

**The end of class for corporate governance?
Transparency moments in UK company law reform**

Previously: “Limiting the new regulatory state:
Coalitions and institutions in British corporate governance”

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New work in comparative political economy poses important questions about corporate governance. First, how significant are emergent cross-class policy coalitions between investors and workers (Gourevitch and Shinn 2005)? Second, is it important that center-left governments are leading pro-investor reform (Cioffi and Höpner 2004)? Third, are new kinds of regulatory authority changing the political dynamics of governance (Howard 2004) (Howard 2006)? These related issues each bear on the politics of contemporary capitalism.

I look for answers to the first of these questions in the particulars of British company law reform. Legislation now in Parliament promises regulatory benefits to shareholders and, at the margins, even employees and environmentalists. Although they are hardly earth-shattering changes, they might be expected to produce both conventional class and cross-class coalitions. If there is a meaningful community of interest between employees and investors—or a partisan shift on the center-left building on this coalition—we should see it here.

Compared to the more dramatic changes in the European coordinated markets, Britain’s liberal market economy is relatively under-researched. Developments since the early 1990s pose no great theoretical puzzle to those who would explain policy outcomes: it is a model jurisdiction for minority shareholder rights and finance capital has long been a crucial influence on policy. But Britain is more relevant if we ask not why certain policies or institutions take root, but instead how they affect active and potential social forces. Observing which interests make common cause—and when they do not—is likely to tell us more about the character of politics in particular phases of capitalist history than isolating policy (or institutions) as a dependent variable.

I argue that the notion of a transparency coalition conceived as an alliance of labor and investors is limited relevance in Britain. There was a brief and limited moment of cooperation between workers (as workers) and investors, and it did indeed center on transparency reforms that managers opposed. But this does not constitute a new political economic settlement. First, financial institutions handling future retirees’ savings do so as shareholder-value maximizing investors and not as workers. These fiduciary investors are not newcomers to liberal market governance and they have not changed their character. They have, however, helped lead the shareholder value movement. Conventional employee representatives—trade unions—join certain attacks on managerial autonomy (for example on pay and transparency and on shareholder suits) but they are not enthusiastic about the shareholder value movement as a whole. Antagonisms remain between capital (investors and managers) and workers, even if they are only rarely explicit in the politics of corporate governance.

Second, this ephemeral transparency coalition involves no trade-off for shareholders. Institutional investors supported only minimum concessions to stakeholder groups (including employees and environmentalists) where these were proposed. They support disclosure requirements for companies but not new board structures or to requirements that institutional investors adjust their own practices. While institutional investors organizationally closest to labor (the local authority pension funds) showed more desire to see pro-employee reform, they were influential in neither markets nor Government.

Third, the transparency coalition is crucially divided on how corporate governance should be regulated. Although the regulatory state has expanded remarkably since 1990, investors and managers strongly prefer private authority or market-led best-practice to state authority. Employees and others prefer greater state regulation to achieve their ends. This appears to be a stable division between insiders (institutional investors, managers, and professionals) and outsiders (employees, other stakeholder advocates, and small shareholders).

In the first section below I explain the logic of transparency coalitions and offer preliminary remarks on their viability. I then look for evidence in Parliamentary proceedings and other publicly available material surrounding the Company Law Reform Bill and earlier consultations. Because this process began in 1998 but is only now bearing legislative fruit the paper trail is significant. Subsequently I comment briefly on other recent UK developments. I conclude with a more wide-ranging discussion.

The transparency coalition: “Worker swords into investor plowshares”?

Corporate governance refers to the ways publicly traded companies are directed and controlled. Most scholarship emphasizes its impacts on shareholders, managers, and increasingly also employees.¹ In the Anglo-capitalist legal tradition corporations exist for their shareholders’ benefit, and finance scholarship has fetishized the principal-agent problem arising from the separation of (share) ownership and control. Governance, it follows, is about ensuring that managers are accountable to investors, as well as sustaining accumulation across the economy. Ensuring accountability is difficult, however, because of conflicts of interest, collective action problems, and information asymmetries. Moreover, managerial agents may make common cause with employees to defend their control-rights when threatened by shareholder-initiatives (most commonly in liberal market economies when hostile takeover looms). Company law helps negotiate these problems, as do a host of quasi-legal, private, and market processes. These shape the ways corporate boards work, what shareholders themselves can (and must) do, and transparency arrangements including accountancy and audit.

Inevitably these arrangements are influenced by public policy and by broader economic change. Policy results from the historically contingent interplay of political leadership, interest group activities, and public opinion played out within particular political institutions, economic structures, and ideological frames. In this paper I emphasize interest group coalitions, conceived not as organizational entities or formal agreements but as shared preferences expressed in the legislative process. Although company law may not, as Lord Hodgson recently acknowledged, “set many parliamentary pulses racing,” it is nonetheless a heavily and publicly lobbied issue. Lawyers and accountants join managers and investors of various kinds to do battle over even minor reform. And increasingly over the last decade, employees and environmentalists have

¹ Creditors also have important governance interests, but chiefly when companies near or enter insolvency.

entered governance debates to advance their priorities. At times investors have joined them in calling for increased corporate disclosure.

That managers and employees have occasion to ally against investors is well understood, as is the more prosaic formation of investors and managers pursuing profit and control at the expense of employees' presumptive short-term interests. But recent comparative analysis suggests that employees and investors can make common cause in attacking the interests of managers (and, where they are entrenched, block-holding shareholders). Gourevitch & Shinn give three reasons this 'transparency coalition' might occur, effectively turning "worker swords into investor plowshares." First, workers' retirement savings are invested in stocks, generally held on their behalf by pension funds, mutual funds, and insurance companies.² As their assets grow they become less concerned with wages and job security:

"if the weight of pension entitlements and securities holdings in their total wealth becomes large enough, their preferences can 'tip' and workers increasing align with owners around shareholder values" (210)

Second, employees may come to feel that job security is enhanced by greater transparency, which is also a goal of minority investors. Knowing more about company management and operations will help workers in industrial relations bargaining. And third, excessive managerial compensation provokes resentment in shareholders and workers alike.

Cioffi and Höpner found these alignments in case studies of Germany, France, Italy and the United States. They also emphasize pension fund savings in aligning employees interests with minority shareholders and giving labor new reasons to seek to control management. Moreover, Cioffi and Höpner go further to document the ways center-left parties take up these economic interests and advance them in public policy. In a theoretical coda they identify corporate governance liberalization (in their case countries) as the political expression of emergent financialized (fiduciary) capitalism (Cioffi and Höpner 2004). Adding a temporal 'stages of capitalism' dimension based on changing corporate ownership is a useful step forward for the 'varieties of capitalism' literature.

The end of class for liberal corporate governance? An agenda for research

The transparency coalition/center-left paradox theses bring a great deal to the study of governance policy and outcomes. It seems especially relevant in the coordinated markets where managers and block-holders might find themselves on one side of a divide with minority shareholders and employees allied against them. And clearly in any capitalist economy workers rely on well-governed companies to create jobs and wealth generally. Their structural dependence on capital puts them, at the trivial ontological level Marx identified, in the same boat as investors and the state. The material implications of this are not trivial, of course. Workers often suffer considerably more than properly diversified shareholders when companies fail, or when economies under-perform. Where their representatives are convinced that systemic managerial failings cause poor productivity or competitiveness they join in calls for national level governance reform—even where this means allying with some classes of investors. After the British corporate failures of the early 1990s unions and parties—representing those with and without savings—called for aggressive state intervention to resolve board and accountancy problems. Prior to the Clinton boom unions on both sides of the Atlantic joined the center-left in

² Specifically, if workers rely on these 'fully funded' pensions more than on state-funded pensions—as those lucky enough to have them do in Britain and the US—their views on corporate governance may shift.

calling for change to promote the interests of long-term shareholders at the expense of short-term investors and recalcitrant managers. Organized labor also exploits opportunities to attack management where it confers broader symbolic or political advantage in related battles (and even where it might not). Most recently, employees welcomed shareholders to the fight against excessive managerial pay—although investors are late to the front. On the other hand, whatever the direction of the coordinated economies, American or British workers would hardly agree their job security was enhanced either by governance for shareholder value or by enhanced managerial control.

Gourevitch and Shinn are surely correct, though, that invested retirement savings is the main economic force in liberal market economic governance (as indeed liberal market retirement savings are a growing force in coordinated market economies). This has long been true in Britain, where institutional investors control large amounts of equity. And insofar as individual employees and voters are beneficial holders of equity as part of their retirement savings they have an objective investor interest in corporate governance. But this tells us nothing about whether this interest is perceived, how great it is relative to other interests, and how it translates into policy preferences. Nor does it tell us how these conflicting interests are aggregated in the market and are organized in the polity—and thus how this concentration of wealth might be used.

An agenda for research

Research is needed at several levels of analysis. First, what explains workers' individual "utility functions"? What is the 'tipping point' when the labor aristocrat becomes the weekend investor activist? G&S allude to that moment when the net present value of their pension benefits rivals or exceeds the net present value of their future wage earnings (p 212). Is it not, therefore, strongly related to age as well as labor market experience? More fundamentally, what of the role of ideas in constituting interest, preference, and strategy for this rational worker-saver? Perhaps workers begin to think like shareholders because of a broader shift in society toward shareholder value (their companies, after all, have long been telling them that shareholder value is the whole point of enterprise). And what of suggestions that worker-investors might be persuaded to view their interests differently, for example in the unlikely scenario of trading reduced retirement income for supposed social, humanitarian, or environmental improvements?

Second, how are these divergent interests aggregated in the economy, and to what purpose? This is not a new avenue of inquiry. Activists and some scholars have long asked whether workers' retirement savings might increase their economic influence on corporate behavior *qua* worker. In this view, the rise of fiduciary capitalism might permit "employees to leverage 'labour's capital' to the benefits of workers as a group" (Ghilarducci, Hawley et al. 1997). The organizational distance between worker-investor and fund manager is great, however. It is crucial, as John Plender (and Gourevitch and Shinn) point out, to understand how ownership is structured and managed. Institutional investors and fund managers tied to for-profit financial enterprises face different conflicts of interest than trustees for public (state) retirement funds. There is the matter too of how institutional investors are governed and regulated.

Third, how are these interests organized in the polity? Who speaks for those for whom 'investor' and 'worker' are interests in tension rather than class categories? Will divisions emerge in organized labor, with representatives of workers lucky (or wise) enough to have retirement savings defecting to shareholder value? Or will the institutional investors themselves remain the flag-bearer for future retirees [in that case, is the British National Association of

Pension Funds the vanguard party of pension fund socialism?] And finally, what of employees without retirement savings, or those on the wrong side of the investment ‘tipping point’?

Fourth, around which policies can transparency coalitions gather? What shareholder protections will labor support? For G&S, workers should favor “more rigorous accounting, audit and disclosure standards,” board representation and structures that favors “employees and shareholders” rather than managers and block-holders, and effective shareholder democracy (222). These items will not be relevant in all jurisdictions, of course. And G&S readily acknowledge that on the issue of takeovers shareholders and workers will part company. But we need also to ask whether investors support policies that benefit workers (as workers) against managers. Is there any exchange involved in building this coalition? Gourevitch and Shinn do not speak to this issue. Finally, who else might join the transparency coalition? For example, social and environmental activists may ally with accountants, some investors, and workers against managers.

The polity-level case material summarized below speaks to the third and fourth of these issues.

British corporate governance: background

Gourevitch and Shinn see the UK as an example of ‘managerism’ in which governance outcomes favored managers despite some alignment of owners and workers with savings.³ In fact, Britain’s framework serves investors well, even where management is strong and very well paid.⁴ While company law was historically oriented more toward preventing fraud rather than actively growing shareholder value, non-statutory reforms over the past fifteen years have put Britain at the top of the investor-friendly league.⁵ Institutional investors have been economically strong for decades, although the degree to which they coordinated governance has varied. Equity markets and takeovers are the normal governance mechanisms rather than active monitoring, oversight and intervention.⁶ These institutions are (and were) fiduciaries for worker-savers, but employees and their direct representatives themselves have no role in governance practice or law. Like other stakeholder groups, they did not participate actively in governance politics until the late 1990s—and when they became involved their demands were quickly rejected by investors of all stripes.⁷

A series of company collapses in the early 1990s led to the creation of several high-level City committees to produce a Combined Code of corporate governance. These coordinated

³ In this sense Britain resembles the United States and France.

⁴ Cassis reports that British companies “consistently produced higher profits than their French and German counterparts and they have achieved higher rates of return on their shareholders’ equity” 233 Dividend payments are generally higher as a share of profits than in Germany, for example, and they are more rigid over time than elsewhere. 88 On the other hand, dividend ratios do vary through time. They grew from around 15% in the early 1980s to almost 30% by 1989 UK compound annual returns on equities were above the European average (at 10.0% to Europe’s 8.4%), and the arithmetic mean return (14.7%) was the highest for all European countries except Norway. Table II Reflecting the wide opportunities for success and failure, the standard deviation of the annual return was 33.6%—again the highest outside Norway.

⁵ A widely reported ranking is conducted by the US-based consultancy Davis Global Associates. They rank eight advanced industrial economies on several indicators; Britain is consistently first.

⁶ The question of active investor governance, as well as their role (or not) in the long-term financing competitive business, is a recurring element in UK governance politics.

⁷ A high level commission investigated and debated industrial democracy during the late 1970s, but the Labour Government of the day was not interested in implementing its recommendations for European style codetermination procedures.

change in board and transparency structures that favored investors while forcing recalcitrant managers to reshape their boards and justify their compensation. Although the Codes are widely admired for their consensual and non-prescriptive nature, they were apolitical and not representative of outsider interest groups (like employees or environmentalists). They were thus able to limit the agenda to managerial and investor concerns and better obtain essential reforms.⁸ During this time, trade unions and the Labour opposition called for more aggressive state action against managers. They also demanded that institutional investors take up their governance responsibilities, and do so as shareholder-proprietors rather than as ‘punters’ investing for short term gain. This call was echoed across the political spectrum, although the investors denied there was a problem with short-termism.

During this time that market-based governance for shareholder value was, in fact, intensifying. Activist North American public pension funds targeted badly run companies and were joined in doing so by British public and quasi-public fund managers. Shareholders also targeted unwarranted executive compensation, where the Codes had failed to correct market imperfections. These trends are consistent with Gourevitch and Shinn’s thesis that those managing workers’ savings will cooperate with others to discipline managers

After fifteen years of activity managers are publicly hostile to the governance movement. On the one hand they argue that the Codes have worked and that Britain was well ahead of the United States in this respect. On the other, they report that qualified company directors are avoiding service because of increased work-load, unreasonable responsibilities and the likelihood of litigation. Some go further. Confederation of British Industry head John Sunderland, for example, has launched counter-attacks on the institutions—asking how they are governed and how fund manager pay is determined.

Company law reform is now going forward in this context. It is not, therefore, a response to corporate collapse, failure, or performance, and so does not aggressively target managers or others. Essentially it is a rationalizing effort to which several more controversial and longstanding measures have been added. My emphasis below is on those measures which divide the transparency coalition, and offer evidence of class conflict. In a later section I summarize measures on which labor’s most direct representatives and investors are agreed.

The Company Law Reform Bill

The Government’s long-awaited company law reforms were introduced in the House of Lords on November 1, 2005 and are now in Grand Committee (March 2006). This Bill is the culmination of exhausting consultation beginning with the Company Law Review in 1998. Rationalization is long overdue, and the great bulk of the Bill is uncontroversial. Ministers commended the 885-clause measure to Parliament as simplifying, deregulatory exercise that would save companies up to £250M a year.⁹ At the same time, they said, its “enhancements to corporate governance, shareholder engagement and the modernisation of decision-making” would serve the economy generally.”¹⁰ While the Conservative Opposition broadly support

⁸ They did offer, however, an easy target for future interventions and the politicization that state oversight brings. This is all the more true on executive pay where they must be seen as having failed.

⁹ While lawyers, managers and others looked forward to consolidating legislation, the Bill is, in the end, an addition to the existing, and very confused, Companies Act. Arguably it only complicates the law further.

¹⁰ Introducing the Bill’s Second Reading in the Lords, Lord Sainsbury also remarked that, “In its clear focus on simplification, on the needs of small businesses, which are so important to our economy, and on deregulation, I believe it represents a break with the past.” Lords Hansard, 11 Jan 2006, Col 181

rationalization, they are targeting measures they see as increasing red-tape and/or ‘gold plating’ European Union directives. They have also highlighted ministerial delays and confusion in getting the Bill to the House and in reconciling it with related regulatory and deregulatory initiatives. Both avenues attack –over-regulation and administrative incompetence—are central to the Conservative’s political strategy in Parliament.

As far as which interests the parties speak for, the Government carefully tailored the Bill to offend neither investors nor managers. It includes provisions of some appeal to Labour’s trade union allies, although (to say the least) there is little that would excite the party’s left or serious stakeholder advocates. On the contrary, backbenchers have introduced motions demanding that it be strengthened. Conservatives, as can be seen below, claim to champion business generally, but are particularly vocal in defending managers and the small investor. Liberal Democrats have spoken up against new regulatory burdens and for greater transparency.

The most controversial issues are the new statement of directors duties, the Operating and Financial Review (OFR), beneficial shareholder rights, any possible easing of shareholder suits, the issue of intuitional voting, and auditor liability.¹¹

In the two followings sections I explore new directors’ duties and the OFR since these involve employees’ priorities most directly. Subsequently I give a brief overview of other matters of concern to managers and investors, including most prominently the question of whether investors should be compelled to use their shares.

Directors’ duties

The Bill includes a new statutory statement of company board directors’ duties. The Law Commission (a high-level technical advisory body) had proposed this during the 1990s to resolve uncertainty in the mix of statute and common law that currently governs directors. Accordingly, the Reform Bill codifies existing obligations. Directors must act in ways they think will promote “the success of the company in the interest of its members as a whole,” where members are understood to be shareholders. Despite concern that the phrases ‘success of the company’ and ‘the members as a whole’ are unnecessarily ambiguous, the politically more significant clause follows. Henceforth, in promoting the success of the company, directors must “have regard (so far as reasonably practical)” to the interests of employees, of suppliers, customers, and the impact of the company’s operations on the community and environment.

Although directors have long had an unenforceable, effectively meaningless, duty to have regard to employee interests, this clause is a significant departure for legal observers.¹² There are two fronts in opposition to codification. One claims it is legally unnecessary or unwise to have a global statement of statutory duties of any kind. The second, more relevant to cross-class coalitions, opposes the inclusion of non-shareholder (or non-creditor) interests. I deal with the latter first.

http://www.publications.parliament.uk/pa/ld199900/ldhansrd/pdvn/lds06/text/60111-08.htm#topichd_8

¹¹ The Opposition is also decrying new powers the Bill gives to the Secretary of State to make future company law amendments with limited Parliamentary involvement.

¹² The law firm Linklaters suggested that courts would be forced to second-guess business decisions. They illustrate the possibility this way: “For example, a company wishes to purchase its raw materials from environmentally sustainable sources, but these are more expensive than those that are not from environmentally sustainable sources. Must it pay more, and if so how much more? Ultimately it would be for the courts to decide whether the directors have appropriately fulfilled their duty, but how can they do so without second-guessing the directors’ business judgment?”

Enlightened shareholder value and the stakeholding debate

The new duties are ostensibly the statutory expression of an ‘enlightened shareholder value’ approach to doing business. Ministers make a ‘business case’ for considering the views of employees and other stakeholders—they say this is what successful companies do anyway. But the provision is also a vestige of stakeholding theory, which was introduced into company law debates in 1998, shortly after Labour came to power. The ensuing ‘stakeholding debate’ is easily dismissed as a sterile academic exercise or as a sop to the Trade Unions Congress. But as it played out for directors’ duties and for social reporting it also sheds light on how meaningful might be a ‘transparency coalition.’

The Company Law Review (CLR) was convened in 1998 to make proposals for legal modernization and incidentally charged with evaluating who company law—and therefore also companies themselves—should serve. Labour ministers thus injected the hitherto academic stakeholding debate into the Review’s early deliberations.¹³ Clearly there was meant to be more debate than reform. The Government (and especially Downing Street) was determined not to threaten Labour’s newfound cachet in boardrooms and on trading floors. Thus, neither ministers nor the Review departed from the view that law should facilitate business “so as to maximize wealth and welfare as a whole.” The Review’s Steering Group said it would studiously avoid distributive questions about “how such benefits should be shared or allocated between different participants in the economy, on grounds of fairness, social justice, or any similar criteria.”¹⁴

That said, the Group aired arguments that British governance hampers wealth creation by failing to foster good relations and trust between stakeholders. A more inclusive capitalism, they said, might be a more successful capitalism. Exploring the arguments, they consulted on two stylized reform alternatives: an “enlightened shareholder value approach” and a “pluralist approach.” In the first, shareholder value maximization is the key to general welfare, but reforms might enable or promote inclusive practices. The second approach sees the interests of other stakeholders as “valid in their own right” and admits that they may conflict with investor interests. This radically entails not only decision-making *for* stakeholders, but also decision-making *by* stakeholders. Pluralist corporate governance was, for some, dangerously reminiscent of industrial democracy. Steering Group member John Parkinson later said that posing the pluralist alternative surprised the governance community, but also that it was seen as a ‘straw man’ to be quickly dispatched.¹⁵

¹³ The stakeholding critique was articulated in Will Hutton’s startlingly successful book *The State We’re In*, and its policy implications were carefully detailed by the TUC and academics. At its core was the sense that the legal and theoretical underpinnings of companies were insufficiently embedded in society. First, managers are not obliged to balance shareholders’ interests with those of employees, suppliers and contractors, customers, communities, and even the environment. Second, stakeholding indicted financial markets for inducing managerial myopia and low investment horizons. Appropriate shareholder governance, in this view, is not about improving short term capital and dividend growth but about ensuring that companies are competitive over the long term. This requires investment in research and development, human capital creation, and productivity raising technology. Fears that institutional shareholders held back the patient capital for these outlays were a longstanding complaint 255.

¹⁴ 2.5

¹⁵ Interview with author, Bristol, June 5, 2000. In setting out the case for pluralism the Steering Group relied on Margaret Blair’s ‘firm specific investments’ theory. The present Anglo-American system of governance, argues Blair, does not sufficiently account for—or promote—employees’ investments in their firms. These may expose workers to greater economic risk than that borne by shareholders. The document offers only a one-paragraph summary of the pluralist view followed by four paragraph-long theoretical counter-arguments and four subsequent paragraphs pointing out problems with its implied reforms.

In practice, a pluralist approach would require a statutory directors' power or duty to act in the interest of non-shareholders. This would involve the dramatic change of boards *owing* duties to those stakeholders, not to the company as under existing law. Opponents said this would produce legal chaos if it were enforceable but, like the existing duty to employees, would be meaningless if non-enforceable. By contrast, only minor changes would be necessary if the enlightened shareholder value approach were to be adopted. Furthermore, the enlightened shareholder value approach could be married to enhanced reporting (ie: more socially aware accounting and auditing) which "could avoid the difficulties" inherent in the pluralist alternative. In its consultation document, the CLR Steering Group asked for comments.

The bulk of consultation respondents were implacably hostile to pluralism, or indeed to any addition to directors' duties. Managerial representatives, of course, were unanimous in opposing pluralism. The Confederation of British Industry (CBI) called for a *non-statutory* clarification of duties, including the existing flexibility to have regard to wider social and ethical objectives.¹⁶ Representing senior managers, the Institute of Directors (IoD), said it would accept the Law Commission's proposed legal restatement of duties (though reluctantly, and only because a majority of member-directors said they would welcome it). Reflecting the views of the other groups, the Chamber of Commerce argued that company law was not the proper vehicle for social and environmental policy.

Institutional investors adopted a similar perspective, opposing pluralism and suggesting repeal of the confusing Section 309. The Fund Managers Association (FMA), rather more colorfully than NAPF or ABI, was "deeply skeptical about the efficacy of legislation to make management good." It pointed out that the stakeholding approach would involve a one-off transfer of wealth from shareholders, increasing the cost of capital, and damaging inward investment. FMA added that short termism is not a problem, because shareholders promote proper managerial horizons and focused on future expected income streams rather than immediate gain. Sentiment was also against legal clarification (NAPF, ABI). The voice of individual British investors, the UK Shareholders Association, opposed *both* the enlightened shareholder value approach and pluralism.

Accountants echoed these positions, as did lawyers. The Law Society—the loudest and most sophisticated voice of its profession throughout the Review—reasoned that company law "should not be used to implement social and cultural changes." A declaratory statement of directors' duties, with no legal change, might be useful.

Employees and environmentalists made the case for the pluralist model, or at least for a more substantial enlightened shareholder model. Again echoing Margaret Blair's micro-economic argument for stakeholding, the TUC argued that interests in any reform might best be judged by cost benefit analysis: employees often bear considerably more risk than shareholders or others in modern companies. Thus, directors should be required to have regard to workers and employee representation should be permitted on corporate boards. The employee friendly business group Labour Finance and Industry Group called for clarification of S309 to make it meaningful. Traidcraft deployed the 'license to operate' argument about corporate responsibility: that incorporation confers duties to society as a whole that are neglected in the Anglo-governance model. A joint NGO submission reinforced this argument.¹⁷

¹⁶ Thus, Section 309 of the Companies Act 1985 would be wrapped into the non-statutory clarification and then repealed.

¹⁷ Among the other groups responding favorably were the World Wildlife Fund, Amnesty International's Business Group, CAFOD (a Catholic group), the World Development Movement, and Forum for the Future.

The Steering Group agreed with critics that the pluralist option was a non-starter, and instead proposed an open-ended statement of duties incorporating stakeholder relationships deemed important for wealth creation. Managers seemed resigned to codification, but continued to express concerns about legal ambiguity. The Institute of Directors feared “creeping pluralism.” It warned against any ostensibly exhaustive legal statement of duties, or list of those whom directors might be entitled to consider, and legally ambiguous phrases such as ‘success of company,’ and ‘exercising powers honestly.’ CBI supported a legal statement but also wanted to forestall confusion and ambiguity; essentially it preferred a code-based approach. The new statement of duties was broadly welcomed by the institutional investors. Confirming its *outré* image in the investing community, PIRC called for mandatory consultation of stakeholders or at least full reporting on stakeholder engagement mechanisms.

The Government’s 2002 White Paper accepting the CLR proposal on duties, and its language is included in the legislation. It was in no way radical and was not received as such by the press.¹⁸ Of the major interests, only the Law Society continued to publicly oppose a statutory clarification—but again largely for juridical reasons. TUC and stakeholder activists wanted the statement to go further, and saw the CLR as a missed opportunity.

Parliamentary debate on the final proposal

If anything, resistance to codification has grown since the first White Paper. The Lords Committee debate on directors’ duties saw strengthened managerial objections to codification. Opponents predict increased litigation and fear undermining the principle that courts not interfere with business decision-making.¹⁹ CBI expressed new concern, reportedly at the behest of its larger members, that the wording could distract directors from their appropriate emphasis on the strategic direction and health of the company. One problem was that the wording of the statutory statement of directors’ duties could be interpreted as introducing concepts not currently found in common law. This would increase legal burdens on managers and create confusion in the minds of directors about their proper role.²⁰ The upshot is that workloads for directors would increase because more due-diligence on committee matters would be required from the full board. This would dissuade qualified candidates from taking directorships.

Moreover, CBI is concerned that future Parliamentary action could increase directors’ duties to other stakeholders. Managerial interests at CBI, joined by the Law Society and Conservative legislators objected to this clause. Even the owner of one share could, Lord Freeman feared, sue a director for failing to act reasonably in relation to the community or environment.²¹ While Lord Freeman acknowledged that courts would decide what cases were

¹⁸ 26 Except for including a duty to creditors (which exists anyway in cases of insolvency). Imposing a general duty to creditors would, it was argued, foster excessive managerial caution.

¹⁹ The ambiguity and flexibility of the existing common law articulation of duties served managers well as courts long demonstrated their reluctance to get involved.

²⁰ So, for example, clause 156 of the Bill states that directors must seek “the promotion of the success of the company in the interests of the company as a whole.” Neither “success” nor “the interests of the company as a whole” are understood in the existing common law. In the past directors have been expected to act in the interests of “the company”—interpreted in British law to mean the company shareholders—not “the company as a whole.” See Law Society’s Parliamentary Brief: Company Law Reform Bill, Committee Stage—House of Lords, 30 January 2006, Proposed Amendments and Briefing for Parts 10 & 11” issued 23 January 2005.

²¹ Company Law Reform Bill (HL). Lords Committee stage third day. Lords Hansard, 6 Feb 2006 : Column GC264. The suit would be a ‘derivative suit’ since directors owe their duties to the company. Thus, under the Act shareholders can only sue on behalf of the company.

reasonable, he said that the Bill offered “additional hooks, means and mechanisms for those who disagree with the direction of a company to attack the board of directors.” Conservative peers insisted that the wording be changed from “must have regard to” to “should have regard to.” The former wording would muddy boardroom waters by confusing directors or circumscribing their business judgment: “I am all in favour of spelling out factors to which directors of companies large and small should have regard when they read the legislation, but I draw the line at “must”.”²²

Meanwhile advocates for corporate social responsibility (including former stakeholding advocates) think the new duties’ do not go far enough. An Early Day Motion was introduced in the Commons calling for a strengthening.²³ The motion was signed by 152 Labour MPs, 19 Liberal Democrats, and 13 Conservatives. It was used as a rallying point for the corporate social responsibility umbrella lobby group CORE.²⁴ In the Lords Committee, amendments were tabled by those wanting to move companies towards a ‘pluralist’ view of their constituent parts and publics. Perhaps overestimating the salience of company law reform, Lord Avebury warned that: “there is a big constituency out there that believes that the Government have got it wrong. There are nine million members of the organisations that helped us with this series of amendments. They will not be satisfied with the noble and learned Lord's reply, and we shall return to this on Report.”²⁵ In an indication of how expansive the debate could become, Lord Lea of Crondall proposed an amendment that would prevent directors from using jurisdictional transfer pricing strategies to avoid taxation. He accused the Government of not acknowledging the global mobility of companies, and tied directors’ duties to MNC behavior in developing nations.²⁶

The Operating and Financial Review

The second legacy of the CLR Steering Group’s efforts to promote inclusive management is the Operating and Financial Review (OFR). This was implemented by secondary legislation in 2005, and would require about 1300 companies to produce reports in 2006.²⁷ It promotes the trend toward ‘forward-looking’ reporting, narrative reporting, and accounting for intangibles that was anticipated by the Accounting Standards Board in the early 1990s. For stakeholders, it would increase disclosure on employee, environmental, and social issues. Although causing

²² Lord Freeman, Company Law Reform Bill (HL). Lords Committee stage third day, Lords Hansard 6 Feb 2006 : Column GC274

<http://www.publications.parliament.uk/pa/ld199900/ldhansrd/pdvn/lds06/text/60206-34.htm>

²³ EDM 697, calling for “a duty for directors to identify, consider, act and report on any negative social and environmental impacts caused by a company's activities in the UK or overseas.” Introduced by Sarah McCarthy-Fry and signed by 201 Members.

<http://edmi.parliament.uk/EDMi/EDMDetails.aspx?EDMID=28989&SESSION=875>

²⁴ CORE is the Corporate Responsibility Coalition, set up in 2001, with 130 member groups. Its steering committee includes: Action Aid, Amnesty International UK, Christian Aid, Friends of the Earth, Traidcraft, War on Want and World Wildlife Fund (UK). Their website is at: <http://www.corporate-responsibility.org/>

²⁵ Lords Hansard 6 Feb 2006 : Column GC275

<http://www.publications.parliament.uk/pa/ld199900/ldhansrd/pdvn/lds06/text/60206-35.htm>

²⁶ Lea offered a second amendment to induce directors to meet both the spirit of laws as well as their letter. It would discourage companies from tax avoidance, for example, even where law permitted it. Amendment 155, Lords Hansard, 6 Feb 2006, Col GC251. The amendment was withdrawn. The Government opposed the amendment as unnecessary and as improperly framed.

<http://www.publications.parliament.uk/pa/ld199900/ldhansrd/pdvn/lds06/text/60206-28.htm>

²⁷ The Companies Act 1985 (Operating and Financial Review and Directors' Report etc) Regulations 2005 (S.I. 2005/1011). <http://www.opsi.gov.uk/si/si2005/20051011.htm>

some discomfort to managers, it was consistent with the liberal British tradition of maximizing information to markets, and also, one would assume, with a ‘transparency coalition’ of employees and investors against managers. It was also a politically feasible (because relatively inexpensive to companies) way to give stakeholding advocates a victory. Still, it was controversial in its details which were hashed out in the Company Law Review and subsequent consultations—these are discussed in coming paragraphs. In the end, Chancellor Brown decided to pull back the OFR requirement and it is now in limbo. A rump report is now being integrated into the ‘business report’ foreseen in the European Union’s accounts modernization directive. The entire process is an example of ministerial timidity, administrative farce, and legislative confusion. It has not helped Labour’s reputation for ‘joined-up government.’

Debating the OFR proposal in the CLR

Responses to the early OFR proposals were evenly divided, although capital interests opposed a prescriptive approach. The main objections were contradictory: it was already widely done or expected, it would be too expensive, it would only produce more legalistic ‘boilerplate,’ and its accuracy could not be guaranteed. Managers alternatively complained that reporting requirements tend to be met by ‘boiler plate’ statements—devoid of substance and drawn up by lawyers—or that companies engaging in best practice voluntary disclosure put themselves at a competitive disadvantage. Substantive and detailed requirements that all companies would meet, of course, would meet both objections (although the problem of overseas competition may remain). In its consultation documents the Steering Group (SG) never suggested detailed requirements be set out in law or standard, but it did argue that an equal burden would remove managers’ concerns about discrimination.

The CLR SG did not abandon the OFR, but their final proposal was modest. Content would be specified in part by law and in part by a franchised standards body. Information on stakeholder relationships, corporate governance and the environment would only be included insofar as directors judged them materially relevant. Employees, and environmentalists were supportive but also wanted an audit of the content and directors’ judgment on materiality.²⁸ They also wanted any OFR standards-setting body to be fully representative.

Naturally business (managers, investors, and accountants) was more concerned to keep the focus of the body financial. The Centre for Tomorrow’s Company warned that it not become “a Trojan horse” for special interests. The accounting industry was overwhelmingly supportive of the OFR proposal, and some even encouraged greater use of audit. Investors either supported it in principle or had no strong views (NAPF), although there was concern that some items not be mandatory (ABI). Investors were not decisively supportive of the Report. On the other hand, managers, including the Institute of Personnel, argued it was too prescriptive and were generally opposed. CBI saw no need for this to be statutory, although the IoD welcomed an audit of the OFR if implemented. Lawyers were divided: the Law Society of England opposed, although the Law Society of Scotland agreed with the change.

Considering these responses, the SG stated that it would maintain a “light-touch” statutory requirement, with standards developing the bulk of the OFR content and directors

²⁸ A substantive OFR would have included the following: mandatory social and environmental reporting; a standards setting body including civil society representatives; mandatory audit of environmental and social reports and the judgments made by directors on what should be revealed; mandatory distribution of the reports; and disclosure of directors’ training and experience relevant to their new inclusive duties. Traidcraft initial comments on Modern Company Law for a Competitive Economy: Developing the Framework.

having “ownership” of the report. It maintained its view that the ‘materiality threshold’ should be whether, in the good faith judgment of directors, the information is “material for the understanding of the performance of the business.”²⁹ Non-mandatory guidance would be given by the standards body on inclusion, but not on standards for preparation of the Review. The final proposals retained the materiality threshold and the content requirements, with occasional changes in wording. The environmental provisions were wrapped into the section on community, social, ethical and reputational issues. The SG had commissioned a pilot project conducted by the Industrial Society (headed by Will Hutton of stakeholding fame), but rejected two of its recommendations. The first was that more information be included on directors and corporate governance as a mandatory item. The second was that information on workforce development and training be mandatory.

The White Paper and after

The Government largely accepted the CLR position on OFR, though it stressed the “business case” alongside the stakeholder justification. It was introduced, however, in the context of the terribly uncontroversial 1993 ASB statement which first “provided a framework within which the directors could, if they wished, provide a narrative report” on the factors underlying companies’ performance. Going forward a modified Standards Board would take responsibility. The process used to produce the OFR would be subject to audit, but not the actual contents of the Report.

Although hardly burdensome and widely accepted in CLR responses, the OFR proposal nonetheless attracted further negative comment. One hostile individual respondent colorfully described the OFR as “a back hander from the political elite to the accountancy trade.”³⁰ Indeed, the largest UK accountancy professional body, ICAEW, welcomed the OFR but, naturally, wanted less detailed guidance from the Government. CBI regretted any further meddling with the OFR, pointing out that the standards’ body ASB had for a decade promoted OFRs and that many large companies already produced them. Later, in the Lords Committee stage, Lady Noakes of the Conservative benches introduced an amendment to ensure that directors would not be liable for statements of the kind anticipated by the OFR and its successor report.³¹ Echoing the 100 Group of Directors, the CBI, and the Investment Managers Association, Baroness Noakes asked “[does] the Government intend to encourage transparency and disclosure or to create a new basis for investors disappointed with performance to make claims for compensation?”

Predictably, stakeholding advocates condemned the WP for not going further. They wanted less discretion for directors and more detailed, tighter rules on what should be included. The TUC specifically argued that the OFR, to have teeth, should be linked to the directors’ newly explicit inclusive duties instead of being formally still a report to shareholders. Finally,

²⁹ There was also dispute over who would have to prepare the OFR. The SG initially proposed that the OFR requirement would apply to all public companies, as well as private companies with a turnover of more than £500M. The Stock Exchange wanted a narrower figure. CBI thought this an inappropriate threshold (it opposed the statutory OFR in any case), although IoD thought it should apply to all public companies. In response, the OFR in Strategic Framework introduced a threshold for public companies of turnover exceeding £5M. The Final Report offered something of a compromise. Companies would have to meet two of the following threshold requirements: turnover of more than £50M, or balance sheet total of more than £25M, or more than 250 employees. In the Government’s 2005 iteration, about 1500 quoted companies would have to prepare the OFR.

³⁰ Duncan Alexander, Response number 17 to the White Paper, Chapter 4.

³¹ Amendment 307A Lords Hansard 1 Mar 2006 : Column GC172

<http://www.publications.parliament.uk/pa/ld199900/ldhansrd/pdvn/lds06/text/60301-39.htm>

Linda Perham MP, representing the Parliamentary Group on CSR, argued that the WP threshold of £50M was so high that it would include only those companies responsible for 1/3 of national economic activity.

Browned off: The Chancellor pulls the OFR

The first annual reports were to be prepared for April 2006, and a good deal of preparatory work had been done by companies and their advisors. However, in a November 2005 speech touting his deregulatory principles to the Confederation of British Industry, Chancellor Gordon Brown abandoned the OFR.³² Its repeal seems rather to have astonished the policy community—including officials at the Department of Trade and Industry (responsible for the OFR), at the Accounting Standards Board and Financial Reporting Council (who had written guidance on the OFR), and at the Better Regulation Task Force (responsible for deregulation).³³ Richard Donkin wrote in the Financial Times that “So many noses were pushed out of joint in this single dismissive blow that the sound of cracking bone was almost audible in the auditing and consulting sectors.”³⁴ Lord Razall punned in the House that people were “browned off” by the announcement.³⁵ In the Commons, an Early Day Motion objecting to Brown’s move attracted some interest (63 signatures, although only one from the Conservative MPs—Peter Bottomley).³⁶

Why Brown canceled the OFR is not entirely clear, although it may have been an effort to gain friends at CBI. Most institutional investors, consultants and accountants were dumbfounded by the decision. The Association of British Insurers said it was

“peculiar that a Government anxious to promote shareholder engagement has created expectations of better reporting and communication...only to undercut them at the last minute and without consultation.”³⁷

The Confederation of British Industry and the British Retail Consortium applauded the Chancellor’s decision. CBI head Digby Jones waged an aggressive campaign against red-tape throughout 2005 and was pleased to be taken seriously. But the Institute of Directors (IoD) and other representatives of managers seemed conflicted. Officially IoD welcomed the move.³⁸

³² The statutory instrument is: The Companies Act 1985 (Operating and Financial Review) (Repeal) Regulations 2005 (S.I. 2005/3442). See also the relevant announcement in the Commons by Alun Michael, Minister for Industry and the Regions, Commons Hansard, 15 Dec 2005, Col 176WS

http://www.publications.parliament.uk/pa/cm200506/cmhansrd/cm051215/wmstext/51215m05.htm#subhd_18

³³ As the head of the Better Regulation Task Force told the Financial Times, “The fact that an awful lot of work had gone into the debate about the OFR and a sensible compromise (on the level of regulation) had been hammered out and it's not now going to happen; that's plainly not an optimal process as a number of the accounting and City bodies have pointed out.” “Brown criticised for abolishing operating and financial reviews,” Financial Times (London), 5 December 2005, 3.

³⁴ “For once, bureaucracy that is good for business...” Financial Times (London), 8 December 2005, 9.

³⁵ <http://www.publications.parliament.uk/pa/ld199900/ldhansrd/pdvn/lds06/text/60111-19.htm>

³⁶ EDM 1283 reads, in part, as follows: “That this House agrees with concerns raised by trades unions, city investors, business leaders and charities over moves to abolish the Operating and Financial Review (OFR) without due consultation; further notes the importance of the OFR for greater corporate transparency...”

<http://edmi.parliament.uk/EDMi/EDMDetails.aspx?EDMID=29666&SESSION=875>

³⁷ “Chancellor's U-turn over reviews sparks fury,” The Times (London), 29 November 2005, 40. The vast amount of time and paper expended in responding to Government consultations over the past eight years is particularly irksome to governance policy participants. Some fear that future participation may be discouraged accordingly.

³⁸ “Making the u-turn now, however, is still very welcome. While some companies have already spent a large amount of time, effort and money to enable them to meet the requirements of the OFR, today’s announcement will save many others the bother.” “Bosses Welcome OFR U-Turn,” Institute of Directors Press Release, 28 November 2005.

Later, however, the Institute told members that transparency norms had changed: “Investors' expectations of the scope and quality of narrative reporting are now based on the OFR and RS1 (the reporting standard).”³⁹ This disturbing trend had *The Times* complaining that:

“Brown's attempt to ease the regulatory burden by dropping the burdensome OFR has met with such opposition from big business groups and their army of consultants that there is reason to doubt that much of a constituency for significant deregulation actually exists.”⁴⁰

Indeed, IoD joined the Association of British Insurers in suggesting that OFR be included in the Combined Code and adopted by companies on a ‘prepare or explain’ mode (ie: explain why they are not preparing it).

It is a great irony for the transparency coalition that an institutional investor may actually have prompted Treasury officials to suggest its withdrawal to Brown. This claim was made in a Commons Committee debate and was not denied by the minister responding.⁴¹ Officials were told that Brown could win points with business by canceling it. Other evidence supports this possibility. Trade and Industry Department guidance that was published at same time as the draft OFR regulations was considerably more solicitous of stakeholder concerns than was the legislative language. This was highlighted as a drawback by Hermes—the fund managers investing BT employees’ savings and serving other clients.⁴² Hermes did not want company directors confused about who they should be reporting to—investors.

An enterprising environmental group, Friends of the Earth sued the Chancellor on the grounds that the decision to abolish the OFR was taken without consultation. The Government settled out of court. The situation is further confused by the Accounts Modernisation Directive, which extends forward looking narrative reporting (the business review) to some 36,000 companies that would not have had to comply with the OFR. Only 12-1300 companies were affected by the OFR. The business review requires much less than the OFR and is not designed to be a social/environmental report. But ministers acknowledge their dilemma. As of February 2006 the Government is once again consulting on what should be included in reports of this kind.⁴³ Indications that the new Review might encompass similar topics (if not the audit requirements of the OFR) was seen as a ministerial ‘U-turn’ for which Friends of the Earth claimed responsibility. Perhaps not, but introducing environmental and social reporting into the new review would be an example of precisely the kind of domestic regulatory ‘gold plating’ of EU law against which Chancellor Brown (and CBI) has campaigned.

Evidence from other corporate governance policy initiatives

Investor governance

The treatment of institutional investors themselves is controversial, and is a source of division between employee representatives and fund managers. The center-left have long worried about low levels of institutional investor voting and activism to improve the quality of

³⁹ “Narrative Reporting Following the OFR,” Institute of Directors, December 2005.

⁴⁰ Irwin Seltzer, “Double-pronged attack puts pressure on cartels,” *The Times* (London), 11 January 2006, 51

⁴¹ Eleventh Standing Committee on Delegated Legislation, Debate on Companies Act 1985 (Operating and Financial Review) (Repeal) Regulations 2005, March 17 2006, Column 10

⁴² Response to consultation:

http://www.hermes.co.uk/pdf/corporate_governance/commentary/OFR_response_060804.pdf

⁴³ <http://www.dti.gov.uk/cld/businessreview.htm>

management. Joined to this issue in somewhat contradictory way is the equally long-standing notion that institutional investors should –but don’t—provide patient capital to British business. Finally, advocates for socially responsible and green investment want more information about institutions’ policies. On each of these fronts the institutions’ oppose state mandates. But associational efforts have not fully satisfied the Government, despite the proliferation of codes demanding greater engagement. Trade unions join labor backbenchers in calling for more regulation. Managers, of course, agree that governance not be compulsory.

In 2002 the Government threatened a statutory duty to use shareholder powers where pension scheme would benefit—a move inspired by the SEC’s ‘Avon Letter’ on ERISA pension fund activism. Since then ministers have accepted that a private approach was more suitable. The current Reform Bill gives the Secretary of State a wide ranging reserve power to require that institutional fund managers publicize their votes (applies to unit trusts, pension funds, investment trusts, and collective investment schemes). This can be seen as a further attempt by Labour to induce private sector action without actually deploying state power. Ministers have required that pension funds disclose their policy, if any, on environmental and social issues.

Indirect shareholders/Beneficial shareholder rights

The long organizational chain between worker-saver and the actual share-holder helps to mystify the worker’s interest in corporate governance. Governance and information rights attach to the share-holder not to the worker-saver. Some propose forcing companies to extend these to nominee shareholding beneficiaries, who own some 40% of all shares now and are expected to own more than half in the future.⁴⁴ Beneficiary shareholders are not included in information circulars and are not entitled to attend meetings and vote. The Reform Bill makes it easier for companies to extend information rights voluntarily, but representatives of small shareholders sought amendments to make full enfranchisement compulsory, particularly since electronic communications reduces managerial costs of doing so.⁴⁵ Amendments were offered to this effect by the Conservatives and Liberal Democrats. The Government argued that cost burdens on industry would be prohibitive, and pointed to the United States as an example of an overly prescriptive and costly mandate that financial intermediaries supply beneficial shareholders with information and solicit proxy instructions. Thus, in this case, ministers sided with managers and institutional investors.

Takeovers

One area where employees, in coalition with managers, had managed to win concessions in the American states was in the legal treatment of takeovers. Introduced in reaction to the late 1980s-takeover boom, ‘stakeholder statutes’ allowed managers to block acquisitions in part based on any potential impact on workers. In Britain, these kinds of measures are prohibited.

⁴⁴ Nominees manage the shares of investors who own shares through tax-advantaged Personal Equity Plans and Individual Savings Accounts. The investors are the ‘beneficiaries.’ The Association of Private Client Investment Managers and Stockbrokers estimates that off 10 million individual shareholdings, 80% are held by nominees (as quoted by Lord Hodgson of Astley Abbots, Lords Hansard, 1 Feb 2006 : Column GC158 <http://www.publications.parliament.uk/pa/ld199900/ldhansrd/pdvn/lds06/text/60201-45.htm>)

⁴⁵ The relevant clause of the Bill is 136. Group supporting this amendment were the UK Shareholders Association and the Association of Private Client Investment Managers and Stockbrokers

The franchise Takeover Panel regulates the mechanics of mergers and acquisitions.⁴⁶ The CLR Steering Group said it saw no grounds for using company law to inhibit takeovers. Moreover, aside from TUC and Friends of the Earth there was no support for allowing the Competition Commission to evaluate the social and environmental impacts of takeovers. Even managers were unwilling to see state authority expand in this area. The CLR Steering Group concluded that changes to company law along these lines would be wrong because they would “weaken an important source of managerial accountability.” There was greater support for including information about the effects of takeovers in the OFR—again, an indication that disclosure is the end-point of concessions to workers.

Widening the transparency coalition: the turn to risk

What of other unconventional governance interest groups? The CLR gave stakeholder groups to bring their concerns to corporate governance for the first time. Environmental groups initially had little access to the issues and, while interest in shareholder governance and green reporting had grown, company law remained an obscure area for most. They were mobilized in part by key individual NGO leaders. In addition they were supported in this effort by the accountancy profession, by advocates of ‘best practice’ in the business community, and by providers of social audit products.

These ‘public interest’ groups took advantage of the desire for more information about corporate activities. Most striking was their ability to exploit concern about risk in corporate governance, and to connect it to the systematic reporting of business information. They reframed claims about ecological damage in business terms: the risk of reputational damage, inadvertent regulatory non-compliance, and immediate financial costs of disasters. This resonated with the appearance of the term ‘risk’ as it relates to internal financial controls inside companies—an example is the sudden discovery of uncontrolled trading activities in the case of Barings Bank. And it appealed to service providers (including accountants,⁴⁷ management consultants, and internal auditors⁴⁸) who were seeking new markets. Furthermore, managers are now highly sensitized to the risks they incur through operations exposing them to both environmental law and activists’ challenges to their reputation. A string of high profile ecological and human rights disasters have raised reputational fears, and at the same time increased the likelihood that public interest groups will be taken seriously by firms. What appears to be new is the fact that these risks are included in conventional corporate governance discourse. The OECD, for example, recognizes that shareholders have a right to risk-disclosure. By adopting the rhetoric of risk, environmentalists were able to better push their agenda in government and investor circles.

In short, public interest stakeholders have allied with others who (for different reasons) want companies to produce more information, and with a government that sees this minimum as the acceptable limit of reform..

⁴⁶ The panel ensures fair and equal treatment of shareholders and orderly framework for offers. They are also subject to indirect regulation under Financial Services Act via the Self Regulating Organizations and Regulated Professional Bodies. Finally, takeovers, mergers, and acquisitions are also subject to the competition regime under the Competition Commission and ultimately also the Secretary of State. Public interest considerations are covered by these authorities.

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Discussion

The evidence recounted above suggests that what Gourevitch and Shinn describe as a transparency coalition is a real but unstable and transient phenomenon in Britain. In the following sections I offer tentative lessons for other liberal market economies. I substitute the term ‘transparency moment’ for ‘transparency coalition,’ because the latter implies reciprocity as well as shared mission, if not permanency.

The transparency moment

Employee groups will support increased transparency information, and will join institutional investors (and other shareholders) and accountants in pressing for greater disclosure and improved audit. They may also support new governance rights for shareholders. They want greater transparency because it helps them in collective bargaining and public relations campaigns. They will also do so because it will help prevent fraud and failure and because it helps build shareholder value for employees who have retirement savings. In this sense, and in this policy arena, workers act as investors as well as employees. Environmental groups and other advocates for ‘corporate social responsibility’ will join, in part to gain access to information, in part to permit more aggressive future interventions in corporate governance. They will be welcomed by consultancies (including accountancy firms) that see market potential. All involved will portray increased transparency as a positive sum measure. Managers will resist this ‘stakeholder transparency coalition.’

Reuniting the capitalist coalition

Three factors promote the transparency moment’s decay. First, stakeholder groups (including employees) will push for too much, seeing governance as a new-found way to shield themselves from market forces. Second, institutional investors will resist mandates to use their potential power in corporate governance except when they decide for themselves it is in their interests. Managers also prefer that investors not be compelled to govern companies. And finally, across governance mechanisms, both investors and managers prefer market, private and semi-public authorities because these are relatively insulated from politics and because they have the economic resources to dominate in these arenas. By contrast, stakeholder groups prefer state authority where their political resources may be influential.

Class conflict or labor aristocracy?

The idea that class conflict may no longer be relevant in corporate governance is attractive. Managers, of course, join investors in pretending that conflicts between employees and business are an exaggerated relic of Twentieth Century political economy. Party leaders of all stripes proclaim our common interest in capital accumulation and play down tensions in the work process and the contested distribution of the corporate product. And governance scholars take for granted that efficiency effects of the Anglo-capitalist governance benefits employees more than any alternative system (Davis and Useem 2002).

Others argue that employees are gaining strength through their ownership stake in the economy or through their influence in Government. Based on their observations of the same case reviewed here (although before Brown’s move on OFR), some legal scholars have gone so far as to suggest that a new, stakeholder friendly variant of liberal capitalism is emerging there (Williams and Conley 2005).

Research is badly needed on the distributive outcomes of liberal market governance. But judged by their receptivity to proposed company law measures, there remains ample interest group division that could be called ‘class-conflict’—with labor on one side and investors joining managers on the other. But perhaps the notion of class deployed in this paper fails to take seriously labor market segmentation and the very different financial prospects of employees. More research is needed to establish whether divisions are likely to emerge within the labor movement per se between those who have accumulated wealth (for their pensions) and those who have not. I found no evidence of this divide being consciously articulated in the polity. On the other hand, in the economic sphere the divide is obscured by the institutional arrangements of fund management. The discussion is not, as a result, taking place.

Parties and governance: preliminary comment on the British case

As mentioned earlier, center-left parties are behind recent pro-shareholder governance reforms in France, Italy, and Germany (Cioffe and Höpner 2004).⁴⁹ Across the Channel, New Labour had also assumed neo-liberal tendencies, and was also engaging in governance reform. Unlike the cases detailed by Cioffi and Höpner, events in Britain are not part of a historic shift in party politics or group preferences. Nor were they driven by economic malaise. Instead, they are consistent with the City’s economic and political power. Earlier Labour governments had never challenged shareholder-oriented governance, and they did so on only the mildest terms now. Despite long-standing critiques of British capitalism, leaders had no stomach for drastic stakeholder reform. But like their continental cousins, Labour did see room for modernization, and company law reform was launched as such. It was not expected to be a populist issue and, as company law reform, was not politically controversial.

As the details of the Reform Bill have played out the Conservative opposition defended management—just as Cioffe and Höpner anticipate. Conservative peers offered amendments that would have reduced impositions on directors.⁵⁰ This is certainly consistent too with the professional orientation of many Conservative members of Parliament. But they were not consistently deregulatory from the perspective of managers.⁵¹ They also played to their voters among the private shareholding public (and they were joined by Liberal Democrats in this).

At risk of caricature, then, Labour’s Bill works on behalf of institutional shareholders and acknowledges their stakeholder-friendly base while avoiding the ire of the Confederation of British Industry. Labour is also more comfortable creating new regulatory structures. The Conservatives, by contrast, stand by company directors and the individual shareholder while arguing that less regulation (and more private regulation) will benefit the economy overall.

Conclusion

Clearly the institutional investors that dominate British corporate governance are managing the funds of future retirees—that is, the funds of workers. In this sense workers and investors are identical rather than a coalition. Gourevitch and Shinn remark that the transparency coalition looks very much like an investor coalition. The direct representatives of workers—

⁴⁹ Among the factors pushing the left in this direction, according to Cioffe and Höpner, was economic stagnation, unemployment, and declining competitiveness. Center-leftist governments needed an inexpensive, modernizing agenda that could also be portrayed as (indeed, was) an attack on entrenched managerial interests. Those interests, coincidentally, were strongly identified with the political right.

⁵⁰ For example on conflicts of interest in transactions dealing with the company [Day 4]

⁵¹ See, for example, Amendment 174, Lords Hansard 9 Feb 2006 : Column GC324

organized labor—will join shareholders in attacking managerial prerogatives, but they will not do so consistently or for very long. They are likely to demand more than investors are willing to concede. And on fundamental matters where capital and labor divide, shareholders prefer managerial autonomy. Beyond the transparency moment lies the class politics of corporate governance.

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