Beyond the Corporation Humanity Working

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by David Erdal

reviewed by Eve Poole

What do these companies have in common? Arup, PA Consulting, Scott Bader, Loch Fyne Oysters? If I were to add John Lewis to this list, you might guess. They are all UK companies that are owned by their employees. As Chairman, David Erdal was responsible for taking his own family company into employee ownership, the paper manufacturer Tullis Russell. He has since helped numerous companies to do likewise (see his previous book *Local Heroes* for the Loch Fyne Oysters story). His latest book *Beyond the Corporation* is his argument for employee ownership as the corporate model of choice. He explains what employee ownership means in practice and how it affects company performance, challenging much economic orthodoxy in the process with impassioned dexterity.

Erdal is a very interesting man. He has a BA in Chinese from Oxford, after which he taught in Mao's China, before returning to work in the family business. He studied at Harvard Business School for an MBA and was awarded the Scottish Business Achievement Award in 1989. After leading Tullis Russell through the transition to employee ownership, he studied part-time at St Andrews for a PhD in the psychology and evolution of sharing, and has worked with the Baxi Partnership to help other companies structure and finance all-employee buyouts of medium-sized companies. With this varied experience his book will appeal to a broad readership. He has been a shop steward as well as a boss, and has studied both psychology and as well as economics, so he knows a thing or two both about business and about human nature.

To start with the basics, 'employee-owned' means that every single employee with, say, over a year's service, has a stake in the company, which is majority owned by these employees. While it is possible to set up an employee ownership structure from the start, it is more common for companies that were previously privately owned or publicly quoted to transition into employee ownership through being bought by the employees, either directly or in phases. Unlike a traditional management buy-out, where senior executives may have recourse to private financing, the vast majority of the employees in an employee buy-out will not be on the kind of salaries that would give them access to this sort of capital. So money is lent (by owners, banks, backers like Baxi or a combination thereof) for a leveraged buyout to pass ownership of the company into a trust for the employees, paid for by the company itself over time. Some employee-owned companies use a combination of a pooled trust and individual employee shares to make ownership feel more tangible.

Erdal cites numerous case studies and examples to support a record of employee-ownership high out-performance. For instance, a study conducted by Rutgers University in 2000 showed that employee-owned companies typically outperform their non-employee-owned counterparts on measures like sales per employee to a degree that, over a 10 year time frame, makes them likely to outpace their competitors by a third - making them a good risk for financing.

However, many traditional economists cannot understand the philosophy of shared ownership. For instance, why would you trust junior staff with such a responsibility, and what would you do to raise funds if you wanted to acquire a competitor? Erdal patiently describes the body of evidence that supports wider employee participation – using John Lewis as exemplar – and in any case questions the assumption that growing through acquisition is a good strategy in any case. Few merged companies seem to deliver the benefits that acquisition originally promises, and growth of any kind can always be financed through loans rather than share capital. And while growing through debt may itself be risky, most traditional companies prefer this route to re-capitalisation, given the pressure from shareholders for immediate return on investment through dividend payments.

Of course, employee ownership is not a universal panacea. Erdal is careful to include examples of failure too. Whatever the structure, weak management, market shocks and poor strategy will stymie any enterprise. But his point is that, all other things being equal, the amount of employee engagement that is released through shared ownership puts such companies ahead of competitors who cannot call on this fundamental level of commitment.

However, Erdal makes the point that our current legal structures have not kept pace with these new forms of corporation, and are in dire need of overhaul. While he will have been delighted by Nick Clegg's January call for more businesses to consider the 'John Lewis' model, with new tax incentives and a review of the legal models available, there is still too little support for larger companies to make this transition, given the amounts of capital involved. As a very crude example, assuming a market capitalisation for Tesco of about £30,000m, each member of staff would have to find about £600,000 to buy an equal share, which is not exactly realistic for a shelf-stacker. And even if the government had wanted to keep Cadbury in the UK by converting it to employee ownership, this could probably not happen without Treasury loans. Given recent experiences of forays into quasi-public ownership, the government seems keener for others to take this sort of risk than to take it on behalf of the tax-payer. And if only those who can afford it take up share options in their employer, the democracy of employee ownership is fatally undermined.

But even if the challenges for converting large companies are daunting, the headlines make it easy for us to forget that it is small and medium-sized enterprises that form the vast majority of commercial activity in the UK. Government statistics from 2011 calculated that SMEs account for 99.9% of all UK enterprises, providing 59.1% of private sector employment and contributing 48.6% of private sector turnover. At the start of 2010, the UK's 4.5 million private sector SMEs employed an estimated 13.3 million people, with an estimated combined annual turnover of £1,600 billion. This book shows why more companies should be taking the opportunity to extend to this equivalent of the population of Greater London the benefits of having a genuine stake in the work that they do. The pioneering work of Erdal and his colleagues has put employee ownership within their reach, and the evidence suggests that the best way the UK could increase its productivity, profitability and happiness would be to help more companies to make this valuable transition.

Indeed, I was at a *Quakers and Business* conference with Erdal in December where one of the themes was the topic of employee ownership. While the Quakers are famous perhaps for a more paternalistic approach to business, the respect for the individual that employee ownership requires is particularly salient for Christians. If we really believe that we are all made in the image of God, why should we not trust ownership to all employees, and not just to senior management and arms-length shareholders? As Erdal points out, the change to employee ownership fundamentally changes the nature of the 'deal'. It changes the organisation from being a legal person, to being a legal relationship, with shares held in trust for the employees. And you can't get more Trinitarian than that.

Eve Poole teaches Leadership and Ethics at Ashridge Business School, following earlier careers working for the Church Commissioners and Deloitte Consulting. Her books The Church on Capitalism *and* Ethical Leadership *(with Carla Millar) were published by Palgrave in 2010. She can be contacted via* eve.poole@gmail.com. *and keeps a blog at http://evepoole.livejournal.com/*