

Mitbestimmung

DAS MAGAZIN DER HANS-BÖCKLER-STIFTUNG • WWW.MAGAZIN-MITBESTIMMUNG.DE

Time for a new blueprint?

Left-wing support for shareholder capitalism?

By John W. Cioffi and Martin Höpner

Published by Magazin Mitbestimmung 08/2005

Hans-Böckler-Stiftung
Magazin Mitbestimmung
Hans-Böckler-Straße 39
D-40476 Düsseldorf
Telefon: 0211-7778-147
E-Mail: redaktion@boeckler.de
www.magazin-mitbestimmung.de

Hans **Böckler**
Stiftung 

Fakten für eine faire Arbeitswelt.

Left-wing support for shareholder capitalism?

In almost all Western industrialised countries, shareholders and supervisory bodies are now being given greater rights. Company takeovers are becoming easier, minority shareholders are receiving greater protection and transparency provisions are being enhanced. Why is it the Social Democratic parties that are championing these pro-shareholder reforms?

By [John W. Cioffi](#) and [Martin Höpner](#)

Dr Cioffi is Assistant Professor at the University of California, Riverside. Dr Höpner received a grant from the Hans Böckler Foundation and is a fellow of the Max-Planck-Institute for Social Research in Cologne.

mh@mpifg.de

■ You don't have to be a Marxist to realise that the various players involved in a company - employees, institutional investors, large-scale shareholders, managers, lending institutions etc - have different objectives. Companies are political arenas for conflicting interests and corporate governance law and government regulators powerfully influence their interaction.

Since the mid-1990s, a wave of reform in company regulation has been under way in the Western industrialised nations. Governments, impelled by technological changes on the stock markets, the growth and international diversification of institutional investors, have been granting greater legal protection to shareholders and increasing the liability of company directors in relation to investors. Examples of this trend are the spread of the 'one share, one vote' principle, reforms in the way accounts are presented, consistent rules governing hostile takeovers, heightened obligations to disclose information to supervisory bodies and shareholders, and reforms to limit the influence of corporate networks and lending institutions. In spite of the ups and downs on

the stock markets, institutional shareholders have seen their position improve over the last decade and a half. Gone is the time when managers could, without hindrance, protect themselves from stock markets, which were, in any case, underdeveloped. In Germany, we are moving away from organised capitalism towards stock market capitalism.

Europe: centre-left parties befriend the stock markets

We should probably expect to find these reforms in the manifestos of conservative and liberal parties. But the left-leaning parties, whose constituency largely consists of those working for employers, would have little to gain from the increasing power of shareholders and stock markets. Or would they?

Let us look at some of these reforms. Just before power in Germany changed hands in 1998, Helmut Kohl's government adopted the 'Law on Company



Regulation and Transparency' (KonTraG Gesetz zur Kontrolle und Transparenz im Unternehmensbereich) which, among other things, prohibited the restriction of voting rights at shareholder meetings, and legalised share option and share buy-back schemes. When the law was debated, it became clear that the social democratic SPD wished to go further than the conservative CDU under Kohl. It wanted to prevent banks from owning shareholdings of more than five per cent of industrial companies' shares, and called for a law to reduce these holdings - a so-called Deconcentration Act - in order to set up a market-oriented form of company regulation.

Once it had gained power, in 2000 the SPD-Green government led by Gerhard Schröder adopted a controversial reform of corporate tax. It abolished the tax on profits from the sale of company shares, making it easier for banks, especially, to sell blocks of shares in industrial companies. Since then, the corporate network that shareholder-activists were trying to combat has indeed been unravelling more quickly. The conservative

CDU/CSU opposed the reform. During the 2002 electoral campaign, Edmund Stoiber, the CDU/CSU's candidate for chancellor, promised to reintroduce the tax on share sales, if elected.

The issue of hostile takeovers divided the parties along similar lines. The CDU was quicker than the SPD in rejecting a relatively liberal version of the European takeover directive, which would have given companies facing a takeover relatively few defensive options. When the government adopted the national 'Securities Acquisition and Takeover Act' (Wertpapierhandels- und Übernahmegesetz - WpÜG) the CDU called for the defensive strategies open to companies facing hostile takeover bids to be extended rather than reduced. For example, to combat a hostile bid, the law allows defensive measures to stay in place for 18 months, provided they have been authorised by a shareholders' meeting; the CDU wanted to extend this to 36 months. In short, the most pro-shareholder and pro-stock market views were held by the SPD. Is Germany a special case? Far from it. In France, pro-shareholder reforms reached a peak under

In front of the Frankfurt Stock Exchange.

Social Democrats as champions of the financial markets?

This article focuses on reforms of financial market regulation in Germany, France, Italy and the USA. It does not cover current developments in Great Britain or Scandinavia.



→ the Socialist government of Lionel Jospin (1997-2002). French party-political attitudes tend to follow a similar pattern to those in Germany, although the picture is not as clear-cut.

In Italy there are particularly clear party-political differences on company regulation. The key Italian law on pro-shareholder reform of company regulation systems dates from 1998 and was adopted by the centre-left government of Massimo D'Alema (1998 - 2001). D'Alema is a member of the PDS, the successor to the Italian Communist Party. The Christian Democrats and Silvio Berlusconi's Forza Italia were against the reform, which was primarily aimed at strengthening the rights of minority shareholders but was also intended to facilitate takeovers.

USA: Pension funds against over-powerful managers

In America, we see that Democrats and Republicans also have differing attitudes towards company regulation. The Sarbanes-Oxley Act of 2002 was the most comprehensive reform in this area since the 1930s. This legal package, a reaction to fraud and mismanagement in companies such as Enron and WorldCom, centralised American company law and extended the supervisory powers of stock market regulators. It enhanced the independence of audit committees and imposed stricter duties on managers, directors and auditors, as well as setting more severe penalties in the case of misdemeanours. The reform was adopted under the Republican Presidency of George W Bush (in power since 2000), but was pushed through Congress by the Democrats with the support of unions and public employee pension funds over the opposition of congressional Republicans and the Bush administration.

In the face of Democrat opposition, Republicans are now attempting to dilute some of the individual Sarbanes-Oxley rules. In addition in California, Governor Schwarzenegger attempted (but failed) to privatise and destroy the pension funds for public sector employees. His main target was the CalPERS fund, which is particularly active in the area of corporate governance issues.

These funds, American conservatives complain, have been carrying out witch-hunts against managers of large companies. Have the company scandals already been forgotten? In February 2005 the California State Treasurer, Phil Angelides, a Democrat who is expected to run for governor against Schwarzenegger wrote in the Los Angeles Times, "the governor and his right-wing ideologues have targeted the pension funds . . . not because the funds have strayed, but because they are leading the fight on behalf of ordinary shareholders to put transparency and accountability back into American capitalism."

It all sounds rather strange: centre-right parties defending German and French 'Rhineland capitalism', Italian 'family capitalism' and American managerialism, while left-wing parties fight for the rights of shareholders and encourage the move towards stock market capitalism. Yet this is more or less what is happening. Admittedly, the differences between right and left parties over corporate governance are not always that great. But wherever parties hold differing views on corporate governance regulation, we come up against the same basic trends. The left championing shareholders and stock markets? At the very least this deserves some explanation.

What, then, is causing left-wing parties to support pro-shareholder reforms? In our view, the attitude of left-wing parties towards corporate governance regulation issues can only be understood if we take account of their concern for employees' rights. It is not, then, simply a matter of center-left parties moving to the right with a view to conquering a new electorate. Rather, the interests of employees and organised labour coincide with those of shareholders in some important ways. These shared interests in preventing the abuse of managerial power have led center-left parties to champion shareholder rights as a way to constrain managers.

Why are the more conservative and right-leaning parties wary of such reforms? The reason is that it is not possible to strengthen the rights of small shareholders without encroaching on the former privileges of management and majority shareholders. The German CDU sees itself as a 'people's party', representing all parts of society and not a particular class. Nevertheless, conservative parties have stronger links with organised busi-

ness interests than left-leaning parties. These links are even stronger when conservative parties have been in power for long periods, either now or in the past.

Italy is the most extreme example. The close, but above all corrupt, links between industry and the center-right Christian Democrats in particular caused the collapse of the Italian political party system in the early 1990s. Berlusconi's Forza Italia is well on its way to adopting the old position of the Italian Christian Democrats. In France, however, the close-knit network of relationships within the upper echelons of French society means that links between political parties and industry are more evenly spread between all the major parties. We suspect that this is why, compared to Italy, there is less of a divergence between party-political attitudes towards pro-shareholder reforms.

Stock market capitalism with employee participation?

There are at least two factors behind the left's attitude. The first relates to the growing importance of shares as a form of investment. An increasing number of employees are also shareholders, which means that shareholder protection is increasingly becoming one aspect of employee-protection. In Italy, unlike Germany, the prospect of joining the Euro triggered a wave of euphoria: the country would finally be able to wave goodbye to the inflationary lira. In order to meet the Maastricht criteria, a reform of public finances was needed and the best means to accomplish this was seen as privatisation. Any left-wing government that wishes to sell shares in state-owned companies to its own electorate must do something to improve shareholder protection. The increasing importance of private pension provision is having the same effect. The more that employees invest their savings in shares - a phenomenon which is, of course, particularly strong in the United States but also exists in Great Britain - the more that pro-employee political groupings concern themselves with protecting minority shareholders against abuses by banks, managers and large-scale shareholders.

Second, the reforms of the last decade and a half have benefited employees not just in their role as investors. It is not in employees' interests to see management given unbridled power, which encourages manipulation and corruption - as the examples of Enron in the USA and Parmalat in Italy show. It is far better to strengthen the hand of shareholders than to allow managers to act without supervision. Furthermore, reforms to strengthen the position of the supervisory bodies may also strengthen employee participation, if employees are involved at this level. When the German law on employee participation was adopted in 1976, many companies reacted by shortening the lists of issues that required approval by supervisory boards, as such boards had employee members. The new shareholder capitalism means that this form of oversight is becoming more important. And any strengthening of the supervisory board represents a strengthening of employee participation.

»The more that employees invest in shares, the more pro-employee political groupings concern themselves with protecting minority shareholders.«

Admittedly, it would be a mistake to be too enthusiastic about these pro-shareholder reforms. Some of the comments on employee participation made in the past by self-declared shareholder champions have been critical. Institutional investors are often not especially conscious of the fact that they are managing employees' money, rather than the funds of wealthy investors. Will the stronger position of shareholders ultimately work against employee participation and the unions? Can stock market capitalism include employee involvement? We are far from knowing the answers to these questions. What we can say is that, since the 1990s, the driving forces behind pro-shareholder reforms in countries as diverse as Germany, France, Italy and the USA have been primarily centre-left parties. Anyone considering centre-right calls for adaptation to globalised financial markets, should bear this in mind. ■