From Mandates to Governance: Restructuring the Employment Relationship

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FROM MANDATES TO GOVERNANCE: 
RESTRUCTURING THE EMPLOYMENT RELATIONSHIP 

BRETT H. MCDONNELL* & MATTHEW T. BODIE**

The law imposes a dizzying array of responsibilities on employers with respect to their employees. Meant to advance a wide array of workplace policies, these demands have saddled employment with the burden of numerous social goals. The employment ecosystem has increasingly come under strain as companies seek to shed employment relationships and workers lose important protections when terminated. In this Article, we propose that employers and employees should have greater flexibility over workplace terms and conditions with a move from mandates to governance. Many of the legally imposed employment protections stem from employees’ lack of organizational power. The imbalance is best and most directly addressed by providing workers with governance rights within the firm. In exchange for these governance rights, governments could lift or relax a related set of employment mandates. In addition, the law should lift certain responsibilities currently assigned to employers and instead place those responsibilities on the larger society, where they would be more appropriately carried. This rebalancing of the employment relationship would lead to a more economically secure and empowered populace while at the same time freeing businesses to better pursue their entrepreneurial endeavors.

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INTRODUCTION

In September 2021, the California legislature passed Assembly Bill 701 (“AB 701”).  

1. 2021 Cal. Legis. Serv. ch. 197 (West).

2. Id.

3. Id.
supply chain issues, Governor Newsom signed it into law after he escaped his recall election.4

Both supporters and critics of AB 701 understand that its primary target is Amazon. The corporate monolith has come under increasing fire for its arduous and carefully calibrated minute-to-minute expectations, driven by algorithmic calculations. Amazon employees have suffered a disproportionate amount of injuries, outpacing their competitors by substantial margins.5 Examples have continued to pour forth as to how the company puts pressure on employees to sacrifice their personal needs for the sake of speed.6 As the company has added employees at an astonishing clip, a recent union victory provides an indication of worker discontent, despite earlier union losses.7

At one time in our history, labor advocates envisioned collective bargaining as a movement to advance industrial democracy.8 Workers would choose their collective representatives, and those unions would negotiate to protect worker interests and shape the terms and conditions of employment. In the latter half of the twentieth century, that vision faded as unionization in the United States cratered.9 An explosion of regulation dramatically changed the employment relationship: minimum wage, overtime, antidiscrimination provisions, and health and safety protections, to name a few. That regulation has replaced unionization as the prime legal strategy for protecting workers, but it can impose levels of complexity and rigidity that undermine its goals.


5. Noam Scheiber, California Bill Could Alter Amazon Labor Practices, N.Y. TIMES (Sept. 22, 2021), https://www.nytimes.com/2021/09/06/business/economy/amazon-california-warehouse-labor.html (citing a report that showed that “Amazon’s serious-injury rate nationally was almost double that of the rest of the warehousing industry in 2020 and more than twice that of warehouses at Walmart, a top competitor”).


9. Id. at 1529.
and result in uneven or lax enforcement.\textsuperscript{10} Even academics and regulators who advocate for greater worker protections recognize the costs of expanding these mandates.\textsuperscript{11}

Many employers chafe at these rules, and increasingly some attempt to evade employment regulation. Notoriously, Uber and Lyft have gone to great lengths to classify their drivers as independent contractors rather than employees. In California, with a long-standing reputation for an employee-friendly approach, the State’s supreme court and legislature adopted a broad definition of “employee” that included ride sharing drivers and other “gig economy” workers.\textsuperscript{12} But Proposition 22, passed in November 2020, created a carve-out for platform drivers and provided a significantly limited set of company responsibilities.\textsuperscript{13} Companies have designs to bring this categorization of platform workers to states across the nation.\textsuperscript{14}

During the post-war decades, corporate governance also evolved. By the 1970s, it had become widely accepted that corporations exist to maximize shareholder value.\textsuperscript{15} Protecting employees and other stakeholders was fine, according to this school of thought, but only if doing so would increase profits. If that led to too little protection, the argument went, then legislators should pass laws to protect workers. Recently, sentiments have begun to change, as corporations are under increasing pressure to shift from that narrow focus on shareholders. The announcement by the Business Roundtable supporting a stakeholder-oriented approach was just one notable example of this shift towards acknowledging environmental concerns, antiracism efforts, and employee empowerment.\textsuperscript{16} But the Business

\textsuperscript{10} See infra Part I.


\textsuperscript{12} 2019 Cal. Legis. Serv. ch. 296 (West).


Roundtable proposed no mechanisms for holding companies accountable for protecting stakeholders, including employees, and thus, the status of the average American worker remains frustratingly stagnant. The novel coronavirus ("COVID-19") pandemic has highlighted the disparity between workers, who face dangerous conditions and unemployment, and shareholders, who enjoyed the highest stock market averages on record.\textsuperscript{17} This contrast in fortunes is not an accident of circumstance. Efforts to regulate the workplace are often important stop-gap measures, but they lag behind employer innovation and only impose minimums with regard to terms and conditions of employment. And ever-increasing the number and complexity of workplace rules can lead to red-tape and frustration—which may in part explain the success of Proposition 22 amongst California’s largely liberal electorate. At the same time, business leaders and investors are recognizing the need to move beyond shareholder primacy in governing corporations.\textsuperscript{18} These two trends support a new approach to work, one that provides workers with more power and employers with fewer regulatory requirements. We suggest an exchange of governance power for employment mandates.

It is not novel to suggest that self-governance is a better workplace model than mandatory terms.\textsuperscript{19} The original Wagner Act was built on the premise of industrial democracy, and various efforts at employee participation through quality circles, works councils, and employee ownership have made appearances within our economic fabric.\textsuperscript{20} Several
scholars this century have proposed regulatory flexibility for companies with employee representation, reflecting limited developments in regulatory practice.21 But we are piling more and more of our societal expectations onto employment just as its fissuring threatens the entire enterprise. The chasm between employee power and corporate power is perhaps at its zenith, even while public sentiment turns in favor of greater worker empowerment.

This Article argues for reshaping the law of employment to emphasize employee empowerment within the firm and deemphasize legal mandates. Continuing the recent work of scholars in the field, we advocate for regulatory flexibility by focusing more on corporate governance implications and on the types of employee representation that could be used to invoke greater flexibility. The Article also considers a wider range of employment regulations that could be made flexible, including the link between a move to governance and parallel moves to provide certain collective goods through government rather than through employers.

In Part I we survey employment law. We describe the wide range and scope of legal mandates that employers face and the difficulties that those mandates create for both employers and employees. We analyze how allowing firms that implement collective employee governance to modify some legal mandates may reduce the costs of those mandates while still protecting employees. Part II considers the corporate governance arguments for empowering employees. While employment law focuses on protecting employees, corporate governance affects the interests of many corporate stakeholders, such as shareholders, customers, creditors, local communities, and the environment. Employee participation in governance would affect the interests of all those stakeholders. The traditional American position is that those running corporations should focus exclusively on the interests of shareholders. We argue that position is wrong.

Part III analyzes different forms of employee empowerment that employers could use to modify employment mandates. We consider three basic forms: (1) union representation, (2) shop floor governance such as works councils, and (3) employee representation on the board of directors. Each form presents a way to significantly involve employee representatives in governance, allowing firms to achieve better tradeoffs in protecting employees at a reasonable cost to other stakeholders than is achieved by our existing complex system of employment law mandates. Each form has its advantages and disadvantages. Any one of them, if instituted with adequate

protections, should allow employers to modify some employment regulatory mandates.

What mandates should employers be able to modify? Part IV provides a brief outline touching on, but not resolving, many issues. A variety of employment law rules, including minimum wage, workplace safety, pension protections, health insurance mandates, and possibly even antidiscrimination rules, could be modified. Mostly, we do not suggest completely eliminating a particular mandate, but rather we suggest either allowing employers with employee involvement to modify the mandate within limits, or changing the process by which the mandate is enforced. We draw a connection between modifying mandates through governance and changing the locus of responsibility for some matters from employers to government. For example, were the state to institute a substantial universal basic income, then it would be more feasible to allow empowered employees to agree to wages below the minimum wage level.

Part IV also considers how moving from mandates to governance would affect, and be affected by, the growth of platform companies and other forms of employment disintermediation and the related debate over defining who is an “employee.” The greater flexibility of governance may help protect workers such as drivers at Uber or Lyft while allowing their employer to avoid the most burdensome regulatory consequences of treating such workers as employees. But such disintermediated workplaces raise serious doubts as to whether our arguments favoring worker empowerment apply as well in such businesses. We are left with open questions, but still with the hope that moving from mandates to governance may improve regulatory options for an important and growing segment of the economy.

I. THE ROLE OF EMPLOYERS AS AGGREGATORS OF RESPONSIBILITIES

In corporate governance, the term “employer” is not legally meaningful. The responsibilities of various parties within the corporate form do not change based on whether the corporation is considered an employer. But in a variety of other areas—labor and employment law, certainly, but also tax, intellectual property, and tort—the law ascribes certain obligations on employers that are different than other entities. As a result, the role of employer has become a legally meaningful one, and entities have taken great pains to try to avoid being labeled as such. In this Part, we first examine the legal responsibilities placed on employers and discuss the differences...
between the mandatory and default approaches to these rules. We consider why employment is such a meaningful category for these responsibilities and then discuss the competing considerations that come from the regulation of labor through mandates in both positive and negative ways.

A. Legal Obligations Imposed on Employers

A complex network of laws imposes a set of responsibilities on employers and employees as part of the employment relationship. Below is a brief overview of the obligations that employers assume through this relationship.

1. Collective Representation

The National Labor Relations Act (“NLRA”) is the closest that labor and employment regulation comes to addressing the management and governance of the employer. Under the NLRA, the employer (whatever its organizational form) must bargain with its employees’ chosen representative over the employees’ terms and conditions of employment. A complex array of subsidiary obligations flow from this central one, such as the prohibition against employer discipline or discharge because of an employee’s protected concerted activity. The employer need not agree to any specific set of terms, but it must bargain in good faith and abide by the complex system of federal labor law for managing this bargaining relationship. Unlike other duties imposed upon employers within the employment relationship, the duty to bargain does not require minimum employment terms or impose substantive obligations on the employer’s business. Instead, the NLRA requires employers to negotiate with employees as a group and prohibits individual contracts. Framers of the NLRA intended to introduce a form of “industrial democracy” and provide employees with a voice at the workplace.

24. Id. § 158(a)(5) (making it an unfair labor practice for an employer “to refuse to bargain collectively with the representatives of his employees”).
25. See id. § 158(a)(1), (3).
26. See id. § 158(d).
27. J.I. Case Co. v. NLRB, 321 U.S. 332, 338 (1944) (“The very purpose of providing by statute for the collective agreement is to supersede the terms of separate agreements of employees with terms which reflect the strength and bargaining power and serve the welfare of the group.”).
28. A Bill to Promote Equality of Bargaining Power Between Employers and Employees, to Diminish the Causes of Labor Disputes, to Create a National Relations Board, and for Other Purposes: Hearings on S. 1958 Before the S. Comm. on Educ. and Lab., 74th Cong. 642 (1935), reprinted in 2 NLRB, LEGISLATIVE HISTORY OF THE NATIONAL LABOR RELATIONS ACT, 1617, at 2028 (1949) (“That is just the very purpose of this legislation, to provide industrial democracy.” (statement of Sen. Robert F. Wagner)).
2. Compensation and Benefits

Employee compensation is regulated both as to the amount and the process. As to the amount, federal law requires employers to provide a minimum and pay certain categories of employees one-and-a-half times their hourly wages if they work over forty hours per week. State and local minimum wage laws often go well above the federal minimums. In terms of the manner of compensation, wage payment regulations require that employees be paid regularly and that they be paid for all time worked, regardless of the length of term. Along with employer wage payment duties under the common law, federal and state statutes require timely wage payments and divisible portions.

With respect to pension benefits, the Employee Retirement Income Security Act (“ERISA”) does not require that employers provide pension or welfare benefits, but it does provide mandatory standards when they are provided. The Supreme Court has interpreted ERISA to borrow principles from the law of trusts with respect to fiduciary obligations. Specifically,

29. See 29 U.S.C. § 206. There are limited exceptions to this requirement for workers under twenty years of age who are new to the job. Id. § 206(g). Restaurant servers get a significantly reduced minimum wage as long as customer-paid gratuities make up the difference. See id. § 203(m)(2)(A).

30. See id. §§ 206, 207(a). The big exceptions for overtime pay fall into so-called “white collar” categories—professional, executive, and administrative workers. Id. § 213(a)(1) (exempting those “employed in a bona fide executive, administrative, or professional capacity”). Other exemptions include certain types of farm workers, id. § 213(a)(6), employees of seasonal amusement or educational centers, id. § 213(a)(3), and computer programmers, id. § 213(a)(17).


32. See RESTATEMENT OF EMP. LAW § 3.01 cmt. b (AM. L. INST. 2015) (“Many states have wage-payment laws that determine the mode and frequency of payment.”).

33. Id. §§ 3.01–3.05; see, e.g., id. § 3.01(b) (“Whether compensation has been earned is determined by the agreement on compensation between the employer and employee or any relevant binding employer promise or binding employer policy statement on compensation.”).

34. See, e.g., 29 U.S.C. §§ 206–207 (requiring the payment of minimum wages and overtime based on specific periods of work); MD. CODE ANN., LAB. & EMPL. § 3-502 (requiring employees to be paid at least every two weeks or twice in a month); MASS. GEN. LAWS ANN. ch. 149, § 148 (requiring the payment of wages within a week of the worker’s pay period).

35. Health and safety benefits are discussed below. See infra Section I.A.4.


37. Conkright v. Frommert, 559 U.S. 506, 516 (2010) (“Congress enacted ERISA to ensure that employees would receive the benefits they had earned, but Congress did not require employers to establish benefit plans in the first place.”).

the administrator of an ERISA plan has the same responsibilities as a trustee when it comes to administering the plan. The statutory scheme provides for four primary fiduciary duties: the duty of loyalty to plan participants, the duty of prudence, the duty of prudent diversification of plan assets, and the duty to follow plan terms. In addition, there are specific requirements about the operation of the plan, such as vesting. The upside of this complicated regulatory scheme is a set of tax savings for both employer and employee. However, this tax savings is only available if the employer offers the benefits to a sufficiently broad number of employees—a doctrine known as “nondiscrimination.”

3. Limitations on Discipline and Termination

The “employment at will” rule, which is the default rule in all states except Montana, dictates that employment is terminable at any time, with or without cause. As a default rule, at-will employment can be changed contractually. The common law of tort provides for additional protections against wrongful discharges in violation of public policy. The employer has a duty not to fire an employee because the employee refused to violate the law in the course of employment, or because the employee abided by professional codes of ethics or conduct. The protections also extend to employees who report on employer wrongdoing, either up the chain within the employer or directly to outsiders such as government agencies or media.

40. 29 U.S.C. § 1104(a)(1)(A) (also known as the exclusive benefit rule).
41. Id. § 1104(a)(1)(B).
42. Id. § 1104(a)(1)(C).
43. Id. § 1104(a)(1)(D).
44. See, e.g., id. § 1053 (providing for minimum vesting standards for employee retirement accounts).
45. See, e.g., 26 U.S.C. § 410(b)(1)(A) (requiring that “[t]he plan benefit[] at least [seventy] percent of employees who are not highly compensated employees”). ERISA’s so-called “nondiscrimination requirements” endeavor to achieve the “social policy goal of ensuring that the employer’s rank and file employees benefit from the employer’s qualified plan.” COLLEEN E. MELDILL, INTRODUCTION TO EMPLOYEE BENEFITS LAW: POLICY AND PRACTICE 164 (4th ed. 2015).
46. RESTATEMENT OF EMP. LAW § 2.01 (AM. L. INST. 2015).
47. See, e.g., id. § 2.02 (providing for contractual exceptions to at-will employment); id. § 2.03 (explaining cause requirements for contractual agreements for employment as to a definite term); id. § 2.05 (explaining the role of employer policy statements within the employment agreement); id. § 2.07 (discussing the implied duty of good faith and fair dealing within the employment relationship).
48. Id. § 5.01.
49. Id. § 5.02(a).
50. Id. § 5.02(c).
members.\textsuperscript{51} Employer discretion is also bounded by numerous antidiscrimination statutory schemes that apply to employer termination or discipline. Federal law protects employees from discrimination based on race, ethnicity, sex, sexual orientation, religion, age, and disability.\textsuperscript{52} State and local laws provide additional protections for these categories.\textsuperscript{53}

When employees are discharged otherwise lawfully, state law provides for unemployment compensation for a set period of time.\textsuperscript{54} Although states manage their own systems, as a general rule they require employers to pay into an unemployment insurance fund and require compensation when the employee is terminated, unless the employee has quit or has engaged in significant malfeasance.\textsuperscript{55} During the pandemic, the federal government paid an additional $600 a week in unemployment through the end of July 2020 and also provided assistance to independent contractors through a federal fund.\textsuperscript{56}

4. Health and Safety

Under the common law, employers have a duty to provide a reasonably safe workplace and warnings for dangerous working conditions.\textsuperscript{57} The Federal Occupational Safety and Health Act ("OSH Act")\textsuperscript{58} imposes on employers a general duty to provide safe working conditions.\textsuperscript{59} In addition

\begin{itemize}
  \item \textsuperscript{51} \textit{Id.} § 5.02(c) cmt. f.
  \item \textsuperscript{52} \textit{See, e.g.}, 42 U.S.C. § 2000e-2(a) (making it an unlawful practice to “discriminate against any individual with respect to his compensation, terms, conditions, or privileges of employment, because of such individual’s race, color, religion, sex, or national origin”); 29 U.S.C. § 623(a)(1) (providing similar protections against age discrimination within the employment relationship); 42 U.S.C. § 12112(a) (providing similar protections against disability discrimination); Bostock v. Clayton Co., 140 S. Ct. 1731, 1737 (2020) (finding that Title VII covers discrimination based on sexual orientation).
  \item \textsuperscript{53} 1 MICHAEL B. SNYDER, COMPENSATION AND BENEFITS § 8:4 (2016) ("Nearly every state has a fair employment practice (FEP) law, and most states also have their own administrative agencies to investigate charges of discrimination and enforce these FEP laws. Almost 200 local jurisdictions also have FEP laws and companion enforcement agencies.”).
  \item \textsuperscript{54} \textit{See} MARK A. ROTHESTEIN & LANCE LIEBMAN, EMPLOYMENT LAW 1051 (7th ed. 2011) ("Fifty states, the District of Columbia, and Puerto Rico have individual unemployment insurance (UI) programs determining the length of unemployment insurance benefits and their amounts for qualifying recipients.").
  \item \textsuperscript{57} RESTATEMENT OF EMP. LAW § 4.05 (2015). The duty has been recognized in all U.S. jurisdictions. \textit{See id.} Reporters’ Notes for cmt. a.
  \item \textsuperscript{58} 29 U.S.C. §§ 651–678.
  \item \textsuperscript{59} \textit{See} 29 U.S.C. § 654(a)(1) (requiring employers to “furnish to each of his employees employment and a place of employment which are free from recognized hazards”).
\end{itemize}
to this general duty, the Occupational Safety and Health Administration ("OSHA") enforces a complex regulatory framework as established through promulgated occupational safety and health standards. When one employee harms another as a result of tortious behavior, the employer is liable if that tort was committed within the employee’s scope of employment or if the employer later ratifies the conduct. Employers also have a common law duty to exercise care in selecting, retaining, and supervising their employees, and they are liable for harm to employees caused by their failure to exercise reasonable care in these responsibilities.

Under workers’ compensation laws, employers are responsible for workplace injuries that require medical treatment and may result in employee disability. The workers’ compensation model represents a bargain between employer and employees struck by state legislatures: Employees are covered for all workplace injuries without having to prove employer fault, and employers are only liable for statutory damages based on medical care and degree of disability. States often require employers to carry workers’ compensation insurance.

When workers are dealing with medical emergencies, federal law requires unpaid leave under the Family and Medical Leave Act ("FMLA"). Employees are given up to twelve weeks of unpaid leave a year for family or medical leave and are allowed to return to their job or an equivalent position. Eight states and the District of Columbia have paid family or medical leave statutes, and thirteen states and D.C. have paid sick leave.

60. Id. § 654(a)(2).  
61. RESTATEMENT OF EMP. LAW § 4.03(a)–(b) (2015).  
62. Id. § 4.04.  
63. See, e.g., Kerans v. Porter Paint Co., 575 N.E.2d 428, 432 (Ohio 1991) ("[A]n employer may be liable for failing to take appropriate action where that employer knows or has reason to know that one of its employees poses an unreasonable risk of harm to other employees."); Retherford v. AT&T Commc’ns of Mountain States, Inc., 844 P.2d 949, 973 (Utah 1992) (describing the elements of a claim of negligent employment).  
65. Shauhin Talesh, Insurance Law as Public Interest Law, 2 U.C. IRVINE L. REV. 985, 1001 (2012) ("[T]he workers’ compensation system emerged from a desire to create a new, workable, and predictable mode of handling accident liability that balanced the interests of labor and management.").  
68. Id. § 2612(a)(1).  
requirements. Federal plans for paid sick leave have been proposed by both parties.

Until recently, health insurance plans were regulated primarily by state law, with ERISA providing only framework protections. However, the Affordable Care Act ("ACA") created a new set of incentives and requirements for employers with respect to such insurance. The employer mandate requires employers of a certain size to purchase health insurance for their employees or provide funding for employees to buy their insurance on state exchanges. If employers fail to do so, they must pay a tax penalty. Despite fears that the ACA would drive employers out of the health insurance market, there has only been incremental movement away from providing insurance despite rising premiums.


73. The employer mandate is developed in 26 U.S.C. § 4980H. For a brief overview of the employer mandate, see Suja A. Thomas & Peter Molk, Employer Costs and Conflicts Under the Affordable Care Act, 99 CORNELL L. REV. ONLINE 56, 58–59 (2013).

74. See Amy Monahan & Daniel Schwarcz, Will Employers Undermine Health Care Reform by Dumping Sick Employees?, 97 VA. L. REV. 125, 127 (2011) ("[C]ommentators have generally focused on the prospect that employers will choose to drop health coverage entirely when ACA’s core reforms are implemented in 2014.").

5. Tax Responsibilities

Firms are also given responsibility for their employees when it comes to taxes. Employers must withhold their employees’ taxes and pay a share of Social Security and Medicare (FICA) and unemployment (FUTA) taxes. The Internal Revenue Service defines employees based on the common law control test. Employer withholding is extremely important to the public fisc; payroll taxes alone make up 35.9% of all federal revenues. And the consequences of an employer misclassification can be extremely costly, as the business is then subject to the mandatory back-tax formula.

B. Employment as Locus of Regulation

The legal obligations that employers must shoulder hinge on the concept of employment. Only employees are entitled to this specific set of legal protections. The concept of the employee dates back to the idea of “servant” in master and servant law. Under the common law of agency, masters are responsible for the torts of their servants if those torts were committed within the scope of employment. It was not until the Third Restatement of Agency that the official change from master and servant to employer and employee was recognized.

The federal legislation of the New Deal infused the concept of employment with specific regulatory responsibilities. In defining who fit the definition, this legislation took two approaches. Many statutes, such as the

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76. 26 U.S.C. §§ 3401(c), 3402.
77. Id. §§ 3101, 3121(d).
78. Id. §§ 3301, 3306(i).
79. Id. § 3121(d)(2) (defining an employee as, among other definitions, “any individual who, under the usual common law rules applicable in determining the employer-employee relationship, has the status of an employee”); 26 C.F.R. § 31.3121(d)(1)(c)(2) (finding an employment relationship “when the person for whom services are performed has the right to control and direct the individual who performs the services, not only as to the result to be accomplished but also as to the details and means by which that result is accomplished”); see 26 U.S.C. § 3306(i) (stating that “the term ‘employee’ has the meaning assigned to such term by section 3121(d)’); Rev. Rul. 87-41, 1987-1 C.B. 296, 298–99 (laying out a twenty-factor test to aid in “determining whether an individual is an employee under the common law rules”).
82. RESTATEMENT (SECOND) OF AGENCY § 220(2) (AM. L. INST. 1958).
83. RESTATEMENT (THIRD) OF AGENCY § 7.07(3)(a) (AM. L. INST. 2006) (defining an employee as “an agent whose principal controls or has the right to control the manner and means of the agent’s performance of work”).
NLRA, did not provide a definition of the term “employee.” The NLRA did not originally exclude independent contractors, and both the National Labor Relations Board (“NLRB”) and the Supreme Court originally held that so-called “newsboys” were statutory employees for purposes of the Act, even though they were considered independent contractors. However, Congress rejected this interpretation of the Act and added independent contractors specifically to the list of excluded categories. The Board then adopted the common law right to control test in excluding independent contractors. The Supreme Court sanctioned this test in *NLRB v. United Insurance Co.*, making clear that the Board had a range of discretion in implementing the test. Over time, the common law test for employment has become the statutory definition if that statute itself leaves the term undefined.

Using a different approach, the Fair Labor Standards Act (“FLSA”) defines “employ” to include “suffer or permit to work.” Because the FLSA defines employ more broadly than the common law standard used in most federal statutes, the Supreme Court has recognized that the FLSA may extend to cover workers beyond the reach of the common law agency test. This approach, known as the “economic realities” or “economic dependence” test, is generally interpreted to provide a more expansive definition to the term “employee.” The term “employee” was “to be determined broadly, in

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84. Excluded employees include agricultural workers; domestically employed healthcare or family care employees; public-sector employees; railroad, airline, and other transportation workers covered by the Railway Labor Act; independent contractors; and supervisors. 29 U.S.C. § 152(3).

85. *NLRB v. Hearst Publ’ns, Inc.*, 322 U.S. 111, 132 (1944). The Court explicitly rejected the common law distinction between employees and independent contractors, holding that the news vendors in question were “subject, as a matter of economic fact, to the evils the statute was designed to eradicate.” *Id.* at 127.


87. 390 U.S. 254, 258 (1968) (noting that “[t]here are innumerable situations which arise in the common law where it is difficult to say whether a particular individual is an employee or an independent contractor”). The Court required courts to uphold reasonable determinations “even though the court would justifiably have made a different choice had the matter been before it *de novo*.” *Id.* at 260 (quoting *Universal Camera Corp. v. NLRB*, 340 U.S. 474, 488 (1951)).


89. 29 U.S.C. § 203(g).

90. *See Darden*, 503 U.S. at 326 (noting that the FLSA “stretches the meaning of ‘employee’ to cover some parties who might not qualify as such under a strict application of traditional agency law principles”).

doubtful situations, by underlying economic facts rather than technically and exclusively by previously established legal classifications.”

That reference to “economic facts” became “economic reality” in later cases defining the category of “employee” in the context of the Social Security Act and the FLSA. According to the “economic realities” test, “employees are those who as a matter of economic reality are dependent upon the business to which they render service.”

In recognition of the FLSA’s broader coverage, courts have either implicitly or explicitly looked to the “reality” of the workers’ dependence on the putative employer. The focus on economic reality is meant to cut through formalistic trappings to get at the heart of the relationship.

Despite these dueling definitional approaches, the concept of employment has been fairly stable over time. It remains the most important economic relationship for most adults, with almost two-thirds working as employees. Because of its centrality, it has been used as a nexus of economic regulation covering a range of public policies. These obligations have incentivized a fair amount of regulatory arbitrage to try to avoid the

255, 278 (2013) (“As opposed to the traditional common law interpretation of joint employment that focuses only on limited indicia of employer control, this revolutionary test enables courts to look at true economic reality factors that reflect the actual situation.”).


93. United States v. Silk, 331 U.S. 704, 713 (1947) (“We concluded that, since that end was the elimination of labor disputes and industrial strife, ‘employees’ included workers who were such as a matter of economic reality.”) (discussing Hearst Publ’ns, Inc., 322 U.S. at 130).


96. See Sec’y of Lab. v. Lauritzen, 835 F.2d 1529, 1538 (7th Cir. 1987) (describing economic dependence as “the focus of all the other considerations”); Hopkins v. Cornerstone Am., 545 F.3d 338, 346 (2008) (“As a matter of economic reality, the Sales Leaders were dependent upon Cornerstone to such an extent that they could not plausibly be considered ‘in business for [themselves].’” (quoting Herman v. Express Sixty-Minutes Delivery Serv., 161 F.3d 299, 303 (1998))).

97. Mednick, 508 F.2d at 299–301 (characterizing the ultimate inquiries as: “Is [the worker] the kind of person meant to be protected by the F.L.S.A.? Is he ‘dependent upon finding employment in the business of others . . . . [one of] those who themselves are least able in good times to make provisions for their needs when old age and unemployment may cut off their earnings?’” (alteration in original) (quoting Fabs v. Tree-Gold Co-op. Growers of Florida, Inc., 166 F.2d 40, 44 (5th Cir. 1948))).

employment relationship. The much heralded gig or platform economy is at the forefront of this shift, with millions of workers moving to more flexible and online work arrangements. Proposition 22 in California has completely upended the efforts of the California Supreme Court and the state legislature to categorize these workers as employees. With momentum at their backs, platform companies are now reviewing their options in pushing for a non-employee agenda across the country. The stable consensus on the meaning of employment and its consequences may be on the verge of complete destabilization.

C. Difficulties for Employers and Workers

Even if workplace regulations are justified from a perspective of equity and fairness, they still exact a cost. The standard complaint from employers concerns the breadth and depth of regulations concerning the employment relationship. Although not often the subject of legal scholarship, the complexity of workplace laws is well-recognized. This is not to say that U.S. employment regulation is unusually burdensome internationally; most nations provide more significant restrictions on employer discretion, particularly with regard to termination. But the United States has been accreting additional layers of obligations upon the employment relationship.

99. In fact, many of these companies are engaging in “regulatory entrepreneurship”—pursuing a line of business in which changing the law is a significant part of the business plan.” Elizabeth Pollman & Jordan M. Barry, *Regulatory Entrepreneurship*, 90 S. Cal. L. Rev. 383, 383 (2017).


102. Stephen F. Befort & John W. Budd, *Invisible Hands, Invisible Objectives: Bringing Workplace Law & Public Policy into Focus* 130 (2009) (calling the U.S. system “a complex maze of common law doctrines and individual statutes on varied employment and labor law topics from racial discrimination to whistleblowing, from childbirth leave to Social Security benefits, from workplace safety to collective bargaining, from explicit minimum wage standards to tax subsidies for private health insurance”); Hirsch, supra note 11, at 89 (“The laws and regulations governing the American workplace reveal a level of complexity and uncertainty that rivals virtually any other area of law.”).

fairly continuously since the New Deal, and there are many complex features to workplace law.

Just to provide one example, the FMLA requires unpaid leave for up to twelve weeks a year for family or medical reasons while permitting the employee to return to an equivalent position after the leave. This requirement sounds straightforward and supports an important societal policy of care for oneself and one’s family. But the translation of statute into action can be quite uncertain. First, along with the birth or adoption of a child, employees are provided with leave if they have a “serious health condition that makes the employee unable to perform the functions of the position,” or if they need to care for a close relative with a serious health condition. The statute defines a serious health condition as “an illness, injury, impairment, or physical or mental condition that involves . . . [either hospitalization or] continuing treatment by a health care provider.” The regulations differentiate between treatment that includes a course of prescription drugs, which would be covered, and a course of over-the-counter drugs, which would not be covered. The regulations further define a serious health condition involving continuing treatment by a health care provider to require “[a] period of incapacity of more than three consecutive, full calendar days,” along with subsequent treatment “two or more times, within 30 days of the first day of incapacity” or “on at least one occasion, which results in a regimen of continuing treatment under the supervision of the health care provider.” Often it will not be clear at the onset of the illness whether it meets the requirements of a serious health condition. The employer must also determine if employees are eligible for FMLA leave. The employee must have worked at least 1,250 hours during the previous twelve-month period, must not be a key employee, and must be one of at least fifty

105. Id. § 2612(a)(1)(D).
106. Id. § 2611(11)(A)–(B).
107. 29 C.F.R. § 825.113(c).
108. Id. § 825.115(a)(1)–(2). The provision further requires that the “requirement in paragraphs (a)(1) and (2) of this section for treatment by a health care provider means an in-person visit to a health care provider. The first (or only) in-person treatment visit must take place within seven days of the first day of incapacity.” Id. § 825.115(a)(3).
109. Compare Caldwell v. Holland of Tex., Inc., 208 F.3d 671, 672–73 (8th Cir. 2000) (finding a child’s sudden onset of an ear infection may have been a serious health condition), with Weidema v. State Dep’t of Transp., No. A11-1397, 2012 WL 2873942, at *2 (Minn. Ct. App. July 16, 2012) (finding a biopsy for a potentially cancerous cyst was not a serious health condition when the cyst was revealed to be benign).
110. 29 U.S.C. § 2611(2).
111. Id. § 2614(b). A key employee is defined as “a salaried eligible employee who is among the highest paid 10 percent of the employees employed by the employer within 75 miles of the facility at which the employee is employed.” Id. § 2614(b)(2). Key employees can be denied
employees within a seventy-five-mile radius of the particular worksite. Other complications include the timing and categorization of employee leave, the use of paid leave, and the interaction between the FMLA and the Americans with Disabilities Act. Not surprisingly, human resource professionals find FMLA leave to be very challenging to properly track, label, and provide notice to employees.

Our network of regulations become manifold more complex when we consider state regulations. These regulations make things significantly more complicated for firms with geographic distribution of employees. As Jeffrey Hirsch has argued:

Most employers are at least regional, if not national and international, in scope. Even many small businesses either compete or have a presence in numerous jurisdictions. States’ current authority over much of the workplace fails to acknowledge this reality, and this failure comes at a cost. At best, multiple layers of regulations create complexities and redundancies that increase compliance costs and make enforcement more difficult. At worst, inconsistencies or outright conflict make compliance and enforcement nearly impossible.

Examining one of these sets of laws, Hirsch found that termination protections were “numerous, complex, and unnecessarily confusing,” with over twenty-five different federal statutes and rules from every state and numerous localities.

The complexity of modern workplace regulation hampers the enforcement of these requirements. Workers must know and understand the law’s provisions in order to understand their rights. If the laws are too complex, workers may have difficulty grasping when they are entitled to protection and when they are not. They may fail to consult with

reinstatement to their previous position if “such denial is necessary to prevent substantial and grievous economic injury to the operations of the employer.” Id. § 2614(b)(1)(A).

112. Id. § 2611(2).
114. Stephen Miller, HR Professionals Struggle over FMLA Compliance, SHRM Tells the DOL, SOC’Y FOR HUM. RES. MGMT. (Sept. 21, 2020), https://www.shrm.org/resourcesandtools/hr-topics/benefits/pages/hr-professionals-struggle-over-fmla-compliance-shrm-tells-the-dol.aspx (discussing “many of the challenges and frustrations that confront HR professionals as they comply with the [FMLA]”).
116. Hirsch, supra note 11, at 95 (describing these laws as “the result of incrementalism run amok”).
117. See Alison Green, No One Knows Their Legal Rights at Work, SLATE (Sept. 14, 2020, 5:55 AM), https://slate.com/human-interest/2020/09/labor-law-usa-know-your-workers-rights.html (“American workers are often largely unaware of the rights they do have.”).
attorneys—a necessary step, since many provisions are enforced through private rights of action.\footnote{118} Complexity even foils attorneys. A study of briefs by plaintiffs’ attorneys in employment cases found that many attorneys failed to raise important claims or rebuttals to defenses in their briefs.\footnote{119} Judges were not immune either, making mistakes on basic principles of doctrine.\footnote{120} At some point an overload causes systems to crash, rendering them unable to provide the workplace fairness that the law would seem to enact.

The rise of human resources management as a field is symptomatic of the growth of complexity in employment regulation. Now its own recognized academic subject,\footnote{121} the human resources field started with the premise that poor management practices were ultimately at fault for the rift between management and labor.\footnote{122} As the field has developed, it has focused more on increasing firm value.\footnote{123} Although the field is not focused solely on legal compliance, the focus on these matters is undeniably their responsibility, at least at an initial level.\footnote{124} The Society for Human Resource Management (“SHRM”) boasts a global membership of over 300,000, and it regularly weighs in with Supreme Court amicus briefs and regulatory comments on labor and employment issues.\footnote{125} With its own set of classes, certifications, and information networks, SHRM serves as the hub for a large set of professionals devoted at least in significant part to making sure that employers follow the law.

The purpose of these regulations and the firm infrastructure tasked with enforcing them is to protect employees and provide them with a higher level of benefits from employment. But the either-or aspect of employment

\begin{footnotes}
\footnote{118} Hirsch, supra note 11, at 99.
\footnote{119} Scott A. Moss, Bad Briefs, Bad Law, Bad Markets: Documenting the Poor Quality of Plaintiffs’ Briefs, Its Impact on the Law, and the Market Failure It Reflects, 63 EMORY L.J. 59, 63 (2013) (finding that “the vast majority of plaintiffs’ briefs omit available caselaw rebutting key defense arguments and lose at more than double the rate of competent briefs”).
\footnote{120} Id. at 66–67 (“[S]ome judges just get it wrong, eagerly granting summary judgment in defiance of Rule 56 standards that are too established to blame the lawyers.”).
\footnote{121} As a recent president of the Society of Human Resource Management (“SHRM”) said, “[p]erhaps the greatest human resources accomplishment . . . has been the worldwide recognition that human resources management is, indeed, a profession with a clearly defined body of knowledge.” Michael R. Losey, Mastering the Competencies of HR Management, 38 HUM. RES. MGMT. 99, 99–100 (1999).
\end{footnotes}
protections may in fact harm workers as well. Although individual workers may in some instances prefer independent contractor status, the package of benefits that accrue with employment status means that almost every worker would be economically better off as an employee.\textsuperscript{126} As a result, the line between employment and alternative statuses becomes increasingly higher stakes. Employment status means entitlement to all the benefits that society imparts upon employees. Others are left out. We have seen this division in other employment circumstances. For example, in the post-bankruptcy General Motors negotiations, the United Auto Workers consented to a split between then-current workers and future employees in which the latter workers received significantly less in pay and benefits.\textsuperscript{127} In academia, because tenured professors enjoy such significant employment protections, universities have strong economic incentives to hire nontenured faculty to teach a larger percentage of courses.\textsuperscript{128} Under these circumstances, the workplace can become divided into haves and have-nots, where one set of workers have significantly more privileged circumstances than others. The employee/independent contractor divide is one of these chasms.

Since these divides within the workforce generally favor incumbent workers, more senior workers, and more traditional workers, they can disproportionately burden younger, less senior, and more diverse workforce participants. Julie Suk has argued that job security protections can exacerbate racial inequality in employment, leading to tensions such as the 2005 riots and student protests against proposed labor law changes in France.\textsuperscript{129} The larger the burden of hiring new workers, the less likely employers will be to hire new workers. This stasis can slow the rate of social change and frustrate a workforce that would otherwise receive a higher number of opportunities.

\textsuperscript{126} ESTREICHER \& LESTER, supra note 113, at 14–15 (explaining that some workers may prefer to avoid “employee” status so that they can sue in tort for an injury rather than being limited to workers compensation, or so they can avoid employment-related fiduciary obligations against competition).


\textsuperscript{128} Colleen Flaherty, A Non-Tenure-Track Profession?, INSIDE HIGHER ED (Oct. 12, 2018, 3:00 AM), https://www.insidehighered.com/news/2018/10/12/about-three-quarters-all-faculty-positions-off-tenure-track-according-new-aaup (finding that about three-quarters of all faculty positions are off the tenure track).

\textsuperscript{129} Suk, supra note 103, at 76 (“The historical and current sociological data support the conclusion that the Labor Code’s employee job security protections have contributed significantly to employers’ propensity to engage in both rational and irrational discrimination against racial minorities in hiring.”).
This description of the cons of employment regulation has been painted with a broad brush. The intent is to frame some of the common costs and concerns raised by our admittedly byzantine system. But there are strong arguments for employment regulations as well.

D. Arguments for Regulations

We have seen that the legal rules imposed on employers are extensive and onerous. For the most part the rules are mandatory, not default rules that can be changed by individual employers. They create significant costs, most obviously for employers, but sometimes for employees as well. What sorts of arguments justify these rules? And do those arguments justify making the rules mandatory? The arguments obviously vary for different rules, but there are certain types of arguments that are widely invoked in justifying these extensive mandatory employment rules.

At the broadest and most philosophical level, there is an understandable interest in promoting the autonomy of employees. Many see the employment relationship as one of dominance of employees by their employers. Such domination is inherently objectionable under a liberal worldview that emphasizes the ability of all to act autonomously in choosing how to live their lives. Domination may also lead to outcomes that disadvantage employees, because they have little bargaining power in setting the employment contract. The arguments that follow can be understood as providing a more detailed understanding of elements of this general concern with autonomy and domination.

One important source of inequality in the employment relationship is that in many ways employees are likely to have more limited information than employers, particularly when one compares the information available to individual employees with that available to an employer that is a relatively large and sophisticated organization. Most employees are not likely to have access to information about the firm’s financial condition. They are also less likely to understand relevant laws and circumstances in relevant markets in which the employer operates. Large organizations with significant resources exist in good part to collect, pool, and deploy information. As we shall see, one important part of our proposal for employee involvement in governance


is to give employees access either to these same organizational resources for information or to the competing resources of a union.\textsuperscript{133}

A variety of cognitive biases may affect the ability of employees to bargain effectively. They may be short-sighted, either in that they do not understand or give too little weight to the long-term effect of arrangements they agree to.\textsuperscript{134} They may be overly optimistic that a variety of risks will not happen to them.\textsuperscript{135} They may be overly trusting when entering into an employment relationship.\textsuperscript{136}

Collective action problems may also block employees from effectively bargaining individually to protect themselves within the employment relationship. These problems may involve collective action among employees working within the same firm, or among employees across firms, or among potential workers seeking employment. Within a firm, many elements of the workplace are local public goods.\textsuperscript{137} The safety of a building or assembly line, for instance, is largely the same for all workers involved. Many of the elements of some collective benefits are also local public goods. For instance, in providing health benefits, an employer will negotiate an arrangement with one insurer or health provider—offering many different insurers or providers for each employee to choose among would involve much higher administrative costs. Like all public goods, there will be a tendency to underprovide, as each employee acts as a free rider and hopes others will lobby the employer to provide more of the good or better quality.

For employees not in the same firm, collective action problems could create a race to the bottom. That is, given the relative bargaining position of employers and employees, if the former make lowball offers, the latter will feel forced to accept them—even if all employees feel they are unfair, if some employees do accept, others will be left out in the cold. Signaling and adverse selection may worsen this problem. For instance, on the subject of at-will employment, employees who insist on for-cause employment may risk signaling they expect that employers will want to fire them, while employers that offer protection against firing may attract employees likely to need that protection.\textsuperscript{138}

\begin{footnotes}
\item[133]See infra note 268 and accompanying text.
\item[134]Sunstein, supra note 21, at 242 (finding that recent evidence suggests workers are myopic or short-sighted).
\item[135]Id. at 241 (noting that “people tend to be risk optimists”).
\item[137]Sunstein, supra note 21, at 211.
\item[138]Sunstein, supra note 21, at 225 (“An employer who is willing to offer job security might find that it is attracting marginal workers. At the same time, an employee who presses hard for job security might be signaling that he will deserve to be discharged.” (footnote omitted)).
\end{footnotes}
Another source of domination and inequality in bargaining power is the underlying inequality of wealth and income. An understanding of social equality may imply that such distributive inequality should “not be automatically replicated into inequalities in other areas of life that are key to participation in society.”139 Employment is one such key area of social participation. Wealth inequality reduces worker bargaining power, especially when unemployment is high, as many vulnerable workers need their jobs far more than their employers need them.140

A final type of reason for strong, mandatory employment law protections is third-party effects. Perhaps the most important third parties are taxpayers and the government. For instance, if employers offer poor health care or retirement benefits, society may be caught having to provide for struggling employees.141 Later, once we have introduced the possibility of employee involvement in firm governance, we will see significant potential third-party effects, such as on customers and the environment.142

E. Mandatory vs. Default Rules and Altering Rules

We have now briefly surveyed both leading benefits of and justifications for employment regulation143 as well as leading costs created by that regulation.144 Most legal obligations imposed on employers are mandatory. That is, if one meets the statutory definition of an employer with the requisite number of employees, and does not fall within an exception, one must follow the rule. There is no procedure by which a particular employer can modify the rule. That contrasts strongly with the area of corporate law, and more generally business association law, where most rules are defaults that can be modified by a particular company. There are some exceptions to the generally mandatory nature of employment regulation. For example, under the Voluntary Protection Program, employers with an approved safety program are subject to a looser enforcement system by OSHA.145 Some states have similar programs in workplace safety enforcement.146 Various internal company procedures, such as training and codes of conduct, help

140. Id. at 238.
141. Davidov, supra note 130, at 17.
142. See infra Section II.C.
143. See supra Section I.D.
144. See supra Section I.C.
145. Lobel, supra note 21, at 418 (“The Voluntary Protection Program allow[s] companies with exemplary safety records to take over the role of OSHA inspectors themselves and to be exempt from regular inspections.”).
146. Id. (describing California Cooperative Compliance Program).
protect against liability under antidiscrimination laws. But these are exceptions to the general rule of mandatory employment law.

A variety of arguments, particularly commonplace for those versed in law and economics, suggest advantages from rules that are default rather than mandatory. Most broadly, the same fundamental value of autonomy that is used to justify workplace regulation can also be invoked to question mandatory legal rules. If individual employers and employees both choose not to be bound by a particular rule, shouldn’t we accept their choice? The other arguments canvassed next suggest various reasons why employees might have good reason to choose not to have some rules applied to them.

Regulators, be they legislators or executive agencies, may make poor choices in imposing employment regulations. They may underestimate the costs generated by a regulation, or overestimate the value that employees place on the protections offered by it. When a regulation is default, such regulatory error will be less costly as employees and employers opt out of ill-considered rules.

Differences among employees create another problem for mandatory rules. Rules typically come as one size fits all, but they may not fit all employees equally well. Limits on hours and overtime requirements may be valued more by middle-aged parents with children than by childless workers in their twenties. Healthy young employees may be willing to gamble with a barebones health insurance policy more than older employees with significant health risks. College professors may care less about having early retirement benefits than manual workers. And so on. With default rules, there is more room to mold the set of applicable rules to the needs of particular workers, or at least workforces.

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147. Id. at 421 (“[G]overnance strategies may operate as a defense against liability or against the grant of punitive damages in case of discrimination allegations by employees.”).

148. Stephen M. Bainbridge, Director Primacy: The Means and Ends of Corporate Governance, 97 NW. U. L. REV. 547, 584 (2003) (“One of the chief tenets of contractarianism is that the law ought to facilitate private ordering. The contractarian preference for default rules rather than mandatory rules in corporate law statutes follows from this proposition, as default rules provide the flexibility necessary for private ordering.”); Steven J. Burton, Default Principles, Legitimacy, and the Authority of a Contract, 3 S. CAL. INTERDISC. L.J. 115, 116 (1993) (“In contrast to mandatory terms, the default rules are displaced by the parties’ agreement to the full extent of the agreement. Thus, default rules respect the parties’ autonomy to structure their own transaction.”); see generally richard h. thaler & cass r. sunstein, nudge: improving decisions about health, wealth, and happiness (rev. ed. 2009) (discussing how regulators can use incentives to make sure people make better choices).

149. For instance, some have argued that OSHA has set overly-strict standards for exposure to some toxic substances. See John P. Dwyer, Overregulation, 15 ECOL. L.Q. 719, 721–26 (1988) (reviewing john m. mendeloff, the dilemma of toxic substance regulation: how overregulation causes underregulation at OSHA (1988)).
The wide range of rules applicable to the employment relationship deepens these problems with mandatory rules. Even if each individual rule is sensible for most employees, the full package of rules may not be. In part that is due to the multiplicative complexity of compliance. In part it is because employees, and whole workforces, may differ in the weight they place on the value of different rules. As the costs of complexity rise, it may make sense to loosen or waive some rules, but which rules are best weakened may vary among employees and employers. Regulators are even more likely to make mistakes in evaluating the interactive impact of multiple rules than they are in evaluating the impact of individual rules on their own.

So far, we have assumed a dichotomy between mandatory and default rules. Section I.D gives some arguments in favor of mandatory rules, while this Section identifies some drawbacks of such rules. But we often face a less stark choice than simply mandatory or default rules. For one thing, a rule can give employees or employers a degree of choice, while setting a mandatory floor (or ceiling). Of more interest for our purposes here, in setting default rules, regulators can also specify what process is required for an individual or organization to opt out of the default rule. These rules for opting out of a default rule have been called “altering rules.”

Attention to altering rules adds new options for addressing the tradeoffs between mandatory versus default rules. One can set a default rule that strongly protects employees. Then, employers could be allowed to opt out of that rule, but the altering rule can be devised in a way to protect employees against abuses while still allowing them to opt out where there seems to be good reason to do so, and where concerns about potential abuses are reduced by the process required for opting out. Corporate law, for instance, contains a variety of default rules protected by somewhat “sticky” altering rules that protect shareholders. These include requirements for shareholder approval of certain major transactions, supermajority provisions, and sunset provisions.

For this Article, the type of altering rule that interests us concerns employee involvement in corporate governance. This could take the form of employee election of corporate directors, union representation, or works

150. See supra Section I.A; see generally Hirsch, supra note 11.
151. See supra note 115 and accompanying text.
152. Sunstein, supra note 21, at 245.
154. McDonnell, supra note 153, at 397–98 (applying this approach to the protection of shareholders in corporate law).
155. Id. at 402–13 (discussing these rules).
councils along the German model.\textsuperscript{156} Allowing companies that follow such an altering rule to opt out of some employment regulations would alleviate some of the problems with mandatory rules identified in this Section.\textsuperscript{157} If the employee governance mechanism is properly structured with necessary safeguards, then when employees collectively have decided to modify some legal rules, we would be relatively confident that the governance process has addressed the informational, cognitive, incentive, and collective action problems identified above\textsuperscript{158} that are used to justify making rules mandatory. Of course, the devil is in the details—what structural safeguards are needed to give assurance that decisions to opt out genuinely reflect the considered best interests of the affected employees? We shall have to address that question below.

II. Employers as Firms

In Part I we explored the many legal responsibilities that are tied to the employment relationship. These all attempt to protect employees. We argued that there should be considerable leeway to vary the rules in firms with adequately empowered employees, an argument we shall elaborate in later Parts.\textsuperscript{159} But advocating for employee involvement implicates the interests of shareholders and other stakeholders. Would it be good for them? Does involving employees in firm governance constitute good corporate governance, not simply good protection of employees? Yes. Employees and shareholders are the key inside participants in firm production, and involving them in governance will increase value created for all firm stakeholders. In defending this claim, we first critically review the leading arguments usually made to defend the prevailing American focus on the interests of shareholders in governing corporations.\textsuperscript{160} We then show how core concepts from the economic theory of the firm support involving employees in governance, situating them as core insiders along with shareholders.\textsuperscript{161} Finally, we suggest reasons why employees will tend to support decisions that favor the interests of other stakeholders, such as customers, local communities, and the environment.\textsuperscript{162}

\begin{itemize}
  \item \textsuperscript{156} We discuss the choice among these various forms of employee governance below. See \textit{infra} Part III.
  \item \textsuperscript{157} Sunstein, supra note 21, at 264–66 (suggesting that some variation from statutory rules could be allowed when approved by a union representing employees).
  \item \textsuperscript{158} See supra Section I.D.
  \item \textsuperscript{159} See \textit{infra} Part IV.
  \item \textsuperscript{160} See \textit{infra} Section II.A.
  \item \textsuperscript{161} See \textit{infra} Section II.B.
  \item \textsuperscript{162} See \textit{infra} Section II.C.
\end{itemize}
A. Shareholder Primacy

The leading economic theories of the firm are far from intrinsically hostile to governance arrangements that empower employees. However, as the economic theory of the firm was incorporated into legal scholarship, it was closely associated with perspectives that focused on promoting shareholder wealth maximization and empowering only shareholders (at most) above all other stakeholder groups. These perspectives both reflect basic structural realities of governance in corporate law and also helped shape understanding of that law.

The core structural facts of corporate law are that the board of directors controls most decisions, only shareholders elect directors, and only shareholders vote alongside the board on certain fundamental transactions. This exclusive shareholder franchise sits alongside the general norm in Delaware law that the fiduciary duty of directors requires an exclusive ultimate focus on the interest of shareholders. Scholars seeking to justify the current reality of corporate law must defend this focus on the interests of shareholders exclusively.

The leading scholarly argument favoring an exclusive focus on shareholder wealth maximization as the objective of corporate decision-making has been that shareholders are the residual claimants. Common shareholders are not promised any set financial return. Rather, they have the ultimate right to profits earned after all other claimants with fixed contractual rights have been paid. Residual claimants have a special role because it is harder to write a contract protecting their interests. All decisions made by corporate managers affect the return of the residual claimants, and no explicit contract can instruct managers how to make all decisions. Under this

163. See infra Section II.B.

164. Leo E. Strine, Jr., Our Continuing Struggle with the Idea that For-Profit Corporations Seek Profit, 47 WAKE FOREST L. REV. 135, 153 (2012) (“The whole design of corporate law in the United States is built around the relationship between corporate managers and stockholders, not relationships with other constituencies. In the corporate republic, only stockholders get to vote and only stockholders get to sue to enforce directors’ fiduciary duties.”).

165. See, e.g., eBay Domestic Holdings, Inc. v. Newmark, 16 A.3d 1, 26 (Del. Ch. 2010).


167. See supra note 166.
theory, choices that maximize firm profits will maximize total social surplus, assuming that all social costs and benefits are adequately priced in the goods and services consumed and sold by firms.\textsuperscript{168}

There are a variety of problems with these arguments for the shareholder wealth maximization norm. Employees are often significant residual claimants too, as the income and future prospects of employees depend upon their employer’s profitability.\textsuperscript{169} Shareholders do not have incentive to maximize the financial surplus a firm generates because limited liability makes them prefer overly risky actions.\textsuperscript{170} Shareholders will not generally agree on maximizing shareholder value as the sole valuable goal.\textsuperscript{171} Finally, the assumption that input and output prices internalize all relevant social costs and benefits is heroic.\textsuperscript{172}

Another leading argument for shareholder wealth maximization is that shareholders have more homogenous interests than other stakeholders, and hence will conflict less in making decisions.\textsuperscript{173} However, more recent scholarship has emphasized that shareholders are quite varied, with differences in time horizon, risk preferences, voting rights, and non-financial preferences.\textsuperscript{174} Even where shareholders agree on wealth maximization as a goal, they may disagree on how to achieve that goal.\textsuperscript{175} Thus, conflict exists among shareholders as well as other stakeholders, including employees.

Many scholars who believe that maximizing shareholder wealth is the proper end of corporate law advocate relatively strong shareholder power to ensure managerial accountability.\textsuperscript{176} However, some who accept that end

\textsuperscript{168} ROBERT C. CLARK, CORPORATE LAW 389–90 (1986); EASTERBROOK & FISCHEL, supra note 166, at 36.
\textsuperscript{169} See infra notes 190–191 and accompanying text.
\textsuperscript{170} Jensen & Meckling, supra note 166, at 334.
\textsuperscript{172} See infra Section II.C.
\textsuperscript{174} See supra note 171.
nonetheless believe that shareholders should have quite limited power, leaving boards and managers wide discretion to decide how best to maximize shareholder wealth. Stephen Bainbridge’s board primacy theory argues this position (which aligns well with Delaware corporate law),\(^{177}\) drawing strongly on the tradeoff between authority and responsibility emphasized by Kenneth Arrow’s theory of corporate governance.\(^ {178}\) However, Bainbridge does not explain why that tradeoff should always be decided in favor of authority.\(^ {179}\)

Margaret Blair and Lynn Stout offer a different defense of board primacy, one that serves as a transition to alternative approaches to corporate governance.\(^ {180}\) Drawing on Rajan and Zingales’s theory of access to resources,\(^ {181}\) they conceive of the board as a mediating hierarch that regulates resource access for competing groups of corporate insiders, with none of them given much power so that the hierarch can deal fairly with all.\(^ {182}\) They thus do not see the interests of shareholders as being privileged, and in other work Blair argues for a more formal role for employees in corporate governance.\(^ {183}\) However, in their joint work Blair and Stout accept the existing corporate law framework in which only shareholders are empowered to elect the board, even though that framework does not seem to follow from their theory.\(^ {184}\)

**B. Employees and Firm Governance**

We reject the above arguments for privileging shareholders. Our approach would transform both the allocation of power and the understanding of the appropriate objective function for businesses. In allocating power, we suggest a role for employees, either in choosing the board of directors (or comparable leading decisionmaker), choosing representatives to a body that makes major employment-related decisions, or choosing a union to bargain for employee interests.\(^ {185}\) In understanding the objective function of

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177. Bainbridge, supra note 166.
182. Blair & Stout, supra note 180.
184. Hayden & Bodie, supra note 171, at 2436.
185. We discuss the choice among these forms of employee governance in Part III.
businesses, we would conceive of it as balancing the interests of shareholders and employees. Employees are at the heart of the core productive activities that define a firm. That makes employees vulnerable to opportunistic decisions that hurt them, gives them access to crucial information that can benefit the business, and makes motivating effective employee behavior critical to firm success.

One argument for empowering employees flows from the economic theory of the firm. If a party to a relationship invests heavily in property that is much more valuable within the relationship, that person may then find it hard to exit the relationship and may thus lose bargaining power. Relationships should be structured to limit this hold-up problem. Giving a vulnerable party power over decisions is one such way of structuring relationships. Shareholders of a corporation are one vulnerable group, insofar as they finance the purchase and development of firm-specific physical and reputational capital. Indeed, this is another standard argument in favor of shareholder primacy.

But many employees invest heavily in firm-specific human capital—economist jargon for knowledge and skill that is valuable only while working within a given business. Think, for instance, of knowledge about who within an organization can best help solve problems of different types, or knowledge of vocabulary and operating procedures unique to a business. This specialized knowledge makes employees residual claimants as well. As their firm-specific human capital grows, employees become increasingly tied to the firm, since they are more valuable working there than anywhere else. Although they may receive wages set at a specific amount by contract, their job security with associated future advancement, wage increases, and pensions depends on the prosperity of their employer. Moreover, the stake of employees in a firm is inherently undiversified—most persons have only one job at a time. Shareholders in public companies can easily diversify their

186. And perhaps the interests of other stakeholders.
189. See supra note 188.
investments. Thus, the standard economic theory of the firm suggests that employees are due at least as much protection and control as shareholders.

Empowering workers can also improve the functioning of firms in several crucial ways tied to information that employees learn through their work. First, employees learn much about a business’s affairs as a byproduct of their work. This information can generate useful ideas for how to produce more efficiently, ways to improve customer satisfaction, and potential new investment opportunities. Knowledge-based theories of the firm point to this as an important factor in productivity, and the growing importance of knowledge in many firms may argue for a better integration of employees within firm governance.

Employee information is also useful for holding managers accountable—employees will often know when those in charge are misbehaving. Particularly in public companies, employees are likely to be far better informed than shareholders. Thus, employee governance may improve the authority/responsibility tradeoff that Arrow emphasizes, assuming one treats this as a genuine tradeoff rather than as an argument for always favoring authority à la Bainbridge. Note that both of these uses of information improve firm functioning generally, making a larger surplus available to distribute for employees, shareholders, and other participants.

There is a surface tension between this informational argument favoring employee governance and the informational argument favoring mandatory employment regulation, namely that employees need protection due to an informational disadvantage vis-à-vis employers. The two points do not conflict. There are various types of information that are relevant to employee welfare and firm governance. Employees have natural access to some types of information, particularly concerning working conditions, and some aspects of relations with customers as well. Most employees lack access to

194. McDonnell, supra note 179, at 142–43.
195. See supra note 132 and accompanying text.
other important sorts of information, including the company’s financial position and complicated legal regulations.

Involving employees in governance decisions may also improve their job satisfaction and motivation. Research on procedural justice suggests that if people believe decisions are made in a fair way, they will be more likely to abide by the decisions and to promote the goals of the business. This will reduce the bonding and monitoring costs required to get employees to do their jobs well. This is another way that employee governance may increase the total firm surplus available to distribute among all stakeholders, including shareholders.

Despite these arguments for empowering employees, there are significant concerns. The argument about the relative homogeneity of shareholders reducing politicization leads to a mirror-image critique of employee governance as increasing decision costs. The problem is worse if one combines both shareholders and employees in governance, as the two groups may conflict frequently. This common criticism of codetermination can be a real concern, but it is often over-blown. We have already seen that shareholders are quite heterogeneous themselves, reducing their advantage over employees. Furthermore, there are a variety of ways to reduce the costs of employee governance. Employees and managers could learn how to manage the decision process more effectively. They could learn in many ways: in school (including business school), through experience in more participatory organizations, or with the help of


199. See supra note 173 and accompanying text.

200. See supra note 173 and accompanying text.

201. For good discussions of codetermination, see Employees’ Co-Determination in the Members States of the European Union 23–24 (Theodor Baums & Peter Ulmer eds., 2004); Katharina Pistor, Codetermination: A Sociopolitical Model with Governance Externalities, in Employees and Corporate Governance 163 (Margaret M. Blair & Mark J. Roe eds., 1999); Stefan Prigge, A Survey of German Corporate Governance, in COMPARATIVE CORPORATE GOVERNANCE: THE STATE OF THE ART AND EMERGING RESEARCH 943 (K.J. Hopt et al. eds., 1998).

202. See supra notes 174–175 and accompanying text.

supporting persons and organizations such as lawyers, consultants, and banks. This suggests significant network effects and path dependence: The more widespread employee governance is, the more likely it would be to find such institutional support, and vice versa.204

C. Employees and Other Stakeholders

Company decisions affect other stakeholders too, such as creditors, customers, suppliers, local communities, and the environment. Increasing attention is being paid to stakeholder interests.205

Much corporate law activism and scholarship criticizing the shareholder primacy approach has focused on the interests of multiple stakeholder groups.206 We agree with the move away from shareholder wealth maximization, but we also think that in general employees and shareholders have a more central place within the firm than other stakeholders.207 The above arguments for employee involvement in governance do not apply to other stakeholders in most circumstances. Other stakeholders do not usually make significant firm-specific investments in physical or human capital, and hence are more able to exit and do business with other firms. Other stakeholders also typically do not acquire as much valuable information about firms in their relationships with them. Since other stakeholders are typically not acting on behalf of a firm in their relationship, they do not need to be motivated to act loyally. In most circumstances, persons other than managers, shareholders, and employees are not directly involved in joint production activities.208 The other stakeholder groups are not insiders in the same manner as employees.209 There are circumstances where a stakeholder group should be given a central voice in firm governance. Consumer and supplier cooperatives have a long history.210 But they are exceptions, albeit notable ones.

Though in most cases it does not make sense to give stakeholders other than employees and shareholders formal voting power, it is good if those who

204. McDonnell, supra note 191, at 376.
205. The literature is voluminous. For recent thoughts on related developments, see Hayden & Bodie, supra note 171; Brett McDonnell et al., Green Boardrooms?, 53 CONN. L. REV. 335 (2021); Brett H. McDonnell, From Duty and Disclosure to Power and Participation in Social Enterprise, 70 ALA. L. REV. 77 (2018).
207. Hayden & Bodie, supra note 171, at 2456–57, 2476; McDonnell, supra note 191, at 349.
208. Hayden & Bodie, supra note 171, at 2457, 2476.
209. Id. at 2455–58.
do have power are inclined to take the interests of others into account. The standard argument for shareholder primacy denies this. So long as market prices for inputs and outputs reflect social costs and benefits, maximizing firm profits will maximize net social value. Markets will do much to reflect social costs, particularly when one considers reputational effects. Where prices and reputation fail to internalize all important social effects, the standard argument is that other forms of legal regulation outside corporate law should limit harmful behavior.\textsuperscript{211} However, while market, reputational, and regulatory protections go a long way in reducing externalities, they all have serious shortcomings.\textsuperscript{212} Hence, we want business managers to take into account the interests of various stakeholders, above and beyond their impact on long-term profits.

Another argument for involving employees in governance is that they are often more likely than shareholders to have interests aligned with those of other stakeholders who we want to protect. It is a common argument that the shareholder wealth maximization norm has caused managers to focus on short-term profits in ways that harm many other interests.\textsuperscript{213} Might employee representatives behave differently? They might. Insofar as public harms generated by businesses have mainly local effects, employees, who live where the business is located, may care more about those effects than more dispersed shareholders.\textsuperscript{214} For shareholders with a significant financial stake in a business, that large stake may cause them to focus more on profits than is the case for employees.\textsuperscript{215} In contrast, there is some evidence that smaller firms and firms located in communities with higher social capital pollute less.\textsuperscript{216} Also, insofar as the traditional understanding of shareholding focuses on financial returns, the focus on money may make it less likely that shareholders will follow other-regarding norms than employees. That is not to say that employee governance will always be a boon to other stakeholders—sometimes it will not. But overall we suspect that employee involvement in governance will be good for other stakeholders.

\textsuperscript{211} Friedman, supra note 15.  
\textsuperscript{212} See McDonnell, supra note 191, at 359; McDonnell, supra note 205, at 347.  
\textsuperscript{214} McDonnell, supra note 191, at 361.  
\textsuperscript{216} Don Grant, Andrew W. Jones & Mary Nell Trautner, Do Facilities with Distant Headquarters Pollute More? How Civic Engagement Conditions the Environmental Performance of Absentee Managed Plants, 83 SOC. FORCES 189 (2004).
III. SYSTEMS OF EMPLOYEE GOVERNANCE

The history of employee participation in firm governance is well-established and varied. In this Part, we consider three types of employee governance: union representation, shop floor governance, and board representation. Under our current system of labor law, employees select unions to represent them in bargaining over wages and the conditions of employment. Alternatively, shop floor governance, such as works councils or the Zappos holacracy model, creates structures through which employees participate in the day-to-day operations at their workplace. And with board representation, employees elect some percentage of representatives to the board of directors. Together, these three systems offer potential mechanisms through which employees can participate in firm governance. Below, we briefly survey these possibilities and evaluate their value in constructing a more robust method of worker governance.

A. Union Representation

Our current labor unions have their genesis in both artisanal craft guilds and the social movements of the early industrial era. Craft guilds date from the middle ages when groups of learned tradesmen created associations to preserve their traditions and protect their business interests.217 Beginning in the early nineteenth century, U.S. journeymen workers formed craft unions which grew to flourish; sixty-two such unions had been formed by the end of the 1800s.218 In the massive factories of the Industrial Age, unions focused on the plight of unskilled workers and relied on mass organizing, strikes, and protest. The line between these approaches was roughly the divide between skilled artisanal workers protecting their trades and industrial workers fighting for survival wages and basic rights.219 Labor law was federalized in 1935 through the Wagner Act, which provided for (1) the right to join and support unions, (2) a mechanism to select union representation through elections, and (3) the regulation of employer unfair labor practices, such as discrimination against union activity.220 This model has been modified over time—for example, to regulate secondary picketing and require democratic governance within labor organizations—but it has kept the basic structure of exclusive representation, collective bargaining, and protection of employee

218. Id. at 18.
rights. Even public-sector unions, which are governed by state law, follow these basic building blocks.\footnote{221 Cf. Martin H. Malin, Ann C. Hodges & Joseph E. Slater, Public Sector Employment 2 (2d ed. 2011) (noting the three primary differences between public and private sector labor law: the extension of civil service and constitutional law in the public sector; the higher union density in the public sector; and the application of certain employment rules in the public sector).}

The raison d’être of private-sector labor law is collective bargaining. When recognized or certified as representatives, unions are empowered to bargain in good faith with the employer on behalf of the workers; the employer must bargain with the union or else it commits an unfair labor practice.\footnote{222 29 U.S.C. § 158(a)(5) (setting forth the duty to bargain); id. § 158(d) (describing the duty to bargain); id. § 159 (establishing the process to select the employees’ collective representative).} The rest of labor law facilitates this bargaining relationship: Employers are not permitted to fire or punish workers for their support of the union.\footnote{223 Id. § 158(a) (prohibiting unfair labor practices by employers).} This system of collective bargaining has been called “industrial democracy” or “workplace democracy,” and it calls forth imagery of elections, representation, and governance.\footnote{224 See Becker, supra note 20, at 496–97 (discussing how NLRA supporters touted the virtues of industrial democracy as a form of democratic governance); Marion Crain, Building Solidarity Through Expansion of NLRA Coverage: A Blueprint for Worker Empowerment, 74 Minn. L. Rev. 953, 967 (1990) (describing the Wagner Act’s “vision of workplace democracy”).} Research has demonstrated that unions have negotiated better terms and conditions of employment for represented employees: higher wages, just-cause termination protections, grievance-arbitration processes, and stronger benefits.\footnote{225 Jake Rosenfeld, What Unions No Longer Do 1–2 (2014); see Richard B. Freeman & James L. Medoff, What Do Unions Do? 43–60 (1984) (discussing studies of the union wage effect); David G. Blanchflower & Alex Bryson, What Effect Do Unions Have on Wages Now and Would Freeman and Medoff Be Surprised?, 25 J. Lab. Econ. 383, 391 (2004) (finding a 17.0% private sector union wage effect and a 14.5% public sector union wage effect in the late 1990s).} Unions can also work with employers to tailor collective bargaining agreements toward the particular experiences of the workers involved. Workers vote for their collective representatives and also generally vote to approve the collective bargaining agreements that they negotiate.\footnote{226 Unions are not required to put their contracts to a vote, but most do as a matter of practice. Alan Hyde, Democracy in Collective Bargaining, 93 Yale L.J. 793, 793–95, 807 (1984) (noting that unions need not offer employees a vote on contract ratification). Several big “no” votes from the last year include the membership vote on the International Alliance of Theatrical Stage Employees (IATSE) Basic Agreement as well as workers at John Deere and Kellogg’s. See Gene Maddaus, IATSE Contract Ratification Decided by Razor-Thin Vote Margins in Two Guilds, Variety (Nov. 15, 2021), https://variety.com/2021/film/news/iatse-contract-vote-razor-thin-margins-1235112711/; Noam Scheiber, John Deere Workers Reject a Revised Contract Proposal, Extending Their Strike, N.Y. Times (Nov. 2, 2021), https://www.nytimes.com/2021/11/02/business/john-deere-strike-union-contract.html; Chris Isidore, Kellogg Workers Reject Tentative Labor Deal, Vote to Stay on Strike, CNN (Dec. 7, 2021, 1:58 PM), https://www.cnn.com/2021/12/07/business/kellogg-strike-vote/index.html.}

Labor organizations can also
consolidate power as collective representatives and may call out the workers to strike to reinforce their negotiation positions. This mix of democracy and power is why many reformers and academics still see labor unions as the best mechanism for worker empowerment and just workplaces.

From our perspective, however, there are some significant weaknesses in the labor-law-only approach to workplace governance. One is pragmatic. Unfortunately, only a small percentage of workers now have collective representation. The percentage of unionized private sector employees has been steadily shrinking since its 1950s heyday, from a high of about 35% to the current 6.7%. Were this a transitory phenomenon, it might be less concerning. But the percentage of unionized workers has been trending downwards ever since the 1960s—an inexorable slope that only began to flatten when the numbers became extremely small. Efforts at labor law reform have occasionally surfaced, only to fail to pass and then disappear. Even if reforms were to pass, increased unionization rates are no certainty: Along with weak labor laws, the decline in union representation has also been blamed on globalized markets, free trade, shifts away from manufacturing towards the service and information sectors, and changes in employee interest in collectivized bargaining. We are certainly not saying to give up on collective bargaining, but at the same time we cannot wait for it to resume its earlier role within the economy.

Moreover, from a governance perspective, there is a larger structural problem with labor law: It does not provide true governance power. Employers need only bargain in good faith—there is no requirement that the

227. See ESTREICHER & BODIE, supra note 219, at 157–58; see also Nicholas Kristof, The Cost of a Decline in Unions, N.Y. TIMES (Feb. 19, 2015), http://www.nytimes.com/2015/02/19/opinion/nicholas-kristof-the-cost-of-a-decline-in-unions.html (describing how unions have been integral to maintain the middle class and suggesting that the decline in unions has led to income inequality).
229. The slow fade of labor unions has been a concern of academics since the 1980s. Estlund, supra note 9, at 1527–28; Michael H. Gottesman, Wither Goest Labor Law: Law and Economics in the Workplace, 100 YALE L.J. 2767, 2767 (1991) (“The long and steady decline in the percentage of private-sector employees represented by unions—a decline now in its fourth decade—preoccupies all thinking about American labor law today.” (footnote omitted)).
230. It seems that this will be the fate of the Protecting the Right to Organize (“PRO”) Act, which has passed the House of Representatives twice in the last two years but has stalled in the Senate. See H.R. 842, 117th Cong. (2021).
231. ESTREICHER & BODIE, supra note 219, at 41–44.
employer make any concessions to union demands.\textsuperscript{232} Employers can unilaterally implement their preferred set of terms as long as they bargain to a genuine impasse.\textsuperscript{233} Federal labor law also leaves much of the core operations of the employer’s business off the bargaining table. Employers are only required to bargain on topics that are categorized as “mandatory” subjects.\textsuperscript{234} The mandatory label applies to the terms and conditions of employment; the employer has no duty to negotiate over issues such as product development, executive compensation, financial structuring, marketing, or even internal firm governance.\textsuperscript{235} The “core of entrepreneurial control” is reserved to the employer itself as a matter of managerial authority that lies outside the bargaining process.\textsuperscript{236} By centering collective bargaining only on the nuts and bolts of the employment relationship, federal labor law has fenced workers and their representatives out of true participation in the firm’s management.\textsuperscript{237} In fact, labor law preserves and encourages a divide between those who run the firm and those who work for it.

At one point in our history, we expected collective bargaining to create a system of industrial democracy in which employees would participate in the governance of their workplaces. The project succeeded in substantial ways, in part by developing worker power sufficient to impose legislative mandates on all employers. But unions now only represent a small fraction of private sector workers. And as a system of democratic governance, collective bargaining is flawed: It maintains the internal firm governance of the employer and only requires the employer to bargain over a limited view of terms and conditions of employment. True worker governance requires a different approach.\textsuperscript{238}

\textsuperscript{232} 29 U.S.C. § 158(d).
\textsuperscript{234} NLRB v. Wooster Div. of Borg-Warner Corp., 356 U.S. 342, 349 (1958) (setting out the mandatory subjects of collective bargaining).
\textsuperscript{235} See id. (emphasizing a party’s freedom to bargain or not bargain over other subjects).
\textsuperscript{236} Fibreboard Paper Prods. Corp. v. NLRB, 379 U.S. 203, 223 (1964) (Stewart, J., concurring) (further establishing that managerial decisions lie outside the scope of mandatory subjects); see James Gray Pope, \textit{Class Conflicts of Law II: Solidarity, Entrepreneurship, and the Deep Agenda of the Obama NLRB}, 57 \textit{BUFF. L. REV.} 653, 658 (2009) (“The doctrine [of entrepreneurial control] provides the focal point for a coherent and positive conception of employer interests that has come to permeate the labor law.”).
\textsuperscript{237} See JAMES B. ATLESON, VALUES AND ASSUMPTIONS IN AMERICAN LABOR LAW 111 (1983) (“Even where collective bargaining exists, the promise of industrial democracy has only been partially fulfilled, for neither the law nor the practice has accepted employees as full partners in the enterprise.”); Edward Silver & Joan McAvoy, \textit{The National Labor Relations Act at the Crossroads}, 56 \textit{FORDHAM L. REV.} 181, 186–88 (1987) (explaining criticisms of the NLRA and the NLRB).
\textsuperscript{238} For one argument for reforms centered on employee voice beyond labor law, see Kenneth G. Dau-Schmidt, \textit{Promoting Employee Voice in the American Economy: A Call for Comprehensive
B. Shop Floor Participatory Governance

The modern corporation is generally managed from within through a hierarchical approach. The board of directors has control over the company but delegates governance responsibilities to a set of officers, who then control the actual workings of the corporation.239 The chief executive officer has ultimate managerial power, with other officers below, and then executives, managers, and the mass of employees. This structure informs our legal and societal perspective on the nature of the organization itself. We assume that corporations must be governed from within through hierarchy, and that the work of employees is controlled by the employer, acting through managers and supervisors.

However, hierarchy is not endemic to the corporate structure. Participatory management is a common term for those managerial methodologies that endeavor to flatten or shift the power relations within the traditional corporate chain of command.240 Systems of participatory management have a long if limited history, both in the United States and abroad. The last significant bloom of participatory management within firms occurred in the 1980s and 1990s, as U.S. firms looked to Japan and Germany for guidance.241 Ideas such as quality circles and total quality management moved away from rote assembly lines to a system of worker responsibility for the ultimate product.242

Reform, 94 MARQ. L. REV. 765, 832 (2011) (“The United States should adopt legislative measures to promote employee voice in corporate governance and labor relations.”).

239. See, e.g., DEL. CODE ANN. tit. 8, § 142(a) (2019) (“Every corporation organized under this chapter shall have such officers with such titles and duties as shall be stated in the bylaws or in a resolution of the board of directors which is not inconsistent with the bylaws . . . .”).


241. See id. at 673 (“Over the last two decades, however, participatory management has emerged as the principal putative challenger to traditional corporate hierarchies.”); Marleen A. O’Connor, A Socio-Economic Approach to the Japanese Corporate Governance Structure, 50 WASH. & LEE L. REV. 1529, 1531 (1993) (noting that “employees are given a voice in strategic decisionmaking—legally in Germany and implicitly in Japan”). However, efforts to integrate employees into the governance of the firm are long-standing. See, e.g., Clyde W. Summers, Codetermination in the United States: A Projection of Problems and Potentials, 4 J. COMP. CORP. L. & SEC. REG. 155, 170 (1982).

As concerns about the social purpose of corporations has grown, companies are rediscovering participatory management models. These approaches do not fall within the established alternatives, such as employee-owned companies, consumer cooperatives, or non-profits. Instead, for-profit companies, organized as corporations, partnerships, or LLCs, have radically restructured the internal hierarchy with labels such as “self-managed,” “self-actualizing,” “evolutionary,” “integral,” “flat,” and even “teal.” They seek to bring more worker participation within the traditional outer shell of business organizations.

Systems of participatory management have been the subject of much discussion in the business management literature but have been less examined in the legal literature. There is less to talk about, as these systems generally sit within the standard corporate governance framework and exist in union-free workplaces. As creatures of management policy, these systems can be installed, changed, and removed without any employee consent or input. At most, employees might have contractual claims to certain procedures, but courts have generally looked less kindly on those claims—as management lawyers know how to insert the right disclaimers. So participatory management exists outside the zone of relevance for the law—it is a managerial strategy.

243. For examples of this broader literature, see Colin Mayer, Firm Commitment: Why the Corporation Is Failing Us and How to Restore Trust in It (2013); Raj Sisodia, Jag Sheeth & David B. Wolfe, Firms of Endearment: How World-Class Companies Profit from Passion and Purpose (2d ed. 2014).


245. One particular instantiation of this broader movement is a system known as “holacracy.” See, e.g., Brian J. Robertson, Holacracy: The New Management System for a Rapidly Changing World 12, 23, 25 (2015); Bernstein et al., supra note 244, at 44. For an exploration of the legal ramifications of holacracy, see Matthew T. Bodie, Holacracy and the Law, 42 DEL. J. CORP. L. 619, 670–71 (2018).


247. The default rule for holacracy is to leave this structure in place. Robertson, supra note 245, at 151 (suggesting that beginning holacracy adopters use a CEO policy, rather than board-level action, “to avoid the extra complexity of getting board-level buy-in up front”).

248. Restatement of EMP. LAW § 2.05 cmt. c (AM. L. INST. 2015) (noting that “the presence of a prominent disclaimer in the text of the statement may indicate that it is a hortatory pronouncement rather than a statement intended to govern the employer’s operational personnel decisions”).
The law could be reoriented to incentivize or require companies to adopt certain aspects of participatory management. Unions existed prior to federal labor law, but the NLRA created a legal system of rights and responsibilities that facilitated their role within the economy; a similar approach could extend participatory management across a wider range of firms. But the current lack of legal intersection points to one of the weaknesses of participatory management: it is a function of managerial decision making, and it exists at the pleasure of management. As currently utilized in the U.S. economy, shop floor governance is designed to bolster quality and productivity within the workforce by empowering workers within their jobs. It is the rare participatory-management system that seeks to empower workers by constraining management. But binding systems of employee participation have generally come through unions or, as discussed next, through corporate governance.

C. Board Representation and Employee Ownership

The most direct method of employee participation in governance is through various mechanisms of employee ownership. Employee-owned firms have taken on different forms: worker cooperatives, employee stock ownership plans (“ESOPs”), equity compensation plans, and managerial leveraged buyouts. By aligning workers’ incentives with the overall value of the firm, employee ownership not only motivates workers to maximize utility—it also gives workers the true benefits of their labor. The idea of employee ownership rights has resonated within the American ethos throughout our history and unites those who favor a hardscrabble capitalism with those who believe in a society of civic engagement.

Despite efforts to facilitate employee ownership, it remains largely marginal within our economic system. The ESOP, introduced with ERISA in 1974, has had sustained if limited success. An estimated ten percent of employees participated in ESOPs as of 1990; in 2020, around ten million

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249. This is arguably what holacracy is designed to do. As Robertson described it in his book, the firm’s constitution under holacracy is the “core rulebook for the organization” whose “rules and processes reign supreme, and trump even the person who adopted it.” ROBERTSON, supra note 245, at 21.

250. See, e.g., McDonnell, supra note 191, at 336 (making the case for employee participation through law and economics as well as civic republicanism).


252. HANSMANN, supra note 173, at 105.
workers are active participants. However, while ESOPs facilitate employee participation in ownership, they do not offer much employee participation in governance. Employees participate in the ESOP as beneficiaries of a plan, and the plan’s trustee manages the shares on their behalf. The law does not require that employees vote for directors or otherwise have rights beyond financial interests. Thus, ESOPs are similar to other compensation mechanisms such as stock options and bonus plans—they provide financial participation in the share price but do not require employee governance representation.

Other organizational structures—most notably the cooperative—offer more direct participation. Structured differently than corporations, cooperatives generally provide for one “share” for each participant and require participation in governance from all members. Consumer cooperatives have been prevalent in some industries, such as utilities and insurance. Worker cooperatives, however, have not been common. A relative of the worker cooperative is the partnership controlled by a set of workers. Law firms were mandated to take the form of common partnerships owned by a set of attorneys who worked for them. Today, however, most states permit law firms (and other associations of professionals) to form as limited liability partnerships and have management structures closer to corporate ones; corporate ownership of law firms is still not permitted.

These models of worker governance are tied to ownership, in that workers have both financial rights to profits or distributions as well as


254. Jeffrey M. Hirsch, Labor Law Obstacles to the Collective Negotiation and Implementation of Employee Stock Ownership Plans: A Response to Henry Hansmann and Other “Survivalists,” 67 FORDHAM L. REV. 937, 960 (1998) (“The structure of ESOPs can vary significantly, but at their core they are equity plans that hold shares of a company in a trust for their participants.”).

255. As Hirsch explained:

Because voting rights can be assigned to a trustee, an individual employee-owner may only possess financial distribution rights in her company, without obtaining any voting rights. Once the shares are distributed (as the loan is paid off), the employee-owner is able to vote those shares; it takes many years, however, for such a distribution to occur. Thus, employee-owners are left facing the risks associated with equity without any voting rights in their stock.

Id. at 962–63.


257. HANSMANN, supra note 173, at 178, 265.

258. Levinson, supra note 256, at 323 (“Yet despite the promise they hold, worker cooperatives are relatively rare in the United States.”).

259. HANSMANN, supra note 173, at 93.

260. MODEL RULES OF PRO. CONDUCT r. 5.4 (AM. BAR ASS’N 2020); Larry E. Ribstein, Partnership Governance of Large Firms, 76 U. CHI. L. REV. 289, 307 n.86 (2009).
governance rights. But other models provide for governance without financial stakes. The system of codetermination provides for employee representatives on the board of directors simply through their role as employees. Employee board representation has a very limited history in the United States, but it is governing law in many European states, most notably Germany. Under German law, employees select fifty percent of the directors on the supervisory board, which has similar responsibilities to the U.S. corporate board. 261 Although shareholders select the chair, who acts as the tiebreaker, employees have significant power within the corporation and have operating control in many companies. 262 In the last few years, bills proposed by Senators Baldwin and Warren have each proposed systems of codetermination requiring U.S. companies to have a percentage of their workers on corporate boards. 263 Scholars have proposed a variety of possibilities when it comes to structuring employee participation in governance. 264

Codetermination represents a more realistic avenue of top-level participation for most workers, as it does not require the same commitment of capital and potential for risk that ownership does. At the same time, workers share in the firm profits through direct ownership and need no reorientation of corporate governance principles to accomplish this control. There is room in the system for a multitude of approaches, but real participation in firm governance at the top of the hierarchy is what distinguishes this type of governance participation from the other two.

D. Assessing Systems of Employee Governance Participation

We have seen two different kinds of arguments in favor of involving employees in firm governance. First, it could lead to better protection of

261. Pistor, supra note 201 at 174; Grant M. Hayden & Matthew T. Bodie, Codetermination in Theory and Practice, 73 FLA. L. REV. 321, 331–32 (2021). Under codetermination there is also a managerial board which acts more akin to the set of officers and executives under U.S. law. Id. at 332.

262. Volkswagen is a special example, since by law the state government of Lower Saxony has an ownership stake and generally supports workers in its voting. See Nicola F. Sharpe, Volkswagen’s Bad Decisions & Harmful Emissions: How Poor Process Corrupted Codetermination in Germany’s Dual Board Structure, 7 MICH. BUS. & ENTREPRENEURIAL L. REV. 49, 72–76 (2017).

263. Senator Tammy Baldwin has proposed the Reward Work Act, which proposes that one-third of directors of public companies be selected directly by employees. Reward Work Act, S. 915, 116th Cong. § 3(b) (2019). The Accountable Capitalism Act, proposed by Senator Elizabeth Warren, would require that companies with more than $1 billion in average revenue have employees select at least forty percent of the seats on the board. Accountable Capitalism Act, S. 3348, 115th Cong. § 6(b)(1) (2018).

employees. Rather than relying on mandatory employment regulations that could go wrong for a variety of reasons, setting default rules that protect employees while allowing those employees through a collective process to modify the rules can lead to better protection at a lower cost.\textsuperscript{265} Second, employee governance may generate a higher surplus that benefits all participants in a business enterprise—not just employees but also shareholders, creditors, customers, and the community at large. If employment regulation encourages employee involvement in governance, it can thus improve the lot of all corporate constituencies.\textsuperscript{266}

How do these three types of employee governance compare in their ability to address the various major arguments that favor mandatory employment regulation?\textsuperscript{267} That is, what types of employee governance will best respond to the problems that employment regulation attempts to correct, so that we will feel comfortable allowing the relaxation of regulation where such governance is present? One argument favoring regulation is that individual workers will have trouble accessing and processing some important types of information more readily available to employers, including the financial condition of the business and the regulatory environment. Board representation is the type of employee governance most likely to reduce this disparity with respect to company-specific financial (and other) information, as it gives employee directors access to all of the information about the company available to the board, which is essentially all the relevant internal information.\textsuperscript{268} For information on the legal and market environment, both board and union representation would seem to have some advantages. Employee directors have access to the same information available to the rest of the board, while unions may have alternative sources of information on labor and employment laws, and on market conditions in other unionized companies, that might be particularly useful from a worker perspective.

Another set of arguments favoring mandatory employment regulation concerns collective action problems. As we saw, these can be internal within a company or external for workers across different companies.\textsuperscript{269} For the

\textsuperscript{265} See supra Section I.E.

\textsuperscript{266} See supra Section II.B.

\textsuperscript{267} See supra Section I.D.

\textsuperscript{268} Directors are less able than officers to fully digest this information, so even board representation will not fully equalize the disparity between workers and officers. Lisa M. Fairfax, \textit{The Elusive Question for Director Independence}, in \textsc{Research Handbook on the Economics of Corporate Law} 170, 180 (Claire A. Hill & Brett H. McDonnell eds., 2012) (“Informational asymmetries inherent in the role of independent directors further limit such directors’ ability to be effective monitors.”).

\textsuperscript{269} See supra notes 137–138 and accompanying text.
internal collective actions, both board representation and shop floor governance are potentially effective, with the latter particularly focused on many of the key local public goods, such as workplace safety. For the external collective actions, union representation would seem the better solution, since unions organize workers in different companies, whereas board representation and shop floor governance only operate within individual companies.

A further set of arguments we saw favoring mandatory employment regulation looked at a variety of cognitive biases that may prevent individual workers from adequately bargaining to protect their interests. Moving from individual to collective bargaining may address at least some of these biases. In part that may happen through a collective deliberation process, although collective processes can produce their own biases (e.g., elected representatives may have a time horizon limited by the length of their term in office). It is not clear which if any of the three forms of employee governance models has an advantage on this dimension.

The final argument we saw favoring mandatory employment regulation concerned wealth and income inequality and a concern for social equality. A drawback of this argument for mandatory regulation recognized by some of its advocates is that it can lead to imposing terms that some workers don’t like, but those advocates reply that eliminating subordination is a crucial social goal. However, collective empowerment through any of the types of employee governance we are discussing is an alternative way of addressing subordination that is less likely to lead to unwanted terms of employment.

How do the three types of employee governance compare in their ability to achieve the potential gains in generating a surplus for all corporate constituencies, while avoiding potential costs that could reduce or eliminate those gains? Board representation would give employees voice over the widest range of decisions affecting them and bring their information and perspective to bear on those decisions. But board representation also may be subject to more conflict and decision costs and do more to scare off investors, at least when compared with shop floor governance and perhaps when compared with unionization too. Much of the informational benefit that comes from employee involvement will involve the kind of in-company, day-to-day issues captured through shop floor governance. It is not clear which form of governance is likely to have stronger motivational effects.

270. See supra notes 134–136 and accompanying text.
271. See supra notes 139–140 and accompanying text.
272. See Bagenstos, supra note 139, at 242.
273. See supra Section II.B.
What about the effect of employee governance on decisions affecting stakeholders other than employees and shareholders? For these effects, board representation seems the most significant, as it gives employees a voice in all major decisions affecting a company. Both union representation and shop floor governance are focused on terms and conditions of employment that are likely to be of most interest to employees themselves and to shareholders through the effect on profits, with other stakeholders less concerned with most of those decisions.

We thus see that each type of employee governance has some comparative advantages relative to the others, and all of them have the potential to justify the modification of employment regulations to allow workers to protect themselves more effectively and cheaply while also creating a bigger surplus to be shared with shareholders and other company stakeholders. The system could require use of only one or two of these three types of governance as a way to allow employers to modify regulatory mandates, or to try to fine-tune the system to require employers to use one form of employee governance to modify some mandates but another form to modify other mandates. For each regulatory mandate subject to loosening and each form of employee governance that could justify such loosening, regulation would have to specify adequate safeguards that would be required to ensure that such governance represents a genuine expression of employee will rather than a façade that masks employer domination. The details of such safeguards are crucial, but addressing them here would expand the scope of this Article beyond reasonable bounds. We do believe, though, that with such safeguards in place, both unions, shop floor participation, and employee directors are all capable of effectively protecting employee interests.

Some argue that we need all three forms of employee governance—that at least some or maybe each of them on their own are inadequate to protect the interests of employees. Leo Strine and his co-authors have recently presented a powerful statement of that position. They argue, with a particular focus on Germany, that other countries that have successfully promoted worker representation on boards also feature high levels of unionization and a requirement for works councils. They particularly point to several ways in which board representation, to work effectively, may rely on the presence of unions and works councils.

274. See supra Section II.C.


276. See id.
serve as sources for persons to become board members.\textsuperscript{277} German law requires boards to consider the interests of many stakeholders, not just shareholders.\textsuperscript{278} They argue that board-level codetermination may work more naturally in the German two-board system, where the supervisory board (the level at which worker representation occurs) has more limited powers than a unitary board.\textsuperscript{279}

We would be thrilled were the United States to develop to a point where unionization, works councils, and worker board representation were all three common and widespread, and we agree that in many ways the three forms of employee governance complement each other. But we suspect that asking for all of that (and then some)\textsuperscript{280} is politically unrealistic. It is a tough question how to effectively stage the introduction of different forms of employee governance. We are somewhat agnostic on that point; we suggest giving employers incentives to adopt each of them, and see how each form does.\textsuperscript{281}

As for the specific ways in which Strine and his co-authors suggest that board representation may depend upon the presence of unions and works councils, there are some counterarguments. Other internal\textsuperscript{282} or external\textsuperscript{283} organizations could help train employees for board representation. The law of many states allows boards to consider the interests of various stakeholders, and even in states like Delaware with a shareholder-only focus, companies may choose to become benefit corporations or to amend their charters to allow for or even mandate the consideration of employee and other interests.\textsuperscript{284} As for the German two-tier board, Strine and his co-authors themselves admit that board codetermination still works well in Nordic countries with unitary boards.\textsuperscript{285}

\begin{itemize}
\item \textsuperscript{277} Id. at 10.
\item \textsuperscript{278} Id. at 30.
\item \textsuperscript{279} Id. at 28.
\item \textsuperscript{280} Id. Part IV.
\item \textsuperscript{281} How satisfactory this response is depends in part upon having adequate safeguards in place. Should our proposal be implemented in a way that allows employers to evade major employment law restrictions with weak, ineffective works councils or board representation, then seeing that form of governance spread would be much less encouraging. For important design questions on how board representation might be structured, see \textit{id}. Part III.
\item \textsuperscript{282} This could include employee resource groups, which have become quite common. \textit{See infra} note 335 and accompanying text.
\item \textsuperscript{283} Unions could play this role. Even where they do not represent the employees of a company, they could establish worker-director training centers, giving them a new role to play.
\item \textsuperscript{285} Strine et al., \textit{supra} note 275, at 28.
\end{itemize}
IV. MOVING FROM MANDATES TO GOVERNANCE WITHIN THE EMPLOYMENT RELATIONSHIP

In this Part we set forth a plan for moving from a system largely built around mandatory employment terms to a system that provides for employee participation in firm governance. We first establish the principles for directing such a move, and then examine concrete changes to employment regulation following from these principles. We then discuss the implications of the move from mandates to governance for the increasingly prominent discussion of how to define who is an employee.

A. Principles of a Governance Model for Employment

The regulation of employment is an incredibly complex endeavor, with many different moving pieces. Below we provide a preliminary overview for a new approach with the guidance of certain principles.

First, we conceive of the “employer” as a business firm. Labor and employment law has focused on the definition of employee and has largely neglected the concept of the employer. But the concept of an “employer” is critical to the idea of employment regulation: The employer is the regulated entity. The law tends to focus on the status of a business entity under organizational law: corporation, LLC, partnership, or other form. But employers can be any of these; the critical aspect of being an employer is that employers enlist workers as part of an ongoing business enterprise in which the workers participate. The economic literature defines such entities as firms and has devoted a subdiscipline of economics to why we have firms within larger markets. Employers are firms and are defined by their use of workers to carry on the ongoing enterprise of the firm.

By recognizing that employers are economic organizational entities, we should then understand the principle of self-governance within the organization. The autocracy of the business firm has long been taken for

286. See infra Section IV.A.
287. See infra Section IV.B.
288. See infra Section IV.C.
289. ESTLUND, supra note 19, at 11 (describing employment law as “an unruly hydra head of duties and liabilities for employers”).
293. Id. at 403.
granted. But democratic principles hold that members of an organizational unit should have a say in the governance of that unit. These principles of participation, voice, and representation support a shift from regulatory mandates to employee governance.

Employee governance also provides the opportunity to pursue more efficient solutions, in an economic sense, by allowing the parties to determine the terms and conditions that best fit their situation. Employment mandates are based in part on paternalism: the idea that the government will mandate a better solution than the parties would reach on their own. Such paternalism may be necessary to protect employees who would otherwise lack bargaining power. But governance participation is designed to provide workers with more power to negotiate their own solutions. The flexibility and specificity allowed in bargaining would allow the parties to achieve results that are more closely tailored to their individual interests and utility. Private ordering has significant advantages when the parties are able to knowingly and freely negotiate for an outcome that best reflects their own preferences.

Finally, employee governance provides additional mechanisms for enforcement. Employment mandates are vulnerable to underenforcement, which has been a chronic problem even during Democratic administrations. Under the Bush Administration in the early 2000s, agencies devolved regulatory responsibilities to employers through self-

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294. Cynthia Estlund, Rethinking Autocracy at Work, 131 HARV. L. REV. 795, 795 (2018) (reviewing ELIZABETH ANDERSON, PRIVATE GOVERNMENT: HOW EMPLOYERS RULE OUR LIVES (AND WHY WE DON’T TALK ABOUT IT) (2017)) (“How is it that a democratic society devoted to individual freedom came to tolerate the private outposts of autocratic rule and unfreedom in which most citizens spend their working lives?”).

295. See BEFORT & BUDD, supra note 102, at 5–6 (discussing the importance of employee voice as a value).

296. See, e.g., Jacob Goldin, Libertarian Quasi-Paternalism, 82 MO. L. REV. 669, 681–82 (2017) (arguing that mandates are paternalistic in that they assume that parties would otherwise consistently make the wrong choices).

297. Samuel R. Bagenstos, Consent, Coercion, and Employment Law, 55 HARV. C.R.-C.L. L. REV. 409, 412 (2020) (“Ordinary workers lack significant bargaining power because they face ‘asymmetric vulnerability’ vis-à-vis their employers: they need their employer more than their employer needs them.” (quoting Bagenstos, supra note 139, at 238)).

298. Lobel, supra note 21, at 408 (“In today’s reality, no single model of work relations exists, and thus unitary conceptions of the workplace and unitary employment policies are impossible.”).

299. See Blake D. Morant, Contractual Rules and Terms and the Maintenance of Bargains: The Case of the Fledgling Writer, 18 HASTINGS COMM’NS & ENT. L.J. 453, 491 (1996) (noting that paternalism within contracts “can be costly, time consuming, and therefore, inefficient”).

300. Cynthia Estlund, Rebuilding the Law of the Workplace in an Era of Self-Regulation, 105 COLUM. L. REV. 319, 323 (2005) (“Both employee rights and workplace regulations are often underenforced in the absence of union representation, especially where employers are committed to competing through the minimization of labor costs.”).
These programs allowed companies to opt out of certain regulatory requirements or inspections in exchange for voluntary compliance programs with reporting and monitoring. Although pitched as boosting enforcement while saving government funds, self-regulation was often criticized as regulatory abnegation. Employee participation in governance is critical to turning self-regulation programs into meaningful oversight with some teeth, rather than a way of claiming compliance while cutting agency funding.

These principles of representation, efficiency, and enforcement inform our approach to rethinking the employment relationship. We have discussed three different types of employee representation which may achieve these gains, in somewhat different ways: unionization, shop floor governance, and board representation. We have argued that an employer should be able to use any one of these three forms to modify regulatory mandates in ways allowed by our approach. A fully developed proposal would need to specify the participation metrics that employers would need to meet for each type of governance in order to be able to opt out of regulations. The already well-developed rules for determining union representation provide the needed framework for that form of representation. Shop floor and board representation need more development. This would require answering questions like: Which workers have voting rights in choosing representatives? Are those voting rights equal for full-time and part-time employees? Might employers be allowed or required to provide for classes of employee representatives, to take account of significant differences in the interests of different types of employees? Should there be a sunset time imposed for opting out of some regulations, so that the body opting out would need to reaffirm that choice after a certain amount of time has passed? If so, how long should that time be? For some particularly important and sensitive opt outs, should the law require a direct employee vote as well as approval by the representative body, and if so, for what regulations would that direct vote requirement apply? These are just some of the more obvious and important questions that arise.

At the same time, we recognize that mandates may continue to play an important role within certain contexts. Mandates may make particular sense when there are public or third-party interests that bargaining would not

301. Id. at 321 (discussing the movement toward self-regulation in the workplace).
303. ESTLUND, supra note 19, at 11 (noting that employer compliance programs may be "mere window dressing—a glossy façade behind which business goes on as usual").
304. Id. at 242 (arguing that self-regulatory regimes need worker representation to be effective).
305. See supra Part III.
otherwise protect. A mandate for a certain benefit may make sense if the public believes that people should have that benefit, even if they may not otherwise want to bargain for it (like health care insurance). An employment mandate may be the most efficient way of providing that benefit for a large group of people, based on existing practices. Alternatively, in other cases the parties may have interests that are counter to those of society—for example, the exclusion of racial groups from a certain firm. In these cases, society may wish to impose mandates not to supplement or protect the interests of workers, but rather to override their preferences in certain contexts. The choice is not simply between a mandatory rule or allowing an employee representative body to opt out of a regulation in any way it likes. One could allow employee representative bodies to change a regulatory provision, but impose limits on how far they can go. For instance, a union could be allowed to agree to an hourly wage below the statutory minimum wage, but only, say, $2 below that minimum.

A final important principle we discuss in our proposal for moving from mandates to governance is the recognition that another key part of the design question is that some decisions may be removed from employers altogether and moved to the government level. For instance, health care and/or pensions may be provided by the government rather than private employers. Or, one may have a mixed system, with provision by both the state and by private employers. In that case, the choice of mandate versus governance within employers will depend in part upon whether there are means for social provision of the good in question.

B. Moving from Mandates to Governance: Policy Proposals

The following proposals discuss specific areas of employment regulation that could be reshaped under a regime of employee participation in governance. We do not discuss all areas of employment regulation mentioned above, and for those areas we do discuss we only present a highly skeletal outline of relevant considerations and possible approaches to how one might allow employers with employee participation to modify the regulation that applies to them. Still, we hope the discussion gives some sense of how our approach might work in practice.

1. Compensation and Benefits

Employee governance rights would directly impact employees’ ability to negotiate for better compensation. The existence of a union wage premium is empirically established, as well as intuitively plausible; the Wagner Act’s preamble specifically states that the “inequality of bargaining power between employees who do not possess full freedom of association or actual liberty
of contract . . . tends to aggravate recurrent business depressions, by depressing wage rates and the purchasing power of wage earners in industry." The German system of codetermination has similarly shown demonstrable effects on workers’ compensation and provides workers with a stronger presence within the firm. The combination of collective bargaining and governance power will address the growing imbalance between shareholders and workers, as evidenced by continued wage stagnation and growing corporate profits.

What mandates could be loosened in response to this change in governance power? Minimum wage is a significant candidate, as workers would have power to negotiate higher compensation for themselves or to trade off lower compensation for other items they value. But society does have an interest in providing a minimum income allocated to each person—at least some threshold amount for working. Firms may also take advantage of smaller subsets of workers and drive down their wages, even if the workers as a whole are empowered through governance. In a firm, for example, where 80% of the workers are professionals and 20% are janitorial, the professional workers might join with management and shareholders to offer subminimum wages to the janitorial employees. Society would still have an interest in establishing a minimum wage for those workers who might have less power within firms due to their market position or societal norms about the value of their labor.

The societal interest in providing a minimum set of resources for all could be met in at least two ways. Most simply, one could set a floor on how low a worker representative body could set wages. This could create new potential compromises for increasing the minimum wage. Many consider the current federal minimum wage of $7.25 as much too low, with some states and cities recently moving to increase the minimum to $15. A compromise

309. The suggestion to allow employers with a form of employee participation to be exempt from minimum wage requirements is not completely novel. Unions that supported a $15 minimum wage in Los Angeles also proposed that they be exempt from the requirement under some circumstances. Jana Kasperkevic, LA Unions Call for Exemption from $15 Minimum Wage They Fought for, GUARDIAN (Apr. 12, 2016, 9:22 AM), https://www.theguardian.com/us-news/2016/apr/12/los-angeles-15-dollar-minimum-wage-unions.
setting the default minimum at, say, $15 but allowing employers with employee governance to set the wage as low as, say, $7.25 might allow movement where none is currently achievable. The minimum wage could thus be used along the lines of a best alternative to a negotiated agreement ("BATNA") or penalty default that the parties could opt out of if they negotiated together. In the alternative, the government could itself provide a minimum level of resources to all citizens as part of the social compact through a uniform basic income or negative income tax. The United States already has variations on this type of entitlement for certain groups, such as Social Security for retirees and Temporary Assistance to Needy Families ("TANF") for low-income parents and children. But the considerable cost to the government to provide a true universal basic income makes it hard to achieve.

The concern about one class of workers taking advantage of another could be addressed by establishing different classes of representatives on the worker representative body, or by requiring a direct vote by different classes.

312. A high minimum wage default would put employees in a much stronger bargaining position—and not just with respect to wages. See Russell Korobkin, Bargaining Power as Threat of Impasse, 87 MARQ. L. REV. 867, 867–68 (2004) ("[R]elative bargaining power stems entirely from the negotiator’s ability to, explicitly or implicitly, make a single threat credibly: ‘I will walk away from the negotiating table without agreeing to a deal if you do not give me what I demand.’ The source of the ability to make such a threat, and therefore the source of bargaining power, is the ability to project that he has a desirable alternative to reaching an agreement, often referred to as a ‘BATNA.’" (emphasis omitted)). Similarly, a penalty default motivates the parties to reach a negotiated outcome because of its harsh consequences on one or both parties. Ian Ayres & Robert Gertner, Filling Gaps in Incomplete Contracts: An Economic Theory of Default Rules, 99 YALE L.J. 87, 91 (1989) ("Penalty defaults are designed to give at least one party to the contract an incentive to contract around the default rule and therefore to choose affirmatively the contract provision they prefer.").
of workers in order to validate wages set below the statutory minimum. Of course, such protections increase the complication in devising a new system of regulation. But such concerns are critical to the work of devising a workplace democracy that works as a democracy.

Pension benefits are already treated in good part as a social good, with public provision through Social Security. However, employers can and often do choose to provide additional retirement benefits to their employees. The law largely leaves to employers the decision whether to provide such benefits, and how much to provide if they do. Once the employer has promised a pension, ERISA fairly strictly regulates the pension plans that employers create, largely to ensure that the plans deliver on their promises.

A move from mandates to governance could conceivably allow employers who involve employees in governance greater flexibility in complying with ERISA, and indeed the statute already exempts employers with unions from certain requirements.

Care should be taken in multiplying such ERISA exemptions, since the likelihood of a governmental bailout if employers default on pension obligations creates a serious moral hazard incentive. Still, perhaps there are some requirements that could be made more flexible with employee representation. One candidate would be ERISA’s requirement that plan fiduciaries focus exclusively on financial returns. With the rise of interest in sustainable investing, the Trump Administration’s Department of Labor sharply restricted the ability of plan fiduciaries to consider sustainability factors in making investments, even though beneficiaries may care about some social consequences of their investments. Most to the point of our analysis here, unions co-administering pensions may not want to invest in companies that engage in employment practices harmful to their members. By softening the profit-maximization principle, unions could better make

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315. Direct votes might also be directed in specific cases of sub-minimum wages—for example, where the wages are set below a specified amount or where the gap between the lowest and highest paid workers within an employer are above a certain level.


317. See supra notes 36–45 and accompanying text.


320. DAVID WEBBER, THE RISE OF THE WORKING-CLASS SHAREHOLDER: LABOR’S LAST BEST WEAPON 37 (2018) ("[I]t is entirely appropriate for trustees to consider workers’ economic interests beyond just maximizing returns to the fund . . . ").
tradeoffs between their obligations to current and future members with their fiduciary responsibilities to past members.

The recent debates within the political parties over the appropriate provision and regulation of health insurance demonstrate its importance as a workplace benefit. Here again we see a mix of public provision and regulation of private provision. The United States does provide some governmental health insurance, primarily through Medicare and Medicaid, but it publicly insures fewer of its citizens than most wealthy countries. Many would like to change this and have the government provide health insurance to all. As a matter of employment regulation, this makes a good deal of sense—health insurance has a pretty weak connection to employment, and the American connection between employment and health insurance discourages mobility in labor markets and may make it harder for more marginal workers to get attractive jobs. However, the costs would be high and the politics are difficult. Absent a move to universal health insurance, would a move from mandates to governance suggest changes in the regulation of employer-provided health insurance? The ACA requires large enough employers to purchase health insurance for their employees and imposes a range of requirements on what that insurance must cover. Should employers with employee governance be allowed to waive some of those requirements? There are some arguments for that—the ACA requirements impose a pretty high level of coverage, which may be more costly than some employees want given the opportunity costs. Unions and internal governance mechanisms are better positioned than individual


322. Timothy Stoltzfus Jost, Our Broken Health Care System and How to Fix It: An Essay on Health Law and Policy, 41 WAKE FOREST L. REV. 537, 545 (2006) ("As health insurance has become more and more expensive, however, employers have found it increasingly difficult to pass on the cost of health insurance to workers through holding down wage growth, as they have largely done in the past."). In 2018, the average annual premium for employer-based family coverage was $19,616 (a five percent increase from 2017), and for single coverage, premiums rose to $6,896 (a three percent increase from 2017). Health Insurance: Premiums and Increases, NAT’L CONF. STATE LEGS., https://www.ncsl.org/research/health/health-insurance-premiums.aspx (last visited Feb. 8, 2021).

323. But see Abbe R. Gluck & Thomas Scott-Railton, Affordable Care Act Entrenchment, 108 GEO. L.J. 495, 502 (2020) ("[I]n 2020, even though the ACA itself does not achieve universal health coverage, it has made that goal not only seem feasible and politically possible for the first time in modern American history but also, to many, now the marker of a just healthcare system.").

324. See supra note 73 and accompanying text.
employees to evaluate the value of complicated insurance plans, which may mitigate the costs associated with greater flexibility about plan policies.

2. Workplace Safety

Employers have both common law and statutory requirements to provide a safe workplace. The OSHA regulations can be detailed and onerous, but they are often toothless. Employee governance would allow for safety standards to be better tailored to individual workplaces. It is impossible to eliminate all hazards from all jobs; tradeoffs must be made. Especially during the COVID-19 pandemic, those choices have been murky and more perilous. Although workers are not aware of all relevant safety risks, they learn a lot about hazards on the job. The collective organization that comes with employee governance would cast a wider and tighter net for this information, pulling it all together for deeper examination. Indeed, employers with adequate internal compliance programs already can receive less stringent enforcement supervision under some federal and state workplace safety initiatives, one of the existing practices that serves as a model for our approach to providing more regulatory flexibility to employers with good internal practices. The keys to permitting such regulatory flexibility are that: (1) workers must have authentic power—not window dressing, and (2) agencies must still provide expertise and oversight for those dangers that unions, works councils, and employee governance representatives do not have the resources to monitor.

Employers with worker governance should be permitted to go beyond lighter supervision practices to allowing employers to modify some substantive restrictions on workplace safety. Although any of the three forms of employee governance should be able to invoke the ability to modify regulations, one common suggestion is the use of work safety committees. We would not grant carte blanche. Instead, regulation should provide a hard floor of standards below which no employer may fall. In response to the debate over employer liability for infections during the COVID-19 pandemic, we suggested a possible proposal: Employers following a COVID-19 safety plan that had been approved by its employees and met threshold CDC

325. See supra notes 57–60 and accompanying text.
327. See supra notes 145–146 and accompanying text.
328. BEFORT & BUDD, supra note 102, at 162–64; ESTLUND, supra note 19, at 174–78.
requirements would have a defense to a tort or workers’ compensation claim from employees who claim to have been infected at that workplace.\textsuperscript{329}

In addressing its warehouse injury problem, Amazon has partnered with the National Safety Council to explore new ways to prevent musculoskeletal disorders.\textsuperscript{330} The partnership seems like a well-intentioned effort to both prevent and address such disorders by conducting research, funding innovative solutions, and sharing solutions with the public. But it does not take a cynic to imagine that these policies are merely for show. We could better envision the possible advances that such a partnership could bring if warehouse employees had a governance role within this partnership, through participation in meetings, decision-making, and implementation.

3. Limits on Discipline and Termination

The common law employment at will doctrine provides little protection for employees,\textsuperscript{331} and hence little scope for using employee governance to reduce the scope of regulation. The common law does prohibit employers from firing an employee who refused to violate the law or professional codes of conduct in ways that injure or risk injury to third parties.\textsuperscript{332} Since those restrictions protect third parties, employers with employee governance should not be able to avoid them.

The extensive modern statutory prohibitions on discrimination in termination and other employment practices\textsuperscript{333} raise rather different considerations. These prohibitions are, in the first instance, about protecting employees, and hence it could be argued that employees acting collectively should be able to limit those protections if they so choose. As a society, however, we understand discrimination on the basis of race, gender, and other protected categories as categorical social evils. Moreover, these protections are often counter-majoritarian in nature, and worker governance is not immune to the influence of bias, discrimination, and bigotry against minority groups. While labor organizations have often served as forces for empowerment for workers of color, they have also served as tools of

\footnotesize{\textsuperscript{329}Brett McDonnell & Matt Bodie, To Reopen the Economy, Businesses Need a ‘Safe Haven’ Protocol to Avoid Liability, STARTRIBUNE (May 27, 2020, 6:00 PM), https://www.startribune.com/to-reopen-the-economy-businesses-need-a-safe-haven-protocol-to-avoid-liability/570815432/.


\textsuperscript{331}See supra notes 46–51 and accompanying text.

\textsuperscript{332}See supra note 49–50 and accompanying text.

\textsuperscript{333}See supra notes 52–53 and accompanying text.}
oppression.  Unions, employee directors, or general works councils are all highly problematic, as they are chosen by all employees collectively, not just by those who belong to groups vulnerable to discrimination.

One possible policy response is to incorporate governance power for organizations representing vulnerable groups. As it happens, versions of such organizations are quite common in contemporary large corporations, most of which have a number of employee resource or affinity groups based on the main categories of antidiscrimination law, such as race, gender, sexual orientation, religion, and veteran status. These organizations typically have no formal authority within a firm. However, one could imagine giving them formal oversight responsibility of some sort over alleged discriminatory practices within a firm. Because of our first concern above, we don’t think that even effective, empowered affinity groups should be able to waive antidiscrimination prohibitions. But perhaps where such organizations are adequately empowered and represent enough employees of a protected category within a firm, it might create some presumptive evidence of legal compliance by the firm that could aid it in responding to complaints of discrimination. Our proposal would tread hesitantly here, but perhaps antidiscrimination law could be tailored to encourage empowerment of affinity groups as it has been used to encourage in-house antiharassment reporting and correction programs.

C. Boundaries of Employment

What good is reforming employment if employment ceases to be a meaningful category? The growth of platform companies like Uber, Lyft, and DoorDash challenges our employee-oriented approach. These companies claim to offer a new way for people to work: outside the stricures


336. See id. at 525.

of the normal nine-to-five job, with more flexibility and opportunity. The gig economy appeared to be overhyped for some time, with only a small percentage of workers falling into that category in the early 2000s. But the growth of that sector has accelerated, spurred on even more by the pandemic. Now various calculations place the number of contingent or platform workers at 51 million—roughly a third of the U.S. workforce. This changing approach to working means that our assumptions about workplace regulation need reexamination.

Recent developments in California illustrate the difficulty in increasing the number of mandates associated with the employment relationship. California has earned its reputation as a state with an employee-friendly approach to labor and employment law. In the mid-twentieth century, the California Supreme Court established much more lenient approaches to implied-in-fact employment contracts, as well as the use of good faith to protect employee expectations. Although these doctrines have been scaled back, the state still has an array of unique approaches to employment regulation, including a high minimum wage, mandated break times, paid sick leave, and the provision of safety equipment. Its recent legislative efforts to protect workers against productivity algorithms illustrate the state’s forward-thinking approach workplace regulation.

In order to render these efforts meaningful to all workers, California had broadened its definition of “employee,” first in a state supreme court decision and then by statute. However, in 2020 California voters

342. Guz, 8 P.3d at 1112.
343. California minimum wage is $14 for employers with more than twenty-five employees as of January 1, 2021, increasing to $15 per hour in 2022. CAL. LAB. CODE § 1182.12(b)(1) (West 2018). The minimum wage for employers with twenty-five or fewer employees is $13 per hour, rising to $15 per hour in 2023. Id. § 1182.12(b)(2) (West 2018).
344. CAL. LAB. CODE § 226.7 (West 2018).
345. CAL. LAB. CODE § 246 (West 2018).
346. CAL. LAB. CODE § 6401 (West 2018) (providing that employers must furnish employees with appropriate safety equipment).
upended this framework by voting decisively in favor of Proposition 22, which removed certain platform workers from the employment category. The future of Proposition 22 is in some doubt, as a California Superior Court judge has ruled it unconstitutional for impeding the ability of the state legislature to regulate worker safety and status. But the success of the proposition with an electorate like California’s should give those who support worker protections pause. Companies such as Uber and Lyft have designs for bringing their recategorization of platform workers to states across the nation.

Drivers at ride-sharing companies and other platform workers present a challenge that goes beyond the definition of “employee.” They are part of a broader trend of disintermediation or fissuring in many companies and industries. Workers are more loosely connected to the businesses for which they work. They are more likely to be temporary and viewed as more interchangeable. They have less employment security and typically receive fewer benefits. This trend is responsible for the ongoing pressure on the definition of “employee,” but it is also discouraging for anyone who, like us, envisions a world where workers play a central role in their workplace, and where a person’s job is personally and professionally as well as financially fulfilling. How can employment law respond to this challenge? Does our proposed move from mandates to governance present a partial response, or is our proposal itself threatened by the move to gig workers and fissured workplaces?

The answer is some of both, as we can see by applying the employment and corporate law arguments we surveyed in Parts I and II to platform companies. Consider first the arguments within employment law. On the one hand, the need for regulation is often at least as strong for protecting those working for companies like Uber as it is for other employees. With their weaker ties to the company, platform workers are likely to be even more limited in access to important information. They also face stronger obstacles to internal collective action, as they interact with each other less

352. See Molla, supra note 339.
353. See supra Section I.D.
354. See supra notes 132–133 and accompanying text.
355. See supra notes 137–138 and accompanying text.
on the job. The dearth of employer-provided benefits, such as pensions or health insurance, offloads the responsibility for these social concerns onto taxpayers.356

On the other hand, the costs of our current complex system of employment regulation are also greater for platform companies like Uber.357 Major elements of that employment regulation genuinely do not fit well with the circumstances of many platform workers. For example, requiring employers to provide health care for all of their workers might not make economic sense for those Uber and Lyft drivers who only work for the companies sporadically.358 There is greater heterogeneity; some Uber and Lyft drivers prefer to work only part-time at hours they determine, while others need it as a full-time job. Their preferences as to how hours and wage regulation should apply to their jobs are likely to diverge significantly (which may be part of the reason that the California ballot initiative succeeded).359 Thus, while the need for protection remains strong for platform workers, the inadequacy of a one-size-fits-all set of rules is manifest. The arguments for allowing firms with employee involvement to opt out of some rules,360 creating space for more nuanced regulation that better fits the needs of both firms and workers, are thus particularly strong for businesses like Uber.

However, in important ways the fissured workplace challenges the idea that workers should be more involved in the governance of their workplace. Some of the strongest arguments for employee governance stem from the centrality of employees to firms, and that centrality is weakened by disintermediation. Platform workers are less tied to specific schedules and may work for a variety of different apps in the course of a day.361 Their disconnection from a traditional firm means that they are in fact more like free agents and less likely to be plugged into a worker information network.362 In addition, the fissured workplace disintegrates the firm by creating relationships between workers and a variety of entities: end-users and temp agencies; platforms and the companies that contract with them to provide services; franchisors and franchisees. In these situations, a worker

356. See supra notes 141–142 and accompanying text.
357. See supra Section I.C.
358. ALEX ROSENBLAT, UBERLAND: HOW ALGORITHMS ARE REWRITING THE RULES OF WORK 58 (2018) (discussing Uber’s claim that most of its drivers are part-time earners).
359. Preetika Rana, How California’s Prop 22 Affects Lyft and Uber Drivers, WALL ST. J. (Jan. 22, 2021), https://www.wsj.com/story/how-californias-prop-22-affects-lyft-and-uber-drivers-34a85bi3 (discussing an Uber driver’s experience as follows: “I used to work for a company, if I asked for a one month vacation, they said no, but now I can have a two month vacation, three months vacation; that’s why I like it.”).
360. See supra Section I.E.
361. See supra notes 187–191 and accompanying text.
362. See supra notes 192–194 and accompanying text.
may not have a particularly strong association with one company. For these reasons, it is less clear that employee involvement in governance is desirable in platform companies or fissured workplaces.

On the other hand, there are reasons to think that workers deserve even more governance protection at platform and fissured companies. Workers’ weak attachment to their companies may reduce their satisfaction and fulfillment; participating in governance may help counteract that problem.\textsuperscript{363} Also, note that Uber, the leading example of a platform company, has not exactly been a model of good corporate governance, and its various scandals have hurt Uber’s stockholders and customers as well as its workers.\textsuperscript{364} The participation of Uber’s drivers in governance, particularly if through electing board representatives, may still provide a useful check on management that would improve corporate governance for all stakeholders.\textsuperscript{365}

Though the arguments are thus ambivalent, we think that the move from mandates to governance could help address the challenge of fissured workplaces and the gig economy. Rather than having a clunky off/on button as to the application of employment mandates, governance mechanisms could allow workers to negotiate with platform companies for a more tailored set of terms. This flexibility might have particular pull in the gig economy, where at least some segment of workers do in fact want nontraditional work arrangements. This compromise might stop the ongoing warfare over the legal definition of employment; there are forty-nine more states and a variety of federal statutes that could easily be read to render these workers employees or not, in an endless cycle. Better to take some of the stakes away from the distinction. Plus, employment status would put the companies and workers in better stead with respect to antitrust law, which might otherwise implicate these companies in widespread price-fixing.\textsuperscript{366} Creative solutions are needed, and governance rights combined with negotiating flexibility hold some promise as a reasonable place for the parties to meet.

\textbf{CONCLUSION}

The United States has responded to the increasing disempowerment and disconnectedness of its workforce through piecemeal federal and state
mandates designed to address particular workplace or societal problems. While these legislative efforts may ameliorate harsh aspects of the employment relationship, they do not address the underlying cause: the lack of worker power to participate in workplace governance. Policymakers need to look beyond labor and employment law to the internal power structure within the organization, where employees have been shut out. A change in governance rights for workers would shift the balance of power back toward the middle and provide the opportunity for workers to participate in critical firm choices.

Our proposal replies to the main concern of corporate leaders and legal scholars who are skeptical of approaches like codetermination in Germany that mandate employee involvement in governance. They argue that corporate governance should be about protecting shareholders, and that employees (like other stakeholders) should be protected in other areas of the law. But corporate law scholars pay little attention to the rigid mandates and complexities of employment law, a style of regulation that contradicts the core values of U.S. business association law with its emphasis on flexibility and choice. We would offer businesses a new option, expanding who gets represented in corporate governance in exchange for more flexibility in employment law. If that choice does not improve life for both companies and their employees, they need not adopt it.

Employment mandates have inherent limitations that can hurt both employees and their employers. Our system needs worker power so that firms and workers rely less on external regulation and more on internal governance.