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1. Introduction

This chapter argues that the legal architecture of the company obfuscates the political relationship between shareholder and employees and transforms captured value from employees into a transferable and fungible property form. It sets out this claim within a Marxian analysis of the political economy mapped onto the legal architecture of the company. Following on from this analysis, the chapter also demonstrates that recent initiatives that exhort shareholders to govern the company and to monitor company executives – through for example, the rapidly proliferating Stewardship Codes – attempt to subvert the legal and economic nature of modern shareholders as rentiers, to ill effect.

Capitalism is an economic system in which production, and investment in production, is driven by revenue creation. These revenues are claimed by the owners of capital, while the production which creates profit is undertaken by labour in exchange for wage. This arrangement is the cornerstone of inequality in the political economy. In early capitalism, the relationship between owning capital and claiming surplus was somewhat blurred as most owners of capital also controlled and managed the business. This led early theorist on the nature of capitalism, Adam Smith, to conceptualise capitalist claims as resulting from their entrepreneurial activities. Their claim to surplus was the proper reward for organising production and investing their own money, toil and risk.[1] Later, David Ricardo theorised that surplus was created by workers, who produced more value than was accounted for in their wages. Ricardo, however, took no normative position on this arrangement.[2] In contrast, in his reworking of Ricardo's work, Marx framed the extraction of value from labour by capital in political terms. Marx showed that the operation of the market was not a mere technical arrangement for exchanging goods and services, but the operation of political power and privilege. Capitalism is a *political* economy, and, like other economies, it delivers rewards for the powerful derived from the energy, time and creativity of the (un)powerful. Marx also demonstrated that the claim to surplus

[1] A. Smith, *An Inquiry into the Nature and Causes of the Wealth of Nations (*first published (1776, Penguin 1999) p.134

[2] D. Ricardo, *Principles of Political Economy and Taxation* (first published 1817, 2004 Dover Publications)

arose not from entrepreneurial energy but from mere ownership of capital.[3] He concluded this through a detailed examination of the workings of capitalism, most clearly evidenced in the limited liability company in which revenues are claimed by non-managing shareholders (who do not toil), and whose liability is limited and therefore risk considerably less than the entrepreneur – a step change that led Marx to re-categorise shareholders as *rentiers*.[4]

The systematic capture of value from labour is constitutive of capitalism and dependent upon the economic and political subordination of labour to capital, operationalised in production. Marx in part describes this process in his conceptualisation of the 'circuit of capital', which traces money invested in production to the distribution of profits, and re-investment in production. In this circuit, money becomes capital and q*ua* capital, it claims surplus.

The analysis of the political economy of the company under capitalism holds true for all capitalist jurisdictions. However, for clarity of analysis, this chapter will focus primarily on capital and the law as it is found in the UK. In the UK, capital formation in early capitalism was generally organised under the legal form of a partnership but by the end of the nineteenth century, it was predominantly organised under the company.

One of the ideological successes of the company form is that it obfuscates the relationship of power and exploitation between capital and labour that was more visible in the entrepreneur/partnership model. It renders the circuit of production a technical arrangement between shareholders and directors over the use, ownership and distribution of company capital. Additionally, it allows for the continuation of the owner control rights present in the entrepreneur/partnership model, notwithstanding that the company has a separate legal personality and shareholders' interests are in the revenues created by the company (subject to capital maintenance rules relating to distributions) but not the company itself. The legal architecture of the company thereby normalises labour exploitation and the claims of capital. It enables the full realisation of the relationship between labour and capital under capitalism, in which ownership of capital alone determines the right to claim value from labour. The share exemplifies the *pure form* of exploitation.

The rise of corporate governance as soft law norms, distinct from the law, has not deviated from the principles of law that describe and structure the company, including the claims of capital. Corporate governance, set in numerous regularly revised Codes, emphasises the central role of the corporation

[3] K. Marx, *Capital: A Critical Analysis of Capitalist Production Volume I*, (Foreign Languages Publishing House, Moscow, 1962) p.370

[4] K. Marx *The Economic and Philosophical Manuscripts of 1844* (First published 1844, Progress Publisher, Moscow, 1959)

in delivering returns to shareholders[5] – albeit peppered with varied exhortations to have regard to 'stakeholders', environmental sustainability, long-termism, or whatever the prevailing (and changing) concerns may be. The Codes are concerned with how the board of directors can achieve the central goal of profit making through sound self-management.

However, since the global financial crisis, corporate governance has shifted its concern with management delivery of shareholder value, to the involvement of shareholders in monitoring corporate decision-making. This concern is manifest in numerous initiatives, although this chapter examines only the Stewardship Codes with reference to the UK, the jurisdiction used in this chapter to illustrate the political economy of the company. This shift to shareholder-based governance has entailed both a reaffirmation of shareholder entitlement to control, and a positive expectation that they will exercise that entitlement. This shift, I will argue, misunderstands the nature of modern shareholders, who are by nature rentiers, mere claimants of revenue, and thus uniquely incapable and unwilling to undertake a stewardship role.[6] Furthermore, these initiatives amplify the pressures to deliver shareholder value. As such, this governance undermines the sustainability of the human and natural resources upon which the economy rests.

The argument begins with an analysis of Marx's critique of the capitalist political economy. It then examines the historical organisation of capital under the company form and how the legal architecture of the company which regulates that capital formation, simultaneously legitimises shareholder entitlement and enables shareholders' moral detachment which undermines social responsibility. The chapter shows that the rentier nature of shareholders means recent initiatives to draw shareholders into corporate governance undermines sustainability. The chapter considers the argument that shareholders are a heterogeneous group, and that some promote socially and environmentally responsible corporate activity.

2. Capitalism, Commodities and the Circuit of Capital

[5] B. Sjåfjell, 'When the Solution Becomes the Problem: The Triple Failure of Corporate Governance Codes' in J. J. du Plessis, C. K. Low (eds.), *Corporate Governance Codes for the 21st Century*, (Springer International Publishing, 2017), pp. 23–55

[6] L.Talbot, 'Polanyi's Embeddedness and Shareholder Stewardship: A contextual analysis of current Anglo-American perspectives on Corporate Governance' (2011) 62 *Northern Ireland Legal Quarterly* 451

For Marx, the wealth of the capitalist economy appears as an 'immense collection of commodities' within which both utility and profitability co-exist.[7] He contended that the economy as a whole can be analysed through the lens of the individual commodity, in part because capitalism is centred on the production of commodities and in part because capitalism tends to commodify everything, including relationships between people. As such, the commodity reveals much about the economy *per se*.

The commodity, Marx demonstrated, is identifiable by common characteristics; it contains both a utility for some people (a use value) and is exchangeable for a value that exceeds the cost of the sum of its parts (an exchange value).[8] Without utility, a commodity will be unsaleable, however without an exchange value, a commodity will not be produced regardless of its utility. Under capitalism, it is the exchange value, ultimately profit, which drives production. The socially necessary element of a commodity, its utility, does not motivate its production. Written large into the economy as a whole, innovating and producing to solve a social problem or meet a human need, comes, at best, second to creating a surplus. Thus, in the general ways of things, socially progressive innovations tend to be abandoned, in favour of producing less useful, but more profitable commodities.[9]

To make commodities in (what might be called) the real economy, involves investment in productive capacity comprising of facilities, and material not yet shaped by the skills, imagination and strength of the workforce, followed by the sale of the shaped material as commodities. That process must yield a surplus so that the original investment returns in an expanded form to the original investor, creditors, as well as providing for reinvestment in productive capacity to produce more surplus. Marx calls this process the circuit of capital.

Marx's formulation of this process is this-

M – C … P … C' – M' - M – C … P … C' - M' and so on.[10]

M' surplus divides between the industrial capitalists, creditors, and capital reinvested in the production process.

KEY: M represents money, C represents labour power and the means of production (productive capacity), P represents the production process, C' represents commodities of greater value produced and M' realised surplus value, or profit.

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[7] Marx *Capital I,* chapter 1
[8] Marx ibid
[9] B. Hughes, *The Bleeding Edge* (New Internationalist Books, 2016)
[10] K. Marx, *Capital Vol II* (London: Penguin Classics 1992) p.109

Fig.1

However, the circuit raises the question of how surplus arises after the sale of the commodities at market price, given that the original inputs themselves were purchased at market price. For Marx, this is because the input of labour power produced more value than it receives in wages.[11] The exploitation of labour takes places under the auspices of equivalent exchange, bound by the law of contract. In the wage-labour arrangement the wage is agreed and fixed but the amount of value labour adds to the production process is not fixed. The absence of equivalent exchange in the labour contract defines the capitalist system in all periods of development and in all jurisdictions.

The dominant organisational form which capital takes is historically contingent and regulated by different legal architectures. The dominant legal architecture of early industrial capitalism, found in the UK, was that of the partnership. The legal norms of this unincorporated business form were developed in the courts, and later codified in the Partnership Act 1890. The law defines partners as prima facie equals in respect of managing, owning and extracting profits from the business. They are also equally and personally liable for the debts of the business. The partnership provided all the legal structures necessary in early capitalism to enable distribution of profit, entitlement to manage and allocation of liabilities. It gave the partners control over their business but also more personal responsibility and unlimited liability.

When the formula for the circuit of capital is shown with the legal architecture of the partnership, we can see that partners are involved in all parts of the circuit of capital. They are personally responsible for investment decisions, and any failure to create a surplus. They are bound to the fortunes of the business.

M – C … P …	… C′ – M′
Partners jointly invest in the means to go into production and jointly manage. They jointly own the business.	Partners sell commodities and realise a profit which they claim jointly. They risk loss jointly and have unlimited liability.
Later Codified in Partnership Act 1890	Later Codified in Partnership Act 1890

Fig 2. The circuit of capital within the legal architecture of the partnership.

[11] K. Marx, *Capital: A Critical Analysis of Capitalist Production Volume III*, (Foreign Languages Publishing House, Moscow, 1954) chapter 6

The partnership form also highlights what Marx identified as the central problem for the capitalist in the circuit of capital. By investing money into production, the capitalist loses the freedom to use that investment. Its liquidity is lost and with it comes risk and loss of opportunity. However, money must enter into the production process in order to claim the surplus. The money lent as credit becomes capital upon the borrower's receipt, because at that point it has a greater value than its money value. It is, for example, £1,000,000 plus 3 per cent. However, the money possessed by the owner (in this case, the partner), becomes capital when it is invested in production. Thereon it ceases to hold the attributes of money – that of being liquid and fungible. However, without undergoing this transformation, money has no claim to the surplus produced in production. It must become capital with all its attendant risks and inconveniences.

Marx represents this boundedness in the figure 1 above, by the dots between C…P…C1 stating that 'the dots indicate that the circulation process is interrupted'.[12] The circulation continues when capital returns to its liquid form – money. That occurs, in part, when the commodities are sold and the investor claims the surplus after divesting part to repay or service loans, and to further invest in production. The periods of liquidity are represented by dashes at M – C and C1 – M1. Alternatively, the investor may find a buyer to purchase his interest in the business, in which case the boundedness passes to another investor.

3. Liquidity and the Company Form

The problem of loss of both liquidity and fungibility is overcome in the modern company form. In the modern company, money purchases a commodity, the share, a financial property that is a contingent claim to revenue. Its value is based on the anticipated revenue accruing to that property, given prevailing interest rates. Once a share market is established, it becomes a form of money capital, and nearly as fungible as money itself. This transformation from bounded interest to fungible property occurred gradually throughout the nineteenth century as the company share became legally disentangled from productive business. Until the early part of the nineteenth century, the company share was treated in law as part of the company's equity and thus shareholders were in law co-owners in equity.[13] Their investment was bound to the production process. However, in the 1837 case *Bligh v Brent*[14] the share was described in *obiter* as a claim to the surplus created by the productive assets and not a claim to the assets themselves. The company share ceased to be a

[12] Marx, *Capital Volume II,* p.109
[13] Williston, S. 'History of the law of business corporations before 1800: part II.' (1888) 2 *Harvard Law Review*, 4, 149
[14] *Bligh v Brent* (1837) 2 Y & C 268

portion of the beneficial interest in the company as a whole and became a legal and beneficial interest in the surplus value alone. Legally severed from the company assets it was possible for the share to become a transferable property form with much of money's fluidity.

While legal changes enabled the company share to act as a form of money capital, this potential could not be realised until the market in shares became fully active.[15] The rise of active buyers and sellers of shares in manufacturing companies was evident toward the end of the nineteenth century and precipitated the London Stock Exchange opening rooms entirely devoted to the selling of these shares – some decades after the popularisation of trading in railway shares.[16] The coincidence of legal changes and an active share market meant that, shares as entitlements to surplus value could be sold at any point in the productive cycle, in a market that was legally, culturally and geographically distinct from the markets in which the tangible products of the company were sold.

The modern company became the business form of choice in the late nineteenth century because it enables capital to transcend its boundedness to a particular business and to seek out new profitable areas. It allows capitalists to have no commitment to the long-term development of a business, only its capacity to deliver profits. Company law enables capital to become alienated from the productive entity and thus to limit its exposure to company debts. That capacity is extended with the proliferation of investment intermediaries noted below.

Shareholder separation from the productive entity was complete with the doctrine of separate corporate personality. The absolute nature of this doctrine has enabled shareholders to be protected against the debts of the company, and from liabilities arising from injuries to persons and to the environment caused by corporate activity. The courts' uncompromising approach to the corporate veil, which has resulted in judgments considered both unjust and absurd,[17] derive from the fact that this doctrine reflects the reality of the current organisational form of capital within the legal architecture of the modern company. The circuit of capital continues to operate, but the investment and claims to surplus circulate in a separate sphere than the productive entity which operates in the real economy. The circuit described by Marx is divided, conceptually, legally and

[15] P. Ireland, I. Grigg-Spall and D. Kelly, 'The Conceptual Foundations of Modern Company Law' (1987) 14 *The Journal of Law and Society* 149

[16] R. Michie, *The London Stock Exchange: A History* (Oxford University Press, 1999)

[17] G. Tweedale and L. Flynne, 'Piercing the Corporate Veil: Cape Industries and Multinational Corporate Liability for a Toxic Hazard, 1950–2004' (2007) 8 *Enterprise & Society* 2, 268, AR, Spotorno, 'Piercing the Corporate Veil in the UK: The Never-Ending Mess' (2018) 39 *Business Law Review* 4, 102

practically. This enables, inter alia, companies to externalise risks and losses to the environment and to society generally.

When the circuit of capital is organised under the legal architecture of the company, the owners of the business under the partnership form, become owners of a different property, the share. This is shown in figure 3 below.

M –	C…P... C'	– M'
Money to purchase shares	The productive entity	Profit
Shares may be sold many times during productive cycle. Exchanges on share market Share ownership designates legal right to revenue	Inhabited by directors, managers, workers, suppliers. Real economy.	After paying creditors and reinvesting in the business the surplus returns to shareholders who are protected from loss and risk

Fig 3. The circuit of capital within the legal architecture of the company.

4. Fictitious Capital and the Alienation of Shares

The legal architecture of the company enables two key changes to capital. First, M has a fictitious value based on expectations of profit given the prevailing rate of interest. Second, (and connectedly) shareholders sit outside the productive entity and their self-interest can significantly diverge from those of the entity. These two outcomes are crucial in understanding the nature of shareholding and the social regressive outcome of integrating shareholders into corporate governance as company stewards.

When a business becomes a company the owners become shareholders and the productive entity gains a separate legal personality. This is lecture one for company law undergraduates. But, what also happens under the company form is that the capital doubles. There are productive assets on the one hand and there is the share capital on the other. The share's valuation is at first based on the value of the assets but once incorporated it gains a fictitious value.[18] Share value is no longer a reflection of the value of tangible properties (including intangibles like good will). Instead, share value is based on the expected surplus the property of the company will produce and how much that exceeds the prevailing rate of interest. For example, where the expectation of returns on capital

[18] Marx, *Capital III* chapter 32

invested is 10 per cent and the prevailing rate of interest is 5 per cent, a share's fictitious value essentially doubles. It is able to produce a return by being a share as if it were twice its money value. A £10 share would have a fictitious value of £20 because the latter sum would produce a £1 return in interest as money. This process is known as capitalisation and refers to the calculation of the capital value of a stream of income. In Marx's words, 'every periodic income is capitalised by calculating it, on the basis of the prevailing rate of interest, as an income which would be realised by a capital loaned at this rate of interest.' [19]

The relationship between fictitious share value and interest rates can be illustrated in the stock market falls at the beginning of 2018. Beginning in the United States, stock market falls quickly spread to the FTSE and Asian stock markets. They were precipitated by the US Federal Reserve's announcement of a small rise in interest rates. Stock markets have been rising for years because of historically low interest rates from central banks, coupled with many states' policy of quantitative easing. Borrowing at such low interest rates to invest in the stock market has given a substantial return, but a small increase in the cost of borrowing led to the biggest fall in the Dow Jones in six and a half years.[20]

Today, share value (in the short to medium-term, fully encompassing the horizon of investors), is increasingly likely to derive from strategies that run counter to the best interests of the productive entity, the company. Investment in production is likely to be beneficial to those who work in and with the company from employees to creditors and consumers. However, from a shareholder's perspective, particularly in a period of low returns on investment in productive assets, investment is a risk with no guarantee of adequate returns. Instead, shareholder value is better achieved if the company borrows money at low interest rates and uses it to buy back existing shares. 'Buy backs' have become the shareholder value strategy par excellence over the last 20 years, accelerating in the last 10 years.[21] Meanwhile the productive entity has become highly leveraged and may struggle

[19] Marx, Capital III, p.466.

[20] ''It Was Excessive Confidence.' Dow Jones Industrial Average Plunges 1,100 in Biggest One-Day Selloff Ever' http://fortune.com/2018/02/05/stock-market-plunge/ February 5th 2018

[21] For recent statistics see R.Wigglesworth 'As the market swoons, share buybacks are back' *Financial Times* February 21st 2018 https://www.ft.com/content/7a3529ce-1667-11e8-9e9c-25c814761640 For statistics on Europe generally see OECD Economic Outlook, Volume 2015, Issue 1, p240 http://www.oecd.org/economy/outlook/Economic-Outlook-97-Lifting-investment-for-higher-sustainable-growth.pdf and for the United States see W. Lazonick, 'Profits without Prosperity' (2014) *Harvard Business Review*

to repay loans particularly as it has reduced investment in productivity and will be highly vulnerable to increases in interest rates.[22]

This emergence of the company share as a form of fictitious value can also be demonstrated through the changing rules on dividend law.

Throughout the nineteenth century, the courts took the view that dividends should be paid from profits only, and not from company capital. Until the end of the nineteenth century, profit was understood according to a balance sheet approach which included loss in value to assets in its calculation. In Flitcrofts Case (1882) Master of the Rolls Jessel stated that 'the creditors have a right to see that the capital is not dissipated unlawfully'; and 'the members must not have the capital returned to them surreptitiously', the latter which might occur if either dividends were paid by assets or, under the balance sheet approach, if dividends were distributed regardless of loss to company capital.[23] However, from 1889, profit was distinguished from loss to assets. In *Lee v. Neuchatel Asphalt Co*. (1889),[24] Lord Justice Lindley introduced an interpretation of what constituted distributable profit that reflected the shareholder as *rentier*, who claims revenues but has no interest in the assets. In this case, a shareholder claimed that as the value of the company's assets had fallen, the company should make good that loss before declaring a dividend. The court stated that a company could declare dividends notwithstanding that its assets were depleted.

5. Alienation and the shareholder

It is striking that in the English cases on dividends decided according to *Lee* (and including *Lee*), the complaints regarding the depletion of assets and the need to protect the ongoing productivity of the company – one aspect of what today we might call its sustainability – arose from shareholders themselves. In *Bolton v Natal Land Co*.,[25] it was a shareholder who sought the reduction of dividend to reflect the loss of value to the company's land assets. The court held that the profits, severed from the assets, were sufficient to justify a dividend. In *Wilmer v McNamara*[26] an action was brought by shareholder in respect of dividends declared when the goodwill assets were over-valued. The court held that previous years' over-valuations should not affect distributions of a new year. In other

[22] OECD statistics on non-financial corporations debt to surplus ratio (2015) https://www.oecd-ilibrary.org/economics/non-financial-corporations-debt-to-surplus-ratio/indicator/english_dc95ffa7-en
[23] Flitcrofts Case (I882) 2I Ch.D. I49.
[24] *Lee v. Neuchatel Asphalt Co*. (1889) 41 Ch.D 1
[25] *Bolton v Natal Land Co* [1892] 2 Ch. 124
[26] *Wilmer v McNamara* [1895] 2 Ch. 245

words, in the earlier cases, shareholders identified with the productive entity and its future productivity. They were embedded in the whole enterprise, of which profit was just one part.

Today there is much evidence to suggest that greater levels of embeddedness in a business correlate to greater commitment to the productive enterprise, and the impact of that enterprise on society. The Nuttall Report shows that the greater the integration of ownership and involvement in the business, the more likely that business will invest in productivity and consequently withstand economic crisis.[27] At the highest levels of integration are employee-owned businesses, the subject of David Erdall's book, *Beyond the Corporation*.[28] However, even in those business forms that are legally constructed as profit maximising, such as partnerships, owner stewardship is still possible. Partners are engaged at every level in the cycle of capital. Partners have an interest in the ongoing productivity of the business because their fortune, present and future, is bound to the business's ongoing success. Partnerships will avoid risky speculation and prioritise raising productivity and building the business. They may avoid negative impacts on the environment, both because they may be liable for the resulting costs, (having unlimited liability) and because they operate within that environment.

In contrast, the rentier shareholder is dis-embedded from the business. [29] The post *Lee* position and the ruling on separate legal personality illustrate this. Shareholder interests, as defined by law, is in the profit alone, regardless as to whether the company assets are troubled or depreciating. Thus, while historically shareholders were heterogeneous, the shape of modern capitalism, and its reflection in company law, made them homogenous.

The homogenous dis-embedded shareholder prevalent in dispersed shareholder companies typically associated with an Anglo-American model, has no commitment to any particular company, nor with the company's impact on society. They have no engagement with the productive activity that creates profit. They are concerned only to identify profitable investment opportunities either personally or through some financial intermediary, and to maintain liquidity. Investing in business,

[27] G. Nuttall, 'Sharing Success: The Nuttall Review of Employee Ownership' July 2012. https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/31706/12-933-sharing-success-nuttall-review-employee-ownership.pdf

[28] D. Erdall, *Beyond the Corporation: Humanity at Work* (The Bodley Head, London, 2011)

[29] Early companies mimicked the norms of partnership. The shareholders were generally managers and even limited liability was ineffective given the tendency to issue shares with large unpaid portions, a *de facto* unlimited liability guarantee to creditors JB. Jefferys, 'The Denomination and Character of Shares 1855-1885' (1946) 16 *Economic History Review* 45

under the company form is little more than 'gambling on the stock exchange'.[30] This gambling provokes a reckless pursuit of profit, which inhibits sustainability and accelerates crises.[31]

The company form also increases the centralisation of business as many small firms are replaced by large oligopolies. This increases the experience of shareholder separation popularly associated with Berle's notion of the separation of ownership from control.[32] It is less popularly associated with a detachment of moral obligation to those involved in production, which arises because the shareholder does not connect the activities of the company with share value. To the shareholder, the surplus accruing to shares appears to be a natural attribute of the share, or of the speculators' skill in trading shares. The share does not appear to be what it really is, a reified right to the value captured from labour into perpetuity. As such, the shareholder is detached from the experience of moral responsibility for the impact of corporate activity including its impact on the workforce, the community or the environment.

6. The problem with bringing shareholders into governance

Following the financial crisis the UK's Financial Reporting Council published the 2010 Stewardship Code. The intention was to increase corporate responsibility by shareholder (particularly institutional investor) driven pressure. Many countries followed suit.[33] However, the effect was to enhance the governance imperative to increase shareholder value by empowering those with only a rentier interest.[34]

The Stewardship Code 2010 was organised around non-legal language involving expectations, encouragement and principles.[35] The principles, seven in all, recommended that institutional investors should publish policies on their stewardship responsibilities; have a robust policy on managing conflicts of interest; carefully monitor investee companies; establish clear guidelines on how they will enhance shareholder value; act collectively to that end; have a clear voting policy and

[30] Marx, *Capital III*, p.430.
[31] Marx, *Capital III,* p.432.
[32] A.A. Berle and G. Means, *The Modern Corporation and Private Property* (The Macmillan Company 1932)
[33] For the full list from Brazil to Thailand see https://www.manifest.co.uk/portfolio/global-stewardship-codes/
[34] L. Talbot, 'Why shareholders shouldn't vote: A Marxist-progressive critique of shareholder empowerment' (2013) 76 *Modern Law Review* 791
[35] 'Implementation of the UK Stewardship Code 2010' (July 2010) available at http://www.frc.org.United Kingdom/images/uploaded/documents/Implementation%20of%20Stewardship%20Code%20July%2020103.pdf (accessed 1 August 2010) p4.

then report on their stewardship and voting activities.[36] The Financial Reporting Council expected those firms that manage funds to 'disclose on their website how they have applied the Code'.[37] It strongly encouraged[38] them to report their compliance with the Code. Compliance follows the comply or explain model where 'listing' takes place on the Financial Reporting Council's website in which investment firms publish their commitment to the code.[39]

However, in spite of the undemanding stewardship requirements made of investors in the 2010 Code there was little resulting increase in their involvement.[40] This prompted the Financial Reporting Council to publish a review of the UK Corporate Governance Codes and the Stewardship Code[41] in which shareholder stewardship was re-described as enhancing *shareholder* value. This conceptual shift was rationalised as arising from the fiduciary arrangement between investor and the ultimate beneficiary of the various funds that required investors to enhance shareholder value. Thus, the Draft Revisions to the Stewardship Code suggested substantial revisions to the short preface to the 2010 Code so that the first section would explain the nature of shareholder stewardship as meaning shareholder value, not social responsibility. The review claimed, 'there is no common understanding of what is meant by the term 'stewardship''.[42] Accordingly, the revised Stewardship Code of 2012 now defines stewardship as promoting 'the long term success of companies in such a way as the ultimate providers of capital also prosper'.[43] Stewardship activities are those that are contingent on promoting the prosperity of the providers of capital. If they do not promote those interests, they need not be pursued. Stewardship under the 2012 Code requires no commitment either to sustainability or to long-term strategies, if they do not profit maximise. It is either a win-win, or a win for shareholder value only.

So, how has this instruction been interpreted and complied with – if at all? The FRC's 2016 Report on Stewardship indicate that good stewardship is, for many investors, closely aligned with

[36] Stewardship Code 2010, The seven Principles, p.4. (Principles 1–7).
[37] Stewardship Code 2010, p.2.
[38] ibid.
[39] http://www.frc.org.uk/corporate/stewardshipstatements.cfm#Service
[40] The FRC has recently introduced a tiered system to identify the better stewardship reporters.
[41] Financial Reporting Council, Developments in Corporate Governance 2011. The Impact and Implementation of the UK Corporate Governance and the Stewardship Codes December 2011 http://www.frc.org.uk/FRC/media/Documents/Developments-in-Corporate-Governance-20117.pdf

[42] FRC Introduction to Draft Revisions p.1.

[43] The Stewardship Code 2012 https://www.frc.org.uk/getattachment/d67933f9-ca38-4233-b603-3d24b2f62c5f/UK-Stewardship-Code-(September-2012).pdf at p.4.

environmental sustainability.[44] Does this suggest that shareholders are more heterogeneous than this chapter has thus far argued? In the following section, I provide a brief analysis of the dominant forms of shareholders in the FTSE 100 and argue that heterogeneity, such as there is, does not alter their rentier nature. I go on to show that even when investors aim to self-identity as non-rentier sustainable investors their interpretation diverges from both the definition of sustainability in this book, and from any engagement with labour exploitation, as defined in this chapter.

7. Does shareholder diversity affect their rentier nature?

Statistics on UK shareholders show us that shareholders are diverse, that institutional investors are diverse and that they represent diverse peoples.[45] The Office of National statistics (Table 1 below) shows us that the holdings of the FTSE 100 companies (worth over £2 trillion) is mainly held by foreign investors, who are mainly based in North America. Of those investors over half are unit trusts, 27.5 per cent are other financial institutions and 17.7 per cent are pension funds. Private individuals own 9.5 per cent of FTSE 100 shares and 12.3 per cent of all UK quoted shares. The proportion held by pension funds of 3 per cent of FTSE 100 companies is at an all-time low. The biggest investors in UK shares are unit trusts based in North America (Table 2). These unincorporated mutual are funds divided into saleable units. The fund manager invests the funds in diverse investments and the profit returns to the unit owners. The unit owner, therefore, possesses an interest in a concoction of diverse companies that are unknown to them. The fund manager seeks out the highest returns and his own rewards are determined by his success in so doing.

Table 1:
Holdings of FTSE 100, Alternative Investment Market and other quoted companies by beneficial owner
At 31 December 2016

	Percent		
	FTSE 100	Other quoted	AIM
Rest of the world	56.0	48.5	42.8
Individuals	9.5	19.4	29.7
Unit trusts	9.1	10.4	11.3

[44] FRC 'Developments in Corporate Governance and Stewardship 2016' January 2017. https://www.frc.org.uk/getattachment/ca1d9909-7e32-4894-b2a7-b971b4406130/Developments-in-Corporate-Governance-and-Stewardship-2016.pdf p.30.

[45] Office for National Statistics. Statistical bulletin: Ownership of UK Quoted shares: 2016 https://www.ons.gov.uk/economy/investmentspensionsandtrusts/bulletins/ownershipofukquotedshares/2016

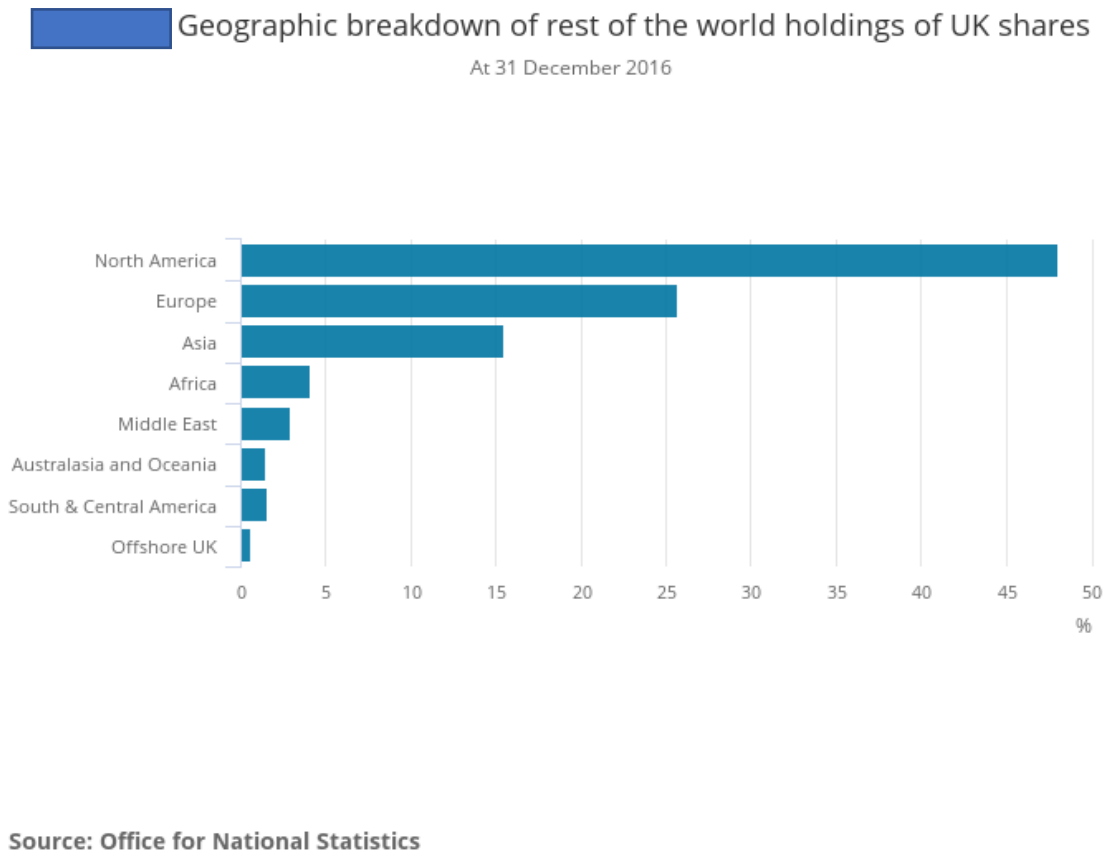
Other financial institutions	8.1	8.3	8.3
Insurance companies	5.0	5.0	1.8
Pension funds	3.0	3.0	2.8
Public sector	1.5	0.0	0.0
Private non-financial companies	2.6	1.1	0.2
Investment trusts	2.0	2.3	2.4
Banks	2.0	1.2	0.4
Charities, churches, etc.	1.1	0.7	0.4
Total[1]	100.0	100.0	100.0

Source: Office for National Statistics

Notes:

1. Components may not sum due to rounding

Table 2



The vast majority of capital, therefore, is owned by people who have no connection with the productive, profit making entity, only an interest in revenues. Most investment is made by highly detached groups, geographically and politically. Indeed, the alienation of investor from company, their rentier nature, has never been greater. Equally, the institutions who represent their interests

are themselves concerned with maximising returns. As the discussion on Stewardship indicates, fiduciary responsibility is associated with maximising returns for the ultimate beneficiaries.

To be sure, there is evidence to show that shareholders may *act* differently. Many commenters have evidenced the different levels of activism associated with large-scale investors. Bushee's work on US investors in shares show that they fall into two main groups.[46] First, investors who are highly passive, 'quasi indexers', who maintain highly diversified portfolios, trade infrequently and rely on diversification alone as a mechanism to increase value and to balance risk. They constitute about 61 per cent of large investors and most of the investors noted on the FTSE 100. Second, investors who are activist and engage with the company in a self-interested manner that is often destructive to the enterprises they alight on. They constitute around 31 per cent of investors, termed by Bushee as 'transient'. Hedge funds would typically fall into this category. However, what is clear from Bushee's work is that while shareholders may strategise differently, they all seek profit maximisation.[47]

In contrast, the socially responsible investment (SRI) literature suggests that there is a third way between passive and activist rentier shareholders – that of the creative activist shareholder who seeks to profit as an investor, but in socially responsible ways.[48] If they are a significant social force then they may subvert the rentier model as private investors.[49] Their existence would suggest that shareholders are heterogeneous not only in their levels of activism, but also in their goals.

What is the evidence? Certainly, there are a large number of private investors who claim they are guided by SRI considerations. In the US, an estimated $8.72 trillion of managed funds use ESG criteria, a 14-fold increase since 1995.[50] Self-proclaimed socially responsible mutual funds adopt their own SRI strategy based on environmental, social and corporate governance criteria. Many funds claim SRI status because they screen out particular investment opportunities such as tobacco, arms or alcohol companies, while others may positively seek out investments that claim to improve

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[46] B.J. Bushee, 'The Influence of Institutional Investors on Myopic R&D Investment Behaviour' (1998) 72 *Acct. Rev.* 305

[47] According to Bushee, a small minority of large shareholders (8%) maintain an interest in a few companies over a long period, defined by Bushee as 75 per cent of their stock for at least two years.

[48] See Richardson, Chapter ??, section 5.

[49] SRI might be possible where the state is the investor, such as The Government Pension Fund of Norway, although some scholars are sceptical. B. Sjåfjell, HR. Nilsen, and B. Richardson, 'Investing in Sustainability or Feeding on Stranded Assets? The Norwegian Government Pension Fund Global' (2017) 52 *Wake Forest Law Review* 4, 949.

[50] 2016 Annual Report: US SIF and US SIF Foundation https://www.ussif.org/files/Publications/2016USSIFAnnualReport_online.pdf p9 '$8.10 trillion in US-domiciled assets … apply ESG criteria'

environmental and social problems.[51] Most funds seek guidance through membership of umbrella organisations. One of the largest is the US based, Forum for Sustainable and Responsible Investment with a membership of nearly 500 institutional investors.[52] The leading organisation for SRI investors globally is the UN Principles for Responsible Investment (PRI) a network of the largest global institutional investors working under the auspices of the UN, to encourage and support signatories to the six Principles for Responsible Investment.[53] There are currently 1750 signatories to the Principles, who manage funds of around $70 trillion and who agree to be guided by the PRI and to report on their adherence annually.

Given the scale of investment in accordance with ESG standards, it might be wondered whether the rentier shareholder is an outdated concept and that the political economy of the company outlined in this chapter had been superseded by a new model that no longer exploits either people or the planet. However, a cursory analysis of two leading signatories of the Principles indicates the limited nature of their social and environmental commitment. PRI signatory, Parnassus Funds, with net assets of $1,067 million claims to be SRI compliant because it does not invest in companies involved in any aspect of fossil fuels and invests in companies which are economically stable (one of the many interpretations made of the concept of sustainability).[54] It claims to outperform the market by identifying companies where the stock value is lower than the industry average given the company assets' value. Their policy, therefore, provides ample scope to invest in companies with exploitative behaviours and indeed to enhance labour exploitation to increase stock value. Another signatory, Jupiter Assets management, which invests solely in UK based companies, has £50 billion in assets under management. Their SRI approach is stated as investing in companies who are 'responding positively to, and profiting from, the challenges of environmental sustainability or making a positive commitment to social well-being' – attractive words but with no further clarification as to meaning or application. Further to this, Jupiter will not invest in companies that earn more than 10 per cent of their turnover in 'activities associated with armaments, tobacco, nuclear power and animal testing'.[55] Accordingly, they invest largely in financial institutions, with 28.2 per cent of their funds invested in banks. In total, they invest 68.1 per cent in FTSE 100 companies.[56] While banks and FTSE 100 companies are unlikely to satisfy the notion of sustainability set out in this book, Jupiter has an

[51] https://charts.ussif.org/mfpc/ which uses data supplied by Bloomberg LP.
[52] https://www.ussif.org/institutions
[53] https://www.unpri.org/download?ac=1453
[54] https://www.parnassus.com/parnassus-mutual-funds/parnassus-fund/investor-share
[55] https://www.jupiteram.com/UK/en/Individual-Investors/Our-Funds/Asset-Classes/Equities/Jupiter-Responsible-Income-Fund?sc=GB00B40TGH32
[56] Jupiter Responsible Income Fund March 2018 https://www.jupiteram.com/UK/en/Individual-Investors/Our-Funds/Asset-Classes/Equities/Jupiter-Responsible-Income-Fund?sc=GB00B40TGH32

altogether different interpretation of social responsibility – active involvement with the management of companies in which it invests, rather than merely index tracking.[57] Active investment frequently correlates to responsible investment for SRI funds because it shows responsibility to the fund owners. However, for SRI to designate behaviours and goals that are different from revenue pursuing rentiers, investment must be guided by responsibility to society and the environment.

While this is but a limited survey of SRI funds, the evidence suggests that SRI investors are little different from non-SRI investors. They seek to profit maximise while utilising vague platitudes like 'ethical practice', or by excluding or limiting investment in some undesirable activities, while investing in others.

Furthermore, over the SRI business as a whole, corporate culture dominates. Mirroring mainstream share indexes, SRI friendly companies are shown in SRI indexes, such as the S&P Dow Jones Environmentally Responsible Index. These indexes seek to put SRI investing on a par with ordinary investment indexes – making the investor's choice between investments that produce profit with harm or investments that create profits with good. But the win-win business case for SRI[58] depends on how SRI is defined.[59] In the corporatized model it is interpreted extremely narrowly by investment funds, and their interpretation is not interrogated by the various umbrella organisations which guide their SRI endeavours, including the important UNPRI. In part, this is because the umbrella organisations themselves have followed the practice of corporate governance codes, adopting principles rather than rules with which to define compliance with SRI goals.

The corporatisation of SRI is also manifest in the proliferation of codes of conduct and performance indicators. The dependence on performance indicators in part accounts for the popularity of environmental targets which are more easily quantifiable and where scientific data on environmental impacts of corporate activity is more readily available.[60] Furthermore, environmental issues are popular with the investing public. The profile of climate change has significantly risen over the last 15 years and particularly following global initiatives like the Paris Climate Accord.

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[57] PRI reporting framework 2017 https://reporting.unpri.org/surveys/PRI-reporting-framework-2017/ABCB465C-7AD7-4575-9BED-10F41A32C604/bf735de92be04caa8c32fcbc25cbdd2c/html/2/?lang=English&a=1

[58] J. Elkington, 'Towards the sustainable corporation: Win-win-win business strategies for sustainable development', (1994) 36California Management *Review* 90

[59] J. Entine, 'The myth of social investing', (2003) 16 *Organization & Environment 3,* 352

[60] P. James 'Business Environmental Performance Measurement' (1994) 3 *Business Strategy Environment* 2, 59-67

The corporatisation of SRI is further manifest in its principal justification – that the socially responsible companies in which they invest make the highest profits.[61] Recent data from MSCI reported in the Financial Times indicated that,

'Equity indices comprised of ESG-compliant companies outperform benchmark emerging market indices, according to data from MSCI. In fact, the MSCI EM ESG Leaders Index has been outstripping the MSCI EM benchmark consistently since the 2008/09 financial crisis. In June, the outperformance gap reached a record of 51.84 points, double its span in early 2013.'[62]

This report indicted a number of key points about profitability and SRI. First, extreme polluters and abusers of human rights do not make the most profits. Second, the minimal standards on environmental protection and social rights engaged by the companies approved by SRI funds, give them the edge. This is likely to be a combination of the increasing penalties for environmental damage and the effect of consumer choice for more socially and environmentally aware products and services. Third, private companies make more profit (whether SRI orientated or not) than state owned enterprises. There is not the space for a detailed appraisal of what this study indicates, but a cursory observation is that today, the most profitable combination of strategies for companies is to make labour productive (unlike in many state owned enterprises) and to adopt small adjustments to environmental impacts. Neither promotes 'strong' sustainability or reduces labour exploitation.

However, some scholars have suggested that the concept of embeddedness can help define degrees of social commitment by shareholders and by implication act as a mechanism for increasing shareholder commitment to socially responsible corporate behaviours. Welker and Wood argue that in order for SRI to impact on company activity and for shareholders to become social investors, SRI activists must draw on 'a relational model of personhood to posit shareholders as moral persons who see their portfolios as an extension of selfhood'.[63] However, the notion of shareholders viewing their share portfolio as an extension of their moral position is very far removed from the current state of shareholding. As noted above, shareholders in UK quoted companies are too distant to experience a social connection with the people who toil for their profits. Furthermore, the individualism that accompanies economic rationalism conflicts with the communitarianism required to prioritise social and environmental concerns.

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[61] P. Camejo, (Ed.) *The SRI advantage: why socially responsible investing has outperformed financially* (New Society Publishers, Gabriola, BC. 2002).

[62] J. Kynge, 'Investors in companies that do good do better: MSCI index of responsible emerging market companies outperforms' July 20th 2017. p.1

[63] M. Welker and D. Wood, 'Shareholder Activism and Alienation' (2011) 52 *Current Anthropology* 3, 560

8. Conclusion

The siren calls of shareholder stewardship and SRI belie the reality of the rentier shareholder. The shareholder is, as this chapter has sought to demonstrate, the embodiment of the power of capital over labour, and the legally endorsed right of capital to claim the surplus value, ultimately profit, from that relationship in production. The share obfuscates this political relationship because the right to extract value with the minimum of risk are rights that accrue to this particular property form.

Capitalism is fundamentally unable to meet social needs, including all the provisions of a 'strong' sustainability adopted in this book because it is driven by the needs of 'the profit dependent classes', as Streeck dubs them.[64] Capitalism is concerned with the production of exchange values, as opposed to the more socially orientated use values, and will dispense with the production of socially valuable products should they fail to generate sufficient profit. It is prone to crisis, the impact which is primarily felt by labour rather than owners of capital.[65] Crucially, it relies on the exploitation of labour and on externalising costs to the natural environment.

These characteristics are common to all capitalist economies and form the primary dynamics in capitalist societies. This view contrasts with the varieties of capitalism approach which claims that national culture and different methods of state intervention in the distribution of wealth, such as through taxation, constitute different types of capitalism that can resist free market individualism.[66] Germany and Japan have been oft cited as examples of more socially orientated capitalism. However, the Marxist analysis adopted in this chapter shows the conceptual inaccuracy of this approach. All capitalist economies are constituted by the pursuit of profit and labour exploitation. Hence, since the economic downturn in Germany and Japan, they too have abandoned their brands of humanist capitalism. This is not to say that political institutions cannot modify the impact of capitalism at all. They can reduce shareholder control mechanisms, enforce effective environmental regulation, or effective regulation to curtail tax avoidance. However, it is important to be realistic about the limits of reform, as well as its benefits. Capitalism is built on inequality and power. The legitimacy of capital owners to make wealth from the activities of others is, in part, ensured by the 'propertyfication' of the right to captured value in the form of the company share. From that perspective, the belief that shareholder governance initiatives will arrest the profit maximizing which

[64] W. Streeck, *Buying Time: The Delayed Crisis of Democratic Capitalism* (Verso, 2014)
[65] T. Piketty, *Capital in the 21st Century* (Belknap, Harvard 2014)
[66] P. Hall and D. Soskice, (Eds) *Varieties of Capitalism: The Institutional Foundations of Comparative Advantage* (Oxford University Press, 2001)

benefit shareholders is absurd. Furthermore, shareholder governance provides greater legitimacy to shareholder claims. However, whatever governance strategy is adopted, the underlying relations of production remain unchanged. Thus while shareholder governance has put the foxes in change of the hen house, the hens were always destined for consumption.