WILLIAM DAVIES

ALL OF OUR BUSINESS

WHY BRITAIN NEEDS MORE PRIVATE SECTOR EMPLOYEE OWNERSHIP

EMPLOYEE OWNERSHIP ASSOCIATION
BETTER BUSINESS TOGETHER

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William Davies
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About the Employee Ownership Association

The Employee Ownership Association is the voice of co-owned companies in the UK. The Association speaks for a sector of the economy – companies with significant to majority employee ownership – worth more than £30 billion annually and growing. EOA members include the John Lewis Partnership; global businesses such as Arup, Mott MacDonald, Unipart and PA Consulting; long-standing co-owned firms like Scott Bader, Tullis Russell and Swann-Morton; and well over a hundred other companies of all sizes from across the UK economy.

The Association exists to serve its member companies and promote employee ownership. EOA publications are designed to generate new thinking and ideas about employee ownership, and to offer advice and guidance to organisations needing to adopt or enhance employee ownership.

Find out more about how the Employee Ownership Association can help your organisaiton at www.employeeownership.co.uk

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Foreword

In the past two years, employee ownership has achieved an almost unprecedented public profile, which is great news for our sector. However, a great deal of this new attention has been on employee ownership as a possible model for the delivery of public services. Talk of 'John Lewis public services' has become part of the Coalition government's public sector mutuals programme, being run by the Cabinet Office. Precedents such as Central Surrey Health have been looked at, and the possibility of mutualising the Post Office is under scrutiny.

Without wanting to detract from these exciting developments, it's important that we remember the tremendous benefits that employee ownership can offer private sector enterprises. Many of the most severe problems afflicting our economy today stem from failures of private sector ownership – an issue the independent Ownership Commission was set up to examine. Excessive profit-chasing, failures of accountability, low levels of employee engagement have damaged many British businesses, and undermined their capacity to deliver value to customers and high quality jobs to their employees.

As we have discovered at Childbase, employee ownership offers a different path for businesses, which puts long-term development of value ahead of short-term demands for dividend. Thanks to employee ownership, we've been able to shift our entire focus on to building strong relationships between staff, children and parents. Our co-owners are engaged in the running of the business, and I believe that makes them more engaged in how they go about their work.

As William Davies argues in this important new report, few businesses are ever set up for the purpose of maximising earnings. But sadly that's often how they are later run, especially after the founders have retired, despite the fact that this has negative consequences for businesses and their various stakeholders. The report identifies two values associated with employee ownership – patience and wellbeing – which will be crucial to future business development in the UK. Taking a longer term view of the future, and a more rounded view of people in the workplace, means that employee-owned businesses are more sustainable and accountable. Whatever happens with the public sector mutualism agenda, it is crucial that these private sector virtues are not forgotten. As much as anything, it is businesses themselves that have the most to gain from engaging with this agenda.

Mike Thompson OBE
Chief Executive, Childbase

1. The Ownership Dilemma

Designco is a major British brand name, which was founded by Caroline Evans in London in the early 1980s, initially as a small designer and producer of consumer accessories.[1] It was owned and run by Caroline as managing director (MD) and a small handful of other partners, although shares were also given to employees when they joined. In the mid-1990s, Caroline spotted an opportunity to re-imagine the market sector that Designco was in, introducing an entirely new product line, which proved stunningly popular, leading to the company's rapid growth. By the early 2000s, Designco had the largest share of this market, with its own stores opening in British high streets.

While the success of the new product line was quite dramatic, it rested on long-standing relationships both within the company (which employed 100 staff in London, primarily designers and salespersons) and with suppliers overseas, who had been retained since the early years of the company. By 2005, Caroline was still the largest shareholder of a highly profitable company, and along with her co-founders and partners, was wondering how she might be able to extract some cash from the business. This is an issue that nearly all entrepreneurs are faced with eventually.

In 1984, just after Caroline had founded Designco, Hugh Facey established Estate Wire in Sheffield, to produce the wire used in agricultural fencing. Hugh wanted to tailor Estate Wire's products according to the precise needs of his customers, so commissioned some market research on how farmers actually worked. Amongst the findings was that farmers tended to tie up loose ends of wiring using their bare hands, but would pay up to 50p for a reusable product which held the wires together, at various tensions. To serve this exact need, the company developed the 'Gripple' in 1986, patenting the invention in 1988, and launching it the following year. By the early 1990s, the Gripple was selling so well worldwide that the wire business was sold, and Gripple Inc was founded.

Initially, Gripple was owned by Hugh and the finance director, although its 17 employees were all encouraged to purchase shares at the outset, of whom 11 did so. Winning numerous manufacturing awards along the way, including the BBC Tomorrow's World Prince of Wales Award for innovation, Gripple grew steadily, to the point where it now has facilities in Chicago, Strasbourg, Sao Paolo and New Delhi, plus a new sister company Loadhog employing 350 people worldwide. Other than one year, when a major customer went bankrupt, Gripple has never failed to return a profit, though Hugh's philosophy was sceptical about excessive attention to the bottom line, which he felt distracted from innovation and steady growth. Yet Hugh was also aware, like Caroline Evans, that the company needed a plan for management and ownership, beyond his own tenure and lifespan.

1 1'Designco' and 'Caroline Evans' are pseudonyms

Similarities

These two companies have various things in common, beyond their similar age and size. They are both major British success stories, having achieved success both at home and abroad. Neither quite fits with the image of the 'knowledge economy', yet both have attained their success on the basis of imagination, invention and creative endeavour. Gripple, for instance, spends 4-5% of its turnover on research and development (R&D) and patents heavily. Leadership by the founding entrepreneurs plays a key role, not least in maintaining the webs of relationships that hold the company together over time, but also in establishing the philosophy of the business. Strategic instinct dominated over profit-chasing.

Neither company is especially large on its own – neither is yet of a size where a stock market flotation could be contemplated, although it is estimated that over half of Britain's private sector is not traded on the stock market.[2] At a time when policy-makers are convinced of the need to 're-balance' the UK economy, away from its reliance on rising house prices, financial services, and consumer credit, it is innovative producers such as these that offer hope that Britain can still make and export useful, high quality goods in a competitive fashion. It is for just these reasons that the CBI has recently argued that medium-sized businesses (of between 50-500 employees) are a crucial yet sorely under-recognised contributor to Britain's economy.[3]

Neither of the entrepreneurs behind these companies wanted to turn their back on the firms that they have created, seeing as they invested so many years of effort in building relationships and reputation; but both acknowledge the need for ownership and control to be transferred sooner or later.

What to do?

Succession dilemmas

In 2005, Caroline Evans's auditor recommended that she consider a private equity sale, as a way of releasing some of her investment in the business. A trustworthy buyer was soon identified, and in 2006 Caroline and her partners sold 60% of Designco's shares. Private equity investors typically look to keep their stake for a 2-3 year period, during which time they may or may not intervene in the firm's management, depending on the type of investor and the perceived efficiency of the firm. They will then sell, ideally for a higher share price, often to a larger private equity firm. Designco's initial investors were happy with the profits they were receiving, seeing no reason to intervene, and sold to a second private equity company in 2008.

2 See. D. Erdal (2010) Beyond the Corporation: Humanity Working. Bodley Head
3 CBI (2011) Future Champions: Unlocking Growth in the UK's medium-sized businesses

The second private equity investor insisted on installing a new MD, though retaining Caroline as a director, where she could carry on developing the brand and prioritising design quality. At the very first board meeting under the new owners, she was horrified to discover that the discussion turned immediately to the investor's 'exit strategy'. Given the time horizons at work, it turned out that the new MD (who came from an entirely different sector) was determined to overhaul Designco's brand and break into the US market at great speed, to coincide with the private equity company's 3-year exit strategy. As Caroline puts it now "they're not business people; they don't have a clue; they don't understand business because they're never around long enough". With internal disputes over the direction of the brand developing over 2009, and fractious employment relations, staff started to leave. Decades-long relationships with suppliers were cut, and new, cheaper ones found.

Within two years of the new MD arriving, 60 of the London-based staff had left the company (some purely due to unhappiness, without other jobs to go to), suppliers had been dropped and then re-contracted when it became clear that the new ones weren't delivering. At the end of 2009, Caroline herself was sacked for obstructing the overhaul of the brand and attempts to cut costs. "They think that the consumer is stupid and won't notice that things have changed", she says. But of course the new owners will hope to have exited the company before that happens anyway.

Hugh Facey was always determined that Gripple wasn't going to fall into the hands of outsiders, or even remain in his own family's hands. He had seen great Sheffield steel companies fall into mismanagement, after two or three generations of family ownership.[4] At the same time, he always believed that employees should purchase shares in the company, using their own money, so as to be fully engaged in decision-making and fully alert to risks and uncertainties that are part of any business environment. From 2007 onwards, all Gripple employees have been obliged to purchase a minimum amount of shares, if necessary using low-interest loans from Gripple. Working with a lawyer, Hugh came up with an original model, which he hopes will ensure that Gripple is still operating with its original philosophy in several generations' time.

In 2011, Hugh founded GLIDE – Growth Led Innovation Driven Employee company Ltd – a company limited by guarantee which exists to hold shares in Gripple and Loadhog, although may also invest in other companies. Every year for the next ten years, Hugh and the finance director will gift 5% of their shares to GLIDE, by which point GLIDE will own around 40% of the total equity. As GLIDE builds up reserves from dividend payments, it will also buy up Hugh's remaining equity until it is eventually the majority shareholder in Gripple. Every Gripple shareholder (ie the employees) is a member of GLIDE, having the right to vote for its Directors, in a way that ensures representation for each of Gripple's international outlets. Meanwhile, two GLIDE directors are elected by GLIDE members to sit on Gripple's shareholder board. In future, GLIDE will be the 'market-maker' for Gripple shares, allowing employees to buy and sell shares, without having to go via Hugh. No outsider is permitted to own Gripple shares or become a member of GLIDE.

4 Less than 30% of all family-owned companies survive into the third generation of family ownership. 'The five attributes of enduring family businesses', McKinsey Quarterly, January 2010.

The most important innovation in this model is the presence of two 'golden shares' in Gripple, one issued to GLIDE (to be exercised by its board), and the other issued to a Facey family trust established by Hugh. These golden shares exist primarily for the purpose of vetoing any shareholder movement to sell the company to external owners, and trump all other voting shares in doing so. They can be used in no other way. So while shares can circulate internally, amongst Gripple employees and GLIDE, they never find their way onto the open market. As a result, Gripple is protected from any takeover, private equity buy-out or trade sale. Hugh's children will inherit enough to live on, including shares in Gripple and Loadhog, but they will not inherit the company itself.

Varieties of capitalism

Business succession is a thorny problem, to which there is no straightforward answer. Overcoming succession dilemmas, or avoiding them in the first-place, is one of the central motivations for the establishment of employee-owned structures in the private sector.[5] Any entrepreneurs, family owners or company partners who want to preserve what is distinctive and valuable about their company, over and above its profit-making potential, would do well to consider the options employee ownership offers. The solution which Hugh Facey invented for Gripple is complicated and unusual, and quite unlike the form of 'indirect' or 'mutual' ownership which characterises the John Lewis Partnership, in which shares are held permanently in a trust on behalf of all employees, but do not circulate at all (see Box 1). But the significance of these two contrasting stories does not lie in the technical intricacies of their respective ownership solutions. What it concerns, and what this report explores, is two different ways of conceiving of economic value and economic efficiency.

Box 1: What is employee ownership?
'Employee-owned' firms are businesses in which the majority of the shares are owned directly by employees, or owned on behalf of all employees in some sort of special purpose legal entity, such as an Employee Benefit Trust (EBT). Where ownership occurs via a trust, this is commonly referred to as 'indirect ownership', and could otherwise be described as an employee 'mutual'. Mutuals have no external shareholders, but instead have members, who are typically granted some voting rights and/or representation at board level, plus receipt of any dividend payments. Private sector employee mutuals include the John Lewis Partnership and Arup. The model has also been applied in the public sector, in cases such as Central Surrey Health. Direct employee ownership involves employees owning shares themselves, much as most listed companies offer shares to their employees as part of their remuneration. Firms owned directly by their employees may take some measures to ensure that shares cannot be sold externally. PA Consulting or the Florida-based company Publix, which employs 140,000 people, are examples of this.

Employee-ownership is achieved in various ways. Firms may be founded and grown without any external shareholders in the first place, financing themselves via retained earnings and debt finance, but distributing shares to new employees as they arrive.

5 See EOA (2005) Employee Ownership as a Solution to Business Succession

Private and family-owned businesses may convert to employee-ownership via an employee-buy-out, either by leveraging the assets of the firm to be bought, or through sympathetic equity finance from funds such as Baxi Partnership. Ownership may be gifted to an EBT as an act of philanthropy, or transferred out of state ownership into an EBT, as the Coalition Government has committed to doing with various public services. The turnover of the entire employee-owned sector is estimated at over £30bn or around 2-3% of the economy. The turnover of the entire mutuals sector, which includes building societies, consumer co-operatives and foundation trust hospitals, is around £100bn a year.

According to one economic philosophy, efficiency is achieved through rapid entry and exit of owner-investors, managers, and other stakeholders, on the basis that market prices are the best signal of value and the best incentive for value creation. The various interests that influence the direction of a company are best expressed through maximising the power of *exit*: management performance is improved, thanks to the knowledge that shareholders, customers and even employees could find and exploit other economic opportunities elsewhere at any time. By this account, commitment to particular suppliers, employees or customer expectations – as Caroline Evans had shown before the sale of Designco – is, in all likelihood, a form of sentimentality or habit that needs breaking, so as to unleash more price competition and faster innovation, resulting in higher profit. Management's task must be to extract the greatest surpluses from the productive process, so as to pass these on to the legal owners of the company, and subsequently swell the value of their shares, before shareholders exit in search of higher returns elsewhere. This philosophy assumes that human beings are largely motivated by the desire to maximise their personal reward, at least in the economic realm, and that they are sufficiently good at calculating the costs and benefits of their decisions that they can be trusted to do so efficiently.

According to a rival economic philosophy, efficiency is achieved through a more subtle, relational form of organising and networking. The various interests that influence the direction of a company are best expressed through *voice*: dialogue between management and customers, suppliers, employees and investors can ensure that concerns are raised, deliberated and factored into decision-making. Without some commitment between management and various stakeholders, it may be possible to affect the level of profit and share price in the short term, but it is impossible to accumulate intangible business value, because there is no institutional memory of any kind. Intangible value, associated with ideas, effort, reputation and trust, is not something that can be easily captured, quantified, stored or accounted for by book-keepers. It is shared gradually via relatively stable relationships, rather than bought and sold instantly in markets. The task of the manager, within this second philosophy, is to build this intangible value slowly and carefully. A more nuanced understanding of human psychology accompanies this, which makes wellbeing both a component and a goal of valuable business activity.

In the past, this choice has often been posed in terms of rival national 'varieties of capitalism', with 'Liberal Market Economies' (such as Britain and the United States) privileging looseness of economic relationships and exit, and 'Coordinated Market Economies' (such as Japan and Germany) privileging commitment and voice.[6] In the mid-1990s, the economic commentator, Will Hutton, argued forcefully that Britain should shift from the former to the latter, using statutory legislation to alter how companies were owned and governed.[7] With Hutton's argument largely lost, British firms and policy-makers nevertheless spent much of the last decade, seeking ways of increasing the commitment and 'engagement' of employees, in the vain hope that this could be achieved without altering business structures or philosophy.[8]

A matter of choice?

The contrasting cases of Designco and Gripple could not be easily combined in a single model. By selling shares externally, and losing control of the company in the process, Caroline Evans saw decades of business relationships unravel, and is now watching the brand's reputation deteriorate. Like many founders and owners who have opted for employee ownership, Hugh Facey specifically wanted his company to remain more than a moneymaking machine.

Some might argue that these two examples simply represent different preferences on the part of two entrepreneurs. There is some evidence that firms with external owners, and looser market-based relationships, are capable of growing faster, through higher risk-taking, though there is very little evidence of this in the UK.[9] Not only that, but Caroline Evans received a significantly greater monetary reward following her departure from the company than Hugh Facey will. Is it not the private choice of an entrepreneur and owner, whether to maximise profit and return on investment, or to prioritise the long-term cohesion and purpose of the firm they created? Certainly it is. But two caveats need adding.

- Firstly, very few managers, founders and entrepreneurs currently understand employee ownership, or the options it offers them. Businesspeople such as Caroline Evans feel cheated by ownership transfers, often despite the financial gain that they make from them. Professional advisors – lawyers, accountants, consultants - are working under the assumption that the purpose of founding, growing, managing and transferring a company is to maximise private wealth, and any other benefits are unintended 'externalities' (this is also assumed in much business school teaching, and is a guiding assumption of neo-classical economics). Yet there is an important psychological and cultural difference between getting 'rich' and getting 'as rich as possible'; many entrepreneurs and business leaders see financial return as just one of many benefits that a business can generate. An economist or financial analyst may not grasp this distinction, but a successful entrepreneur or businessperson almost certainly will.

6 See P. Hall & D. Soskice (2000) Varieties of Capitalism: The Institutional Foundations of Comparative Advantage. Oxford
7 W. Hutton (1995) The State We're In. Jonathan Cape
8 See D. Mcleod & N. Clarke (2009). Engaging for Success: enhancing performance through employee engagement. BIS
9 See H. Reed (2010) Reinventing Venture Capital: Towards a new economic settlement, Demos, on the failings of private equity in Britain

- Secondly, and more pertinently for the public and for policy-makers, the negative consequences of short-term profit maximisation, for society and for business, are becoming ever plainer. The Harvard Business School guru, Michael Porter, traditionally seen as a free market conservative, argues the following:

  Companies must take the lead in bringing business and society back together. The recognition is there among sophisticated business and thought leaders, and promising elements of a new model are emerging. Yet we still lack an overall framework for guiding these efforts, and most companies remain stuck in a "social responsibility" mind-set in which societal issues are at the periphery, not the core.[10]

What Porter calls for is a new focus on 'shared value', at the overlap between public and business interests, rather than a mentality which deals with 'social' issues, only after shareholders have been paid as much profit as possible. But what would this look like in practice?

The argument to be made over the next two chapters is that employee ownership models offer an alternative conception of an enterprise that fits closely with contemporary social and economic needs. The choice between an economic philosophy based upon rapid profit and exit, and one based upon gradual growth and voice, is becoming stacked ever more in favour of the latter, for reasons that we now explore.

10 M. Porter & M. Kramer (2011). 'Shared Value', Harvard Business Review

2. Old Malaises, New Values

Large swathes of the British private sector have become mired in controversy and distrust. Whether or not this is directly related to the banking crisis, there is a widespread suspicion that companies are being run in the interests of small coteries of elites, be they executives swelling their own remuneration, or financial deal-makers focused primarily on discovering new ways of charging fees, related to the financing, buying and selling of companies.

The 2010 takeover of Cadbury's by the American company Kraft pushed questions of ownership, control and the fundamental purpose of British companies into the limelight. The High Pay Commission has published a startling array of evidence, demonstrating that business executives have now all but given up any pretence of 'earning' their vast pay deals: between 1998 and 2009, average CEO pay of FTSE100 companies rose by 6.7% a year, to £3.4m, while average earnings per share fell by an average of 1% a year over the same period.[11] Boardroom pay rose by an astonishing 49% in the year leading up to October 2011.[12]

Meanwhile, much of the apparent dynamism and wealth creation of the British private sector, pre-2008, has subsequently proved to be an illusion. The Treasury calculates that the economic crisis has wiped out 25% of the wealth that was created in the decade running up to 2007.[13] Outside of the South East, the New Labour economic boom generated no private sector job growth at all, a fact that was disguised by public sector growth.[14]

A diffuse political and cultural sense has emerged that Britain's model of capitalism involves sacrificing long-term gains for short-term monetary rewards and excessive returns. The dominance of the financial sector within the British economy, of finance capital over businesses, and of London over the UK, created an economic culture of impatience, which makes long-term value creation seemingly impossible. Ironically, the obsession with short-term earnings even defeats itself over the longer-term, and profit-maximisation eventually leads to smaller profits – a paradox that the economist John Kay identifies as an example of 'obliquity' at work.[15]

What is emerging from the interlinked crises of capitalism and of Britain's elites more generally is a sense that institutions, including businesses, have become instruments to serve particular minority private interests. The economic culture of rapid exit mitigates against the psychology of responsibility, duty or accountability, of the sort our political leaders claim to favour. It transpires that CEO pay has been pushed up even further by the growing tendency to appoint new CEOs from outside of firms.[16] Due to so many economic and moral failings, orthodox definitions of 'efficiency' and 'value', and the role of external financiers in promoting them, are now without credibility. The more positive question is – what would an alternative concept of efficiency and value look like? Here I identify two dimensions of an alternative, which are interlinked: patience and wellbeing. As Chapter 3 will explore, employee-owned companies do far better at factoring these values into their decision-making, largely because they lack pressure from external shareholders. Managers are held to account by employee-owners who understand a business's intangible value and the subtleties of how it is created.

11 High Pay Commission (2011) Interim Report of the High Pay Commission
12 IDS (2011) Directors Pay Report 2011/12
13 BIS (2011) The Plan for Growth
14 J. Buchanan et al (2009). Undisclosed and Unsustainable: Problems of the UK National Business model. CRESC Working Paper No. 75
15 J. Kay (2011) Obliquity: Why our goals are best achieved indirectly. Profile
16 High Pay Commission (2011), which states that "A growth in external hiring and the costs this represents, resulting from poor succession planning, has had an upward pressure on pay, again without necessarily resulting in improved performance"

Patience as a business value

The ‘shareholder value’ ideology, which depicts businesses as financial products to be exploited in the interests of shareholders, has haemorrhaged support for a number of reasons. The fact that the ideology has in fact worked much better for executives than for shareholders robs it of its credibility – according to shareholder value theory, executives should be remunerated in direct proportion to the value they deliver to shareholders, but we have already seen that this has not occurred. It also works well for the investment banks and lawyers who oversee mergers and acquisitions, which are performed under the veneer of increasing returns to shareholders, but which typically fail even by this limited standard of performance.[17] It is increasingly clear that the primary beneficiaries of the current British business model are the consultants and brokers who facilitate it and mediate its transitions.

As a result of this focus on fees and maximisation of individual remuneration, the speed of financial activity has increased markedly over the last few decades. In 1960, shares were held for an average of 5 years, whereas in 2007 this had shrunk to 8 months.[18] At best, the dominance of equity shareholders focuses attention on the medium-term future: private equity investors do at least spend 2-3 years engaged in the running of a company, even if this means sacrificing any longer term strategy as the case of Designco demonstrated (for example, the private equity industry admits that R&D levels fall under private equity ownership, given that its benefits typically take longer than 3 years to realise).[19]

Research on listed companies shows that investors and managers make scarcely any attempt to value the company in terms of its potential future earnings and base nearly all of their decisions on fluctuations in most recent earnings.[20] It is scarcely surprising then that 78% of managers say that they would avoid pursuing a project that offered long-term value creation, if it was damaging to short-term earnings.[21]

The capacity of a business to create wealth depends on its ability somehow to resist these forces for maximisation of earnings and fees. Andrew Haldane, the Bank of England’s executive director for financial stability, argues that we urgently need to recognise delayed gratification as a necessary ingredient of economic growth, indeed of progress.[22] The creation of value in any business is a slow process, which requires a degree of stewardship on the part of both managers and owners. Insiders will have far greater insight into how this value will be grown, because often it is tacit and ambiguous in nature, and not entirely reducible to the numbers which show up in accounts.

17 BIS (2010) A Long-term Focus for Corporate Britain
18 BIS (2010)
19 J. Gilligan & M. Wright (2008) Private Equity De-mystified: An explanatory guide. ICAEW Corporate Finance Faculty
20 See A. Rappaport (2005) The economics of short-term performance obsession. Finance Analysts Journal. Vol 61 Number 3
21 High Pay Commission (2011)
22 A. Haldane (2010) Patience and Finance. Speech at the Bank of England

When owners and managers are constantly changing, they are consequently far more likely to focus on monetary representations of value, as these are unambiguous. Chairmen of listed companies have complained that shareholder engagement, to the extent that it happens at all, suffers from complete reliance on accounting information, and an absence of any interest in 'substance'; but this is a feature of the weakness and brevity of a typical shareholder relationship with a firm more generally.[23] Returning to the theme of 'obliquity', the activities that make profit possible at all – invention, R&D, customer service, training – must somehow be insulated from the profit motive and a logic of market valuation, if they are to succeed. Patience means treating profit as a beneficial bi-product of business, and not its purpose. Private sector mutuals, such as John Lewis Partnership might be described as 'profit-making' but not 'profit-maximising', but it is no coincidence that many of them are far more profitable than their competitors who are supposedly run on behalf of shareholders.

The value of patience is quite clear in other areas of business and the economy. Rapid turnover of staff is highly inefficient, especially where non-transferable skills, tacit knowledge and employee engagement are required. Building the reputation of a brand is a slow process, as it is fundamentally about winning the trust of existing and potential customers. Where intangible assets are concerned, accumulating value requires the development of institutional memory – customers return to the supplier who served them well before, organisations discover paths to innovation through trial and error, employees discover over time if managers are to be trusted.

The challenge of economic patience arises at household and macro-economic levels, as entire nations have discovered that prioritising immediate desires over long-term investment and saving, produces disastrous economic, social and environmental results. Patience is no longer an old fashioned economic virtue, but the single most important ingredient of whatever business and economic model will arise out of the present crisis.

Wellbeing as a business value

'Wellbeing' refers to a cluster of psychological, social, economic and physiological benefits, but with a particular priority attached to the psychological. Amongst these is happiness, or what is otherwise referred to as 'subjective wellbeing'. Governments, statisticians and economists have shown growing interest in levels of wellbeing and happiness in recent years, recognising that economic growth and monetary wealth may not be adequate representations of a society's progress. One reason for this is that wellbeing is something that policy-makers care about, in and of itself; but another is that low levels of wellbeing rebound on public services and employers, bringing economic costs and inefficiencies with them. Carol Black's review of the wellbeing of working age adults in the UK discovered that health-related absence from work (including stress and mental-health) was costing the UK economy almost as much as the entire NHS, in terms of sickness benefit, lower workplace productivity and lost tax receipts.[24] Wellbeing is not only a social or moral issue. As a result, policy-makers have been trying to engage the HR profession in taking wellbeing more seriously, and recognising its importance to business.

23 BIS (2010). "it is claimed that engagement is falling short because not enough effective engagement is taking place on issues of substance. Some chairmen have complained that too much engagement takes the form of discussion about quantitative analysis rather than business fundamentals." P. 20

24 C. Black (2008) Working for a Healthier Tomorrow, DWP

The connection between a healthy, happy workforce and productivity has been recognised for decades. Efforts by management to study and improve the psychological experience of work date back to the early twentieth century, and are always motivated by some combination of philanthropic and business instinct, in varying balances between the two. However, recent developments in wellbeing research mean that it is no longer something that should be seen as something 'external' to the core economic purpose or governance of a business, for a number of reasons.

- Firstly, the level of stress in British workplaces is creating significant strains upon both employers and government. The number of people who claim to be working 'very hard' or 'under a great deal of tension' in the UK has been rising steadily since the 1980s.[25] Low levels of wellbeing themselves translate into low levels of productivity, and a higher level of staff turnover and absence.[26] The CIPD has calculated that 320,000 people each year leave a job due to stress, placing a burden on employers that very few properly appreciate. In 2011, stress became the single biggest cause of absence from work, overtaking physical ailments and injuries for the first time.[27] A much more acute understanding has emerged in recent years, regarding the interplay between the health, commitment, happiness and productivity of employees, with sustained disengagement from work and decision-making now being recognised as a potential source of both mental and physical ill-health.[28]

- Secondly, research on wellbeing, and in economic psychology more generally, highlights the various deficiencies of treating people as motivated entirely by the maximisation of income. Happiness research demonstrates that ever greater increases in income cease to correspond to increases in happiness, once individuals reach an above-average level of income.[29] By the same token, it is not clear that ever larger performance bonuses or salaries can possibly convert into proportionate increases in motivation for senior executives. Instead, behavioural economics shows that human beings rapidly adjust to increases in wealth, take them for granted, and start to measure themselves against those around them, rather than against the social average.

- What *does* create motivation (and conversely, stress and disengagement) on the other hand, has far more to do with participation in decision-making and clarity regarding the strategic direction of an organisation. What raises stress and disengagement is erratic, short-term decision-making, such that employees start to feel that they have no say in or insight into the business problems that shape their lives. The CIPD finds that employees are most engaged in the voluntary sector, and least engaged in the private sector. Meanwhile, research by The Work Foundation discovers that less than a quarter of employees identify levels of pay as a primary indicator of 'good work'.[30] No doubt there are workplaces where maximisation of personal reward is the dominant ethic, but these are not pleasant ones to work in.

25 D. Coats & R. Lehki (2008) Good Work: Job quality in a changing economy. The Work Foundation
26 See World Economic Forum (2010) The Wellness Imperative: Creating more effective organisations.
27 CIPD (2011) Absence Management Survey 2011
28 D. McLeod & N. Clarke (2009)
29 See R. Layard (2005) Happiness: Lessons from a new science. Allen Lane
30 S. Constable et al (2009) Good Work. Work Foundation

None of this is to suggest that feelings and dialogue now trump hard economics, but that organisations (and societies) which neglect the psychological and communicative aspect of business will perform worse by many measures, including monetary ones. Nor is it a justification for disregarding pay – especially fair pay - as a contributor to job satisfaction. To recognise wellbeing as a business value is simply to appreciate that human beings thrive – in their minds, bodies and selves – when they are in relationships that are reasonably enduring and respectful, and which enable them to view the future in an informed and confident fashion. It can be more stressful to be in a secure, well-paid job, but in a culture of insecurity, greed and uncertainty, than to be in a less secure, less well-paid job, but where one is spoken to as an equal and provided with information regarding the future.

A new economic and business model cannot promise to eradicate inequality and insecurity altogether, but it could promise a new egalitarian ethos when it comes to consultation and sharing of information, as a basis for greater humanity in the economy.

Making the connection

Patience and wellbeing are the values that must be at the heart of a new era for British business. To describe them as 'values' is not to suggest that they are simply rhetorical add-ons to profit-maximising entities, in the manner of corporate social responsibility. They are values in the same sense of the term 'economic value': measurable entities to be invested in and grown, but which have spillover benefits for society. Shifting Britain's business culture towards longer time horizons and a broader understanding of its human impact is a challenge for both public policy and organisations.

The connection between the two, and the relevance of employee ownership in this, lies in the place of profit in society. Profit and happiness are both things which are best pursued 'obliquely': they tend to be best achieved by focusing on other things. Hence, profit-maximising firms and self-interested individuals tend to neglect the very activities that deliver what they're after. In both cases, enduring and dependable relationships are the most valuable resource, whether for making money or achieving happiness.

But the psychology of earnings maximisation, in the boardroom, the shop floor or in society, mitigates against the very assets that are most needed. As the historian Avner Offer argues, "well-being is not measured merely in terms of the abundance of goods and services. It requires a sustainable balance between the present and the future".[31] The question is how to tip Britain's business culture towards a more honest valuation of the future.

Andrew Haldane of the Bank of England argues that the British economy requires more 'pre-commitment devices' – institutions which deal with the psychological tendency to under-value the future, and pursue excessive short-term enrichment.[32] One of the distinguishing characteristics of employee-owned companies is that they are profit-making (usually) but not profit-maximising; profit is one of various desirable side effects of their core business purpose, which will lie in work, cooperation and production. It inculcates and thrives on patience and consideration of wellbeing. The next chapter examines how employee owned companies display the very traits that are sorely needed in Britain's private sector economy.

31 A. Offer (2006). The Challenge of Affluence: Self-Control and Well-Being in the United States and Britain Since 1950. Oxford University Press, p. 3

32 A. Haldane (2009).

3. Employee Ownership as 'Commitment Device'

Many organisations, in the public, private and voluntary sectors, will suffer from the problems of impatience and unhappiness described in the previous chapter. Moving beyond a psychology of short-term earnings maximisation, and towards a greater valuation of future outcomes, is a cultural challenge that extends across our economy and society today. Of course employee ownership is not going to transform the character of British capitalism on its own. However, there are good reasons to believe that employee ownership offers a means of organising businesses which makes them far less liable to fall into a mindset that privileges quick fixes and greed.

This doesn't simply mean that they are 'nicer' than their shareholder-owned rivals, although some might be judged as such. It certainly doesn't mean that they are less 'business-like' or less well managed. What it means is that they operate with different concepts of efficiency and value whichrest on more nuanced understandings of both *time* and of the *human* dimension of work and production. They don't make saints of managers or employees, but create obstacles to the human temptation to maximise personal gain and to duck out of difficult situations; collaboration and hard work become harder to avoid. In this sense, employee ownership is a 'commitment device'.

Many businesses expend a great deal of effort and money in seeking to counter-balance the worst ravages of their own short-term profit maximisation. As firms become more focused on the bottom line, so they develop new problems of staff retention and public reputation. Rakesh Khurana of Harvard Business School argues that the rhetoric and cult of 'leadership' in Anglo-American business culture only emerged in the 1980s to disguise and counter-act the fact that a new generation of executives had emerged, who saw their responsibilities in primarily monetary terms, namely of increasing earnings (ostensibly shareholders', though also their own).[33] Human resources and corporate social responsibility specialists, working to increase 'motivation' and 'ethical reputation' respectively, are only necessary because the core structure and focus of British firms discounts their own longer-term human and public dimensions.

The promise of employee ownership, and one of its many efficiencies, is that 'motivation' and 'ethical reputation' come to appear as non-problems. Being organised and owned differently, without the constant threat of investors exiting, engagement with staff and other stakeholders can become the primary focus of management, rather than the add-on once shareholders have been satisfied. And to the extent that relationships are more enduring and reliable, then more tacit knowledge and intangible business value can be shared, both inside and outside the firm. Dialogue and engagement can focus on qualitative issues of 'substance', in addition to the accounting information that concerns speculators and external investors. Of course bad management is a problem that can affect any organisation, however owned, but managers of employee owned firms have the option to marshal greater commitment from their staff, over longer time horizons.

33 R. Khurana (2007). From Higher Aims to Hired Hands: The Social Transformation of American Business Schools and the Unfulfilled Promise of Management as a Profession. Princeton.

Patience via employee ownership

There is abundant evidence that employee ownership generates productivity and performance gains for business. Firms that are not majority employee-owned experience some productivity gains from distributing shares to employees and from increasing the number of employees who own shares.[34] Firms with a 'significant' amount of employee ownership have out-performed the FTSE100 by an average of 10% annually, since 1992.[35] The American model of Employee Share Ownership Plans (ESOPs), which sees employees slowly increase their collective ownership of their company, sometimes up to 100%, has been studied extensively, and the majority of studies have discovered significant productivity benefits.[36] Other business benefits have been identified, including sales per employee and innovation.

To understand why these benefits might come about, we need to recognise that they cannot be explained purely in terms of monetary incentives. One of the most common findings in the academic research on employee ownership is that it will only deliver productivity benefits if it is accompanied by additional forms of employee participation in decision-making.

Employees need to be given the rights and responsibilities that come with ownership, and not only the dividend payments. Research on employee share ownership (i.e. direct ownership, not mutual/indirect ownership) indicates that it only delivers clear productivity enhancements when *all employees are included in an ownership scheme*.[37] Stock options, which drive much of the inflation in executive remuneration, are found to deliver no clear productivity benefit, unless they are offered to all employees.[38] Motivation and effort do not carry on increasing in proportion to earnings, as neo-classical economics would assume; the mismatch between executive earnings and corporate performance is proof of that. Instead, the critical issue is whether the ownership structure produces a sense of genuine shared purpose across the workforce.

Both the mentality of employment and the mentality of ownership are liable to suffer from impatience, as we saw in the previous chapter. Both employees and shareholders are accused of being disengaged, which is another way of saying that they do not take an interest in the long-term performance of the company. Under typical business circumstances, both tend to see 'exit' as a greater source of power in the company than 'voice'. But when the two roles are combined - when the employees are also the owners - the myopia of both perspectives is potentially overcome. The employee-owner is able to identify with the longer-term strategic interests of the company, confident that they will benefit from the creation of intangible business value in the long run, including via dividends. One study looked at a US firm, where employee ownership was increasing from 22-80%, and discovered that reported intention to leave the company declined dramatically.[39] Reduced staff turnover is one of the frequently-cited benefits of employee ownership, in surveys of managers in this sector.[40]

34 Oxera (2007) Tax Advantaged Employee Share Schemes: Analysis of productivity effects. Report 2: Productivity measured using gross value added; A. Bryson and R. Freeman (2008). How does shared capitalism affect economic performance in the UK?. NBER
35 Field Fisher Waterhouse (2011). The Employee Ownership Index.
36 EOA (2010). The Employee Ownership Effect: A review of the evidence.
37 A. Bryson & R. Freeman (2008); EOA (2010).
38 A. Bryson & R. Freeman (2008)
39 EOA (2010).
40 See P. Burns (2006) Good Business: The Employee Ownership Experience, EOA

One of the most rigorous economic studies of employee-owned business in the UK confirmed the sense in which these organisations operate with different time horizons. Carried out over the course of the 2009 recession, the study by Cass Business School was able to look at how employee-owned and non-employee-owned firms responded to the business cycle.[41] It found that the growth, profitability and job creation of employee-owned firms was more resilient than non-employee-owned firms. Both sales growth and profits were slightly lower than non-employee-owned rivals prior to the recession, but less affected by the recession; moreover, employee-owned firms created more jobs during and immediately after the recession. Less permeated by the booms and busts of the financial economy or short-term imperatives, employee-owned businesses have a steadier long-term trajectory. Valuing patience brings less exuberance during the good times, but less doom during the bad times.

Wellbeing via employee ownership

New research conducted by Professor Ron McQuaid of Edinburgh Napier University Business School has compared wellbeing in employee-owned companies with similar data from the rest of the UK's private sector.[42] McQuaid finds that employee-owned businesses create higher levels of wellbeing amongst their workforce than their conventionally-owned competitors - judged by a range of indicators, such as absence, stated intention to leave a workplace and willingness to recommend an employer to others. It is also known that staff turnover in employee-owned businesses is lower, which reflects on the wellbeing of their staff.[43]

It is difficult to specify exactly why this might be the case, but we can draw some inferences from studying existing evidence on wellbeing and work from elsewhere in the private sector. Firstly, employee-owned firms typically prioritise dialogue between employees and managers, and transparency of information and business decisions. Employee-owners are highly engaged in concerns about the direction and management of their company, to an extent that can be challenging for managers, but is ultimately beneficial. Being engaged at work, listened to by management and committed to achieving long-term outcomes has a positive effect on mental wellbeing: 86% of employees classed as 'engaged' report that they very often feel happy at work, compared to 11% who are classed as 'disengaged'.[44] 54% of disengaged employees report that work has a negative impact on their physical health.[45]

The degree of power that is devolved to employees in employee-owned firms varies considerably. Many will introduce formal, democratic structures, via which employees gain board-level representation, but remain managed by professional managers. Others will offer little formal recognition that the employees are also the owners. Companies such as Gripple involve founders drawing up constitutions, through their own imagination. There is no perfect governance structure, guaranteed to maximise the engagement and wellbeing of staff.

41 P. Lampel et al (2010). Model Growth: Do Employee Owned Businesses Offer Sustainable Performance. EOA
42 Research to be published by the Employee Ownership Association
43 M. Festing et al (1999). Financial participation in Europe – determinants and outcomes. Economic and Industrial Democracy, vol 20 No. 2
44 McLeod & Clarke (2009)
45 McLeod & Clarke (2009)

What may be just as important in employee-owned firms is the informal effect of their ownership structure, which is the more egalitarian culture that pervades these workplaces. Research by The Work Foundation shows that 85% of employees believe their workplace culture is defined by formal processes, but only 6% are happy about this.[46] Employee-owned firms may or may not have a formal, written constitution, but they do particularly well at generating thriving, informal workplace cultures, in which relationships develop across the division between managers and non-managers. The 'bottom up' aspect of workplace culture is often the most important psychological and motivational resource for employees, and also a more efficient means of information-sharing than any formal process.

But what distinguishes employee-owned firms is that this includes everyone, without any distinction between who is a partner or owner, and who is 'just' an employee. Their flatter, more egalitarian culture represents a clear advantage, an ethos that conventionally-owned firms pay rhetorical lip service to, but find it but generally find it impossible to generate to the same extent.

Secondly, employee-owned firms are likely to generate higher levels of wellbeing, by virtue of having a long-term organisational purpose, beyond the pursuit of higher profits. All of the evidence collected by the CIPD suggests that the most important contributor to workplace wellbeing is the sense of working collaboratively towards well-understood, long-term goals. Studies of happiness show that employees are most happy in the voluntary sector, and least happy in the private sector.[47]

The problem of stress in British workplaces is not simply a problem of working too hard or too long, but of working towards unclear goals and without any sense of collective spirit. Managers in employee-owned companies frequently report that they can extract far more effort from their staff when it is needed, than they could in a conventionally-owned company - (Hugh Facey boasts that Gripple was the only company operating in Sheffield's Don Valley the morning after the 2007 floods, because his staff chose to be up all night clearing water from the factory floor). Hard work and wellbeing are not mutually exclusive. Hard work becomes stressful when its contribution to a broader purpose is not clear to the employee, and goes unrecognised by the manager. This is where employee-owned companies have an advantage: employees are able to identify the longer-term benefit of hard work, and feel part of a collective that is larger than just themselves and their immediate colleagues.

46 Work Foundation (2009)
47 CIPD (2010) Employee Outlook: Emerging from the downturn?

Thirdly, it is now widely known that high levels of economic inequality across society are bad for our physical and mental health, and this pertains within organisations as much as across nations.[48] While there are no quantitative data on levels of pay inequality inside employee-owned firms, anecdotal evidence would suggest that they are significantly lower, though by no means negligible. Charlie Mayfield, executive chairman of the John Lewis Partnership, received total remuneration of £850,000 in 2010, compared with £7.3m (plus £7m 'golden hello') for Marks and Spencer's CEO, Marc Bolland, who only joined the company that same year. These are both extremely high levels of income, but one is 520 times the salary of a sales assistant, whereas the other is only 60 times. There are choices to be made regarding the most acceptable and efficient level of inequality within a company.

Employee ownership appears to put a break on accelerating pay inequality, for various inter-related reasons. The Equality Trust has pinpointed greater voice for employees as a critical factor in the battle against ever-greater inequality across society, arguing that:

> *greater economic democracy is essential in order to transform our economy, reduce income differences by bringing pay differentials under democratic control, redistribute wealth and create the foundations for a healthier, happier and more sustainable society.*[49]

But again, informal norms may be just as powerful as formal rights and responsibilities. When managers confront the owners of a firm on a day-to-day basis, and know them personally over many years, this exerts a greater sense of accountability towards them. Awarding oneself a pay package that is several *hundred* times greater than that of many staff would be psychologically that much harder in an employee-owned firm.

48 R. Wilkinson & K. Pickett (2009) The Spirit Level: Why More Equal Societies Almost Always Do Better. Allen Lane
49 http://www.equalitytrust.org.uk/take-action/economic-democracy

4. The Private Sector Agenda

Chapter One identified two rival philosophies of economic value, that businesses can embody. The first privileges the power of 'exit', and rapid turnover of all stakeholders, including shareholders, management and employees. Its proponents argue that this philosophy breeds efficiency, dismantling obstacles to innovation and profit. But in the last four years, it has become mired in a legitimacy crisis, as it appears to lead primarily to the personal enrichment of those who enforce and facilitate this model.

The second philosophy privileges the power of 'voice' and institutional memory, such that relationships between owners, managers and employees are sufficiently strong that information can be shared, and difficult economic times can be weathered. This can be difficult to realise in our culture of short-termism and distrust, but the argument made in this paper is that it is substantially easier in situations where the owners are also employees, and the employees are also owners. Employee ownership is a 'commitment device', which can save businesses from their own worst tendencies.

The employee-owned sector is not currently large enough to bring about a wholesale change in the character of the British business model, although the mutuals and co-operatives sector at large (which includes building societies, credit unions and consumer co-operatives) can make a significant contribution to alleviating many of the malaises of corporate governance, especially in the financial sector. They are also more numerous and high-performing than many policy-makers appear to realise. The point that this report seeks to stress is that it is not only employees who suffer from a model of short-termist, earnings-obsessed business, but also shareholders, entrepreneurs and businesses, whose long-term interests are frequently neglected by the ethos of profit-maximisation. Eventually, society and public services are impacted negatively by business models and business culture that take such a narrow view of human psychology, as has prevailed in the UK over the past thirty years. The spill-over costs of bad workplace relations are now increasingly falling on the NHS. Viewed this way, it's not clear that dominant notions of 'efficient' business practices are really as efficient as all that.

There is a single question which constantly haunts enthusiasts for employee-ownership: if it's so great, why isn't there more of it around? While the sector is worth an impressive £30bn-plus to the UK economy, that is still smaller than many of its proponents would wish. What needs to happen, if more of the benefits recognised in this report are to be realised?

First and foremost, more business people – entrepreneurs, managers and private owners – need to be made aware of the possibilities that employee-ownership could offer them, then seize the opportunity to start shifting the core values of the British private sector. Ultimately, if business is to be run for a greater purpose than the fastest, biggest buck, that represents a challenge for the business community itself.

The business agenda

It is crucial that business leaders, the business lobby and educators demonstrate support for alternative models of ownership which place long-term productive purpose at their heart. The CBI has rightly drawn attention to the potential benefit that medium-sized enterprises can deliver to the UK economy, highlighting that these businesses are more innovative and investment-focused than either small or large businesses.[50] This is an area of the economy which is well-suited to employee ownership, for founders of new companies, those looking to grow small companies without selling shares externally, or those – such as the case of Caroline Evans discussed in Chapter One – facing a question of business succession. However, at present it is assumed by professional advisors, business spokespersons and business training that maximisation of earnings is the motivation for going in to business, and that return on equity is the best indicator of performance.

The CBI can take a lead here, in celebrating the diversity of Britain's private sector, and the virtues of businesses which exist for long-term value creation. With 50% of the private sector not listed on the stock market, there is no reason to view PLCs and the pursuit of shareholder value as the 'normal' way of running and owning businesses. And with business facing something of a legitimacy crisis, in the context of sustained economic stagnation and high levels of economic inequality, it is crucial that business spokespersons offer a different vision of entrepreneurship and leadership from the one that treats a CEO as the delegate of the financial sector, sent to run a business in the interests of rapid return on equity. The business lobby could benefit hugely from demonstrating its commitment to long-term wealth creation, and recognising public concerns about how many companies have become vehicles for the enrichment of small circles of consultants, financiers and brokers.

Business education is also in a legitimacy crisis. It has long been known that business education is highly subject to fads and untested theories.[51] Recently, the dominance of a certain tradition of financial economics has come to dominate business education, promoting the idea that the firm has a single and measurable purpose, namely financial return. The assumption that this is good for business, consumers or society (or even, paradoxically, for shareholders) is highly questionable, but goes unchallenged in many business schools and economics departments.[52]

Genuinely new ideas need introducing, including ideas which recognise the social complexity of business, and the multiplicity of stakeholder interests that successful businesses consider. Business cases (the teaching materials at the heart of many MBA courses) need to look beyond an emphasis on heroic CEOs and competitive strategy, to consider the interaction of businesses with their external social environments and stakeholders, and their capacity to create long-term value.

50 CBI (2011)
51 E.g. R. Khurana (2002) Looking for a Corporate Saviour: The irrational quest for charismatic CEOs. Princeton; Khurana (2009)
52 B. McSweeney (2008) Maximising shareholder-value: A panacea for economic growth or a recipe for economic and social disintegration?; J. Froud et al (2006) Financialisation and Strategy: Narrative and Numbers. Routledge

The tide may be beginning to turn. In 2011, Harvard economics students staged a walkout of a class, in protest against the limited, unsubstantiated world view that they felt they were being taught.[53] More MBAs are being taught which also cover 'social' entrepreneurship and 'social' enterprise. However, the diversity of ownership forms, and the possibilities for employee-owned and mutual enterprises, are rarely addressed. A new generation of entrepreneurs, with a focus on profit-making not profit-maximising, will need new forms of education and business angels, with a broader world view than at present. The greatest hope for a different business culture in Britain necessarily lies with those who found new businesses upon different principles over the coming years, though this of course depends partly on accessing forms of finance with different principles.

The public policy agenda

The government plays a crucial role in determining the types of businesses which develop and prosper in Britain. For example, a core institution of modern capitalism is that of 'limited liability' for shareholders, which ensures that equity investors are not liable for a company's full losses, and without which the PLC in its current form would be inconceivable. As a number of economists have recently argued, this produces serious risks, in industries such as banking and oil, where the potential public costs of an error or accident far exceed the amount of capital held by the business.[54] Whether it intends to or not, government acts in such a way as to support certain sorts of business structures, and impede others. The Coalition Agreement pledged to 'foster diversity and promote mutuals', whilst the Business Secretary has argued for a more long-term culture of ownership and investment in UK enterprises. Evidently the government is willing to influence the shape of the private sector, to a far greater extent than it was prior to the financial crisis.

Government has seized this role in recent years, to support the growth of 'social enterprise'. Over the past decade, Ministers have given speeches on social enterprise, celebrated the public good delivered by social enterprise, and legislated for a new business structure, the Community Interest Company, which marries social purpose with business ethos. Over the last two years, political parties have shown a similar level of interest in 'mutuals', although primarily as a vehicle to deliver public services. They have shown great interest in what have been referred to as 'John Lewis public services', but far less interest in developing more 'John Lewises' in the private sector.[55] But apart from offering the form of cheer-leading that has been offered to social enterprises, there are a number of practical steps that can be taken.

Firstly, there is currently no 'standard' or established way of setting up an employee-owned company. Each founder or owner who wants to establish a company this way, or to convert to employee ownership, often has to imagine a structure of their own, then persuade reluctant lawyers, accountants and bank managers to support it. The Employee Ownership

53 See 'An Open Letter to Greg Mankiw', Real-World Economics Review Blog, November 2nd 2011, http://rwer.wordpress.com/2011/11/03/an-open-letter-to-greg-mankiw/
54 A. Haldane (2011) Control Rights (and wrongs). Speech given by Andrew G Haldane, Executive Director, Financial Stability and Member of the Financial Policy Committee Wincott Annual Memorial Lecture, Westminster, London 24 October 2011; Bebchuk & Spamann (2010). Regulating bankers pay. Georgetown Law Journal, Vol. 98, No. 2, pp. 247-287,
55 On this curiosity, see W. Davies (2010) 'Bringing Mutualism Back into Business'. Policy Network.

Association and the John Lewis Partnership have acted as de facto advisory and support services in this regard. The Department for Business Innovation and Skills can take a lead here, by developing and promoting a single route to employee-ownership, supported by legislation, as occurred with Community Interest Companies. A distinct new business form could have its own requisite reporting requirements and legal constitution. It would have the knock-on effect of inducing lawyers to become better acquainted with employee-ownership, and more equipped to advise on it.

Secondly, there are certain tax neutral incentive changes that are within the Government's power to make, which would support growth in this area. Employee Benefit Trusts lost their tax advantages in 2003, making indirect employee ownership considerably less attractive. These tax advantages need restoring (with certain conditions to prevent their abuse as proposed by the Employee Ownership Association), which would cost the Exchequer an estimated £51m.[56] As proposed elsewhere, this could be more than compensated for by reducing tax advantages on other share ownership schemes, which currently work regressively in favour of high earners.[57]

Other tax incentive changes that would support the sector include extending the Enterprise Investment Scheme (EIS) to employees, and not only to external investors, and to investment in preference shares and loans (presently restricted to ordinary shares). At present the EIS tilts the balance towards private equity buy-outs by outsiders, and against employee buy-outs. Again, these changes would have the knock-on effect of inducing professional advisors – in this case accountants – to start taking these ownership models seriously.

Finally, the government can use light-touch industrial policy in a number of ways. Now that the government is deeply involved in the credit market (through ownership of banks, 'credit-easing' and the possibility of a 'national investment bank') it has the power to intervene in how credit is made available. There is a shortage of credit across the British economy, affecting small businesses in particular. But this is a particular problem for businesses which do not sell shares externally, as they are entirely dependent on bank loans and retained earnings, as sources of finance. If businesses are to be built patiently, for the long-term, they need patient capital, from banks who are sympathetic to their needs, rather than equity investors who seek rapid entry and exit. If the entire British model of capitalism cannot be changed, then government can at least support experiments in co-operative business clusters, supported by local credit markets and advisory services, in the manner of the famous Mondragon network of co-operatives in Spain.

If the Government can designate East London to be a 'tech city', which will be lobbied for, celebrated and lent political capital, why not also designate particular urban clusters elsewhere, in which entrepreneurs, banks (directed by the government if necessary), universities and existing employee-owned companies develop networks which nurture a new business and ownership culture. Find out what works, and what doesn't. Take some risks through innovation in organisational and ownership structures. After the epic failure of the orthodox model of finance, and the legitimacy crises afflicting conventional models of the corporation, what is there to lose?

56 EOA (2010) Ownership Matters: A Manifesto for Employee Ownership
57 See W. Davies (2009) Reinventing the Firm. Demos. P. 95