Employee Ownership Association

The voice of co-owned business

Ownership matters

A manifesto for employee ownership

EMPLOYEE OWNERSHIP ASSOCIATION

The Employee Ownership Association is the voice of co-owned business in the UK, representing a sector of the economy now worth an estimated £25 billion in combined annual turnover.

A network of companies where employees own anything from a substantial to controlling stake in the business, EOA's members include the John Lewis Partnership; other long established co-owned companies such as Scott Bader, Tullis Russell and Swann-Morton; global corporations such as Arup, Unipart and Mott MacDonald; other major enterprises such as eaga, Pertemps, Wilkin & Son and Blackwell's; and a range of smaller companies from a wide spread of sectors.

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As an instrument of government policy, employee ownership is economically effective, politically attractive and socially just.

Without any net cost to the public purse, employee ownership could make a major contribution to re-balancing the economy, distributing wealth more widely, re-invigorating civic society, re-building trust and re-connecting people with more satisfying, more productive and happier work.

Employee ownership can help to re-balance the economy

We now realise just how narrowly the collapse of the entire financial system was averted, thanks to unprecedented emergency measures taken by governments and central banks. But there is a growing unease that, having tackled the symptoms of the crisis, the urgency to tackle the root causes is receding. It is vital that we avoid complacency. We still need bold policies that make the market economy once again self-regulating, sustainable and vibrant and which set our economy back on a path to prosperity.

Economies benefit from diversity, and that includes diversity in the ownership of business. We believe ownership matters, because the way business is owned largely determines its behaviour, its horizons, its values, its longevity and its performance. Different ownership systems will either diffuse wealth or concentrate wealth, they will connect people to business or disengage them, they will encourage a long term view or short term view that either husbands resources or exploits them.

Ownership determines the nature of stewardship. Some types of owner will care about investment, the well-being of individuals and the impact of their actions on society. Other types of owner won't care at all because they won't be owners for long enough.

In the UK, individuals held over half of UK shares in 1963. Today, they hold around an eighth. Reflecting the globalisation of capital, there has also been a rapid increase in foreign shareholders, from less than a sixth of shares in 1993 to 50% in 2007.

Properly structured, employee owned businesses have the potential to transform our economy.

Employee ownership distributes wealth widely

Just as it influences behaviour, ownership also determines whether wealth is spread widely or is further concentrated. Broadly based ownership creates more vibrant and sustainable economic activity, touches more people's lives, alleviates the more corrosive effects of status anxiety and leads to a happier, healthier, safer society.

Owner-employees are productive, and can contribute disproportionately to wealth creation: the share prices of public companies that are more than 10% owned by employees outperform the market as a whole by on average 10% per annum[1].

In 1976, the bottom half of the UK population owned 12% of the marketable wealth, excluding property; by 2003 that had fallen to just 1%[2].

The last decades of the 20th century began a process of widening asset ownership – with more home owners and share owners. The next decade should build on that foundation by creating a new generation of employee owners.

Governments can and should influence the ownership of work. This can be achieved without draconian redistribution, and in ways that are perfectly compatible with the incentive and rewards for entrepreneurialism that will be so vital to fuel growth.

Employee ownership drives accountability and reinvigorates civic society

Direct ownership puts all the fruits of ownership – income, capital appreciation, information and votes – in the hands of the shareholder. Indirect or intermediated ownership, of the kind that is now dominant through pension funds and insurance companies and hedge funds, creates a long chain of middlemen, weakening the line of accountability between boards of directors and the investing public.

Direct ownership, uncluttered by such intermediaries, creates the strongest lines of accountability.

The say that employees have in traditional companies is way behind the democratic rights we all take for granted in society as a whole. This must be addressed so that we can take advantage of the full motivational benefits of employee ownership.

The fact is that through engagement as owners, people made responsible at work will act responsibly in society.

Employee ownership creates satisfying, productive & happier work

Employee-owned businesses perform <u>at least as well</u> as other businesses, and in most cases significantly better; employee owners work hard, are more productive and are happier.

When employee ownership is introduced with employee involvement in decision-making, the rate of productivity growth is boosted by 52% compared to the position before employee ownership was introduced[3].

Sales growth and employment growth is 2.4% higher, and the same businesses are more likely to remain independent[4]. Over 50% of businesses with employee share schemes surveyed by HMRC reported improved organisational performance as a result[5].

Employee ownership is associated with greater willingness and ability to contribute innovative ideas, [6] and absenteeism, a strong indicator of employee morale, and labour turnover are lower in employee-owned businesses[7].

How Government can help

There is a 30-year track record of governments promoting tax-efficient employee share schemes, helped by the strong political consensus for the idea. Profit sharing in 1978, Save-As-You-Earn share options in 1980 and latterly the Share Incentive Plan in 2000 all received cross-party support. These schemes have produced a large number of employee shareholders in the public company sector but this accounts for just 17% of the national workforce, and the extent of employee ownership in most public companies is less than 1%, not enough to make a difference to company behaviour and performance.

How can government tilt the field in favour of more extensive broad-based ownership at a time when the public finances are so constrained?

There are three policies that could do this: advocacy, conditionality and public services reform.

First, government should champion the employee-owned sector's contribution to the 'bio-diversity' of the UK economy. The financial crisis of the past two years has reminded us that, in terms of business models, diversity is strength. In the case of employee ownership, that should mean **active advocacy**. For too long, government's attitude to this sector has been one of benign silence, occasionally broken by tax reliefs for share schemes in large public companies. Advocacy for employee ownership should include explicit aspirations for growth of the co-owned sector and expansion in the number of employee-owners.

Secondly, where present tax reliefs are subsidising regressive ownership outcomes, such as unlimited tax relief on corporate debt in private equity buyouts, they should be changed to encourage wider ownership and become **conditional** on the business having an all-employee trust of a minimum size. Similarly, where tax reliefs are subsidising discretionary executive share schemes, such as share option plans and EMI schemes, which are perfectly legitimate tools for entrepreneurial businesses, they should become conditional on the business having an all-employee trust. Tax reliefs ought to lead to progressive ownership outcomes – particularly where they have been shown to improve economic performance – not to further concentrations.

Thirdly, the pace of public service reform could be accelerated by mandating the transfer of businesses in the health service and local government into **"partnership trusts"**, businesses majority owned by all-employee trusts. First refusal could be given to in-house teams. If declined, external bidders would be required to accept the in-house team and establish a partnership trust business for the contract.

The legal form of a trust is an important element of these proposals. Trustees have a legal duty to manage the trust's assets, in this case shares in a business, in the best interests of the beneficiaries. Reference to future beneficiaries in the trust deed encourages a long term view. Distribution of trust assets can, but need not, be constrained to remove the temptation of winding up or selling businesses for personal gain. The trustees, who may include independent non-executives as well as elected employees, can act as a supervisory board to the company's board of directors, a stable model of corporate governance that has been proven in many different settings.

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[1] UK Employee Ownership Index, published quarterly by law firm Field Fisher Waterhouse

[2] Phillip Blond, writing in The Guardian, 2 July 2009

[3] "Employee Stock Ownership Plans", US General Accounting Office (1987), study of the performance and productivity of 110 companies before and after the introduction of an ESOP

[4] "In the Company of Owners: the truth about stock options" by Blasi, J et al (New York: Basic Books, 2003), study of 343 ESOP companies and the same number of non-ESOP companies matches for size, industry and location

[5] "Evaluation of tax-advantaged all-employee share schemes" by Kerr, J and Tait, C (HMRC 2008)

[6] "Creating a Bigger Pie? The effects of employee ownership, profit sharing and stock options on workplace performance" by Blasi, J et al (NBER, 2008)

[7] "Financial participation in Europe – determinants and outcomes" by Festing, M et al (Economic and Industrial Democracy, 1999)

OTHER EOA PUBLICATIONS

Download these reports free at the EOA website: www.employeeownership.co.uk

From Colleagues to Owners

'From Colleagues to Owners' explains how and why companies make the transition to employee ownership. Based on ten case studies, the report explains what motivated a highly diverse mix of businesses to consider employee ownership as a succession or start up route. Sponsored by co-owned Child Base, whose chief executive writes the report's foreword. Author: Andrew Bibby. Published: April 2009.

Structuring employee ownership – a guide to trusts, shares and tax help for co-ownership

This guide is for co-owned companies and businesses considering a transfer to minority or majority employee ownership. It aims to help companies optimise their co-ownership structure. Designed to be clear and practical, the guide provides expert guidance on employee trusts, individual share schemes, combined trust and share schemes, share option plans and key tax advantages. Author: Robert Postlethwaite. Published March 2009.

Making employee ownership work: a benchmark guide

'Making employee ownership work' is a new guide from the Employee Ownership Association and co-ownership advisers the Baxi Partnership, based on a survey of 25 EOA member companies including John Lewis, Unipart, Arup and Mott MacDonald. Designed for easy reference, the guide compares company practice under five headings: employee engagement, reward, governance, employee ownership culture, and social responsibility. Author: Sarah Silcox. Published: February 2009.

Innovation included: why co-owned businesses are good for public services

Written by internationally acclaimed business writer Charlie Leadbeater, Innovation Included makes the case for more public services to be provided by co-owned companies. Sponsored by eaga plc, the paper claims that employee owned companies offer public services a level of employee commitment and innovation that can transform the experience of service users. Author: Charlie Leadbeater. Published: November 2008. Foreword: John Clough MBE.