THE GOOD WORK COMMISSION

Provocation Paper 6

Ownership and good work

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Contents

- There are two dimensions of ownership that potentially affect good work. The first involves broadening ownership structures within organisations – for example, through employee share schemes and partnership structures. The second concerns ‘external’ ownership – how different forms of corporate governance define the rights and responsibilities of owners (for example, the difference between shareholder versus stakeholder models of governance).

- Simply including employees in ownership is not enough to link their interests with that of the company. Indeed, it is quite possible to devolve ownership and still fail to secure good work outcomes. There is no necessary relation between ownership and the quality of work.

- What matters more to the good work link is the translation of ownership into democratic, political and constitutional arrangements. When ownership brings influence over the decision-making, core purpose and the structure of organisations, this, when coupled with ownership of shares, is arguably more critical to furthering good work.

- The UK compares relatively favourably with other nations in Europe on the issue of employee share ownership in terms of the market capitalisation of large companies.

- The impact of private equity ownership on work is mixed and inconclusive. On the one hand, freedom from the demands of diverse shareholders or short-term pressure from stock markets may enable managements the breathing space for decisive action; after all, the value of the business must improve if it is to be attractive to subsequent buyers and investors. On the other hand, there is some evidence that investment in skills, employee involvement practices, team based working, and job security all suffer under the ‘short-termism’ of private equity ownership.

- Interest in the possibilities of different forms of ownership in the public sector is rising – for example Foundation Trusts and School Academies emphasize the end-user as participant as well as customer. However, the notion of a social economy – or indeed social enterprise – remains poorly defined, and it is perhaps best conceived less as a discrete sector and more as an approach to providing services at the local and community levels.

Introduction

Power comes in many forms: physical, economic, political, cultural and personal. So does it have differing effects. Power can thus be hierarchic, it can take the form of capacity and it can make things happen. Ownership of a resource convenes power, for it enables the owner – via the assertion of property rights – to ‘trump’ the wishes of other stakeholders. Ownership is thus a form of economic power that enables the owner (whether legally and/or culturally constituted) to decide organisational goals and dictate the means by which they will be achieved. This report examines how such ownership impacts upon good work outcomes.

The Work Foundation has identified good work outcomes to include:

- Secure and interesting jobs that employees find fulfilling, which contribute to the achievement of high performance and sustainable business success;
- A style and ethos of management that is based on high levels of trust and recognises that managing people fairly and effectively is crucial to skilled work and high performance;
- Choice, flexibility and control over working hours;
- Autonomy and control over the pace of work and the working environment;
- Voice for workers in the critical employer decisions that affect their futures.

Much of the existing discussion on how ownership influences the quality of working life focuses on attempts to broaden ownership structures within organisations through, for example, employee share schemes and partnership structures, etc. Here, the argument is that widening ownership to employees has the effect of aligning their interests with those of the organisation. This, in turn, is said to result in increased employee motivation and engagement and thereby, increased productivity. The report critically examines the evidence for this view.

Yet this turns out to be only half the story. The other half concerns the impact of external ownership on the realisation of good work outcomes. It focuses particularly on the ways in which different forms of corporate governance define the rights and responsibilities of external owners in relation to realising good work outcomes. Here, the argument takes the form of shareholder versus stakeholder models of governance. The report examines debates around these models in order to better understand how corporate actors can enable commitment to good work outcomes.

Usually, ownership of a private company is a form of economic power that serves to orient both managers and owners to the goal of increasing the inherent value of the stockholders’ equity in the company. This idea (under the banner of shareholder value) has dominated discussions of business strategy and investment over the past quarter of a century. Since at least the 1970s, more ‘political’ questions, such as how decisions are made, the degree of management autonomy and the level of engagement of employees, are here subordinated to that end. Ownership does not, in this case, lead to good work outcomes because it does not translate into political, or constitutional, arrangements that result in good work.

Political and constitutional arrangements pertain to the core purposes, organisational structures and decision-making arrangements that guide the company. This report argues that ownership matters to good work *when it translates into constitutional means* that generate good work outcomes. There is, therefore, no necessary relation between ownership and the quality of work. Rather, what is of the utmost importance is the transmission mechanism by which it does so. This mechanism is nothing other than the political power to expand corporate missions, re-structure decision-making, empower stakeholders and engage employees.

By conceiving of the impact of ownership on good work outcomes in terms of an intermediary element: that of constitutional means, the report is able to:

1. Clarify the relation between ownership and good work;
2. Incorporate current research on governance and organisational control;
3. Distinguish between the impacts of (employee) ownership ‘in’ and (corporate) ownership ‘over’ companies, and to explore their respective impact on good work outcomes;
4. Explain why share ownership schemes only generate good work outcomes when they are combined with other means of employee engagement and participatory decision-making;
5. Explore innovations in ownership that serve to embed the constitutional means necessary for good work outcomes.

To achieve these aims, the report first examines the impact of employee ownership structures ‘in’ the workplace. This includes an examination of the evidence that supports the proposition that enhanced employee ownership increases productivity, the relationship between ownership and motivation and the actual mechanisms by which employee share schemes serve to align the interests of employees and owners. To observe how ownership ‘in’ the workplace actually functions, we present here a case study of the Mondragon Corporation. Finally, we examine a key text in current debates on the future of firm ownership and the role played by employee owners.

The second section explores the impact of corporate ownership ‘over’ the workplace. Here, the USA/UK model of corporate ownership and control is compared to that of other countries, and the long-established uncoupling of ownership and control in the USA/UK is counterposed to European notions of the block share. This examination again illustrates the importance of constitutional means as an intermediary transmission mechanism for ownership to translate into good work outcomes. This section concludes with an analysis of stakeholder models, and a case study on private equity.

The third section extends the discussion into the public sector, examining recent research on how ownership impacts upon public service provision, particularly in regard to notions of mutualism. The key text here explores innovations in the associative models of ownership. In the public sector, political concerns are of more overt importance, and it is for this reason that public ownership underscores the centrality of constitutional means as the causal driver of good work outcomes.

The report concludes by highlighting the inherently economic orientation of shareholder ownership and the inescapably political character of stakeholder models. Like the late Harvard philosopher John Rawls' emblematic two principles of justice, one concerns distributive (economic) questions while the other tries to assert the importance of measured (political) judgment when it comes to what companies actually do and how they do it.

1. Ownership as employee engagement

This section examines the impact of employee ownership structures ‘in’ the workplace and inspects evidence in support of the proposition that widened employee ownership increases productivity. This requires an analysis of the relationship between ownership and motivation and the actual mechanisms by which employee share schemes serve to align the interests of employees and owners. A case study of the Mondragon Corporation shows how ownership ‘in’ the workplace functions on the scale of a modern industrial corporation and an examined key text explores the future of firm ownership and the potential of employee owners to shape it. The section begins to construct the central argument of the report, this being that ownership matters inside organisations when accompanied by a constitutional mechanism that translates it into good work outcomes.

Employee ownership in the UK

Employee ownership can take different forms and can be implemented in isolation or in combination with other schemes. Ownership can be direct or indirect. Direct employee ownership refers to schemes where employees individually own shares in an organisation and therefore become (formally at least) individual stakeholders in the progress of that organisation. Indirect ownership, on the other hand, means that the employees collectively own the shares in an organisation through a trust scheme. The trust is the stakeholder and the trustees vote collectively on how the benefits of their ownership are to be used and distributed.

The legal models adopted by companies in the UK with employee ownership provision include:

- Share Incentive Plans (SIP). Employees are given the right to buy shares which can include free shares, partnership shares, matching shares or dividend shares.
- Save As You Earn (SAYE). Every member of the organisation is offered similar terms for participation in the scheme. Employees are offered the right to buy a certain number of shares at a fixed, or discounted, rate using savings made over a certain period.
- Enterprise Management Incentive (EMI). This scheme does not require prior approval from HMRC and is intended to help small or independently owned trading companies to attract, reward and retain key members of staff.
- Company Share Option Plans (CSOP). Employees are given the option to buy shares from the company at a fixed rate.

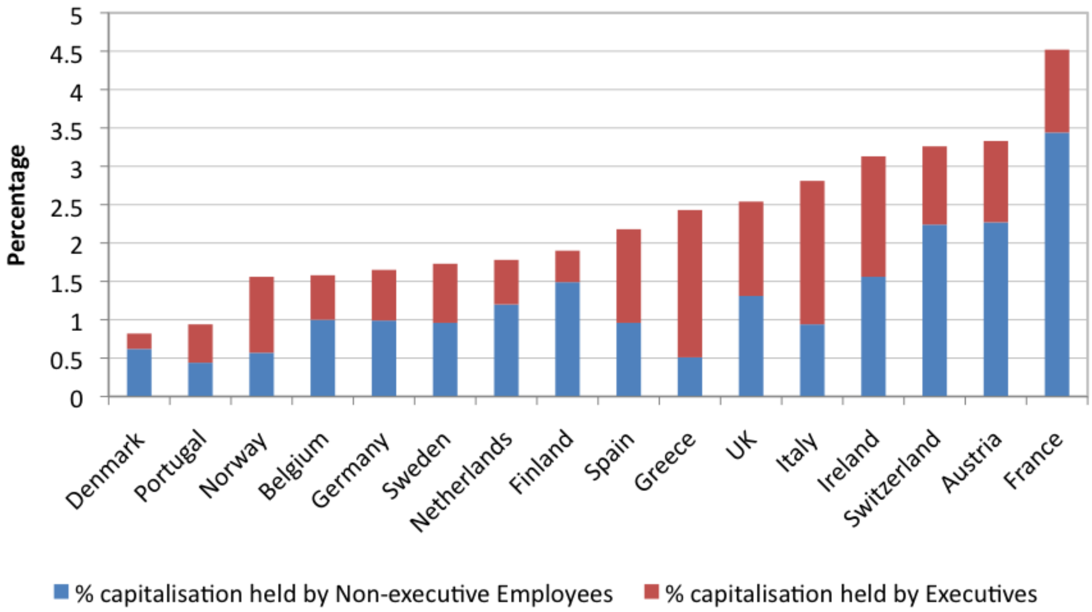
According to WERS data SAYE schemes were the most popular all-employee saving scheme, with 12 per cent of all employers offering them.

Much of the comparative data on employee share ownership is not consistent over the broad range of different enterprises that afford such opportunities. As a result, much of the sample data used to explore the take-up and practice of such schemes is difficult to compare and to generalize from.

Of recent studies, only Mathieu (2008) provides data that enables like-for-like comparison of share ownership structures amongst similarly sized companies. In this case, the focus is on more than 2,500 of the largest European corporate groups, operating in 29 European countries, overseeing more than 250,000 companies and 32.4 million employees.

The evidence suggests that the UK compares favourably to other European countries in regard to the total capitalisation owned by all employees. The relative distribution of this capital amongst executives and non-executive employees appears, in the UK, to afford a greater proportion of total employee ownership to executives than is the case in much of the rest of Europe where a greater proportion of firm capital accrues to non-executive than executive employees.

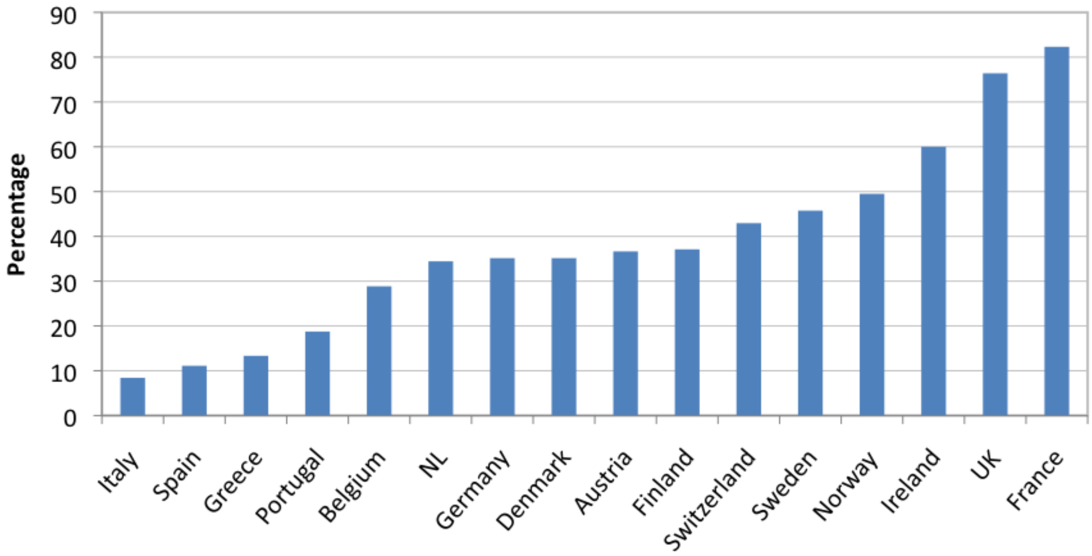
Figure 1: Per cent of capitalisation in large European groups owned by executive and non-executive employees 2007/8



Source: Mathieu (2008)

UK companies have been particularly active in developing ‘broad-based’ schemes (ie those available to non-executive employees), affording opportunities for wider employee participation.

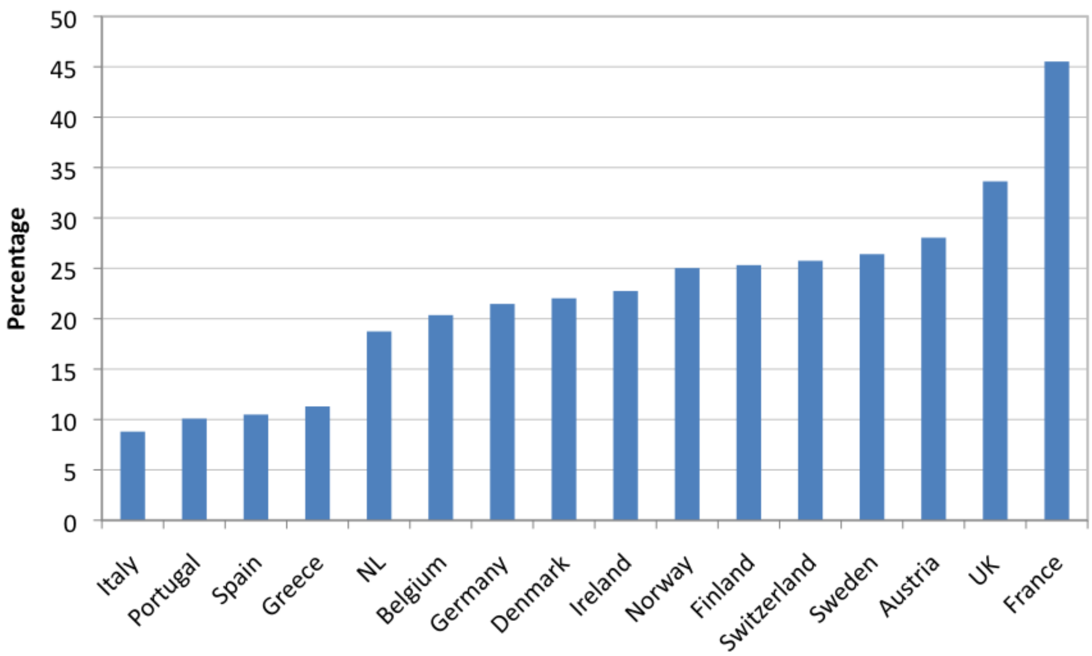
Figure 2: Per cent of large European groups with 'broad based' employee share plans 2007/8



Source: Mathieu (2008)

And relative to employees in other European economies, UK employees have been particularly keen to take advantage of the opportunity to become employees-owners.

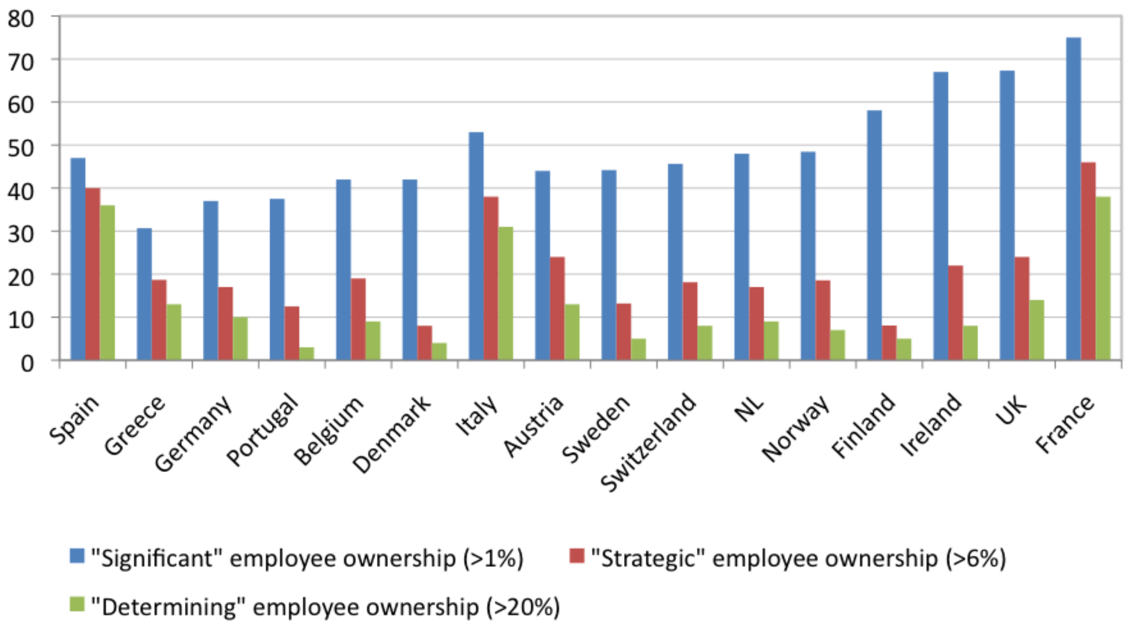
Figure 3: Per cent of employees in large European groups who are employee owners



Source: Mathieu (2008)

Finally, it is worth noting the relative importance of employee ownership within the broader ownership structures of companies. In Figure 4 below, we can observe that in Spain and Italy (where worker cooperatives remain a significant force) and in France, the relative importance of employee share ownership remains high. In each of these countries, in excess of 30 per cent of companies have a level of employee ownership that is ‘determining’ (of strategy, decision-making, purpose, etc.). In the UK the figure is considerably lower at 13 per cent but by no means insignificant. Indeed, the UK companies appears to have been particularly successful in enabling ‘significant’ levels of employee ownership at the firm level (1 per cent).

Figure 4: Per cent of large European companies with sig, strat and det levels of employee ownership



Source: Mathieu (2008)

What is employee ownership good for?

Generally, economists have been skeptical of employee ownership. The assumption has usually been that employee owners tend to favour their own self-interest over that of the firm, and to orient to short-term gains over the long-term health of the company. Sometimes, this is accompanied by complaints that decision-making becomes diffuse and supervision lax. Against this, many see employee-ownership as effectively tying employee interests to those of the firm, aligning compensation with success, increasing motivation, discipline and productivity.

Though the empirical evidence for the direct link between different structures of ownership and different outcomes in productivity is somewhat thin, it is nevertheless possible to see a direct causal relationship between ownership and worker motivation – and thus also to increased productivity. Heskett (1997) describes the ‘Service Profit Chain’ as a driver of enhanced employee satisfaction and retention, which in turn increases productivity, service value, loyalty and ultimately profitability and growth. Recent innovations in organisational practice that enable workplace autonomy and reduce hierarchic management structures suggest a potential for more competitiveness and productivity (Lloyd & Payne 2006).

The link that needs to be established for such an argument to work is that between the processes that function within differently owned organisations and the generation of good work, or what has been termed ‘win-win performance’ (Sparham & Sung 2007). We should note, here, that such a link is at least possible. Organisations on the Employee Ownership Index have, for example, over the past seventeen years, outperformed organisations on the FTSE 100 by an average of 10 per cent. A good place to look for this link would seem to be in the various forms taken by employee ownership schemes, and particularly when these underpin, or are underpinned by, progressive governance process and human resources management. The sources of organisational health are thus likely to lie beyond the mere forms of economic ownership (Wright et al 2001).

Clearly, employee engagement is a key driver of organisational performance. Engaged employees feel part of an organisation, and the more so the more they are consulted and participate in important organisational decisions. Participation in decision-making thus correlates to motivation and effort. Kruse and Blasi (1997) found that of 25 studies into employee attitudes and behaviour, trends suggested that a culture of collectiveness and teamwork lead to increased effort and output. Similarly, the Corporate Leadership Council (2004) found that ‘engaged’ employees perform at a level 20 per cent above their ‘disengaged’ colleagues. Perceived participation in organisational processes interacted positively with worker attitudes toward their employers. Furthermore, the ‘company spirit’ also leads to a culture of self-regulation and assessment that helped eliminate the free-rider problem often associated with direct employee ownership. Skills and motivation are thereby pooled for the benefit of the organisation as a whole.

In sharp contradiction to the belief that high staff turnover leads to freedom and organisational flexibility, Michie (2001) has suggested that a culture of commitment and participation leads to increased employee retention, which in turn increases the organisational ability to innovate production and management processes. Kruse and Blasi’s 2000 study supports this assertion, arguing that the longevity of employee commitment increases greatly when ESOP schemes are adopted. Furthermore the rate of growth increases by around 2.5 per cent after ESOPs are adopted. It has also been asserted that innovation in governance and democratic management leads to lower turnover of staff and higher productivity (Huczynski & Buchanan 2001). To be successful in the long-term, companies therefore need to adapt both what they produce, and how they produce it. In an earlier study, Michie and Sheehan-Quinn (1999) found a positive correlation between more participatory human resource practices and levels of company innovation. There has also been a positive correlation reported between employee ownership, innovative HRM and company value (an average of 8.12 per cent relative to industry medians; Kim & Ouimet 2008). Conyon and Freeman (2007) claim that profit sharing via share schemes raises productivity by up to 19 per cent.

The link between motivation and employee ownership has been made explicitly by Richard Reeves in his report on co-owned companies. He argues that:

> *'there is no direct causal evidence for a link between co-ownership and worker happiness. However, there is research relating worker wellbeing to a range of factors – including autonomy, trust, respect, involvement and information – which are also characteristic of co-owned organisations.'*

Employee ownership does not of itself lead to higher yields in motivation and productivity, but it tends to encourage the kind of governance structures that improve worker wellbeing and lead to increases in those areas. Benz and Stutzer (2004) used the WERS 1998 data to show that worker satisfaction increases significantly when they are consulted about procedural matters (such as wages). Various studies have suggested that compensation practices in companies with employee ownership schemes have been more beneficial to the employee that in companies with traditional ownership structures. However, the democratic and participatory environment that progressive HRM helps cultivate applies to other, more intangible factors than just wages, such as those listed by Reeves above. The fairness of organisational structures is seen as a more important criterion in assessing their behaviour. Benz and Stutzer found that organisations implementing fairer organisational protocols were more motivating to workers than compensational returns.

When employee ownership matters

Connecting all these factors and outcomes is the notion of effective communication within the firm. Where governance structures exist that give employees a voice and allow them to participate in deciding organisational direction, the increase in motivation and commitment is pronounced. In short, we appear to be gazing upon the positive effects of democratising the workplace. This tends to contribute to a long-term approach to organisational motivation and development (Conyon and Freeman 2001). When combined with ownership structures that divert from the shareholder value, short-term profit oriented approach, the outcomes for productivity and worker satisfaction can be significant. Michie, Oughton and Bennion (2002) have argued that it is necessary to combine communicative practices of governance with inclusive ownership structures to induce a sense of responsibility and commitment, rather than just increasing the intensity of the working environment. Participation as well as ownership is therefore vital. Spreading ownership amongst employees encourages prosperity and more democratic work places add to the well being of employees.

Michie & Sheehan (2001) found that human resource management practices contributed more to competitive success when introduced as a 'bundle' of practices, suggesting that a shift in the cultural attitude to governance and ownership is required. The instrumental implementation of a solitary policy with the same individualistic, short-term financial goals in mind will not deliver the desired increase in commitment and motivation. A culture of interrelated HRM practices contribute to what is referred to in the literature as High Performance Work Systems (HPWS). These have been shown to be particularly successful in the public sector (Melkers & Willoughby 2005) and have been taken up with positive results across Europe (Boudreau & Ramstad 2005; Brödner & Latniak 2002). Guthrie (2001) describes these as bundles of HRM practices that involve high commitment management, high employee involvement, flexibility and productivity. The principle aim of HPWSs is to develop, motivate and retain a workforce that leads to sustainable competitive advantage. Where companies have implemented these, increases in productivity can be as high as $4,000 per employee (Huczynski & Buchanan 2001). Facilitated by ICT, it seems to be the synergetic nature of HRM practices that gives them the title of 'systems', and their distinction from other variations of HRM innovation. To support this view, Michie and Sheehan (2001) carried out a survey that suggested that 'low-road' practices, ie short-term contracts, low commitment to job security, low levels of training and low levels of progressive HRM, showed a negative correlation with corporate performance. On the other hand, they also found that 'high-road' work practices, ie commitment within organisations to participation and long-term job security, were positively correlated with good corporate performance (see also Brödner & Latniak 2002).

Perhaps the most direct recent analysis of the effects of shared capitalism in the UK is Bryson and Freeman's 2008 report for the LSE. They use WERS 2004 data to analyse the effects of different forms of shared capitalist payment on workplace productivity. Different forms of payment were found to complement each other. The positive effects of these payment schemes was seen to increase when combined with factors such as performance related pay and different managerial arrangements. Devolving decision-making to employees, reducing managerial monitoring of workers and implementing subjective appraisal of performance were all positively associated with shared capitalist payment forms. According to the most recent HMRC report on this issue, companies with employee share schemes enjoyed an increase in productivity of 2.5 per cent in the long-term (Oxera 2007). Yet the report also states that where such schemes are implemented as part of a package of share ownership, productivity can increase by 4.4 per cent in the long-term.

As the evidence reviewed above shows, benefits are maximised when new measures are bundled, rather than deployed individually. Payment and organisational change should thus be introduced together in order to align worker and employer interests in maximising productivity. Incentivising and empowering workers as individuals as well as in groups also leads to the sharing of knowledge and skills. Furthermore, mixed forms of pay, based on the individual and the group, encourages cooperation among staff while reducing the free-rider problem. Implementation of pay schemes and managerial practices as a combined package provides the necessary combination of incentive, motivation and autonomy that then deliver the desired goals.

Alone, including employees in ownership is not enough to link their interests with that of the company. Indeed, it is quite possible to devolve ownership and still fail to secure good work outcomes. What is crucial to such outcomes seems to be the translation of ownership into democratic, political and constitutional arrangements that, in tandem with ownership, are able to secure the enhanced motivation and engagement of employees. The transmission mechanism from ownership to good work is here revealed to be that of constitutional means. We can see this again in a more empirical demonstration.

Case study: Mondragon – scaling up co-operative ownership

Established in 1956 as a company producing petrol based heaters and cookers, Mondragon has developed into one of the world's largest worker federation co-operatives. The organisation has 92,773 employees, making it Spain's 7th largest business group, with a turnover of €15.6bn in 2008. The entire business group is based on purely co-operative principles, with a one member, one vote democratic model. Fortune magazine voted it one of the ten best firms to work for in Europe, based on its commitment to equality, participatory governance, customer satisfaction and high-powered, innovatory management systems.

Though Mondragon is based in the Basque region of Spain, 16 per cent of its workforce is international, and it operates in four distinct areas:

- **Industry** – producing consumer goods, industrial components, telecommunications equipment, computer software and construction, among other things.
- **Retail** – Eroski, Mondragon's leading retail group boasts a €9bn turnover.
- **Finance** – banking, insurance and its own voluntary social welfare body, with assets of €3.8bn, through which it offers retirement, widowhood and other benefits to workers in addition to the Spanish welfare system.

- **Knowledge** – education, business and teacher training as well as technological training, largely at the University of Mondragon.

When the workers at Mondragon set up the Caja Laboral Popular Credit Co-operative Bank in 1959 they established the basis and key principles for co-operative development. These were made uniform across the whole business group at the first co-operative congress, held in 1987. They include a commitment to open admission to the federation; democratic, one member one vote, structure; a belief in the sovereignty of labour, and wealth distribution according to work done, not shares owned; participatory governance; payment solidarity, both within the corporation and externally; and a commitment to education and training. Fostering a sense of shared values has been essential to the co-op's development, providing it with a firm, common direction. This is made possible thanks to the commitment to democratic governance structures and participatory management.

As worker-owners, members of the Mondragon co-operative are citizens of a worker commonwealth, with all the privileges and democratic rights that this confers. Profit and control is granted to labour, rather than to capital. The democratic management systems are constantly evolving and are structured differently according to different areas of the corporation. There is a central management structure, however, but it is not the traditional corporate model of a parent company, rather it is based on an agreement between the various groups to pool their management resources. Every four years workers in each sub-group of co-ops elect the 650 members of the Co-operative Congress, which establishes the corporation's strategic criteria. The Standing Committee receives its mandate from the congress and oversees the development and implementation of policies and agreements. Each co-op has a general council that is further responsible for the implementation and development of corporate strategies in specific sectors.

The organisational structure is set up in such a way to harness the knowledge and technical skills that exist within the corporation. Communication and participation is invaluable to link the shop floor with management. These management groups also decide pay structures and, through their commitment to payment solidarity, keep the ratio of pay between the highest and the lowest earners at 3:1. Payment is also kept in sync with equivalents in each sector outside of the co-op. The success of Mondragon has been attributed as much to its organisational sophistication as its ideological commitment to the co-operative. Harnessing knowledge, skills and innovation in this way has allowed Mondragon to establish an average four new co-ops a year, nearly all of which survive beyond five years. Democracy in the workplace is a significantly powerful tool for creating a culture of high performance and innovation, which Mondragon embodies (Manville & Ober 2003).

Add to this the investment in training centers and business teaching and the co-operative becomes a dynamic, successful and evolutionary long-term business model.

Key text: William Davies – ***Reinventing the Firm***

The constitutional link between ownership and good work is further explored in a lucid and ambitious reconsideration of the traditional model of firm ownership delivered by William Davies for Demos. Davies (2009) advances an argument for organisational pluralism, rejecting the mono-culture of firms oriented toward shareholder value alone. He argues that this form of organisational orientation damages the long-term value and ignores the wider, and interlinked, social and political implications of a firm's activity.

The present juncture of capitalism is a crucial time for the re-evaluation of economic organisation, not least in terms of how these relate to issues of ownership and management. In a situation of uncertainty and turbulence, Davies asserts, there are greater opportunities to expand the framework of analysis beyond economic efficiency and productivity, thereby to include the broader socio-political considerations. The task, therefore, is to develop organisational ideas that balance the economic and political forms of participation, empowerment and autonomy. Employee ownership, which can take multiple forms, is seen as the best way of diversifying and improving organisational structures.

In the period 1873-1903, British capitalism saw the dominance of the small scale, family owned business model recede, and in its place arose the publicly owned business corporation. Today's economic environment should experience an analogous change, whereby the shareholder-value model of ownership gives way to more democratic and autonomous forms. It requires a quite radical sea change in the way we perceive the notion of ownership. Davies argues that 'the assumption that corporate assets are worthless unless they are tradable has been made to look extremely short sighted by the financial crisis'. Ownership, he argues, is a far less tangible concept than has been traditionally perceived in recent capitalism. The notion that an association of people can be treated and traded in a like manner to an item of physical property leads to 'bizarre legal fictions' such as the creation of limited liability, which distort our image of ownership. He argues that 'legal ownership of shares (rights to control and benefit from a slice of risk capital) is equated to ownership of the company itself (right to dominate a complex socio-political entity').

What this perception of ownership really boils down to is the ability to legally control access to particular resources, be that a labour, wealth, intellectual property or goods produced. In reality, Davies argues, ownership is far less tangible and models should be developed which represent that. The present period needs to be one of what Davies calls 'progressive austerity', we should rediscover the liberal-left tradition of mutual and cooperative economic movements, we need to head in new directions for the delivery of public services, not treating the profit-maximising motive, or shareholder orientation as the be all and end all. Rather, the modern firm should be oriented toward long-term organisational interest.

Employee owned firms quite significantly reverse the trend of ‘naked unfairness at the heart of British firms’. In the FTSE 100 the average ratio of managerial staff to low level workers’ wages is 66:1. When adjusted to include stock options and share distribution the gap widens even further to 98:1. In coordinated market economies such as Germany or Japan, the gap is far less pronounced. Managers in these countries are more typically promoted from within the firm itself and their motivation is more often toward organisational wellbeing than short-term, personal financial interests. Davies is here arguing for a redevelopment of ownership and governance structures that engender a sense of inclusiveness and identification with one’s organisation. Mutuals, cooperatives and, more recently, open-source networks provide alternative models and perceptions of ownership which challenge the short-term individualism of the dominant forms.

Employee ownership brings significant democratic gains to an organisation and produces a greater sense of commitment and feelings of belonging amongst employees. Inequalities in the dispersal of wages are ironed out, individual members have a voice and the company itself can develop a sense of mission, which is more difficult when shareholder value is the priority.

Davies goes on to describe a number of different forms of employee ownership and the potential benefits they can bring to individual workers, as well as to companies in the form of increased long-term productivity. What he argues for is an environment of diverse forms of ownership, supported and safeguarded by functional governance structures, which reflect a different, socially aware perception of what organisations are for.

Once again, we are here treated to a demonstration of the importance of combining ownership innovations with those of inclusive decision-making and participatory engagement. This section, in reviewing the evidence for interest alignment in employee share schemes, has consistently found that the transmission mechanism between ownership and good work is fundamentally constitutional. Economic power is important, but never more so than when combined with political power. Employees require both if they are to fully engage, enjoy good work outcomes and thus enhance the productivity of their organisations.

While the previous section inspected the impact of ownership in terms of employee engagement, the following explores the impact of corporate ownership 'over' the workplace. Here, the USA/UK model of corporate ownership and control is counterposed to that of other countries, and the long-established uncoupling of ownership and control in the USA/UK is compared to European notions of the block share. The historical development of this differentiation serves to underscore the importance of constitutional means as an intermediary transmission mechanism for ownership to translate into good work outcomes. This section concludes with an analysis of stakeholder models, their impact on good work outcomes and a case study on private equity.

Severing ownership from control: the peculiar development of the UK's corporate governance regime

Capitalism in the UK is uniquely decentralised, with large companies typically traded publicly and ownership of shares diffuse. Generally speaking, there is a lack of shareholders with a sufficiently large enough stake to control management and direct corporate policy, which translates into something of a severance of *ownership* from *control*. Ownership is thus shared between a diversity of individual and institutional shareholders and control is left to professional managements and bureaucracies that direct the everyday workings of large, publicly traded companies, if not the long-term strategies that are to be pursued.

This severance of ownership from control is far more acute in the UK than in other countries, where pyramid structures, family ownerships and dual class shares are of more significance, and markets in corporate control less so. In Europe, for example, shares are not so diffuse, with 50 per cent of companies controlled by so-called 'blockholders' that command a majority of votes. In the UK – and the US – the corresponding figure is less than 3 per cent. Indeed, the average size of blocks is 27 per cent in Germany and 20 per cent in Italy, whereas in the UK the largest blocks control fewer than 10 per cent of votes (Becht and Mayer, 2001).

One interpretation of this situation is that capitalism developed in the UK in a unique manner because Britain was the first industrialised nation and London the first developed financial centre; traditional forms of ownerships, such as family enterprises, were duly swept away by modernisation; and the unique ownership structures in the UK arose because of efficient and extensively developed stock markets and financial institutions, which do not pursue private gain to the extent that 'blockholders' do in Europe. However, this interpretation is overly optimistic. Rather more plausible is the argument that the UK is unique because of its overly centralised banking system and the subordination of the corporate sector to the financial sector.

Indeed, the severance of ownership from control is a relatively recent phenomenon in the UK. During the period between 1750 and 1850, dominant firms remained sole-proprietorships or small-scale partnerships – with the possible exception of the railway companies and the banks –

despite favourable conditions for the emergence of widely-held companies. In a comparative study of industrial performances, Chandler argues that the UK was slow to develop the professional managerial techniques that were developing in Germany and the US because ownership was far more influenced by kinship ties than in those countries, and families resisted ceding control of their enterprises to external investors (Chandler, 1990). Also, a lack of legislation that might protect shareholders facilitated resistance to the decentralisation of control.

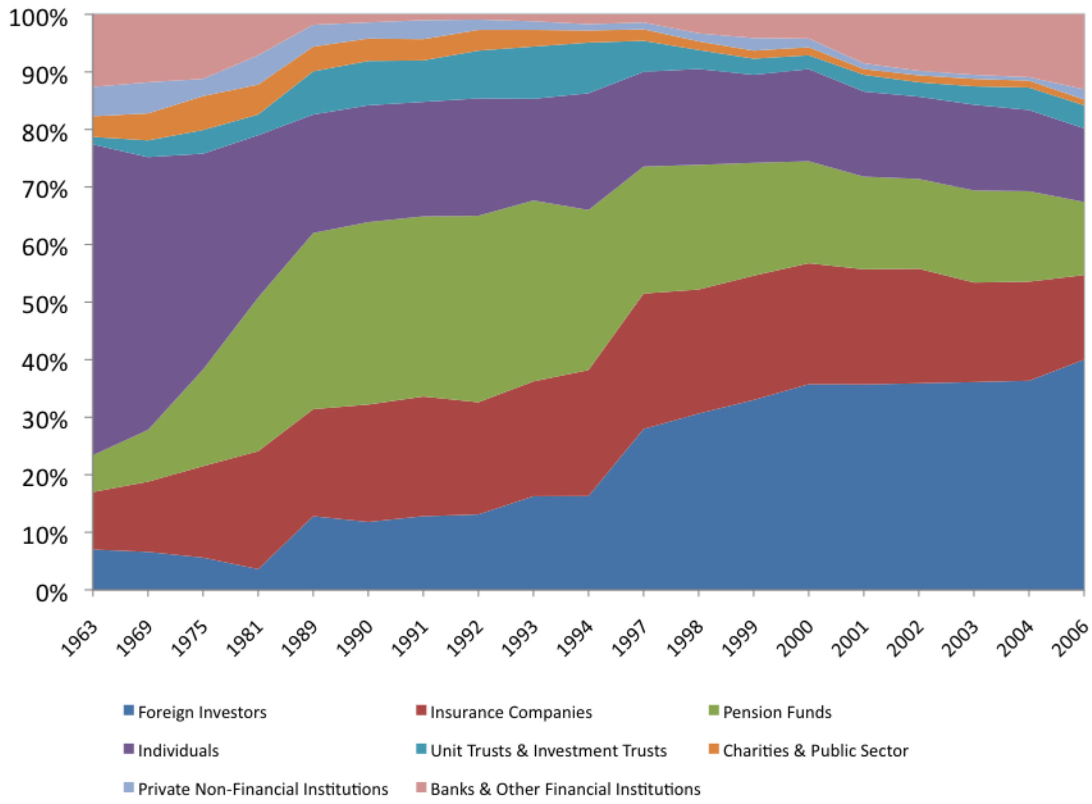
During the first half of the 20th century, however, reforms were implemented that loosed the connection between ownership and control. Tax laws encouraged greater shares activity and the LSE tripled in size during the inter-war period. Gradually, the predominance of family ownership dissipated because of the widespread issuance of shares to finance growth, mainly through acquisitions. British industry was indeed transformed by a concentration of ownership structures in three waves of immense takeover activity in 1900, 1920 and 1930, which consolidated the corporate groupings that have since dominated the UK economy (Hannah, 1976). In 1935, for example, small firms – ie 200 employees or less – numbered 136,000, a number that dropped to just 60,000 by 1963.

Alongside these developments, there was a rise of professional managements and bureaucracies that severed the connection between family and work once and for all. This process had already begun in the 1920s, but reached its zenith in the period of post-war nationalization, when family-orientated capitalism was in decline. Indeed, whereas in years prior to the 1920s, head offices were located in or near production, advances in communication technologies allowed a far more disparate approach to management. Head offices began controlling and directing production from a distance, often from London, and large administrative structures developed to serve that end, with clerical and technical jobs on the increase – from 11.8 per cent in 1924 to 19.7 per cent in 1948 in manufacturing alone – and management increasingly viewed as a competitive profession in its own right.

Also, in the 1940s and 1950s, minority investors were afforded greater protection; there was an increase in institutional shareholders; and a market in corporate control emerged in which ownership was determined by stock market transactions and control passed to external investors (Roberts, 1992). In 1953, moreover, Charles Clore launched the first hostile take over bid in the UK. From then on, shares issued by target firms could be bought at a significant premium, which substantially increased the cost of full acquisitions. As a result, partial bids were far more attractive for investors than full bids. Meanwhile, in order to protect themselves, companies discriminated against unwanted investors by issuing so-called dual class shares and strategic block voting became the norm.

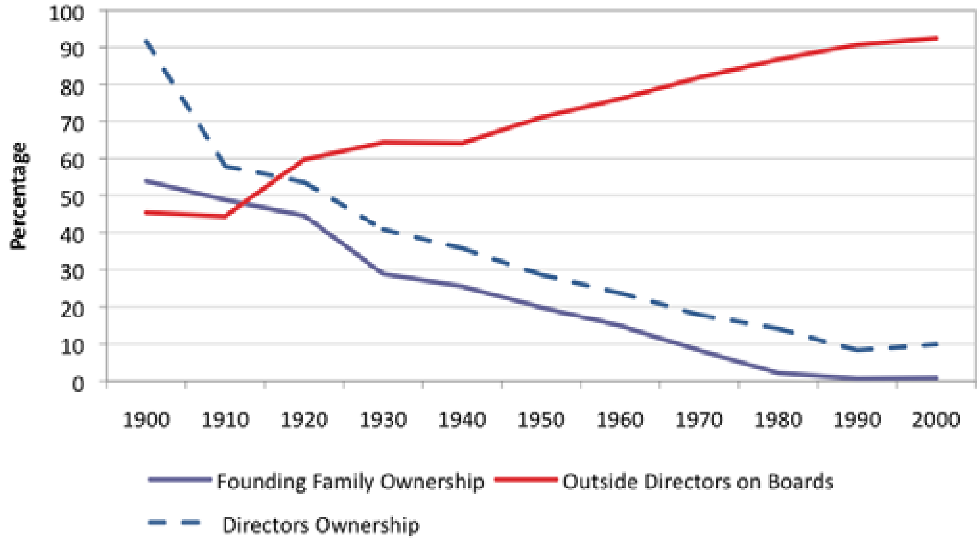
Thus, something approaching the European ownership model of dual class shares and pyramid structures did prevail in the UK. However, this model did not last long. Throughout the 1950s and 1960s, financial institutions had grown in stature and during the 1970s, institutional shareholders, including insurance companies, banks and financial funds, agitated to put an end to the protective measures and discriminatory practices that protected the corporate sector by impeding their access to capital markets. And, by 1980, the current control and ownership structures were in place, including a large institutional shareholdings sector, a hostile takeover market and extensive protection for minority investors. The changing nature of the owner and investor base for UK listed shares over the past 40 or so years is illustrated in Figure 5 below.

Figure 5: Ownership of UK listed shares by type of investor (1963-2006)



The historical development of dispersed ownership and the progressive serving of ownership from control in UK firms, is strikingly illustrated by Mayer and Rossi (2003) who trace the evolution of ownership and external management for 20 companies incorporated at the turn of the 20th century and still in existence today. As Figure 6 below shows, the story of corporate governance in the UK over the past 100 or more years has involved a ongoing diminution of ownership stakes amongst founders and directors and a continuous rise in the importance of outside (non-owning) directors.

Figure 6: The evolution of UK listed firms in the 20th Century



Source: Mayer and Rossi, 2003

Frameworks of ownership and control

Franks and Mayer (in Siebert, 1995) usefully differentiate between the 'outsider systems' of ownership and control in the US and the UK and the 'insider systems' of ownership and control in Europe and Japan. In the US and the UK, there is a large amount of listed firms, share ownership is diffuse and it is common for outsider shareholders, be they individual or institutional, to employ managers to manage corporations on their behalf. In Europe and Japan, meanwhile, there are a small amount of listed firms, share ownership is concentrated and 'cross-shareholding' arrangements and family holdings are far more prevalent than in the US and the UK.

It is ambiguous as to which model performs better in terms of corporate performance and competitiveness. Much of the debate on this topic has focused on the responsibility and accountability of management. Proponents of 'insider systems' argue that this model affords:

- Greater stability in decision-making. Cross-shareholdings, for example, endow managements with more direct sanctions against inappropriate action by owners because they control shareholdings in those very same owners (Mayer, 1997);
- Greater commitment to other stakeholders, for diverse investors are in a position to eschew implicit agreements by selling out anonymously and on a whim – yet do not risk a loss of reputation (Franks and Mayer in Siebert, 1995);
- Greater incentives to monitor management, which might lead to better business performance. Thus, whilst it is the job of shareholders to monitor management via the collection of information, if ownership is dispersed there is less incentive for shareholders to adequately do so;

- Protection from the oft-mentioned free-rider problem amongst shareholders (Grossman and Hart, 1980).

Thus, concentrated ownership is said to provide checks and balances against managerial corruption and inefficiency and allow for a long-term managerial perspective that takes into account a greater diversity of stakeholders. However, critics of the ‘insider model’ argue that:

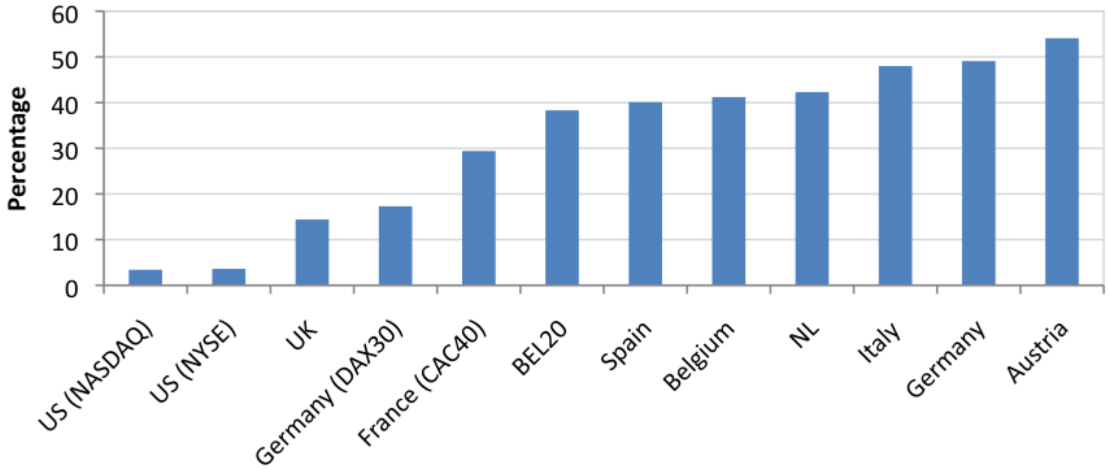
- ‘Blockholders’ might pursue goals that are contrary to the interests of minority shareholders, thereby extracting private benefits;
- Where companies are the majority shareholders, they might transfer resources to other projects, thereby creating inefficiencies;
- To the extent that firms are committed to particular policies and the interests of stakeholders, they might be less flexible in the face of external factors such as competition or technological innovation (Mayer, 1997);
- Optimal diversification implies that no shareholder should seek to invest too high a proportion of wealth in a single firm (Dhillon and Rossetto, 2009).

It may be the case that different ownership structures are appropriate for different activities. On the one hand, more diverse forms of ownership might be more appropriate for industries characterised by technological innovation and intense competition; and on the other hand, more concentrated forms of ownership might be more appropriate for industries in which greater commitment to stakeholders or skills and training are required, for these require long-term corporate policies. Thus, it might be argued that the optimal ownership structure would compromise between these models.

In fact, significant reforms in Europe have sought to facilitate something close to the ‘outsider’ system. The European Commission has sought some harmonization of corporate governance practices with the Takeover Directive of 2003; most EU nations have introduced codes of corporate governance and regulatory reforms that seek to address disclosure and accountability issues, as well as minority shareholder rights; and, on the ground, companies are seeking to present an image of themselves as model corporate players, so as to secure finance and higher share prices.

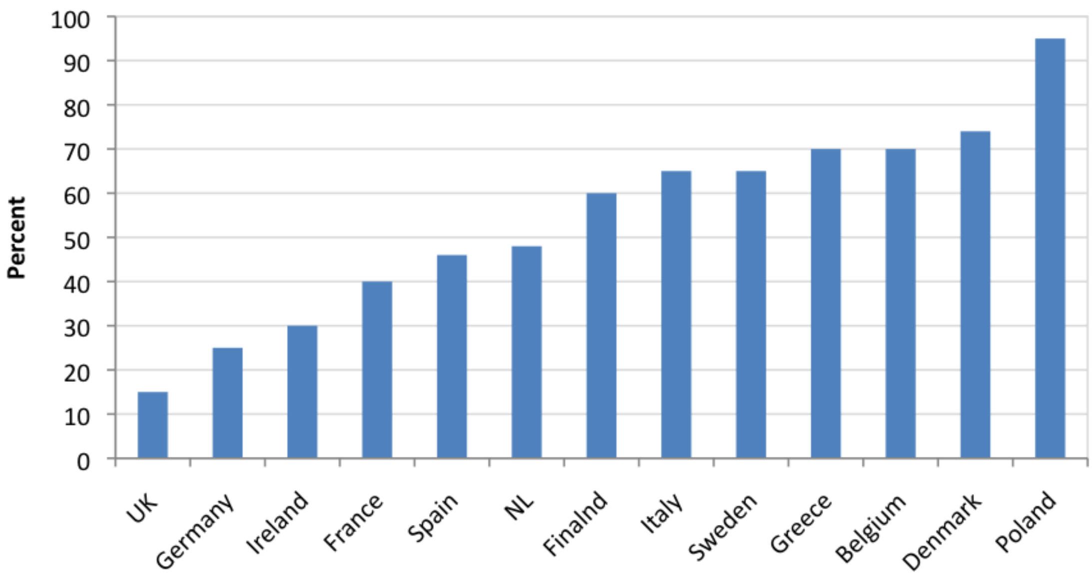
A possible interpretation of this shift proceeds as follows: since organisations are efficiency driven, and given the amount of money that is at the disposal of institutional investors, it was always only a matter of time before ‘insider’ organisations were going to disappear as they adopt best practices (Hansmann and Kraakmann, 2000). However, the problem with this interpretation is that there remain observable differences in approaches to corporate governance that endure despite the extensive involvement of foreign investment in national equity markets throughout Europe, along with the existence of potential funds should ‘insider’ organisations adopt ‘outsider’ practices in full. For example, as Figures 7 and 8 below make clear, the structures of corporate control and ownership in the UK and US remain very different to those other jurisdictions where concentrations of share ownership (and the ‘insider’ protections they afford) remain well entrenched.

Figure 7: Comparison of voting concentration in listed industrial companies ultimate voting block (mean largest voting block)



Source: European Corporate Governance Network

Figure 8: The presence of significant shareholders (above 20 per cent) in large caps (2007)



Source: Institutional Shareholder Services, 2007 / EU

Box 1: Public policy and UK corporate governance – dogs that don't bite?

Discussions about corporate governance in the UK are more often than not, framed by crisis, the most recent examples being the Enron and WorldCom scandals and, of course, the banking crisis of last year. When these crisis points are reached, policymakers have tended to respond in the form of highly publicised reviews, commissioned by government. The benchmark for this process, for the restrictions placed on corporate activity and on accountability was the Cadbury Report of 1992. Following the scandal of Maxwell Communications' financial collapse the report was commissioned to investigate the state of accountability and financial reporting in relation to corporate governance. The findings recommended, among other things, the division of responsibilities at the executive level, the inclusion and independence of non-executive officers in auditing and financial affairs and the requirement of corporations to produce an operating and financial report each year.

The reports recommendations were incorporated into the Combined Code of Corporate Governance, which was adopted, wholly or in part, abroad and in the OECD and World Bank. Sine the Cadbury report there have been numerous other reviews of corporate governance, including the Greenbury report in 1995, the Hempel report in 1998 and the Company Law Review. These added or subtracted elements of the Cadbury report and the Combined Code, as well as prompting debate over the issue of governance practice. The first major review of corporate activity since Cadbury did not occur until the Higgs Review of 2002-3, however. The Higgs Review was commissioned in the wake of the collapse of Enron and WorldCom, as governments sought to allay fears that such a crisis could happen again, elsewhere. It looked at the role of non-executive directors, the independence and relation between CEO and chairman, transparency of boardroom practice, as well as investigating revisions to the Combined Code. Following Higgs, the Walker Report on activity and accountability in the banking sector has recently been published in the midst of heated debate surrounding corporate governance.

The influence and implementation of such government reviews is questionable, however, if they are expected to lead to effective reform in corporate practice (Pollitt & Jones 2003). The Higgs Review made a host of recommendations for changes in the Combined Code and called for swift implementation by the Financial Reporting Council (FRC). However it was severely criticised in its review stage by influential corporate groups such as the CBI, the Institute of Chartered Accountants for England and Wales (ICAEW), many CEOs and the Financial Standards Authority (FSA). Chief among the criticisms was the prescriptive nature of the amendments to the Combined Code that the report suggested. Only one point of principle was suggested and 37 individual code points of practice. The recommendations were severely limited thanks to pressure placed on the commission by the interested parties mentioned above (Jones 2003). When the report was published in July 2003, many of the key changes to the Combined Code that Higgs had suggested, were watered down and modified. The demand that CEOs be prevented from becoming Chairman of the same company was removed, as were points regarding the independence of non-executive directors. Though it did implement calls for stronger communication channels between shareholders and the board of directors.

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In the midst of heated debates about the why corporate governance regimes failed to prevent the crisis that finally enveloped the banking sector during 2008, the Treasury-commissioned Walker Review has recently reported on approaches to accountability and transparency amongst UK banks. The review established the need for certain procedural and organisational reforms within UK banks but remained more limited in its suggestions for substantive reform of the UK's approach to corporate governance. The essential model of shareholder priority remains in place and the Combined Code continues to operate on the basis that companies should 'comply or explain' – allowing for deviations and exceptions that may be unhelpful to the task of ensuring the spread of good corporate governance practice amongst UK firms.

Shareholders and stakeholders

There are two competing perspectives on corporate governance. The first stems from classical economics and views the corporation as a vehicle through which shareholders maximise their investments. This perspective reinforces shareholder rights and measures success to the extent that managers deliver 'shareholder value'. A broader – and competing – perspective takes into account, not only shareholders rights and returns, but the interaction and contractual arrangements between the firm and a variety of 'stakeholders', including creditors and debtors, employees, suppliers and customers, along with governmental regulation and the wider social context of the business. Here, then, corporate governance refers to all of the forces that influence – or, indeed, should influence – decision-making within corporations, not simply the drive to maximise 'shareholder value'. For proponents of this perspective, the shareholder-centric view of the firm is problematic because it lacks democratic legitimacy; given the range of 'stakeholders' who affect – and are affected by – corporations, company boards ought to be run as democratically as possible.

In contrast, proponents of 'shareholder value' hold that accountability is a matter of concern only for shareholders and those delegated to run the corporation on their behalf – managers. A number of commentators have, however, questioned the extent that managers are accountable. Adam Smith once observed that managers in joint stock companies should not be expected to take as much care with other people's investments as they would their own. Stemming from this astute observation, there has been a great deal of debate regarding the degree to which those in control of corporations can be trusted with shareholder investment. Critics complain that the severance of ownership from control, along with the dispersed nature of shareholdings, has created a democratic deficit at the heart of Anglo-American corporate governance. In the US, for example, management effectively controlled 44 per cent of the largest corporations in 1929, a figure that had already reached 84 per cent by the early 1960s (Larner, 1966).

However, classical economic theory suggests that this does not necessarily constitute a democratic deficit. Indeed, there is the possibility that the uncommitted and dispersed character of shareholdings in the US and the UK is a democratic boon in that investors are able to ‘exit’ on a whim, which provides the necessary liquidity for a functioning market in corporate control. Thus, managers and directors are subject to extensive market discipline, even if that discipline does not take the form of committed ‘blockholdings’ with a lot at stake in the successful running of the business (Manne, 1962). Also, the competitive pressures of product and managerial labour markets similarly discipline managers, for if managers desire to keep their jobs, they will run their business in a manner that efficiently produces goods and services, which in turn keeps share prices high – and safeguards their position in the business.

Such theory fanned the increasing popularity of the shareholder perspective vis-à-vis corporate governance. Indeed, during the 1980s, the goal of delivering shareholder value by increasing profits and the quarterly price of shares was progressively seen as the only viable business strategy. However, from an earlier stage it was also clear that the blinkered pursuit of shareholder value had particularly deleterious impacts on labour. Indeed, a number of scholars highlighted something of an elective affinity between the rise of ‘shareholder value’, along with a corporate law system orientated to that metric, and rising levels of job insecurity, work intensification and lowering investments in training and skills (eg Froud, 2000). Moreover, highly liquid markets, dispersed share ownership, hostile takeover bids and the fundamental importance of institutional investors that entrench the importance of shareholder value, force managers to orient their businesses to short-term shareholder demands. As a result, employee participation and collective bargaining are likely to be eschewed since they complicate and hinder the drive to create short-term shareholder value.

A number of developments brought this issue to the fore, including the growing importance of finance for economies as a whole; the development of a raging bull market; the opening up of London securities; the expansion of shareholding with the privatisations and demutalisations of the 1980s and 1990s; the ageing of the population, for retirement savings depend upon the performance of shares; the occurrence of a number of high profile cases where deliberate asset stripping and the use of group structures led to corporate collapse, leaving employees without compensation and basic entitlements; and, importantly, a perceived imbalance between the rights enjoyed by shareholders in such situations vis-à-vis the rights of employees.

Indeed, given the seemingly intractable relationship between modes of corporate governance and the health of the employment relationship, a number of scholars began questioning the validity of separating corporate law from employment law. This is directly relevant to the debate between the shareholder and stakeholder perspectives, for if it is shown that making shareholder rights sacrosanct has a detrimental impact on other, equally important rights, pressing questions arise as to the validity of pursuing 'shareholder value' above and beyond other considerations, such as the position of stakeholders.

Furthermore, the so-called 'organised' or 'welfare' capitalism of Germany, Sweden and Japan arguably allows for a far healthier employment relationship. This model of corporate governance, based as it is on bank-based debt, a combination of debt and equity ownership, and crossholdings, is often argued to encourage long-term and in-depth monitoring of corporations so as to assay their value, rather than a reliance on short-term share indicators. This long-term approach enables managers to engage more cooperatively with their employees and provide greater levels of job security, participation and training.

However, it is not only from the perspective of social justice that 'shareholder value' has been critiqued, but effectiveness and efficiency, too. In his seminal '*The State We're In*', for example, Will Hutton was sharply critical of the perceived short-termism of the City of London that – he argued – has adverse consequences, not only for employees and the general public at large, but British industry, too. A combination of high-cost capital, short payback periods and takeovers prioritise stock market rewards over long-term investment. The challenge, according to Hutton, is:

> *'to create a new financial architecture in which private decisions produce a less degenerate capitalism. The triple requirement is to broaden the area of stakeholding in companies and institutions, so creating a greater bias towards long-term commitment from owners; to extend the supply of cheap, long-term debt; and to decentralise decision-making'* (Hutton, 1995).

Once more, the 'organised' or 'welfare' capitalism of the Continent and Japan is held up as a model that trumps the short-termism of the Anglo-American model.

The crisis of 2008 provides an opportunity to reappraise the 'shareholder value' model. Indeed, whilst 'shareholder value' is – and will remain – a fundamental integrant of business, it is apparent that it cannot (and should not) act as the sole principle that guides corporations, particularly in the short-term. For a start, capital markets are not always efficient, nor do they reflect only the present value of future profits. Rather, price bubbles can distort the value of stocks, with capital markets often remarkably inefficient. Invariably, investors are tempted to take advantage of these bubbles by buying into ever-rising markets, often en mass. Clearly, then, such markets are not propelled by a desire of long-term stable growth and future profits, but the expectation of short-term returns, and when greed gives way to fear and the bubble bursts, all is lost. Also, there is the possibility that share options schemes exacerbate the short-termism of the 'shareholder value' model. Since the vesting periods of such schemes are typically three years, managers will naturally orientate their businesses so as to maximise their share options during that period. Yet the temptation to manipulate share price can be irresistible, which inevitably creates short-term gains that are undone once the share options have been expended. Such incentives encouraged many bankers to take short-term investment risks in the years leading up to the crisis of 2008.

Indeed, if the crisis has taught us anything, it is that the single-minded pursuit of higher share prices does not guarantee stable, long-term success. The problem is that shareholder value has become a goal in and of itself. Sound business practices will increase share value, but this is an *indication* of success; it does not cause success. More positively, then, the crisis suggests that long-term success will only be achieved if businesses take a long-term perspective. Also, to the extent that a longer-term perspective permits good work practices, including the implementation of new payment schemes to encourage employee commitment; investment in training to improve employee skills; employee and team-based working strategies and organisation; and a commitment to job security (Appelbaum et al, 2000), shareholder value is only likely to be increased, as research has consistently demonstrated the value of such practices. To that end, it is important that shareholders not only allow, but actively encourage, a long-term perspective on business management and investment.

Finally, it is worth noting that Jack Welsh – the former Chief Executive of General Electric and someone whose name was once synonymous with 'shareholder value' – recently declared: 'On the face of it, shareholder value is the dumbest idea in the world'.

Box 2: Differential forms of share owners: are they really so bad?

Throughout European market economies (save for the UK and Ireland) there exists a wide variety of Control Enhancing Mechanisms (CEMs) that work to differentiate financial ownership of shares from the conferral of voting rights. As a recent study of CEMs by the EU notes, such mechanisms are often the norm in 'insider' systems where an array of structures are utilized across different jurisdictions, including pyramid share structures, voting right ceilings, ownership ceilings and priority share structures (ISS, 2007). Such structures highlight the relationship between the economic aspects of ownership and the political or constitutional aspects that are involved by granting different rights and powers to different classes of shareowners.

Whether, in fact, dual share structures are a good or a bad thing has become an increasing source of debate and disagreement amongst investors. Large institutional shareholders most often lead opposition to the dual structure, arguing that it can be detrimental to economic performance.

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It is said to disadvantage public shareholders by contributing to poor governance, which is insulated due to the lack of accountability to investors without privileged voting powers. Those with enhanced voting powers, it is argued, can also exercise a disproportionate control over cash flow by using their power leverage to expropriate funds from those who do not have it, through self-dealing, improved executive pay and increased bonuses or stock options. Furthermore it allows the cash flow to be directed, by controlling shareholders, into channels that are not always in line with the company's core interests.

The benefits of CEMs and differentiated share ownership structures have been debated widely. It is argued that they insulate a company from short-term financial pressures that exist in single share structured economies. These pressures can be detrimental to long-term firm value. Proponents suggest that they provide a mechanism for founders to develop a company without giving up control, utilizing expertise and commitment for the benefit of stakeholders. This could help encourage an environment of innovation and entrepreneurship. Because voting shareholders will require increases in cash flow and equity from time to time, they will maintain a good relationship with financial stakeholders. The latter, it is claimed, will often not be concerned with the political aspects involved in corporate ownership, but merely want to share in the dividends; this is particularly true of smaller investors.

The arguments and empirical evidence surrounding the issue of dual share structures are widely disputed. Chaesssens et al (2002) show that the separation of control and equity can decrease a firm's value. However the same study shows that where ownership is concentrated, value increases. Lins (2003), meanwhile, has argued that the financial impact of dual share structures is not significant in developed markets. There have been numerous other investigations into the issue. Cronqvist and Nilsson (2003), for example, find that various other factors such as family based controlling minority shareholders have more of a significant effect on firm value. In a 2006 study, Zhang found that dual structured firms may under-perform in some respects but they do not do so in terms of book equity and price to earnings ratio. Smart and Zutter (2003) find that there is less underpricing of shares in dual structured firms and that this creates an easier, cheaper way for private companies to become public without losing control. While Maynes (1992) found a reduction in firm value when firms reorganized into a dual structure, Dimitrov and Jain (2006) argue that in the 178 US firms who restructured from single to dual systems between 1979-1998, long and short-term shareholder value was enhanced. Here, the evidence is at best inconclusive.

While there is a general preference for single share structures amongst international investors, an EU sponsored survey of investment managers (ISS, 2007). suggests that there remains room amongst investors to accommodate differential ownership structures as long as their rationale is clear and arrangements transparent. By and large the major issue identified by investors is accountability and transparency. UK asset and hedge fund managers agree that if the mechanisms are simple, fully open and well reported they can be effective and appealing to investors. Furthermore, there must be mechanisms in place for the protection of minority voting rights and the effective exercising of these rights. While dual share structures have their drawbacks, they present a framework within which to realise the dual nature of ownership; on the one hand financial, and on the other constitutional.

Case study: Private equity – in pursuit of shareholder value

Although characterised by dispersed share ownership, there has been a definite trend in recent years to a concentration of the type of owner operating in the UK. Increasingly, shares are held by institutional investors, which might include pension funds, life insurance companies, unit trusts and investment trusts. Such institutional investors yield significant influence over management and are crucial factors in corporate governance and control in the UK (McCahery and Vermeulen, 2008). Indeed, large private equity firms such as TPG and Goldman Sachs own and control vast volumes of capital and are of central importance to vital areas of the economy. They also employ significant numbers of employees.

One way in which institutional investors can affect corporate governance and control is via private equity buyouts. Private equity investors analyse the performances of publicly listed companies. If value is deemed to be leaking, either to shareholders or from inefficient business practices, private equity investors may choose to buy the company in question, often by leveraging debt. Then the company is taken into the private realm, made to work efficiently and sold off at a profit, either to another private owner or in an initial public offering (IPO). Phil Thornton (2007) has described this as the 'most virulent new form' of 21st century capitalism.

The global market for private equity has grown exponentially since the 1980s, with rising stock markets enabling institutional shareholders to buy public firms when stock prices are at a low. Institutional shareholders view private equity favourably and it is gaining in popularity amongst pension funds. Furthermore, within the high-end managerial profession, there are signs that private takeovers are increasingly favoured by top managers, who cite their frustrations with corporate governance legislation and short-sighted shareholders as reasons for their dissatisfaction with public business, as Alex Navab, a partner of KKR, attests: 'As the buy-outs we pursue get larger and more complex, senior executives at public corporations have taken notice and become more attracted to those opportunities as it gives them a bigger canvas to paint on'.

There was a particular increase of private equity takeovers in the last decade because of the cheap and widespread availability of debt. Whereas in the 1980s, private equity takeovers were pursued solely to improve poor company performance because of the high cost of debt, in recent years they have often been pursued for the simple reason of obtaining cheaper finance. Such activity peaked in the period between 2005 and 2007 due to decreasing interest rates, lax lending standards and regulatory reforms for publicly listed firms in the US. The UK is also a prime target for private equity activity because of its extensive features as an 'outsider system' and abundant availability of capital. Recently, City minister Lord Myers suggested that it is easier to purchase a company in the UK than any other national economy. Share ownership in the UK bears no real responsibility, only the right to buy and sell at will, to vote (where those rights are conferred) and to collect dividends.

Undoubtedly, there have been successes. Some private equity takeovers have benefited company performance immensely (Cumming et al., 2007). Proponents of private equity takeovers argue that this is down to enhanced corporate accountability and efficiency. So, where managers have been acting contrary to the long-term interests of the business and shareholders, it is said that private equity buyouts remove those managers or pressure them to perform better because of four main factors:

1. Tighter monitoring, which enhances accountability;
2. The existence of managerial equity ownership, which provides incentives to reduce spending (Jensen, 1986);
3. Increased levels of external funding, which forces managers to reduce spending;
4. The existence of after-buyout external funding, which also forces managers to end unprofitable activities.

Also, and in response to claims to the contrary, proponents of private equity takeovers have argued that they allow for a longer-term business perspective, for the simple reason that the takeover must improve the business if it is to be deemed attractive to subsequent buyers and investors. Thus private equity holders have to take into account factors such as employee skills and commitment because otherwise shareholder value will inevitably decline. Furthermore, because the targeted company is under the complete control of its new owners, it is said that managers do not have to take into account short-term stock market pressures or answer to a diversity of shareholders. For proponents of private equity, this newfound stability provides breathing space for decisive action, which enables management to utilise company assets to their fullest so as to boost productivity and profitability.

However, it is unclear whether private equity investors genuinely act responsibly vis-à-vis the workforces they are responsible for; or indeed other stakeholders in the wider community. When new management is imported from outside the company, employment can been slashed – often by as much 18 per cent (Thornton 2007). Thus, it may be the case that the pursuit of immediate shareholder value is detrimental to other aspects of business life. Private equity firms and long-term stakeholders clearly operate on a very different time-scale. The typical life-span of leveraged buy-out is just three to four years, whereas for managers, employees, customers, suppliers and the wider community in which the firm is embedded, three to four years is a very short time indeed. As such, critics argue that the emergence of private equity funds is another instance of the short-termism that brought the global economy to a precipice during the global crisis in 2008.

There are a number of areas of concern: for example, because debt is available at a cheaper cost than equity, increasing company debt has the affect of inflating profits. But it also has the affect of increasing the level of risk faced by the company. Whereas a standard ratio of debt to equity is 30 per cent to 70 per cent, private equity takeovers reverse that ratio. Often, debt can increase to 80 or 90 per cent and many companies are struggling to service this high-level of debt, particularly in a recession. This inevitably increases the costs of business and necessitates cuts. As a result, private equity takeovers often involve freezes on investment, asset stripping and staff redundancies. However, whilst this can improve short-term profits, the long-term viability of the company is called into question because investments in product development and employee skills are unlikely. Furthermore, it is often the case that mid-range private equity companies perform less well that do their equivalent public counterparts, sometimes by as much as 20 per cent (Kirkland 2007; Swenson 2005).

There are also concerns that the emergence of private equity funds represents the dominance of capital over labour, with workers baring the brunt of the cuts in expenditure that are required to service increasing levels of debt. The Financial Services Authority (2006) has voiced concerns regarding potential employment risks and trade unions have argued that private equity takeovers create returns through wage cuts and job losses, with reductions in employment (Wright and Coyne, 1985) and increasing levels of under-employment. For the International Trade Union Confederation private equity investors have ‘no interest in investing in its employees, no need for employer-employee partnerships, and no reason to provide anything but the minimum when it comes to wages, benefits and conditions’ (ITUC, 2007), whilst Unite highlights rising levels of job insecurity and under-threat pensions. Improvements in efficiency outweigh the importance of employer-employee cohesion (Thompson 2007), though existing literature is not unanimous on this. Many of the changes brought about through buy-outs are said to have directly negative effects on employee stress levels.

Also, to the extent that private equity investors have no need for employer-employee partnerships there are likely to be serious implications for long-term business performance, for research has consistently shown the value – indeed, the central importance – of good work practices. Private equity buyouts reduce the likelihood of investments in HRM, which might include new payment schemes to encourage employee commitment; investment in training to improve employee skills; employee and team-based working strategies and organisation; and a commitment to job security (Appelbaum et al, 2000). One reason given for the growth in private equity takeovers is the frustration oriented towards the regulations and constraints of public ownership (Thornton 2007). Without such investment, however, businesses stand to lose out on the growth potential of long-term high commitment management practices, but could also suffer the adverse performance-related consequences of job insecurity and poor staff morale. This manifest short-termism can even affect companies that aren't taken over. To the extent that managers in publicly listed companies fear the risk of a buyout, they are likely to focus on producing results in the short-term rather than plan for more sustainable, longer-term growth. It is of little surprise, then, that private equity has attracted a great deal of criticism in recent years. Protests have greeted the targeting of endeared British companies,

Whilst the private equity investors will profit greatly, 'Everyone else will be the poorer' (Hutton, 2009). Indeed, the possibility of layoffs, wage depression and loss of industry affects not just employees, but the wider community, for these are 'social risks' that will have to be absorbed by the general public. What is required, then, is greater regulation and transparency so that private equity investors accept their wider responsibilities. For employees, these relate to their role as an employer, including a respect for consultation, transparency, transfer rights, working conditions, pay and collective bargaining; for the wider community, meanwhile, there is a need for a greater appreciation of the many stakeholders that have a role in – and are affected by – business practices.

In this section, we have explored the impact of corporate ownership 'over' the workplace. To that end, we have sought to understand the role that ownership plays as a driver of (good and bad) corporate governance. We have noted how the development of the UK's corporate governance framework has been very different to those adopted in other European states. In particular, we have noted how distinctions between insiders and outsider systems of corporate governance and between strategic goals oriented to shareholder value as opposed to stakeholder value have shaped a sometimes deep ideological divide about the role that corporate ownership might (or might not) play in realizing broader policy objectives including those relating to good work. What our analysis suggests is that, for all for the arguments advanced in the cause of disperse ownership models and clarity of purpose afforded by the pursuit of shareholder value, there remain important lessons to be learnt from 'insider' systems oriented to meet the needs of a broader constituency than stockholders alone. To that end, we have noted the continued importance of alternative constitutional arrangements (such as differential share structures) that provide for ownership to translate into good work outcomes.

3. Ownership as mutuality in the public sector

This section examines emerging debates around ownership in UK public services, thus extending the previous discussion into the public sector. Here, political concerns are of more overt importance, and recent notions of mutualism, localism and new forms of public organisation reveal, once again, the centrality of constitutional means as the causal driver of good work outcomes. The fact that, in this sector, ownership is already in public hands, allows constitutional innovations of broader scope, and a policy-driven re-orientation of public services to ends other than simple gains in financial efficiency.

Mutuality and social enterprise in the UK public sector

Since 1997, there has been extended discussion of the benefits of mutuality and social enterprise in the public sector. This orientation has its origins emerged, in large part, from the voluntary sector and the co-operative movement. Additional interest in mutualism has been shown by self-starter enterprise schemes in the USA. There has also been growth in local level funding bodies, such as the European Regional Development Fund in the late 1990s, which seek to innovate forms of local regeneration in disadvantaged communities. Their purpose has been to shift the focus away from reliance on big capital and hierarchical infrastructure, and towards local, organic and bottom-up service planning and provision.

It is this organic and community-based approach to public services that mutuality attempts to underpin. Social enterprise, based on the third sector model, provides services that prioritise the end user, who then participates in the constitutional moment as a stakeholder. In recent years, government has committed to developing locally based public services through such organisational innovations such as Foundation Trust hospitals and School Academies, which are both intended to emphasize the role of the end-user as participant as well as customer. Moreover, tax concessions are now available for investment in social enterprises and defined legal structures – such as the Community Interest Company – have been established in order to enable ownership structures compatible with the delivery of public services by not-for-profit organisations. Further activity has included a host of recent local, community-based initiatives, such as the Sustainable Community Strategy, which seek to promote the establishment of social care groups, environmental sustainability groups and adult education, among other areas. However, the notion of a social economy remains rather ill defined, and it is perhaps best conceived less as a discrete sector and more as an approach to providing services at the local and community levels. Certainly, though, as Cliff Mills points out, 'the idea [of mutualism] is becoming mainstream again, whether under the guise of localism, community ownership or social enterprise' (Mills, 2009). This is further evidenced by the recent announcement of a government part-sponsored Commission on Ownership, with its brief to investigate the potential gains of mutualism in UK public services.

Public organisations have a wide range of stakeholders, be they governmental, financial, public, etc. In such organisations, the constitutional arrangement defines which particular stakeholder group will be prioritised (Hunt 2006). Third sector providers of services focus on the outcome for the end user. Here, then, the issue of provision is not so much the economic one of access to resources, but the political issue of how and in what ways goods and services are produced, distributed and delivered (Mills 2009). The public sector thus serves to highlight a range of wider social and environmental impacts that might be delivered by any such constitutional arrangement.

Orienting to social provision and community responsibility

In the public sector, therefore, price and efficiency are not the only factor involved in the provision of goods. This is particularly apparent in the growth of fair trade and the green movement. Indeed, interest in such organisational arrangements has increased with the current economic crisis, as the dominant investor profit model of service provision and the argument that the market is best placed to provide for public needs and wants has been increasingly undermined in the popular imagination.

In the public sector, then, the constitutional arrangement is already featured more strongly than in the private, is supported by existing practices and strengthened by current conditions. The question remains, however, as to whether this translates in to good work outcomes.

Mutual reform of public services requires a change in organisational orientation away from shareholder return and cost/benefit efficiency, towards social provision and community responsibility (Leadbeater 2007). This does not mean, however, that social enterprise is a one size fits all organisational form. Often they follow the co-operative model, but social enterprises are often also run on a traditional business model. In both cases, however, the purpose of the business is, first and foremost, to provide for the end user, or community of users, not primarily that of profit. It is thus the constitutional features that define a social enterprise as mutual, not a single corporate form (Mills 2009). Indeed one of the features of social enterprise is that what profit is made is reinvested into the enterprise or community itself (Smallbone et al 2001). To be fully realised, however, such a scheme would have to be implemented against the background of a more comprehensive strategy for social innovation (Leadbeater 2007).

Schofield (2005) has argued that such a background does not exist in the UK. He writes that though there are 15,000 organisations that could be defined as social enterprises, with a turnover of £18bn and employing 475,000 workers, the organic basis for community development of this sort is not there. He attributes the popularity of mutual innovation in public services to ‘bandwaggoning’ of attractive looking business models, which could be made to fit a third way approach to public services. He further argues that the terms and definitions that make up social enterprise are ill defined and often contradictory. Are they co-op based? Does it mean co-ownership? Do they operate according to traditional business models? The key feature of the social enterprise, mutual model for public services seems to be, as has been argued, a constitutional orientation towards community, end-user reward.

What this suggests is that the model of citizens as consumers is no longer adequate (Mills 2009). Evidently, citizens participate in the constitutional arrangement of public service organisations in a number of ways: as customers, workers, savers and investors. The nature of active involvement requires greater accountability than exists in the 'arms-length' provision of services. When services are outsourced, or privatised and modeled on shareholder business organisations, there is a gap between democratically elected representatives and the management of services themselves. The degree of accountability and responsibility is here diminished (Hunt 2007; Mills 2009). Once again, the preferred treatment of the lack of good work outcomes is to attend to the causal power of the constitutional arrangement, rather than to rely on tweaked arrangements of economic ownership.

Key text: Phillip Blond's *The Ownership State: Restoring Excellence, Innovation and Ethos to the Public Services*

Phillip Blond's makes a case for restructuring and diversifying the ownership of public services in the UK. He argues that effective reform in the public sector requires not only participation and dedication from frontline members of staff within organisations, but also the inclusion of citizens as engaged partners, as members of community owned 'civic companies'.

The idea he is trying to promote is one of social enterprise. He seeks to move away from what he calls the 'false dichotomy' of statist, centralised provision of services on the one hand, and market-driven, consumer-oriented provision on the other. Instead he proposes an 'open' system of governance which is flexible and organic. It adapts to the needs of intelligent consumers and empowered frontline staff, reversing the trend of disengagement, increasing satisfaction at both ends and making available a previously disregarded source of frontline expertise.

Public sector staff, Blond claims, find themselves in a transitional stage of governance practice – dominated by new public management – which is neither efficient nor modern. His report is a critique of the neo-liberal management practices that emerged throughout the 1980's and 1990's and have been 'absorbed into the bloodstream of the corporation'. The present government's solution to management crises displays this fealty to Chicago School economics and public choice ethics: more outsourcing, more competition and more managerial supervision. Where public sector funding has risen by 55 per cent in the past decade, productivity has fallen by 3.4 per cent. In the private sector, productivity rose by 27.9 per cent over the same period.

Blond argues that the relation between productivity and empowerment is mutually reciprocal. In support of this assertion, he cites a 2008 NHS survey in which only 27 per cent of staff felt involved in important managerial decisions, 26 per cent believed their work was valued and 15 per cent felt that communication between managers and staff was effective. Over intensive, bureaucratic management of productivity targets not only stifles productivity, it also disengages staff from the work they do and degrades the service they provide. In the same poll, 18 per cent of staff thought patient care was not a top priority for NHS trusts, and a further 27 per cent gave an ambivalent answer.

Blond's solution involves in-sourcing rather than out-sourcing responsibility and ownership. Employee ownership models provide more potential to innovate and a greater sense of mission to an organisation, as well as drastically reducing the need for managerial regulation and supervision. A culture of self-regulation and assessment develops when employees have a stake and a voice in their work. Here, then, Blond seeks to socially engineer good work by adjusting structures of ownership.

Blond argues that the main roadblock to effective reform is the structural message of disempowerment which public organisations send to the communities they serve. He therefore claims 'the state must enable new associations of service users, community members, voluntary contributors and existing social organisations to *take ownership* of their services as partners with direct influence over providers'. Policy makers must overcome the ingrained scepticism of civil society that has for too long been the hallmark of organisational governance. He argues for the development of a public culture of engaged individuals who take direct interest and ownership in their shared social environments. This is largely a public value theory of the general public as stakeholder, involved in 'flexible personal relationships' and 'meaningful user engagements' with scaled-down public organisations. Blond's idea of 'civic associations' is therefore one in which frontline workers *and* service users interact as co-producers, designers, decision makers and evaluators of public service organisations.

Box 3: Structural Innovation in the ownership of social enterprise

The ‘surplus sharing’ mechanisms recently developed by Rory Ridley-Duff of Sheffield Business School represent an interesting new way to benefit all stakeholders in social enterprise organisations. The rules of this structure account for the role played in an organisation by the founders, the workforce and by investors by differentiating the shares available to each. The different shares are provided on different bases and confer different rights and responsibilities to the bearer. The goal is to reconcile ownership and control through a participatory organisational structure.

Founder shares are held by the people who establish the original concept and initiation of an organisation or enterprise. According to Ridley-Duff the allocation of these shares allows the founder to veto decisions that divert from the original purpose of the organisation, without having a heavy hand in strategic decision-making. Therefore they protect against organisational ‘mission drift’. Labour shares are granted to any party under contract to the organisation. The methods for allocating these shares decided democratically within the organisation at a General Meeting. These may be based on hours worked, one member one vote or other grounds. It is important to note that these shares are available to anyone under contract to the company, including self-employed contractors and suppliers, as well as employees. Finally, investor shares can be held by any individual or group, including employees, and grant the holder the right to participate in the democratic processes of the organisation. A proportion of the company’s surplus is distributed among the investors who also own the company, though the labour shareholders attend to the day-to-day governance. The rate of shares owned individually can be determined depending on the nature of the organisation; for a consumer cooperative, for instance, a cap on the percentage of shares available might be fixed.

Further to being offered labour shares, anyone under contract is also granted the chance to buy investor shares to the value of 15 per cent of their annual salary. In a similar manner to the Mondragon Cooperative Corporation, this model brings together the ideas of consumer cooperatives an employee-owned business, granting membership to employees and consumers. Rules are established in the structure to confer voting rights and distribution of company surplus among members as stakeholders. This distribution helps ensure the balance is maintained in various entrepreneurial or social settings.

Conclusion

This report has highlighted the importance of the nature of ownership in determining many aspects of value, over and above financial return for shareholders. The predominant conception of ownership in the UK only takes into account certain aspects of what is involved in ownership itself. Yet there are other, equally important parts. Organisations have a wider social impact and a wider responsibility toward employees and communities. For too long, we have imagined that economics can solve all our problems. While it may be that markets generate the most profit when unhampered by political concerns, they surely work better – and attend to other values more effectively – when properly guided to seek not only profit, but also, good work. To this end, ownership is merely one tool – one that needs constitutional expression.

Stakeholders, whether owners or not, can and should be constitutionally empowered to instigate the means by which good work outcomes can be attained. The constitutional arrangements required for good work outcomes can derive directly from economic power, but so can they be the result of measured political judgment. Policies that empower stakeholders, that grant them access to decision-making, that involve them in determining the purposes of business not only increase the productivity of employees and organisations, but also generate good work outcomes. There is a broad distinction to be drawn, therefore, between the economic character of shareholder-oriented ownership and the political orientation of ownership based on stakeholder models.

Good work outcomes require participatory practices, an orientation to end users and responsiveness to local needs. Such changes in the means of decision-making can be achieved by changes in ownership, certainly, but so can they be generated by other – more political – forms of power. Whether demanded as the outcome of good public judgement, or as a specific expression of economic right, it is the means that give the ends, not the owners.

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