Entrepreneurs and Democracy

What legitimizes power within a corporation? This question is of concern to the millions of citizens whose lives depend upon the fate of business corporations. The rules, institutions, and practices of corporate governance define the limits of the power to direct, and determine under what conditions this power is acceptable.

Effective corporate governance has long been defined in terms of economic performance. More recent studies have focused on philosophical, political, and historical analyses. *Entrepreneurs and Democracy* unites these strands of inquiry – the legitimacy of power, the evolution of multiple forms of governance, and the economics of performance – and proposes a framework for future study. It explores the opposing tensions of entrepreneurial force and social fragmentation that form the basis of legitimate corporate governance in modern societies. In doing so, it identifies a common logic that links both the democratization of corporate governance and the growth of economic performance.

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Entrepreneurs and Democracy

A Political Theory of Corporate Governance

PIERRE-YVES GOMEZ
and
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Foreword

Entrepreneurs and Democracy is an important and timely book. For scholars of corporate governance, the book establishes a truly comprehensive political and social context for current debates on the roles and responsibilities of investors and owners in the modern corporation. And for practitioners, *Entrepreneurs and Democracy* is a highly readable guide to the historical and philosophical antecedents of some of the dilemmas they face in reconciling the demands of diverse and increasingly fragmented groups of shareholders. For example: what duty is owed to investors who do not care about the long-term prospects of the firm and wish merely to profit from the short-term upsides (or downsides) available to them through rapid changes in stock market valuations?

Authors Gomez and Korine are suitably modest in asserting their purpose as simply to create a common space for historians, economists and political philosophers 'to talk to each other'. In fact they embrace a breathtaking array of sources, ranging from Hobbes, Locke and Smith to Tocqueville, Schumpeter and Keynes, to create a strong theoretical basis for their central assertion that democracy is vital to the effective functioning of the capitalist enterprise because 'democracy imposes the competition of markets on the entrepreneur'.

With their arguments firmly rooted in the domain of liberal political philosophy, Gomez and Korine advance an elegant critique of the contradictions inherent in purely economic approaches to corporate governance. Interestingly they do this without recourse to the well-established arguments of stakeholder theorists who note that the assertion of shareholder versus stakeholder rights is a distraction and a false dichotomy, if not simply redundant. Instead Gomez and Korine argue that the rights of disparate and fragmented investors and owners have never been especially important to strategic decision-making in firms – especially compared with the hegemonic influence of the family owner-entrepreneurs and technocrats who dominated corporate boardrooms and executive suites for the first two hundred years of industrial capitalism.

The authors describe the legitimacy and credibility of the entrepreneur as a vital force in establishing the confidence of investors. And they note the historic importance of the establishment of property rights and the ability to pursue profit to the notion of liberty. But Gomez and Korine describe the emergence of shareholder activism – the attempt to assert the rights of large numbers of small investors and their fund managers – as essentially a late twentieth-century phenomenon, accelerated by the somewhat ideological arguments of neoliberal economists.

Of course any attempt to assert the supremacy of the rights of non-homogeneous shareholders of the firm as though they were a uniform entity is ultimately doomed to failure because not all investors or owners want the same thing. We have only to think about the radically different interests of mutual funds, hedge funds and social investors to understand the point. Depending on orientation, shareowners may hope for short-term gains *or losses* in share price; dividend policy may be vital or irrelevant to them; and mode of engagement of the owners (regardless of size of shareholding) may range from abject failure even to vote on resolutions to physical disruption of the annual general meeting.

Add to these observations the breaking down of traditional barriers between owners, investors, managers and workers, the emergence of civil society groups and the declining relevance of labour unions (historically the main counter to the wilder excesses of industrial capitalism) and we see that simplistic advocacy of shareholder rights in a world of global capital markets is highly problematic. In the last section of the book the authors update the conclusions of Berle and Means' systematic economic analysis in *The Modern Corporation* to take account of these institutional phenomena and the growing democratization of capital. They follow this with a very respectful *coup de grâce* to the 'Pure Economic Model' of corporate governance: 'Paradoxically, the clarity of PEM allows us to see that all of the critiques of the model have a common route: what is underestimated is the degree to which property ownership is fragmented.'

Clearly, liberal democracy demands an effective response to the problem of disenfranchizement of investors and owners, whether that phenomenon is associated with agency issues or the absence of effective information exchange, exacerbated by technological or transaction cost issues. As Gomez and Korine explain, we are too early in the game of shareholder democracy and indeed theories of corporate governance to predict exactly how things will evolve. But surely corporate governance practices will need to change to embrace the increasingly powerful democratic influences that now permeate the capitalist project.

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