Governing the Firm

Workers' Control in Theory and Practice

Most large firms are controlled by shareholders, who choose the board of directors and can replace the firm's management. In rare instances, control over the firm rests with the workforce. Many explanations for the rarity of workers' control have been offered, but there have been few attempts to assess these hypotheses in a systematic way.

In *Governing the Firm*, Gregory Dow draws on economic theory, statistical evidence, and case studies to frame an explanation. His fundamental hypothesis is that labor is inalienable, while capital can be freely transferred from one person to another. This implies that worker-controlled firms typically face financing problems, encounter collective choice dilemmas, and have difficulty creating markets for control positions within the firm. Together, these factors can account for much of what is known about the incidence, behavior, and design of worker-controlled firms.

A policy proposal to encourage employee buyouts is developed in the concluding chapter.

Gregory K. Dow is Professor and Chair of the Department of Economics at Simon Fraser University, British Columbia, Canada. He previously taught at the University of Alberta and Yale University, and he has served as a visiting professor at the University of New South Wales, the Erasmus Institute for Philosophy and Economics, and the Swedish Collegium for Advanced Studies in the Social Sciences. Professor Dow is associate editor of the *Journal of Economic Behavior and Organization*, and he has published numerous articles on labor-managed firms and other topics in economic theory in leading journals such as the *American Economic Review* and the *Journal of Political Economy*. He has also written many book chapters in edited volumes.

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GREGORY K. DOW
Simon Fraser University, Canada

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For the women who ran the braiding machines,
the men who ran the tipping machines,
and especially the guy who worked in the wax room.

The form of association, however, which if mankind continues to improve, must be expected in the end to predominate, is not that which can exist between a capitalist as chief, and work-people without a voice in the management, but the 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.

John Stuart Mill, *Principles of Political Economy*, Book IV, Chapter VII, Section 6. First published in 1848; this passage was added to the third edition in 1852. Reprinted in 1987 by Augustus M. Kelley, Fairfield, NJ, 772–773.

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Preface

Most large enterprises in the developed world are controlled by shareholders, who choose the board of directors and can therefore replace the firm's top management. But in a few firms, control rests with the employees, who have an analogous right to choose the board of directors and hire or fire top managers. Why is the first pattern so common and the second so rare? Economists have had surprising difficulty in framing a satisfactory answer to this seemingly straightforward question.

Because economists have no generally accepted explanation for the prevalence of capitalist firms, they lack a good explanation for the persistence of capitalism itself. They have also been obliged to remain largely silent on various contemporary policy debates. Should employees be represented on a firm's board of directors? Does it make sense to subsidize stock purchases by employees? Should governments encourage worker buyouts of closing plants or failing firms? Most economists could undoubtedly formulate opinions on these matters, but they would have trouble locating a systematic body of theoretical or empirical research with which to inform their opinions. With or without participation from economists, however, policy issues of this sort have become increasingly prominent across Europe and North America.

This book seeks to explain why investor-controlled firms are common and worker-controlled firms are rare. The answer is not as simple as the question, but one can develop a theoretical story that is logically coherent and accounts for a good deal of the empirical evidence. While there is certainly room for debate, I believe that at least in broad outline a satisfactory explanation will need to look like the one suggested here.

Most of the book is devoted to the explanatory task, in part because it is interesting and in part because it is hard to formulate policy recommendations without first gaining an understanding of how the world works. But the idea of workers' control has stimulated a great deal of fervor and hostility over the last two centuries, and it is impossible to disregard the normative issues at stake. Accordingly, one chapter is devoted entirely to normative ideas, and the concluding chapter proposes a strategy for expanding the scope of workers' control in modern economies. I am not wedded to this particular strategy, but I believe that workers' control is currently undersupplied and that the theory developed in this book has implications for what could be done about it.

The book is intended for a broad audience, including readers with backgrounds in business, law, and public policy, as well as political science, sociology, philosophy, and other academic disciplines. At the same time, I have tried not to water down the theoretical discussion in a way that would make it seem simplistic to economists. I do not back away from theoretical concepts, and an economist will often be able to spot the models lurking in the verbal underbrush. However, prior familiarity with economic theory is not needed to grasp the key arguments, and there is almost no use of mathematics. The book should thus be useful for graduate students and advanced undergraduates in any of the social sciences.

Because the book offers a theoretical synthesis rather than just a literature review, I have not discussed every worthy piece of research on workers' control, which would have been impossible in any event. Sometimes I discuss a few groundbreaking articles on a topic but ignore later extensions. In other cases, I cite surveys or summaries to avoid extensive reviews of original research. Questions of emphasis have been resolved by applying my own idiosyncratic preferences, and my knowledge of the field remains highly incomplete. Apologies are due to all writers whose valuable contributions have been overlooked.

I have accumulated many debts over the years, not all of which are obvious from the citations in the text. At the risk of indulging in superfluous autobiography, the easiest way to acknowledge these debts is to recount how I became interested in the topic. I first came across the idea of workers' control in 1974–75 as an undergraduate sociology major at Amherst College, in a class on modern social theory taught by Norman Birnbaum. At about the same time, I attended a lecture given by Sam Bowles in which he emphasized the authoritarian nature of the capitalist firm. Sam observed that when a boss wants a worker to go to the other end of the factory, he doesn't go there and hold up a five dollar bill; he just tells the worker to go. The relevance of this point will become clear in Chapter 5.

While working on a master's degree in public policy at the University of Michigan, I began to explore the literature on workers' control more systematically. During this period, I discovered Katrina Berman's 1967 book *Worker-Owned Plywood Companies*; Carole Pateman's 1970 book *Participation and Democratic Theory*; David Ellerman's 1975 article in *Administration and Society*; and Jaroslav Vanek's 1975 anthology *Self-Management: Economic Liberation of Man*. These authors persuaded me that workers' control was both morally attractive and viable in the real world. But in the course of haranguing my fellow policy students about the virtues of workplace democracy, I began to see some loose ends. For example, if workers ran the firm, who would finance investment projects? Capitalists?

For a while, I put these questions to one side and tried to learn enough economics to get a doctorate from Michigan. Upon becoming an assistant professor at Yale, my previous interests resurfaced, stimulated by some reading in comparative economics that included Benjamin Ward's famous 1958 article on the Illyrian firm, discussed in Chapter 7. In 1983, this led to my first working paper on labor-managed firms and membership markets.

The initial stirrings of the present book occurred in 1992 at the Swedish Collegium for Advanced Study in the Social Sciences (SCASSS) in Uppsala. Bo Gustafsson asked me to give a seminar directed mainly to non-economists on the theory of the labor-managed firm. I decided to survey the reasons economists had given for the rarity of such firms. A few years later, Sam Bowles and Pranab Bardhan asked me to write up a similar survey for their project on "The Costs of Inequality" funded by the MacArthur Foundation. I dusted off the earlier SCASSS notes, called in Louis Putterman for reinforcement, and together we wrote a long working paper that became the foundation for Chapters 8 and 9. Other versions of this material appeared in a 1999 volume, *Employees and Corporate Governance*, edited by Margaret Blair and Mark Roe; in a 2000 article in the *Journal of Economic Behavior and Organization*; and in a 2001 article in the *Review of Industrial Organization*. Louis will not agree with everything in Chapters 8 and 9 but he will undoubtedly recognize the arguments.

The book as a whole was written during a year of study leave from Simon Fraser University made possible by Nancy Olewiler and John Pierce. Initial drafts of Chapters 1 and 5–9 were put together in October

and November of 2000 at Erasmus University in Rotterdam. My visit to Rotterdam was organized by Uskali Mäki of the Erasmus Institute for Philosophy and Economics, John Groenewegen of the Faculty of Economics, and Bart Nooteboom of the Faculty of Business. All three commented on the material in these chapters while it was still in a highly disorganized state. I am also grateful to the graduate students at EIPE who suffered through my rough drafts and gave me an opportunity to refine the presentation. Chapters 2, 10, and 11 were first assembled during a visit to the School of Economics at the University of New South Wales in April 2001. This enjoyable sojourn was arranged by Peter Robertson with the support of John Piggott and Hazel Bateman.

Not everyone who deserves explicit thanks can be mentioned here, but a few names stand out. Louis Putterman and Gil Skillman have often enriched my understanding, and their friendship has been a pleasure. I am also indebted to another co-author, Xiao-yuan Dong, for educating me about China and emphasizing that workers' control has a place on the agenda of non-Western economies too. Sam Bowles and Herb Gintis have frequently given me the benefit of their comments and criticisms, and I have learned a good deal over the years from Avner Ben-Ner and Bentley MacLeod.

Sam Bowles, Doug Kruse, John Pencavel, and Louis Putterman commented on large parts of the manuscript, and Gil Skillman offered exceptional service as a sympathetic critic. Partly due to constraints of time and space, I have not taken all of their advice, but I am grateful for it and regret the flaws that went unrepaired. Three anonymous referees also helped shape the book. Scott Parris of Cambridge University Press supported this project enthusiastically, and his e-mails were always a welcome sight. At the production stage, Ronald Cohen carried out the copyediting with a light and deft touch.

A group of hard-working journal editors deserves recognition: Mike Montias, Joe Brada, and John Bonin at the *Journal of Comparative Economics* and Richard Day at the *Journal of Economic Behavior and Organization*. All have waded through rough drafts of my journal articles and tried their best to make sense out of them. My colleagues at Simon Fraser have been generous and candid in commenting on my seminars and working papers. Margaret Blair of the Brookings Institution provided financial support and invited me to a series of conferences on employment and the organization of the firm that helped focus my thinking. Much of my research in this area has been supported by the Social Sciences and Humanities Research Council of Canada. The colleagues and funders

listed here are absolved of all responsibility for the opinions expressed, especially the foolish ones.

My greatest thanks go to Margaret Duncan for . . . well, everything. But let's just recall all those dinner conversations about dysfunctional organizations. Theory is one thing and practice is another, but sometimes the twain do meet.

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