ECONOMIC DEMOCRACY: A BRIEF HISTORY AND THE LAWS THAT MAKE IT

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Abstract

How has our economic constitutional order developed, and which laws make our economy democratic? Democracy in politics is familiar and starts with ‘one person, one vote’, but economic democracy is less familiar. In its ideal, it means ‘three stakeholders, one voice’. Workers, investors, and service-users make different contribution types in the economy, so rules to give them voice differ and are still evolving. This paper gives a brief history of how economic democracy developed, the evolving theories, and practices for democratic workplaces, capital, and public enterprise. It then unpacks the laws that make it. First, a board of directors will answer to an enterprise’s stakeholders, not simply appointing itself via so called ‘independent’ directors. Second, workers elect at least one-third or properly one-half of a board of directors, rather than shareholders monopolising all votes, and worker cooperatives are encouraged. Third, all capital fund directors, whether pensions or mutuals, are majority-elected by beneficiaries, and they set the shareholder voting policies, not allowing asset managers or banks to vote on other people’s money in what they deem to be the interests of the ultimate investor. Fourth, in public enterprises, where private competition fails and consumers cannot truly ‘vote with their feet’, service-users hold voting rights for representatives on the board, rather than appointments being monopolised by the state or board incumbents. These norms are spreading, and overcoming evidence-free theories that excuse illegitimate corporate power.

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1. Introduction

How has our 'economic constitutional order' developed,[1] and what laws make our economy democratic? As inequality escalates, the climate is damaged, and extremists attack free elections, we see ever more acutely that economic power shapes political power, just as politics shapes the economy. We all understand democracy in politics: it starts with one person, one vote for a legislature. Ideally an executive carries out the law, interpreted by an autonomous judiciary, scrutinised by a deliberative media and active public. Democracy in the economy is understood less: the votes of workers who invest labour, investors who contribute capital (private, local or state), and consumers or the public that use services or goods. Just as a democratic advocate said in 1916, 'the contrast between our political liberty and our industrial absolutism' is a major source of social conflict.[2] Divisions of stakeholder class still explain a great deal in political party composition across modern democracies, and the concentration of economic power exposes political democracy's limits. 'A democratic constitution, not supported by democratic institutions in detail, but confined to the central government,' wrote John Stuart Mill in 1848, 'not only is not political freedom, but often creates a spirit precisely the reverse.'[3] Democracy in politics, but tyranny in the economy, is fragile. One side or the other will probably give, and we live now in an era of rupture. Yet in the face of rupture, more and more countries have leading progressive political parties who are proposing further measures to democratise the economy, notably a raft of US candidates for president in the 2020 election, a coalition of French presidential candidates, and in 2023 a newly elected government of Spain.[4] With experience and data, we are better equipped to see what works, and what does not. This helps us protect and advance democracy everywhere, in the economy as much as in politics.

Part 2 of this chapter gives a brief history of economic democracy. How did theory and reality develop? Why are economic institutions more democratic in some countries than others? Beatrice and Sidney Webb's *Industrial Democracy*, Karl Kautsky's *Labour Revolution*, Franz Naphtali's *Economic Democracy*, and Robert Dahl's *Preface to Economic Democracy*, with many others, shaped the debates and often development over the 20th century.[5] As these thinkers expressed, codetermination and worker cooperatives, with public ownership of key enterprises, were two bases of 20th century democratic theory. But some of the theory remained limited, and reality went further, not always coherently, in tackling two main questions. First, how should capital and investment be organised, particularly where it traces to workers' savings? Second, where an enterprise's capital is made public, replacing private finance, how should government organise governance? As Albert Einstein posed the dilemma in 1949, how can we 'prevent bureaucracy from becoming all-powerful and overweening? How can the rights of the individual be protected and therewith a democratic counterweight to the power of bureaucracy be assured?'[6]

Part 3 unpacks four prevailing legal features of more democratic economies. First, directors of enterprises answer to core stakeholders (whether workers, private investors, the state, or service-users), through open appointments, not appointing themselves via so called 'independent' directors. Second, workers elect at least one-third or properly one-half of a board of directors, rather than letting shareholders monopolise all voting rights, and worker cooperatives are encouraged. Third, pension and all capital fund trustees are majority-elected by beneficiaries, and these elected persons set the shareholder voting policies, rather than letting asset manager or bank intermediaries vote how they want, using other people's money. Fourth, in public and regulated enterprises, where private competition fails and consumers cannot truly 'vote with their feet', service-users vote for representatives on the board, rather than appointments being monopolised by the state or board incumbents. This focuses on large enterprises, but similar principles apply to small enterprises. Part 4 concludes.

2. A brief history of economic democracy: theory and practice

Before outlining the laws that make an economy democratic, a brief history of theory and practice is useful. The ideals of economic freedom, of liberty and not poverty or tyranny, are as old as recorded time.[7] Yet the movement for democracy in the economy was inseparable from politics, and it mounted from the industrial revolution. As he watched the coal, engines and steam from his Glasgow law lecture halls, Adam Smith wrote in *The Wealth of Nations* that workers were always in an unequal position, because employers had wealth to 'hold out' in any negotiation.[8] Instead, small partnerships like 'the butcher, the baker, and the brewer' were the ideal basis for the economy,[9] and in this vision Smith believed an 'invisible hand' might guide producers to distribute wealth 'as if the Earth were shared in equal portions'.[10] Smith's idealisation of 'co-partnery' echoed the democratic ideals in the 18th century common law of small companies (used for parishes or charities as much as business) based on equal member votes and majority decisions.[11] Smith castigated the 'negligence and profusion' by directors in large joint-stock companies, something inevitable, he thought, when directors managed 'other people's money'.[12] His invectives against the colonial East India Company, the bankrupt South Sea Company and the slaving Royal African Company gave way in certain cases where the state could run enterprise better, namely in banking, insurance, canals, water or public works 'necessary for facilitating Commerce in general', including roads, harbours, the post and defence.[13] As unions and workers were slowly freed from criminal law,[14] early reforming and revolutionary writers, such as Robert Owen,[15] Franz von Baader,[16] Friedrich Engels and Karl Marx,[17] developed their ideas on the themes Smith did, even if they did not give detailed reform proposals. They all grappled with the proper design of (1) workplaces, (2) capital, and (3) public enterprise.

2.1 Workplaces

The legal genesis of workplace democracy lay in the revolutions of 1848. In a brief window, a democratic Parliament at the Paulskirche in Frankfurt was established, and it debated a law for business districts to be chosen by factory committees that were one-third elected by workers. The goal was to limit employers' absolute power, to resolve workplace disputes, and to write regulations for pension or health schemes. Though the plan did not pass, and the Parliament soon failed, one of the law's drafters, Carl Degenkolb, decided to put a similar scheme into practice at his own factory, and with three other owners, until he died in 1862.[18] Even more dramatic in England, pressured by a series of staff protests, the government started an Oxford University Commission in 1852, and a similar one for Cambridge. It was to reverse 'successive interventions by which the government of the University was reduced to a narrow oligarchy', and for the university to again be 'an association of teachers united only by mutual interest'.[19] This resulted in an Oxford University Act 1854 and Cambridge University Act 1856 where academic staff secured the right to elect a majority of each university's governing council.[20]

These examples were small, but reflected John Stuart Mill's views in *Principles of Political Economy*, that there must be a 'necessary control and check over those few' who managed enterprise, by 'members of the association, or merely its hired servants'.[21] The better enterprises would not see 'work-people without a voice', but be an 'association of the labourers themselves on terms of equality, collectively owning the capital with which they carry on their operations, and working under managers elected and removable by themselves.'[22] Then, Mill went further, arguing that anything a corporation could do 'will often be as well, and sometimes better done... by the state', because shareholders often found it hard to remove corporate directors, and the state has 'greater publicity and more active discussion and comment'.[23] But in contrast, the first modern UK company laws were opposed to involvement by workers, or the public in general. Its leading draftsman was Robert Lowe MP, an inveterate opponent of universal suffrage, who thought unions were based on 'grinding tyranny',[24] but believed that limited liability for capital investors in companies was necessary for 'human liberty'.[25]

By the end of the 19th century, as more working people did win the vote in politics, and as unions were freed to organise, controlling establishments made concessions. Some employers experimented with employee share schemes. Though they were at root a risky, undiversified form of truck for workers, in some cases workers were given representation on boards. In 1869 at Henry Briggs, Son and Co the miners were allowed to elect a sole director of the Yorkshire colliery, but this plan ended during a strike over wages in 1875. In 1879 at the US cigar manufacturer, Straiton & Storm, George Storm established an arbitration board with four worker, four employer and a 'neutral' representative for work conditions to be ‘settled upon a fair basis’.[26] In Germany, alongside Otto von Bismarck’s repression of social democracy, the Health Insurance Act 1883 required managers of company health schemes to be two-thirds employee elected, one-third employer.[27] More substantively, after strikes in the gas sector, the South Metropolitan Gas Act 1896 enabled workers to elect up to three directors if they together held over £40,000 in shares.[28] Trying to secure its place as the home for US corporations, the Delaware Constitution 1897 allowed stock to be issued for ‘labor’ as well as money.[29] Perhaps most salient was that the Port of London Authority Act 1908, drafted by David Lloyd George and piloted through Parliament by Winston Churchill, enabled one worker to be elected to the board in consultation with trade unions, without any shares.[30]

Around the catastrophe of WW1, and the creation of the International Labour Organisation, *Industrial Democracy* emerged as a leading social theory.[31] Beatrice and Sidney Webb initially favoured a separation of powers in the economy: consumers should determine ‘what’ is produced, directors or shareholders ‘how’ it is produced, workers and unions settle the ‘terms’ of production by collective agreement, and the ‘State is a partner in every enterprise’.[32] But they soon said they should have ‘put this differently’, given the observed benefit of worker-elected directors in Swiss Rail.[33] Worker-elected directors were ‘most easily accorded’ in industry put into public ownership, they said – they wrote less about direct service-user voice. Post-war, the Webbs called for a socialist commonwealth, and progressive common ownership in the Labour Party constitution, clause IV. Sidney Webb chaired a government report on the coal industry, which recommended that it should be managed by a 21-person board, 10 selected by the union.[34] But this was rejected by a Liberal-Conservative government. Stuck between manager opposition to everything, and union calls for nationalisation, a government proposal for the Railways Act 1921 to require one-third of railway company boards to be worker-elected never materialised.[35]

In the US, in the parallel debate, Louis Brandeis, a soon-to-be Supreme Court judge, was advocating at the Congressional Commission on Industrial Relations that ‘the end for which we must strive is the attainment of rule by the people, and that involves industrial democracy as well as political democracy.’[36] The Wilson administration tested employer/worker joint-arbitration panels under the War Labor Board, but it collapsed when he left office.[37] More lasting, the Massachusetts governor and soon-to-be president, Calvin Coolidge, passed a voluntary law for manufacturing companies to let employees elect ‘one or more of them as members of its board of directors’.[38] This reflected emerging practice from department stores to factories, and was found across other states, sometimes tied to stock ownership, but often not.[39] The law persists in Massachusetts today.

In Germany the shifts were most dramatic. As the Kaiser abdicated, unions bargained a huge new collective agreement with business, agreeing to ‘common resolution of all economic and social questions in German industry and trade’. It was written into the Weimar Constitution 1919 by Hugo Sinzheimer, that workers and employers must be ‘on an equal footing, in the regulation of... the entire field of the economic development of the forces of production.’[40] Legislation implemented this in two ways. First, the Work Council Act 1920 codified the rule that elected work councils had ten specific rights, including the control of dismissals.[41] This built upon both the wartime Auxiliary Services Act 1916 and gains that unions had made in collective bargaining.[42] Second, the 1920 Act and a further implementing Supervisory Council Act 1922 codified the right of workers to be elected to the supervisory board of companies, which in turn appointed management.[43] Businesses did their best to evade the law, and courts to interpret the law out of existence,[44] but the German union movement stayed committed. In 1928, the General German Union Federation (ADGB) approved a programme of *Economic Democracy*, edited by Franz Naphtali, for equal participation for labour in all economic organisations, state and planning councils, companies, and in education.[45] But in the background Hitler and other conservative parties were being bankrolled by big business, including with a million marks for the 1933 election. Hitler promised his ‘Circle of Economic Friends’ to ‘crush the other side completely’, namely social democracy because, as he put it, ‘private enterprise cannot be maintained in the age of democracy’.[46] On seizing power, the Nazis’ first actions were to imprison and murder trade unionists, abolish all worker directors and work councils, and fire judges. Then they nationalised and merged all trade unions, made cartels mandatory, re-privatised banks and industry, enshrined bank control over shareholder votes, and made it nearly impossible for company directors to be removed except by Hitler.[47] In virtually every way, fascism was the dark photo-negative of a democratic economy.

After WW2, trade unions, now freed in occupied Germany, swiftly regrouped to restore work councils and company board seats. Under the Allied Control Council Law No 22, written with the British, American and French governments in April 1946, unions were entitled to collectively bargain for work councils with binding rights in workplace management, and in October 1946 the coal and steel unions bargained for equal representation on their company boards. More widespread plans for worker directors were passed by city and state legislatures, but the Allied occupiers invalidated the measures on the ground that they had to be collectively bargained, or wait till a national law was passed.[48] In the event, the Mining Codetermination Act 1951 codified the collective agreement in that sector. The Work Constitution Act 1952 required one-third board representation, and codified work councils as law for all companies.[49] The rules were extended to prevent evasion through corporate group structures in 1956, and the Codetermination Act 1976 raised the requirement to just under one-half worker-directors on the supervisory board in companies with over 2000 staff.[50] First and foremost codetermination came from collective bargaining. Law codified these patterns, and then it spread worldwide.

For Germany was just one of many countries to create a workplace democracy system. For example, Sweden's Board Representation Act 1987 requires, through collective agreement, two representatives on company boards over 25 staff, and 3 over 1000 staff, and this usually is equal to around one-third or up to half of a unified board.[51] Denmark's Companies Act 2010 requires one-third worker representation on boards with over 35 staff.[52] By 2023 a majority of EU member states, and OECD countries, had laws for board codetermination. Although countries like the UK, Australia, or the US do not yet have general rights, there have been multiple proposals, and laws in specific enterprises. The UK had worker directors in steel, the post, telecoms, and buses, and continues to in universities and on National Health Service hospital boards. The UK came close to a general law in 1977, which even Margaret Thatcher did not initially oppose,[53] but once in power and with her programme of re-privatisation, worker directors were retrenched even though clearly beneficial.[54] Workers on boards were proposed again in 2016 by a soon-to-be Conservative Prime Minister, as they were by the Labour Party. But the government watered its plans down to a comply-or-explain option in the UK Corporate Governance Code 2018.[55] In Australia, the ABC media channel has a staff-elected director, and many universities have staff-elected directors too. In 2019 the Australian Council of Trade Unions called 'on a future Federal Labor Government to implement a policy of installing employees on company and government managed boards.'[56]

Meanwhile, in the US, labor unions organised shareholder resolutions for worker directors in the 1970s, including at United Airlines, AT&T or Anheuser-Busch, but these attempts were rejected. The Nixon administration's Securities and Exchange Commission, in a 'no action' letter, said companies could refuse proposals altogether.[57] The United Auto Workers bargained for a seat on Chrysler's board in 1976, and were rebuffed, but then as Chrysler's finances went into difficulty, a worker director was brought on board.[58] More worker directors were seen at Pan American Airways, and in five companies as negotiated by the United Steel Workers in 1993.[59] There were many more linked to employee share schemes.[60] But since employee shares were undiversified, staff bore an unacceptable risk that no investor should, epitomised when Enron went bankrupt, destroying 62.5% of retirement savings that employees were lured to putting in Enron shares.[61] Before the 2020 presidential election, Senators Tammy Baldwin, Elizabeth Warren, and Bernie Sanders released proposals for employee directors, from one-third worker directors on listed company boards, to 40% of $1 billion company boards, to 45% of $100 million company boards.[62] Codetermination plans were also endorsed by Kamala Harris and Barack Obama, while a 2018 opinion poll showed large majority support among American voters, including Republicans.[63] But although there were no general rules yet for workplace democracy, the countries lagging behind like the US, UK and Australia had been building strong traditions for more democratic capital, to which we now turn.

2.2 Capital

The second shift toward a democratic economy was in capital. Over the mid-20th century the archetype of an individual investor as a shareholder faded, because workers collectively bargained higher pay. Countries such as Germany or France had income-linked state pensions, but in those countries without such schemes (for instance, the UK and US) worker savings built up vast occupational pension funds. Together with life insurance and mutual funds, institutional shareholders came to hold the majority of stock market capital. This led to an even greater 'separation of ownership and control' observed by Gardiner Means in 1931, or Karl Marx in the 1880s, that mirrored the separation of workers from the products of their labour.[64] But who would govern these capital funds, and shareholder votes, especially when it was workers' capital?

In the UK, early naval and military pensions included 'representatives of labour' on local committees to administer funds.[65] The Bournville chocolate factory pension in the 1920s was created with 'trustees representing both sides' of employer and workers.[66] And over the 20th century more and more pensions were collectively bargained with equal employee/worker representation.[67] But this was not always the case. The government-commissioned Goode Report recommended in 1993 that to prevent funds being 'unduly influenced by the wishes and concerns of the employer',[68] there should be member-nominated trustees (beneficiary-elected or union-chosen), and these should be two-thirds in the case of defined contribution funds since beneficiaries bore the risk of investment losses. The Pensions Act 1995 only went part of the way, setting a default rule that pension trusts should have member-nominated trustees,[69] and the Pensions Act 2004 made it mandatory that at least one-third were member-nominated. The Secretary of State could raise this threshold to one-half by order, and remove exceptions (such as in the university pension fund) but it has not done so yet.[70] In Australia from 1987 superannuation boards were required to have 'equal numbers of employer representatives and member representatives'.[71] Yet the problem remained, in Australia like the UK, that where asset management was contracted-out by a pension fund, voting rights on shares were being taken and cast by asset managers.

In the US, university pensions were established in 1921 with staff representation after Andrew Carnegie made a large donation,[72] spurred to philanthropic action by Congress grilling him over his labour record.[73] As unions grew, and pension funds expanded, many unions bargained for sole pension fund control. But this was limited to a maximum of one-half representation in multi-employer plans by the anti-labor Taft-Hartley Act of 1947.[74] In 1952, the AFL-CIO's ten-point bargaining agenda included joint investment boards,[75] but when the Employee Retirement Income Security Act of 1974 passed, there was nothing on democratic fund governance. Instead, there were incentives to outsource investment management. Individual pension vehicles including "401(k)" plans boomed.[76] From this grew an enormous asset management industry surrounding Wall Street. It would have more bargaining power (and could charge higher fees) the smaller the plan, or the person, that they bargained with. There were repeated proposals for democratically accountable funds, for instance in a 1989 Bill to insert a new §403(a)(2) in ERISA, so that for single-employer plans, employee associations would have half the seats on pension plan boards.77 These did not pass, and there was no law to stop the systemic conflict of interest where asset managers could cast votes in the companies whose pensions they managed,[78] even to 'smash and scatter' workplace pensions into risky, costly individual accounts to earn more fees.[79] The Dodd-Frank Act of 2010 showed one model: it banned banks as broker-dealers voting shares on key issues unless they were following client instructions.[80] In 2019, the presidential platform of Bernie Sanders for 'shareholder democracy' included a proposal to 'Ban asset managers voting on other people's money unless they are following instructions', and to guarantee 'the right of every saver to elect representatives who set voting policy in corporations, in multi-employer pensions, single-employer pensions, in 401(k) funds, and every other form'.[81]

The most far-reaching reform so far occurred in Switzerland. In 2013, it prevented its banks (which performed functions equivalent to asset managers) from voting on shares except in accordance with a voting policy that pension funds were required to draw up.[82] In Germany, France, or Italy, essentially the same problem persisted, with banks taking votes on other peoples' shares, including from all kinds of workplace funds. In Germany, bank control over shareholder voting rights was written into law by the Stock Corporation Act 1937, itself modelled on a bank cartel agreement,[83] and this was not scrapped by the post-war 1965 Act.[84] There was a proposal in the Geßler Report 1979 to have elected governance committees controlling the votes on shares in banks, but this did not pass. A related proposal, in Sweden from 1976, was that anti-democratic capital funds could be balanced by requiring a portion of companies' annual profits to be transferred into wage-earner funds, governed by the workforce, which would in turn invest in shares. It did not pass.[85] When Robert Dahl published *A Preface to Economic Democracy* in 1985, he placed particular emphasis on this proposal, on worker cooperatives, and representation for workers on boards, as within the meaning of economic democracy – he did not systematically analyse pension and stock market capital.[86] Dahl was also tepid about public ownership of enterprise. But in the vast majority of countries, and increasingly the US itself,[87] this was a third key to a democratic economy, and the subject of the next part.

2.3 Public enterprise

The third shift toward a democratic economy was in creating public enterprise, and giving people votes in it. Public ownership is very old,[88] and not necessarily a mark of progress if politics itself was not democratic. But even if most democratic countries took education, health, banking, energy, housing, water, transport, communications, and media into public hands, in whole or part, a consensus on bringing services closer to users has only emerged more recently. Building on the Webbs, a member of Germany's post-WW1 'Commission on Socialisation', Karl Kautsky, made the case for service-user voice in *The Labour Revolution*. Writing in 1924, he said that it was better that 'consumers and producers would be brought together in every branch of production' in governing boards to avoid 'always quarrelling and only coming together before the supreme court' – or indeed leading to confrontations in strikes. Kautsky favoured progressive public ownership, and argued local or municipal ownership should be preferred to nationalisation where possible.[89] Like the Webbs, he did not identify what (if any) limit there should be to public ownership, yet service-user voice was plainly apt for it.

Perhaps the oldest example of service-user voice was that under the Harvard Charter of 1650 university alumni would elect the 'Board of Overseers', which in turn could give or withhold consent for the president appointment.[90] Other universities included alumni and student voice, as well as staff. In the UK's National Health Service, from 1974 there was a requirement that local government representatives hold one-third of regional health authority seats,[91] and in 2001 more patient representatives were included, inspired by Spanish hospitals' inclusion of unions, patient representatives and community groups.[92] When Paris Water was taken back into public ownership in 2008, staff and local residents were given votes for its board. Like these, in the 21st century, there were ever more experiments worldwide to 'democratise public models' of ownership, including in energy, transport, and media,[93] and to expand service-user voting rights even in lighthouse corporations, marketplaces, and football clubs.[94]

Many countries are still far from the leading practices of economic democracy, but the sheer number of models to learn from and adopt means the long-run trend is likely to continue. Why are economic institutions more democratic in some countries than others? This brief history suggests three factors are crucial: (1) the conscious drive of organised labour and the public to demand the vote at work, in capital, and in public services, (2) the ability to overcome legal suppression of democratic voice, by courts or executive agencies, and (3) wider understanding that many models of economic democracy work. It is to these models, in law, that we now turn.

3. The laws of economic democracy

If political democracy starts with ‘one person, one vote’, economic democracy is ‘three stakeholders, one voice’. The direction of all economic enterprise depends on inputs from workers, investors, and service-users. Often these people are the same, but because the types of input differ – labour, capital, or prices and tax – the law made different rules. In developed democratic systems we see a dominant trend that (1) an enterprise’s directors are accountable to these stakeholders, not themselves, (2) workers have votes for at least one-third, or properly at least one-half of a board of directors, not letting shareholders or the state monopolise governance, (3) capital fund managers are elected by and answerable to the real investors, and shareholding middle-men do not cast other people’s votes as they please, and (4) in public enterprises, where markets fail and consumers cannot ‘vote with their feet’, service-users have votes, not leaving governance just to the state. This section focuses on corporations as the dominant legal form, though similar rules may exist for partnerships or other associations.

3.1 Directors

First, pre-eminent legal theory holds that directors of enterprises should be voted in and out by stakeholders, and not answerable solely to themselves. The worst of all possible economic systems, even worse than ‘shareholder primacy’, would be as Berle and Means wrote in 1932 ‘leaving a set of uncurbed powers in the hands of control’ by directors, so that factually – whatever professions of stewardship – these ‘men in control of a corporation can operate it in their own interests’.[95] Whoever the stakeholders with votes are, there is a prior imperative that in a democratic economy those in charge are accountable through the vote, and duties in court.

The rival view is that most or all directors should be ‘independent’ from any stakeholder. This view solidified during the 1970s in its modern form,[96] in opposition to demands for greater corporate social responsibility to workers, consumers, the environment and the public.[97] The US Business Roundtable’s response was to argue that the law should ‘assure a strong, independent, working board of directors’, with its nominating committee ‘composed in its majority of non-management directors’.[98] But all of these people would be chosen by the incumbent board. Thus, so called ‘independent’ directors were among the most *dependent* group of people possible. They owed their jobs to the directors they were meant to monitor, unbound to any stakeholder. They were appointed from a closed circle, often even without interviews.[99] This sham ‘independence’ became the standard in the New York Stock Exchange Listing Rules,[100] the UK Corporate Governance Code,[101] and many others like it. But as soon-to-be UK Prime Minister Theresa May let slip in 2016, in practice those independent 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.'[102]

The push-back against directors appointing themselves is seen in two main ways. First, there exists the all-important right of the general meeting (whether composed of investors, workers, or other stakeholders and company members) to remove directors. After the Wall Street crash, the erosion of simple removal of directors by a majority of company members, was identified as a key cause of director accountability being weakened.[103] The common law had long seen it 'necessary to the good order and government of corporate bodies' that a majority of company members could remove a board.[104] Since 1947 in the UK, there has been a mandatory right of a general meeting to remove any director by simple majority, after 28 days' notice and a fair hearing. The same rule holds in Canada but with 21 days' notice,[105] and in Australia with two months.[106] Other countries can have lower standards. For instance, in Delaware, where most major US corporations are based, there is the option of having by-laws that only allow directors to be removed 'for cause'.[107] Further, many companies entrench directors so that they cannot be removed at all by creating multiple-voting or non-voting shares (notably Meta, Alphabet and Alibaba). But this practice is banned or severely curtailed in most democratic jurisdictions.[108]

The second push-back to directors appointing themselves is in laws securing positive appointment rights. In the private sector, there is a varied picture. In Canada and India, the general meeting appoints the board by default.[109] Alternatively, the law may say, as it does in Germany, that shareholders appoint one group of board members, and employees appoint another group.[110] In the public sector, appointments are commonly made by a Secretary of State, but the law may empower appointments by staff, service users, as well as public officials, as at the University of Toronto (below, part 3(4)). In the UK or Australia, little is said about appointment procedures in companies with shareholders, so directors invariably fill the void with their own self-appointing nomination committees.[111] In the US, after the global banking crash of 2007-8, the Dodd-Frank Act of 2010 ultimately led to a new SEC Rule 14a-8 that companies may adopt by-laws for shareholders to propose director appointments. With institutional investor pressure, by 2019, 76% of S&P 500 companies shifted to give shareholders positive appointment rights.[112] Not all countries live up to the ideals, but the worst system of all is directors answering to themselves.

3.2 Labour and workers

Second, workers should elect at least one-third, or properly one-half of a board of directors, rather than allowing shareholders or the state monopolise voting rights. This is based on the view that labor 'is prior to and independent of capital. Capital is only the fruit of labor', as President Lincoln said in 1861. 'Labor is the superior of capital, and deserves much the higher consideration'.[113] Labour is the heart of enterprise. So 'the attainment of rule by the people' involves 'industrial democracy as well as political democracy'.[114] This means workers are at least 'on an equal footing, in the regulation of salaries and working conditions, as well as in the entire field of... economic development'.[115] Investors of capital often have a legitimate right to vote. Service-users do if they cannot 'vote with their feet'. Labour's vote is *always* paramount for good governance, and economic democracy.

The rival view is that while workers may be informed and consulted about governance, they have no right to participate.[116] It is said workers on boards would drive the economy into the abyss of Marshall Tito's Yugoslavia,[117] that workers' investments of labour are inferior to investments in share capital because only share capital (being paid last in insolvency) bears systemic risk,[118] and that workers' votes for company boards are (as CEO Michael Bloomberg asserted in 2020) like 'communism'.[119] The answers to these assertions are well-established. Far from economic Balkanisation, countries with higher shares of workers on boards tend to be more prosperous.[120] Workers bear an undiversifiable job risk that is far weightier than any risk to a diversified share portfolio. Moreover, institutional shareholders – the asset managers and banks that control most voting rights today – bear no risk whatsoever because they are holding other people's money.[121] Their legitimacy is a myth. In communist regimes, like in all authoritarian regimes, workplace democracy and free trade unions were crushed.[122] Democratic workplaces are the conscience of a free society.

The right to participate at work, and 'take part in the determination and improvement of the working conditions and working environment', beyond information and consultation, is found in the European Social Charter, and is increasingly seen as a human right worldwide.[123] It is in constitutions and corporate laws. A majority of EU and OECD countries have some form of codetermination law.[124] Brazil has a constitutional requirement for worker representation in companies with over 200 staff, but not yet an implementing law.[125] India has a constitutional right for worker participation in management, but not yet a law.[126] Even in China there is a right for one-third of supervisory boards to be elected by workers, though unions are not free.[127] In democratic countries, the standard model is at least one-third to one-half employee or union elected directors. Sweden requires around one-third of a board of directors to be elected by its staff or the union in companies with over 25 employees.[128] Germany requires that in companies with over 2000 staff, the supervisory board, which elects the management board, must have just under one-half employee-elected directors.[129] Even in countries such as the UK, Canada or the US without a general law, many of the most successful corporations have codetermination. For example, the University of Cambridge has 16 out of its 25-person Council elected by academic staff.[130] NHS hospital trust boards have staff representation by law.[131] In the US, elected Academic Senates hold important powers,[132] and there are codetermination rights in many states such as at Cornell University where staff elect two members to the governing body.[133] Notably in Wikimedia, incorporated under Florida law, the volunteer encyclopedia editors and account-holders may elect one-half of the board of directors through direct and regional constituencies.[134] If the US federal government could legislate, and corporate money did not swamp the democratic process, worker votes would probably be US law now.[135] Laws codify best practice. But in its inception, workers' rights to elect directors came from collective bargaining and action for change.[136]

Thus the second major feature of economic democracy is that at least one-third or properly one-half of an enterprise's governing body is elected by workers. Worker cooperatives, which many countries' laws and tax systems encourage, often involve 100% of a board elected by workers, though many cooperatives fall short of democratic standards. Non-privileged groups of workers may be excluded, such as the John Lewis Partnership and Waitrose excluding sub-contracted cleaning staff,[137] or law firm partnerships excluding the staff who are not yet 'partners'. Worker cooperatives and codetermination systems, where the vote derives from labour, must also be clearly distinguished from employee share schemes where worker votes are tied to capital investment, and often undiversified risk.[138] Investments in capital should always be in a diversified portfolio. That is best achieved by larger shareholding institutions, where the law demands votes too.

3.3 Capital and shareholding institutions

Third, in a democratic economy, capital fund managers are elected by and answerable to the real investors, and shareholder intermediaries are bound by the real investors' voting preferences, not casting other people's votes as they please. Economic democracy literature sometimes skirts around the more opaque details of capital organisation. But at its core, most money in the stock market comes from pension, life insurance, or other mutual funds where workers save for retirement. This money goes through a chain of investment funds before being invested in company shares, or otherwise bonds, commodities or derivatives. So a typical fund chain in the UK, Australia, the US, or other similar jurisdictions looks like this:

Real investor → Pension, insurance, mutual fund → Asset managers, banks → Custodian → Company

e.g. You → USS, Unisuper, TIAA, etc → BlackRock, JP Morgan, etc → CREST, etc → Apple Inc

Countries with good, income-linked state pensions differ, because if the public pension guarantees a high level of social security (e.g. two-thirds of pre-retirement income), people have less need to save in capital funds. So, stock markets tend to be smaller in countries with large state pensions (and with smaller workplace pensions), and larger in countries with worse state pensions (and larger workplace pensions or mutual fund savings).[139] Real investor voice, binding all middle-men, makes capital democratic.

The rival view is that shareholding intermediaries should be 'stewards' and vote on other people's money, based on what *they think* (or say) is in the interests of the real investors. 'Stewardship Codes' have proliferated worldwide since 2010, based on UK and ultimately US rules that asset managers should actively use their votes.[140] An older version of this was a German bank cartel agreement in 1930, where banks agreed with each other to cast votes, after merely consulting share-owners two weeks before a company general meeting.[141] The Aktiengesetz 1937 §114 codified this, founded on the goal that 'democracy of capital will vanish, just as it did in politics'.[142] Post-WW2, three big German banks repeated the cartel policy, to cast other people's votes 'in the shareholders' best interests',[143] and it was again re-codified in the Aktiengesetz 1965 §135. On the last available statistics, German banks still voted around 60% of all German company shares, all other people's money. This is essentially similar to BlackRock, State Street, or Vanguard today, the US 'big-three' who together would control 40% of large company shares by 2039 on current trends.[144] Worldwide, most asset managers are the same. BlackRock stated in 2021 that in their self-appointed 'role as stewards of our clients' investments' they vote 'for those clients who have given us authority, through voting proxies in the best long-term economic interests of our clients.'[145] But this 'authority' comes from take-it-or-leave-it contracts with investors. No real attempt is made to gather investors' views. Their voting policies routinely contradict the ultimate investors' actual preferences. By 2023, BlackRock expanded a 'voting choice' policy for large investors to send voting policies, but this still only covered $2.1 out of $4.5 trillion assets under management, and restricted the choice of vote policies to a 'slate' chosen by BlackRock,[146] while BlackRock set voting policies for the rest. To give just two examples of the gulf between asset managers and real investors, 16 major UK asset managers opposed shareholder resolutions for employee representation on corporate boards every time,[147] even though there is strong majority support for workplace democracy.[148] Major US asset managers oppose even tepid resolutions to curb climate damage,[149] even though the vast majority of real investors support clean energy.[150]

So, the two central features of a democratic economy are that capital fund managers will be voted in or out by the real investors, and any intermediaries are strictly bound to a shareholder voting policy. First, the UK's Pensions Act 2004 required that at least one-third of a pension board is elected by beneficiaries or nominated by a workplace union, and the Secretary of State may raise this to one-half, and remove exceptions.[151] Australian law requires that a superannuation board is one-half employee and employer elected each.[152] In the US, some pre-1947 pension funds have boards wholly appointed by unions. Multi-employer 'Taft-Hartley' plans have boards with equal employer/employee representation.[153] Public pension laws typically require beneficiaries to elect some directors. Federal proposals have been repeatedly made to raise all standards.[154] In mutual funds, or open-ended investment companies, the rule is typically that clients elect all directors of the fund's board.[155] The Canada-based Committee on Workers' Capital organises with elected directors worldwide.

Second, because large funds often delegate to even larger asset managers, there are rules to bind the use of voting rights. In Switzerland, since 2013 banks have been required to follow voting instructions from their clients, while pension and other funds have been required to develop voting policies.[156] In the UK, and all jurisdictions following basic equitable principles, there is a right to compel an asset manager, who is always deemed in law to hold money on trust,[157] 'to compel the trustees to use their voting power in the best interests of the trust estate'.[158] This has not, however, been put to a legal test and the UK asset management industry has been holding out on following voting instructions from major clients.[159] In the US, the Dodd-Frank Act of 2010 required that banks acting as brokers could not vote without instructions on key issues,[160] and it has been proposed that the same principle can be extended to all US funds.[161]

It follows that while capital is often opaque, best practice is to organise all funds in a democratic fashion. Indeed within capital funds, the concentration of power is even greater than the concentration of wealth and income overall.[162] Without positive legal change, there is a real risk that a group of roughly 12 men within the big 3 asset managers have decisive influence over the votes in the global economy.[163] This makes voting control of the real investor, and intermediaries being bound to voting policies, essential. It also points to the importance of creating public enterprise and capital, to which the next section turns.

3.4 Custom and service-users

The fourth field of law in a democratic economy concerns public and regulated enterprise. If competition fails and they cannot 'vote with their feet', service-users need votes for real. Private competitive enterprise is justified when, and only when, it advances the public good or the 'general opulence'.[164] Ideally, as Adam Smith wrote in 1759, working competition will 'make nearly the same distribution' as if the 'earth had been divided into equal portions among all its inhabitants', as if guided by 'an invisible hand'.[165] But we know, and Smith knew, that working competitive enterprise, particularly with corporations, is exceptional.[166] So, prosperous democracies routinely take key enterprises into public ownership, and place them under regulation that sets democratically determined standards of service and access,[167] including in education, health, banking, energy, water, agriculture, housing, transport, communications, marketplaces and security.[168] In these services, we see people less as 'consumers', even if they must pay prices instead of, or as well as, tax. We use the language of students, patients, passengers, bill-payers, viewers or traders – language more akin to citizenship than 'marketship'. Service-users' voice should be 'brought together in every branch of production' with workers, so that governance resolves distributional tensions, rather than let them play out through external economic or legal conflict.[169]

The rival views are that, first, public enterprise is bad and small government is good, or that second, if the public *does* own enterprise, government must monopolise governance. The arguments for 'small government' are usually premised on cries like that of Friedrich von Hayek for 'liberty',[170] which strangely deny that corporate power threatens liberty or can take over states. Markets are a 'spontaneous order', and (supposedly) not set by the state that writes property, contract or corporation laws. In this context, we are told, social justice or injustice is a 'mirage'.[171] Any regulator is likely to be captured, and merely produces rules that enrich regulated corporations.[172] The difficulty is, most countries simply do not accept this evidence-free line of conjecture, and have found that privatisation and deregulation coincides with falling living standards, and worse outcomes for human rights, like in the UK.[173] But second, when there is public enterprise, a dominant model of governance, advanced by Labour minister Herbert Morrison in 1933, was that only experts should be appointed to public company boards, and labour or consumer voting rights would (ostensibly) distract from that.[174] These 'experts' would therefore be appointed by the (apparently) biggest expert of all, the government Minister, who just happened to be someone like Herbert Morrison. This was the pattern of many nationalised industries after World War Two, the unbeloved likes of British Rail or the CEGB, where Einstein's warning of a 'bureaucracy from becoming all-powerful and overweening' all too often seemed to come true.

The rights of service-users to vote proliferated in the late 20th century, even if hesitant and uncodified. Universities empower students, alumni and staff with voting rights in governing bodies. Cambridge requires, on its 25-person Council, that 16 are elected by staff, 3 by students, plus 6 external and management appointees.[175] In France, each university board of management now includes 8 to 16 professors and 4 to 6 students.[176] The University of Toronto Act 1971 section 2 requires roughly one-third of the Governing Council to be chosen by staff, one-third by students and alumni, and one-third by a leading state politician. The UK's National Health Service hospital boards have one member appointed by the local council (representing patients in the area), and one by local universities, plus over three elected by staff.[177] German state laws require that locally owned energy companies represent local councillors or any mayor, as well as up to one-half elected by staff, plus the state investors.[178] Germany's Bundesliga's '50+1 rule' requires football club members to have at least 50% of the votes, plus one, in the club's management, over private capital investors.[179] Paris Water (*Eau de Paris*) is required to have councillors, staff, customers, and city-appointed experts on its board.[180] France.tv requires at least 1 member of its board to be from a recognised consumer association.[181] The Wikimedia foundation requires that one-half of the board is elected by members with a registered account.[182] A final example is that the Covent Garden Market Act 1961 states that the market authority had to consult a management committee elected by traders and suppliers,[183] a norm that could be adapted to Amazon or Meta. Indeed, Facebook gave its users voting control over privacy policy, but abolished it in 2011.[184] When consumers can no longer truly 'vote with their feet', a democratic economy gives its members votes for real.

4. Conclusions

Our economic constitutional order has sophisticated rules for democracy at work, in capital and public services, and yet the principle is simple. If we have one person, one vote in politics, this principle of equality must be applied to all our institutions, including in the economy. The principle of equality is necessarily applied in different ways between politics and the economy, because there is not one unified stakeholder group, but three: workers, investors and the public. Rules of voting necessarily change according to the context, and to recognised that where competition fails and consumers cannot vote with their feet, they must have votes for real. Economic power matters. It can be as benevolent in its improvement of people's lives, or as vicious in driving its victims into penury, as any political act. People's daily experience of authority, and abuse of power, is felt as much, and often more in workplaces and the services people rely upon, than through the core organs of government. Yet government sets the rules for the economy. Government makes governance. So democratic governments must ensure that the basis of its legitimacy, equal voice, is protected throughout society, because that is the best guarantee of justice. Ultimately what makes our economy democratic is the conviction that everyone has equal value, and everyone has the vote.

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