the reach of solely non-profit distributing organisations' (ibid: 4 & 9).

One example of a mission-led business is the B Corp. The B Corp movement is a global movement which aims to introduce new standards of social and environmental performance and use these to identify businesses which are using 'business as a force for good'. There are now more than 2,500 certified B Corps across more than 50 countries. Notable examples include Innocent Drinks (owned by Coca-Cola), Ben & Jerry's (owned by Unilever), and dairy giant Danone. According to Hunter (2018), 109 UK companies had taken the opportunity to register as B Corps since this became possible in September 2015. Becoming a B Corp requires passing three elements of the B Corp 'test', namely: (i) an impact assessment (which measures the overall impact of a company on its stakeholders); (ii) a legal test (it is a requirement for all B Corps to amend their constitutional documents to enshrine a commitment to the 'triple bottom line', principally through a new objects clause); and (iii) a declaration of interdependence (setting out a commitment to all stakeholders). Importantly, however, a B Corp is *not* a new legal form. Rather, it is a *certification* – an effort to provide an independent assurance that a business has met various criteria. Appropriate comparators are the certification schemes operated by the Fairtrade Foundation or the Forest Stewardship Council, which offer consumers a means of identifying products that meet a certain standard. B Corp certification is therefore regarded as a mark of trust for companies demonstrating high standards of social and environmental performance, but – given the lack of legal underpinning – the weakness remains in 'the theoretical ease with which a company may unpick the credentials that made it a B Corp and revert to a more traditional *modus operandi*' (Hunter, 2018: 258).

In the US, several individual states have now introduced legislation enabling businesses to adopt the legal status of a 'benefit corporation', which has strong similarities with a B Corp, but also key differences. As Hunter (2018: 264) notes: 'the terminology is inevitably confusing, but one way to think about it is that B Corps must eventually meet the same legal standards as benefit corporations (i.e. through the legal test)'. In the US, the benefit corporation is distinguished from a traditional company through: (i) a general public benefit requirement (a benefit corporation must pursue 'a material positive impact on society and the environment, taken as a whole, assessed against a third-party standard'); (ii) a stakeholder-centric business model (whereby the company considers the effects of its actions not only on shareholders but also on employees, the local community, and the environment); (iii) reporting requirements (benefit corporations must produce an annual report detailing how their activities have met their general public benefit requirements, based on an independent third-party standard); and (iv) benefit directors (in some states, benefit corporations must have a benefit director on the board, with stringent conditions attached to their appointment to ensure objectivity and impartiality, who is responsible for overseeing all of the reporting requirements).

These four factors could relatively easily be brought into English law, and a rough analogy can already be seen in the Community Interest Company (CIC). The test for whether a company is a CIC is similar to the first factor listed above, and is found at Section 35(2) of the Companies (Audit, Investigations and Community Enterprise) Act 2004, which rather tautologically states that 'a company satisfies the community interest test if a reasonable person might consider that its activities are being carried on for the benefit of the community'. The main difference between CICs and benefit corporations is that CICs are strictly not-for-profit. Nevertheless, the CIC legislation at Sections 26–63 of the 2004 Act could act as a useful template for a new type of benefit corporation. With particular regard to the third and fourth factors listed above (reporting requirements and benefit directors), Section 27 establishes a Regulator for Community Interest Companies, with powers granted under Sections 41 to 51. The Regulator has powers of investigation (s42), audit (s43), and can bring civil proceedings in the name of, and on behalf of, a CIC (s44). An equivalent regulator could be established with respect to benefit corporations, subject to similar, but more stringent, requirements. An executive arm might have the power to bring proceedings against benefit corporations who fail in their corporate obligations, just as the Insolvency Service does with ordinary corporations. A regulator would, however, need powers to investigate and act prior to the winding up of a benefit corporation. Such a regulator could form a constituent part of a new Business Commission (which we advocate in the following section).

Despite some remaining weaknesses and objections, the steady proliferation of different corporate forms in the UK is encouraging an increasingly critical focus on the purpose of business. Whether it follows the specific nomenclature of the B Corp or the benefit corporation, there is room for a new legal form in the UK to express the principle of a 'mission-led business', or what Boerger and Hunter (2018) prefer to refer to as a 'stakeholder company'. With reformulated directors' duties, rigorous reporting requirements, and a robust and verifiable statement of purpose, such a business would be set apart from the standard for-profit corporation. As Hunter (2018: 261) concludes: 'Over time, one would expect the cumulative effect of decision-making on this basis to have a significant impact on how that business operates'.

7. Regulation and enforcement

The regulation of business activity can occur at different levels and through a range of different mechanisms, from private regulation (voluntary management action), to soft law (code principles, recommendations, guidelines, etc.), through to hard law (government legislation). In recent decades, the 'regulatory space' for corporate governance in the UK has become decentred into a myriad of different regulatory bodies and principles (Vibert, 2014), the operation of which seeks to ensure high levels of autonomy for business and facilitate shareholder value. Whilst concerns with this approach have been consistently expressed, the various government reviews and reform initiatives over this period have left this neo-liberal, semi self-regulatory framework largely unchallenged (Moore and Petrin, 2017; Talbot, 2013). It remains the case that the corporation's focus on maximising shareholder value at the expense of other considerations is in effect only constrained by adherence to codes of practice.

The two essential characteristics of such codes are that they are *voluntary* and that their wording is *ambiguous* (and therefore open to interpretation). The injunction has been to either 'comply' or else 'explain' why you are not complying, but this would only be a strong motivator for behaviour if *non*-compliant explanations were subjected to rigorous analysis and reporting, but this is rarely the case. Explanations can be woefully inadequate, or simply not given at all, without repercussions of any kind (Hadden et al., 2014).The time has therefore come to acknowledge that voluntarism has largely failed, and to shift towards a more coherent and extensive regulatory regime, backed up with clear enforcement mechanisms. What unifies the regulatory changes we have proposed is progressive state policy, as the 'glue' binding reforms together, and so we suggest that a coherent form of 'regulatory overlay' will be required to facilitate this reform agenda. With sufficient political will, it is entirely open to governments to *re*-regulate the corporate governance framework, and UK company law could accommodate a stakeholder-oriented agenda if public policy shifted in that direction (Deakin, 2018).

An historical perspective is useful here. As Ireland (2016, 2018) explains, a period of intensely financialized governance at the end of the 19th century and start of the 20th century was followed by a period of increasingly 'socialised' governance after World War Two – what we might now look back on as the halcyon years of social democracy. With organised labour strong, shareholders dispersed and weakened, and controls on capital movements in place, finance seemed to have been tamed. During this period, proposals for corporate governance reform were therefore muted, as many on the left did not think them necessary. However, as we have explained above, over the past forty years the rights and powers possessed by shareholders have been gradually enhanced – as a consequence of the relaxation of the rules governing the free movement of capital, the rise of global financial markets and new types of financial investment, and the waning power of organised labour. As a result, shareholders 'have been increasingly able to use the residual proprietary rights attached to shares to (re)assert their power in and over the corporation … [both] *directly* in individual companies and *indirectly* on the corporate sector as a whole through financial markets … [and this has] propelled us back to a finance-capital-dominated world' (Ireland, 2018: 29).

Over recent decades we have therefore seen the emergence, as explained above, of an extractive form of capitalism, characterised by a short-termist and financialized form of governance. The point is that it is the *corporate legal form*, as currently constituted, that has made these forms of governance possible. It is therefore in the *reform* of the corporate legal form where the possibility lies of a (re)turn to a more democratic and sustainable capitalism. Once again, there is nothing inevitable about the current institutional configuration. It is a product of political and economic choices, and these choices can be remade. As we have illustrated, financialization and marketization are not inevitable processes, but require a particular political and regulatory framework – 'the marketization of corporate control does not take place in a political vacuum' (Callaghan, 2015: 346). The rights and powers of shareholders and other capital investors are publicly granted and legally defined, meaning that they are also *re*-codable (CommonWealth, 2020; Pistor, 2017).

We have sketched above several potential areas for reform – relating, for example, to the voting rights of investors, directors' duties, executive pay, boardroom diversity, employee representation, and corporate form and purpose. Other areas for reform, which we have not covered in detail, relate to the wider institutional framework, and should also be considered. There have been regulatory deficiencies over decades, with too many weak regulatory bodies, conflicts of interest, and a lack of transparency. The 'big four' accountancy firms (KPMG, Deloitte, PWC, E&Y) have been too dominant. The Takeover Panel has been largely controlled by professional finance associations (e.g. ABI, CBI, UK Finance). Auditors have consistently failed to raise concerns (Carillion being perhaps the most egregious example), and lack sufficient independence and transparency. Lord Tyrie announced on 18th June 2020 that he was stepping down as chair of the Competition and Markets Authority, stating that the role prevented him from pursuing a more aggressive campaign for change. He had only served about two years of a five-year appointment. Taken together, a series of reforms is necessary to establish what Sikka et al. (2019) refer to as a 'new regulatory architecture' for business.

Some of these reforms will only be effective if they are backed with adequate and enforceable sanctions. Take, for example, company directors. Currently there exists no satisfactory enforcement mechanism or sanctions for breach of duty. The duties of a director are only owed to the company and, under Section 170(1) of the Companies Act 2006, only the company can enforce them. This is clearly inadequate, as often there will be a conflict of interest between a director personally and the company. A company board will be very reluctant to launch proceedings against one of its directors or former directors. In certain very limited circumstances a shareholder can launch proceedings for breach of duty. However, as this involves bringing litigation, the procedure is complicated and expensive. Moreover, if a claimant is successful, they are only entitled to damages under civil law. There is thus no criminal liability under the Companies Act 2006 for mis-management of the company in breach of directors' duties. In most cases, if a director acts in good faith, the courts are unlikely to substitute their own judgement for that of the director. There is, however, a big gap in remedies when that is not the case. There is therefore a strong argument for extending a company director's 'duty of care' to reach beyond shareholders to benefit *all* stakeholders.

Directors can already be held criminally liable under other Acts of Parliament – for example the Insolvency Act 1986, the Theft Act 1968 (for theft and fraud), the Bribery Act 2010 (for failure to prevent corporate corruption), the Financial Services and Markets Act 2000 (for market abuse) –

and also laws relating to health and safety, anti-trust, environmental protection, and data protection. Further, directors are liable under the Companies Act 2006 for breach of regulatory filing of documents, and can be disqualified under the Company Directors Disqualification Act 1986, which is a statutory criminal offence. Whilst these statutes deal mainly with the consequences of financial loss, there is no reason why *in extremis* company management in breach of duty to company stakeholders should not be visited with a similar sanction. No one would suggest that issues relating to the conduct of business should be subject to frequent direct legal or judicial intervention, and it is not expected that introducing criminal liability for company mis-management would bring a flood of criminal litigation and expose directors to unnecessary risk, but there are nonetheless legal improvements that can be made (Hockman, 2014). There is scope for the creation of additional criminal offences, not necessarily involving proof of deliberate dishonesty. One example might be the creation of an offence of recklessly managing a company. The real question is whether the threat would act as an effective deterrent against acting in breach of duty.

Accordingly, we suggest that new rights are needed – for the board, for shareholders, and for other stakeholders – and that a new regulator with enforcement powers should be established, to monitor adherence and take action for breach of duty. The new regulator shall perhaps be named the Business Commission, and would oversee standards among both listed and private companies, acting as an independent regulator with investigative powers and legal remedies for non-compliance. The Business Commission should have the power to intervene at the behest of shareholders and stakeholders for mis-management. Similar structures exist, for example, for finance (the Financial Services Authority) and for solicitors (the Solicitors Regulation Authority). Whilst the widening of the duties of directors should apply to all companies, there should be a minimum threshold, either based on number of employees or annual turnover, to exempt SMEs from intervention by the Commission. This is also an access to justice issue, and all of a company's stakeholders should have a protecting authority to deter directors from acting in breach of duty, and also a right to intervene. The intention of these new rules would not be to penalise firms in a punitive way, but rather to encourage responsible business practices, whilst making the deliberate evasion of responsibility a riskier endeavour. Far from stifling business growth, this framework would also provide greater clarity and confidence to investors.

8. Conclusion

As a result of the Covid-19 pandemic, the UK economy has experienced a sudden and deep disruption that will have lasting consequences. Legal and regulatory frameworks will need to adapt in response to rapidly changing expectations. If we wish to 'build back better', then, as the Financial Times put it in a recent impassioned editorial: 'Radical reforms – reversing the prevailing policy direction of the last four decades – will need to be put on the table. Governments will have to accept a more active role in the economy … Beyond the public health war, true leaders will mobilise now to win the peace' (FT, 2020). In this context, the arguments for intervention to encourage business models that are more democratic and sustainable will only grow stronger, and there is a positive role for corporate governance reform in facilitating this.

Currently the role of capital markets and financial intermediaries pressures firms towards short-term and dysfunctional business decisions, reducing the scope for re-investment and re-skilling. The corporate governance framework should therefore be re-configured to support responsible business, facilitate the delivery of long-term and sustainable economic growth, and provide an overarching regulatory framework within which good businesses can thrive. This framework must be welcoming to investors, with shareholders incentivised to act as a force for socialisation rather than as extractive *rentiers*. At the same time, the governance of corporations must reflect the reality of the firm as a political entity consisting of multiple constituencies who share overlapping economic and political claims on its resources, and acknowledge the legitimate interests of all the stakeholders involved in or affected by its operations.

This report has sought to establish some of the options for reform, sketch out those policy areas that will need attention from a progressive Labour government, and offer a narrative and vocabulary for taking these arguments forward. We have focussed on the key actors in corporate governance – shareholders, directors, employees – as well as certain aspects of the broader regulatory architecture for business. Taken together, our proposals are consistent with an increasingly mainstream set of arguments for state-led reform, reflecting current debates concerning the potential of the 'entrepreneurial state' to co-create and co-shape markets (Mazzucato, 2013, 2018), and recognising that 'corporate governance … constitutes a field of contention that allows for political intervention in pursuit of economic and social objectives' (Driver and Thompson, 2018: 2). It is also clear that the decline in bargaining power of workers continues to hold back economic recovery, and was one of the principal causes of the financial crisis, with rising household debt used to compensate for stagnating real wages (Hockman, 2014). A more democratic and sustainable capitalism must therefore also address income inequality, for reasons of both social justice and economic stability (Wilkinson and Pickett, 2010). Rebuilding the workplace institutions that influence the initial distribution of incomes (before the tax and benefits system intervenes) will be an equally important aspect of policy development. We intend to address these issues in a further report focusing on workplace employment relations and employment law reform.

There is a broad recognition across the political spectrum that some transformation of capitalism is desirable. The challenge for the Labour Party is to advance a renewed vision of democratic socialist reform, with an active state working in partnership with businesses, workers, and their trade unions. Since his election as leader in April 2020, Sir Keir Starmer has referred to the 2019 Labour Party manifesto as a 'foundation document' for policy development. It contained many of the kinds of policies suggested in this report (e.g. limits on short-term shareholdings, restrictions on voting in takeovers, one third of board seats for workers, broadening the ownership base of firms, and ending the corporate capture of regulatory institutions). We now need to build on this foundation, in the context of a rapidly changing economic landscape. After a set of timid and toothless interventions from the Conservative government, Labour must progress the agenda on corporate governance reform, as part of a wider vision of a democratic and sustainable economy. Attitudes towards capitalism and the role of business are shifting rapidly. Labour must show itself to be leading and shaping that argument. This begins with the articulation of a principled and pragmatic agenda for change.

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