

# The Ownership Effect Inquiry

## Final Evidence Report

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## **Acknowledgements**

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## **Executive summary**

This part of the report summarises the Inquiry's main findings, under six main headings:

- Growth and diversity
- Performance and productivity
- Standards of corporate governance
- Transition to employee ownership
- Regions and communities
- Barriers to expanding employee ownership

### **1. Growth and diversity**

- 1.1 Growing sector: The number of businesses moving to employee ownership is increasing, indicating growing awareness and viability of the model
- 1.2 Wide appeal: Models of employee ownership are present across a variety of business demographics such as sector, size, age, and region, indicating its relevance and wide appeal
- 1.3 Adaptability of the model: Employee ownership appears to be an extremely flexible model – allowing companies to adapt it to their strategy and industry conditions

### **2. Performance and productivity**

- 2.1 Business performance: Transitioning to employee ownership is associated with improved business performance assessed as a combination of revenue growth, repeat business, and long-term customer relations
- 2.2 Productivity and efficiency: Transferring to employee ownership is associated with rapid improvement in productivity, typically the result of cumulative impact of more engaged and motivated

employees making changes that reduce waste and improve efficiency

- 2.3 Long-term orientation: Employee Owned Businesses (EOBs) show evidence of long-term orientation in decision-making. Employees are more likely to work harder and forgo short-term rewards in the interest of the organisation's long-term growth and survivability
- 2.4 Breadth of performance objectives: EOBs assess performance using both financial and non-financial criteria. They pursue a balance between growth and profit, and other objectives such as protecting the health and well-being of employees, and contributions to the community

### **3. Standards of corporate governance**

- 3.1 Corporate governance: Transitioning to employee ownership is associated with improvement in standards of corporate governance
- 3.2 Transparent and accessible reporting: Transitioning to employee ownership tends to increase the sharing of information, and encourage open discussion of the organisation's strategy, financial outlook, and overall performance with employees
- 3.3 Engagement and involvement with employees: EOBs tend to have higher employee retention, more engaged employees, and employee-owners who are more motivated to invest time and effort in improving the organisation
- 3.4 Level of scrutiny by employees: Employee shareholders in EOBs are more likely to scrutinise major management decisions and hold management accountable for their actions than their counterparts in conventional businesses

- 3.5 People-centric management outlook: Management in employee owned business focus significant attention on the development of their employees. Employee ownership has a positive impact on employee health and well-being, perception of fairness, employee commitment and retention

#### **4. Transition to employee ownership**

- 4.1 Awareness and uptake of employee ownership in succession planning: Privately owned, and particularly family owned firms, show increasing awareness of the potential value of employee ownership as a succession option and alternative to trade sale
- 4.2 Owners' values and transition to employee ownership: Owners' values in assessing balance between financial and non-financial outcomes from succession are a central determinant in selecting employee ownership over other models – most notably exit through a trade sale

#### **5. Regions and communities**

- 5.1 Employee ownership and local job creation: EOBs have a greater propensity to recruit locally and promote talent from within the organisation, and are less likely to relocate or offshore jobs in pursuit of financial objectives
- 5.2 Employee ownership and the resilience of regional economies: Quantitative evidence shows EOBs' show relatively greater resilience and sustainability during economic downturns, contributing to the strength of regional economies
- 5.3 Employee ownership and community development: EOBs' relatively high degree of commitment to the communities they operate in leads to greater willingness to participate in, and contribute to, community development, often by explicitly



dedicating a share of the profits and/or employee time to local causes

## **6. Barriers to expanding employee ownership**

- 6.1 Professional advisory support: Despite apparently growing interest from owners there is a limited number of high quality professional advisors on succession planning and moving to employee ownership
- 6.2 Organisational readiness support: Few professional advisers currently have the knowledge or experience to advise owners on the organisational and leadership factors involved in transition to employee ownership
- 6.3 Employee ownership in higher and business education: Despite the sector's growth, employee ownership is almost completely absent from the higher education and business education curriculum

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# 1 Introduction

The aim of this report is to present evidence submitted to The Ownership Effect Inquiry: an independent, business-led Inquiry into the impact of employee ownership as an economic and social enabler, particularly as a positive contributor to UK productivity and standards of corporate behaviour.

## 1.1 What is employee ownership?

For the purposes of this report, we define employee-owned firms as companies in which employees own a significant and meaningful

✓ *For a firm to be employee owned the employees' stake must underpin organisational structures that promote employee engagement in the company*

Nuttall Review 2012

stake in the business. We use the Nuttall Review (2012) position which states that in addition to financial participation, for a firm to be meaningfully employee-owned, “the employees’ stake must underpin organisational structures that promote employee engagement in the company” (p.20) [1]. Although the Nuttall definition guided the Inquiry’s selection of participating firms and qualifying evidence, our literature analysis included some research where ownership stakes were not quantified.

## 1.2 Sources of data

The report draws on the following five sources of evidence, listed in the sequence in which they were collected for the Inquiry.

- ✓ *Five different sources of data*
- ✓ *101 different employee owned businesses, advisors, and industry bodies have given evidence*
- ✓ *Most exhaustive review of employee ownership in UK*

- The desk research report – ‘The Ownership Effect: What Does the Evidence Tells Us?’ – summarises existing research evidence on the ownership effect. This literature search was conducted in relevant databases (business and economics) that include peer reviewed journal articles, as well as other types of research publications including conference proceedings, book chapters, and books, as well as reports, policy documents, and prominent news articles.
- Written responses to the Inquiry’s online survey from 76 EOBs and advisors. These submissions contain profile information about all the participating businesses including corporate information such as the nature of products and services, locations and key markets, as well as corporate data such as number of employees, summary financials, and information about being employee owned such as the type of ownership model, date of transition, and future plans.
- Witnesses’ spoken evidence at seven panel hearings around the UK - three in London, and one each in Birmingham, Cardiff, Edinburgh, and Manchester. These produced more than forty-five hours of audio recording, and over six hundred and fifty pages of

transcription. In all, 60 EOBs and 18 advisors gave evidence at these oral hearings. Questions at these hearings focused on four central themes: corporate governance, productivity and performance, the role of employee ownership in business succession and growth, and advisors and funders' perspective of EOBs.

- Written information submitted by panel hearing witnesses – employee owned companies and specialist advisers – to underpin their evidence. In all there were 55 unique submissions of written evidence from the oral hearings.
- Additional data from hearing participants - including data, submitted by 12 EOBs, on their co-owners' perspective of employee ownership.

Overall, 101 different organisations have provided either written or oral evidence for the Inquiry and all the sources put together have produced close to fourteen hundred pages of evidence.

### **1.3 How to read the report**

The report consists of six main chapters focusing on the following topics. (i) Growth and diversity of employee ownership (ii) Impact of employee ownership on productivity and performance (iii) Impact of employee ownership on standards of corporate governance (iv) Transition to employee ownership (v) Impact of EOBs on communities and regions and finally (vi) Barriers to expanding employee ownership. Each chapter has sub-sections, presenting the evidence collected from different sources along more detailed areas of investigation.

These sub-sections also use short case studies of EOBs to illustrate the overarching themes. Case studies report only the comments witnesses made on the specific issue profile, rather than everything they said. Case studies were selected to reflect confidentiality, relevance, and distribution of cases across sectors, regions, and type of employee ownership models.

## 2 Growth and Diversity of Employee Ownership

The growing number, greater awareness, and the striking success of so many EOBs demonstrate the relevance and usefulness of the employee ownership

- ✓ *Number of employee owned businesses is growing. The EOA has more than 300 active members*
- ✓ *By enabling the formation of Employee Ownership Trusts the Finance Act 2014 has directly led to the creation of more EOBs*

model. While the exact number of EOBs is impossible to ascertain, evidence strongly suggests increasing awareness combined with new tax incentives have been instrumental in growing the number of EOBs. Furthermore, the inherent flexibility in the different models of employee ownership enables transition into the model at a pace that can be adjusted to the needs of the owners.

In this section, we will first discuss the growing numbers of employee owned business and then profile the participants who provided evidence to the Inquiry.

### 2.1 Growing number of EOBs

The economic contribution of EOBs in the UK is significant. It is estimated that EOBs deliver 4% of UK GDP annually and this share is

- ✓ *EO businesses have a 4% share of UK GDP*
- ✓ *Revenues of top 50 EO businesses grew by 3% more than like-for-like non-EO businesses*

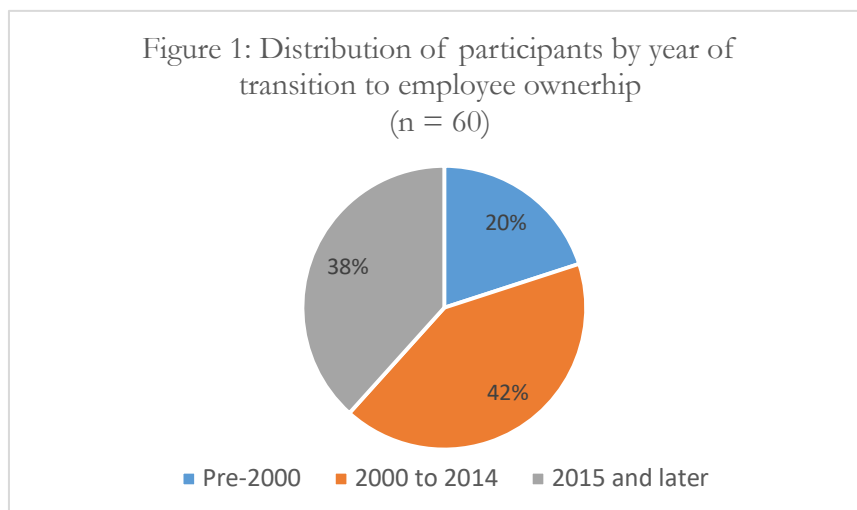
growing. The Employee Ownership Association, estimates that in 2017, the Top 50 EOBs had combined sales of £22.7 billion, which



increased at 3% more than like-for-like sales of non-employee owned firms [2].

The number of EOBs is also growing, most notably after the Finance Act 2014. Of the 60 oral hearing witnesses who gave the date of transfer to employee ownership, 23 (38%) said this happened in 2015 or later. Asked about the drivers for the transition, a substantial number of witnesses mentioned the Finance Act as contributing to growing awareness of the employee ownership option.

The following figure (figure 1) shows the distribution of the participants at the oral hearing by their year of transition. Of the 23 firms that transitioned to employee ownership in 2015 or later, there is a good distribution across all sizes: one firm reported having more than 1,000 employees, three between 250 and 1,000 employees, five between 100 and 250 employees, while 14 reported fewer than 100 employees. This indicates that since the Finance Act there has been a steady increase in adoption of employee ownership across firms of different sizes.



Greater awareness combined with Finance Act 2014 incentives have tipped the balance in

✓ *The Finance Act 2014 provides financial incentives to transition to employee ownership*

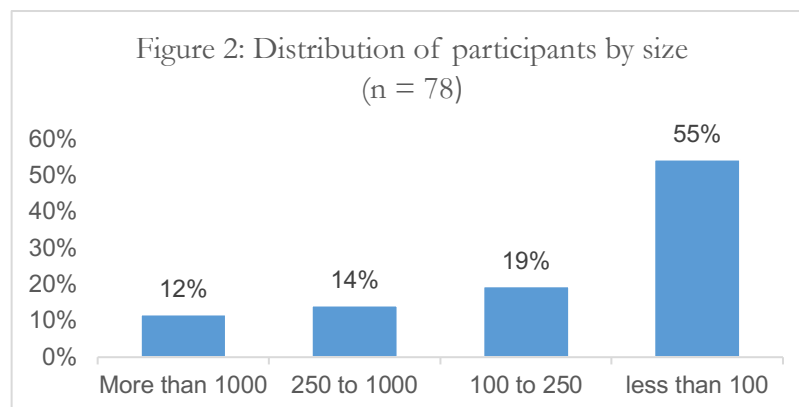
favour of a transition to employee ownership – especially for owners who want to preserve their legacy and reward their employees for their service. According to Simon Mounsey, HR Director at Agilisys Ltd., a digital technology provider with more than 1,600 associates and contractors and £145 million in revenue, “the co-founders had been looking at different succession options for a while and really none of them quite suited what they were looking for and then the Nuttall Review came out and the associated legislative changes [the Finance Act 2014] came through ... and it was the package of all of those things that became really attractive to them [the founders]... I would say they were interested in rewarding and creating some value for the employees who had helped build the business to that point”. As these reflections confirm, the main reason for considering transition to employee ownership is rarely if ever financial. However, the incentives from the Finance Act have made the transition clearer and easier to handle.

## 2.2 Spread across different sizes, sectors, and regions

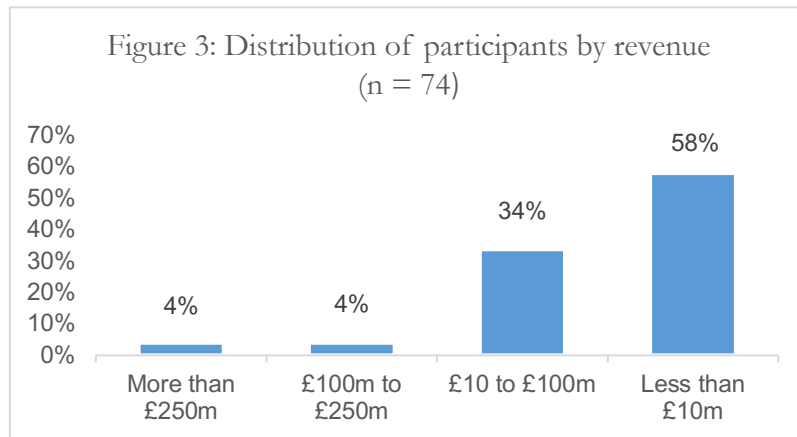
In the past few decades, employee ownership has been adopted by a wide variety of firms across different sizes, sectors, and regions. We now know that the employee

✓ *The EO model can be found across all sectors. It is relatively more common amongst professional services*  
✓ *EO appears to be relevant for all company sizes, though most EO businesses tend to be small and medium sized*

ownership model is relevant for both large and small businesses. For example, the largest employee owned business John Lewis Partnership has more than 90,000 employees; in contrast, the 50th largest business Rider Levitt Bucknall has just over 350 employees [2]. Broadly speaking, however, most of the employee owned business are small and medium sized with less than 250 employees. The following figure (figure 2) shows the distribution of participant organisations at the Inquiry hearings by size. This distribution is also in line with, and representative of, the UK, where over 99% of businesses are Small or Medium Sized businesses – employing less than 249 people, of which 96% businesses are micro-businesses – employing less than 9 people. Microbusinesses accounted for 33% of employment and 22% of turnover in the UK.



Another indicator of size is revenue. The following figure (figure 3) shows the distribution of hearing participants by their self-reported revenues for the most recent year. 92% of the participants reported revenues of less than £100 million.



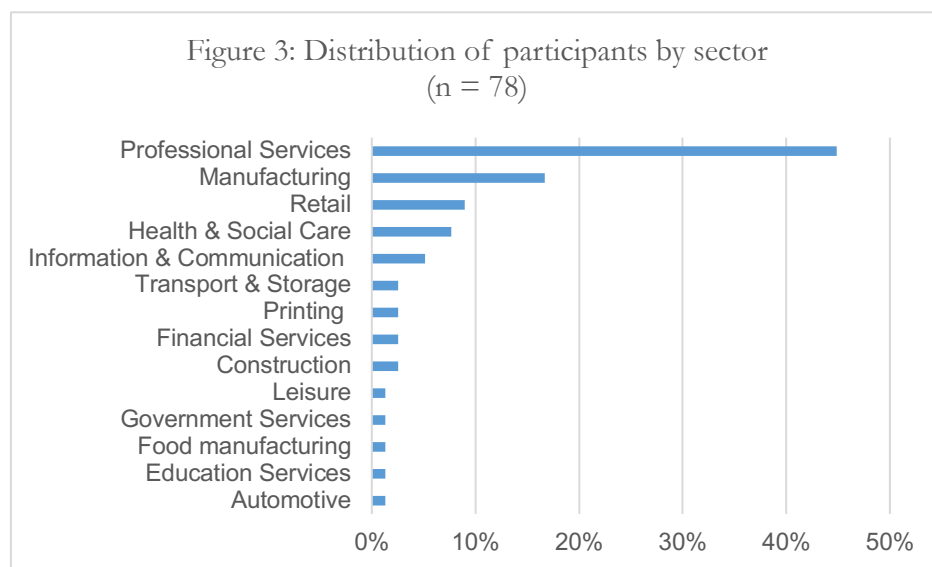
Employee ownership is being adopted across a range of sectors. In statistical terms, employee ownership is most common amongst firms in services industries, particularly professional services – this probably reflects the high proportion of professional services firms in the UK. The Department for Business, Energy and Industrial Strategy (BEIS) estimates that 71% of all businesses in the UK are in services sector, of which, aside from 33% that are in retail, 8% are in professional and scientific services, and 6% are information and communications technology (ICT) related business [ 3]. It is estimated that the services sector accounts for 74% of UK businesses,

represents 79% of employment and 71% of turnover, while the manufacturing sector account for about 5% of businesses, and represent

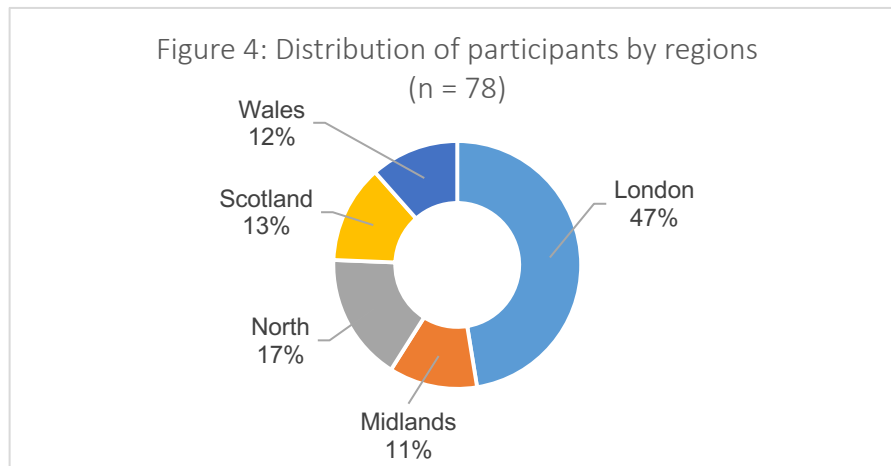
- ✓ *The Ownership Effect Inquiry collected data from England, Scotland, and Wales.*
- ✓ *There is broad representation from different sectors, sizes, regions and types of ownership models*

10% of employment and 15% of turnover. Another reason for the preponderance of employee ownership in services may be that the values that govern employee ownership are more easily implemented in a sector where knowledge and expertise are often the main selling

point. Therefore, while some sectors such as professional services or firms undertaking scientific activities are early adopters of employee ownership, the principles of employee ownership have significant appeal in the wider services sector as well as manufacturing. The following figure (figure 3) shows the distribution of the participants at Inquiry hearings by sector; professional services firms were close to 45% of the participants, while manufacturing (including various sub-groups of manufacturing) were near to 20% of the sample.



There was also a good distribution of EOBs by regions. While 47% of the participants identified as London based (and Southern England) this is also representative of the density of businesses in this region [4].



A central enabler of the growth in the number of employee owned business is the flexibility in the employee ownership model. There three different types of employee ownership.

### 2.3 Direct employee ownership

In the direct employee ownership model employees become

✓ *Direct ownership: When employees personally own equity in the business*

shareholders, personally holding a specified number of shares, and using one or more tax advantaged share plans. 8% of the Inquiry participants reported having a direct employee ownership model.

#### 2.3.1 Case of Golder Associates



Company overview: Golder Associates is a global consulting company, specialising in environmental, health & safety, and ground engineering services. The company considers itself to be client centric, aiming to be a global leader in chosen markets of manufacturing,

urban development, power, oil & gas, and mining. Its revenues for the most recent year were more than \$ 1 billion. It has over 6,500 employees worldwide of whom about 120 are based in the UK.

Model of employee ownership: Golders has a direct employee ownership model, with 100% of its equity owned by employees. Currently 55% of the company's employees own equity. The company has been operating as an employee-owned group since its formation in 1960. Employees take

✓ *With increasing share ownership, an employee has more voice in the operations of the business*

pride in being employee owned and view their differentiator as a strong culture of ownership and ethics, professional excellence, and investment in people. Golders sees their employees as central to their success.

To ensure that employee views are part of the decision-making process Golder has developed a model that allows a direct ownership model to work in a large international firm. Once an employee reaches a certain level of shareholding as a result of a peer review process, the employee can become an associate of the company. With increasing ownership stake, the employee can become a principal of the company with greater involvement and influence on strategy.

### 2.3.2 Case of Shawston



Company overview: Shawston is an industrial distribution company which delivers to UK building sites. It has a staff of 120 and annual turnover of £17m.



Model of employee ownership: Shawston has been in partial employee ownership for 15 years since a management buy-in, but in 2015 it moved to a direct employee ownership model. By the end of 2017 the company was planning for the employee stake to reach 100%. The first year of the direct ownership model was difficult as there were challenges in persuading a staff consisting largely of lorry drivers and other lower-paid occupations to buy shares. However, there has been good progress and currently 85% of employees own shares. A rise in employee engagement is also becoming apparent. The company has made an explicit effort to change the culture and mind-set, using consultants to discuss shareholder roles and how decisions are made because of the belief that it is important "...to educate and present decision-making theory and reality in our business... [To explain to employees] what's their job and what decisions will they make. You kind of negotiate it upfront...We've spent quite a long time...but I think it's clear where the decisions are going to be made and 90% of them are in the hands of the employees."

✓ *Direct ownership models are often the result of a process wherein employees steadily buy shares of the business*

## 2.4 Indirect employee ownership

In the indirect employee ownership model shares are held collectively on behalf of employees,

✓ *Indirect ownership: When all the equity of the business is held in an employee trust*

normally through an employee Trust. Just over a quarter, 28% of the Inquiry participants reported having an indirect model of employee ownership.

### 2.4.1 Case of Arup



Company overview: Arup delivers design, engineering and management consultancy professional services predominantly in the built environment. It has 94 offices in 40 countries including all nations of the UK. It has over 14,000 employees globally, and reported revenues of £1.51 billion in 2017, an increase of 21.7% over the previous year.

Model of employee ownership: Arup became employee owned in 1977. 100% of its equity is held in an Employee Benefit Trust (EBT), and the role of the directors of the EBT, known as the trustees, is to hold the board to account.

This model of indirect employee ownership enables Arup to take a different perspective on their

✓ *Indirect ownership lets employees focus on more impactful projects instead of an excessive focus on short-term returns*

business. For instance, as described in the evidence by a representative of Arup, one of things that the company takes pride in is taking every opportunity "... to describe profit in a different way. So, we make it very clear to our people who join us because they want to be in a creative industry, and to shape a better world - which is the Arup strap line... that profit is important but it's not a priority. So, we now describe profit as our enabler. If we do not have sufficient profit we cannot do all the amazing things that we want to do as an organisation". Arup's declaration that profit is not the primary motivator in their business is a widely shared sentiment in EOBs.

#### 2.4.2 Case of Aquascot



Company overview: Aquascot is a dedicated supplier to one of the UK's primary retailers, sourcing superior quality salmon and trout for use in counter, pre-pack and easy to cook formats. Aquascot is responsible for both the innovation and development of new products and processes that ensure the growth of their retail partners. It currently employs over 170 people with a revenue of £46 million.

Model of employee ownership: Aquascot has an indirect model of employee ownership with 100% of the equity held in a Trust. Established over 30 years ago, Aquascot became fully employee owned in 2016, after a seven-year managed transition period. The founding members took a decision to transfer the

✓ *Transitioning into full indirect ownership can happen over a number of years, usually as part of a transition plan*

equity into a Trust as a route for succession planning that reflected their values and was the best course of action in light of the challenges facing Aquascot. They felt employee ownership was the best option to protect jobs and keep the business in the local area. Aquascot is therefore driven by a strong sense of the need to "... establish a sustainable business in the local community for the benefit of all the partners".

The company feels that this focus on its employees and partners has been reciprocated. As commented on by a representative, "There is a sense that because we are committed to the partners, the partners in turn are committed to the business". This commitment is reflected in high retention rates, and the ability to the

firm to attract people “... there are people who buy into the employee ownership, who maybe understand it more than some of the others and employee ownership is important for them. We feel employee ownership ...will be an even bigger draw to make sure that people have options and Aquascot is their first choice”.

## 2.5 Hybrid model of employee ownership

A hybrid model that combines direct and indirect ownership is a combination of individual

✓ *Hybrid ownership: When part of the equity is held in a trust and the rest is held by individual employees directly*

and collective share ownership. 64% of the Inquiry participants reported having a hybrid model of employee ownership. From the sample, the hybrid model of employee ownership appears to be the most common model. This likely to be because of the inherent flexibility of the model.

### 2.5.1 Case of Eagle Plant



Company overview: Eagle Plant provides services to the construction, utility, and engineering sectors. It trades across England and Wales from 28 centres and employs 260 people with a revenue of £28.5 million.

Model of employee ownership: The firm is currently in a hybrid model of employee ownership with 55% of the equity held in an employee Trust and

✓ *Hybrid models enable a steady transition to employee ownership*

the rest with the founder. The firm became employee owned after the founder chose this option as part of a business succession plan. The founder points to several criteria as playing a crucial role in the transition decision – “... I wanted to maintain the culture of the business, I wanted to maintain the jobs within the business. These [issues] were all important things and I wanted to avoid a trade sale and MBO ... I didn’t like the idea of that because I felt a lot of MBOs ... start off very well and people start thinking let’s cash in the chips, let’s get rich quick and so forth”.

### 2.5.2 Case of Novograp



Company Overview: Novograp is a brand development company. Its customers include Co-op, Tesco, Iceland, Morrisons, Accor, Travelodge, Scotrail, and Wabtec. It employs 82 people and has a revenue of £7.6 million. The Company became employee owned in 2016.

Model of employee ownership: The Company has a hybrid structure with 72% of the equity held in a Trust, 20% available for employees, 8% held by the founder and managing director. In 2015 the owner directors of the company who held all the equity were looking for

✓ *Hybrid models provide flexibility to transition at a pace that works for past and future owners*

succession options. As the managing director explains “... we realised we needed to start thinking about succession, exit planning - what we’re going to do. We looked at the traditional routes – management buy-out, but in our opinion that was kind of kicking the can down the road because in four, five, ten years they [future owners] were going to want to do the same thing and plan an exit, so we didn’t go down

that road. There was a trade sale option and we had been approached by a company who unbelievably during negotiations let it be known that they would probably run us for nine months - a year - and then potentially shut the place down, take the technology, and the jobs would go”.

A consistent theme across several cases of ownership succession has been the current owner’s concern with the threat to the culture and legacy of the company. The hybrid model of employee ownership allows owners to meet their financial objectives during transition while at the same time implementing the transition at a pace that is more likely to preserve jobs and the culture of their organisation.

### 3 Impact of Employee Ownership on Performance

Business performance is influenced by a number of intrinsic and extrinsic factors. In this section we present evidence on the performance of employee owned business, measured using a number of financial and non-

financial metrics. We find that employee ownership positively influences business performance, and how employee ownership produces this effect.

The effect of employee ownership on performance can be studied using at least the following three comparisons.

- First, we can compare firms that are employee owned with firms that are not employee owned or partially employee owned.
- Second, we can compare performance of firms over time as they increase their employee ownership stake.
- Third we can compare performance of firms before and after transition to employee ownership.

In this section, we present evidence from existing research that uses these comparison factors and then the evidence from the Inquiry, which primary focuses on the third design to assess the effect of employee ownership.

Long-term research evidence shows that overall employee-owned firms tend to have either superior or similar economic performance

- ✓ *Transitioning to employee ownership is often accompanied by improvement in business performance measured by increase in sales, return on assets (ROA), profitability*
- ✓ *The positive effect of employee ownership on performance is clearer in smaller firms*



when compared to non-employee owned firms, in particular where employee ownership is combined with co-owner involvement. The observed differences in economic performance are clearer for small and medium-sized enterprises (SMEs), which account for 60% of employment and 47% of turnover in the UK private sector [5]. The impact on performance is also clearer over a longer time horizon and is stronger in firms with larger employee ownership stakes. Furthermore, the difference in performance is more significant in times of economic crisis, which is indicative of the resilience of EOBs [6]. UK studies that use sales turnover and profitability as measures of economic performance show that employee ownership is positively associated with greater stability in economic performance. This is accompanied by longer investment payback horizon when compared to non-EOBs [6, 7]. Studies have shown that firms that launch new employee ownership schemes during and economic crises are seen as less risky investments in capital markets [8].

Similar results have been reported by US studies that use sales, or sales per employee as indicators to assess economic performance. A notable study of 300 US firms reports that sales per employee are higher for firms that are employee-owned. The study finds that this effect (i.e. higher sales per employee) was greater among smaller firms, and increases as employees' ownership stake in the firm rises [9]. Another study of two groups of US firms, finds that while there is no statistically significant difference in economic performance, whenever there is any difference it is favourable to employee-owned firms, especially for smaller firms [10]. As this study is based on firms that have small employee ownership stakes, it also underlines the observation that the effect on economic performance is clearer for firms where employees hold higher ownership share.

EU studies confirm a similarly positive influence of employee ownership on the economic performance of firms. A study of the Spanish retail sector reports evidence of faster sales growth in employee owned retail stores [11]. This study is consistent with studies that show that employee owned firms perform better in terms of economic value-added, an indicator of the operational or economic activity of the firm [12].

Studies of economic performance by public companies point to employee ownership as a strong predictor of share value. This supports research findings that suggest that employee share ownership plans (ESOPs) positively influence financial returns [13, 14]. These results have been found to be robust even after adjusting for a variety of influences such as risk and business cycles [15]. Analysts have concluded that the positive influence of ESOPs on financial performance is further enhanced as employee ownership tends to strengthen monitoring and hence efficiency [16].

Similar results have also been observed for EU firms using Return on Assets (ROA) as a measure of economic performance. But in the case of ROA, the relationship between employee stock ownership and economic performance is strongly influenced not only by firm specific characteristics, but also by governance systems, country, and industry [9]. Researchers have drawn particular attention to employee participation, arguing that for employee ownership schemes to have a strong positive impact on economic performance it should be accompanied by high levels of employee participation in decision making [6, 17].

### **3.1 Impact on business performance**

Evidence from the oral hearings illustrates that the employee ownership model sustains an organisational culture that fosters

responsible and patient growth. Such an organisational culture encourages the adoption of good practices that cumulatively add up to better and long-term performance.

It is important to note that employee ownership is not uniquely able to boost performance and productivity. But Inquiry evidence does suggest that employee ownership is more likely to create a workplace where employees work harder, and are more motivated and engaged to seek improvements in their own roles, as well as the organisation. Transitioning to employee ownership is positively associated with improved business performance, assessed as a combination of revenue growth, repeat business, and long-term customer relations. These improvements are often driven by employees making better decisions because they're encouraged to think and act like shareholders. As the following case illustrates:

### 3.1.1 Case of Aber Instruments



Company Overview: Aber Instruments was founded in 1988 and supplies advanced systems for use in the brewing, biotech, bio-renewables and biofuel industries. In 2017, it reported turnover over £4million with customers including some of the world's biggest pharmaceutical and brewing companies – such as Glaxo SmithKline, Novartis, ABInBev, Heineken and SAB Miller. Based in mid-West Wales, 95% of its revenues are generated from international markets.

Employee ownership: Aber became employee owned in 2008 and currently employs 31 people who collectively own 32% of equity, which is vested in the EBT and employee share plans. The respondent from Aber Instruments told the Inquiry that the hybrid Trust model has served as the binding 'glue' between management and employees

who hold the board accountable for executive decisions. "...The general structure of our company is to have a Trust which effectively holds the board that runs the trading company to account to its guiding principles, which have been defined by the employees. So it is the kind of a close loop between the employees and the Trust so we have got that positive upward spiral going if you like"

Business Performance: In 2015, When Aber's founders left the company, it triggered a cultural shift that encouraged employees to start taking ownership more seriously. This involved greater attention to the bottom line, and more employees launched initiatives to improve returns. During a period of difficult trading all employees were asked to take a 10% cut in the pay in order to improve the bottom line, with the proviso that this should not compromise productivity: "What happened is actually everyone took the 10% cut in pay but they worked the 10% anyway, working the extra mile which quickly put us back where we should have been. I don't think we'd have got that if we hadn't have been employee owned, or not to the same extent anyway."

The cultural shift that emerged from founders' exit and employee ownership has had a direct impact on Aber's business performance. Over the

- ✓ *As high as 30% increase in revenue after transition to employee ownership*
- ✓ *Growth often attributed to employees taking more initiative*

past two years, Aber has experienced a 30% increase in its revenues... "That's what's happened to us now. We've grown 30% in the last two years, and that's really where this ownership kicked in. People who were really ambitious, and really want to drive it forward across the employee base... they don't have to just do what the founders' mission was, they can run with it now but when that happens you get a whoosh effect."

Employee ownership has also enabled Aber to compete effectively. First, it gives Aber's the ability to obtain business from large corporates which usually prefer to deal with large suppliers but gravitate towards Aber due to its ownership structure.

"Our customers are very big, billion-pound

✓ *Some customers prefer employee owned businesses as suppliers due to the protection from takeovers offered by the ownership model*

companies and their question when they buy our products is not how good your products are, but will you be here tomorrow because you are such a small company. If you then talk about the employee ownership... they then realise that actually some big corporate can't just swallow you up, their competitor can't just buy you out tomorrow, or whatever – [they] have quite good protections against that."

Second, employee ownership allows Aber to compete against larger competitors. Despite its size Aber believes its

✓ *Employees' intrinsic motivation to deliver extraordinary customer satisfaction enables employee owned businesses to outcompete larger players*

growth has come from employees taking initiatives to develop new products and establish deep customer relationships. "Aber is the market leader in its instrumentation [market segment], but it does have a significant competitor – a very large Swiss firm. We have lots of competitors that are close to what we do, but it's not the same technology. There is only the one direct competitor which is a very, very large Swiss firm which sells a whole range of instrumentation all across the world. At the moment, touch wood, we beat them hands down and it is purely because of employee engagement, trying to give the best possible customer service, customer experience to our customers, because we'll always go the extra mile, because we're invested in what we do."

### 3.1.2 Case of Union Industries



Company Overview: Union Industries is the trading title of Ralph Ellerker (1795) Ltd. The company was formed as a tarpaulin manufacturing and repair company operating out of a small factory in Hunslet, Leeds. Acquired by Paul and Isobel Schofield in 1973 'Ellerkers' was run along traditional lines until 1991 when its activities were absorbed into Union's newly enlarged and refurbished factories in Leeds. Today, Union has become a leader in the development of industrial roller doors for factories, cold stores, warehouses and distribution centres. In 2017, Union reported a net profit of £1.2 million on a turnover of £7.4 million.

Employee Ownership: Union Industries became an employee owned company at the end of November 2014 because in the absence of successors the Schofield family believed that the employees would make better owners than a large corporation.

“They had no direct line of succession so really in the traditional world a sale was the only real option of what to do with this business. They went to the degree of employing somebody to find a buyer. A buyer was found, and due diligence occurred, and the meetings got more intense. As they got more intense, words like integration and relocation started getting into the dialogue and to our former owners said there came a moment where they thought, ‘it’s going, we’re going to lose it’. The ‘we’ isn’t just them, the ‘we’ was the family that had built that business over 40 or more years. So they had invested themselves in it but they were also very conscious that the workforce - many of whom were long serving employees - built it too. They didn’t do it on their own, there was a family that had created this business and if they

weren't careful, its identity, all that made it special and unique, would evaporate, it would be assimilated into another organisation. They did not want that."

Business Performance: Since becoming employee owned three years ago, Union has experienced significant growth.

Andrew Lane, Union's managing director, reported: "Our turnover, since we've been employee owned,

✓ *Consistent improvement in revenues and profitability over number of years for transitioning to employee ownership*

went up 5.3% the first year, then 14.1% and then 23.4%. Our profits were 600% the first year.... a fairly disappointing 72% increase! How do we get there? Some businesses prepare for growth, and they put in infrastructure, and they put in people, and they put in cost, and then the growth doesn't come and they're in bother. What we find is our people are absolutely committed, because of the employee ownership culture - which is not [just] one thing. A lot of it is about communication, sharing the needs of the business with people. They've risen to the challenge – they've worked longer, they've worked harder, they've put the whole thing together. So we've got growth without any of the expense of growing."

In the oral hearing, Union emphasised that greater employee commitment was the result of being transparent, and ensuring each employee knew that their contribution mattered in the overall picture. "We meet quarterly, and we do a big financial presentation, we highlight 'This is what we wanted to do', and then 'This happened' and then 'We did that' and to recover from that we need to do this. People get an understanding, and the key bit, the bit that we really try and focus on is to link each job to the big picture, so this is my piece of the jigsaw; this is where I fit in, and how I influence the people around me



and provide the platform to grow. Last month everybody in the company got £3600 tax free as a bonus. Now for people earning £12 an hour, that's a huge sum of money to get in one chunk. That brings it home to them, they've put the sweat in, they've seen the results and they're sharing in our result."

Empowering employees through ownership and putting in mechanisms in place to ensure that their voice is heard has allowed Union to engage employees at all levels. Lane went on: "Lots of people spend their lives being conditioned to a role, to a level – you are a shop floor person, you don't get to understand what happens in there, that's intelligent management stuff that you wouldn't understand if we told you. What I find astonishing is the quality of the suggestions. Once people understand the whole picture, the quality of the questions and suggestions that come from really left field people. You think my God, he's right, we missed that. Sometimes we do miss stuff that's staring us in the face, and the guys on the shop floor and girls can spot it and just point it forward."

### 3.2 Higher Productivity and Efficiency

A transition to employee ownership is associated with rapid improvement in productivity, often driven by employees taking initiative, and implementing changes in work practices that reduce waste and improve efficiency.

✓ *Improvement in productivity after transitioning to employee ownership is often driven by efficiencies by individuals across levels*

Studies that combine micro-level factors such as individual motivation and team dynamics, with macro-level factors, in particular governance, tend to show statistically significant higher levels of

productivity in EOBs [18]. A problem facing studies of the relationship between employee ownership and productivity is factoring in the regional context - since productivity is strongly influenced by regional infrastructure, or cost of inputs sourced locally. A review of current evidence on productivity indicates the need for more UK based research on this issue. There is a strong case for using a wider range of productivity measures, in addition to the purely economic ones like labour productivity, or self-reported measures of productivity that are prone to measurement bias.

Researchers point out that the proportion of ownership held by employees could be a key explanatory variable in understanding productivity. For instance, some US studies suggest that the level of employees' ownership stake – defined as proportion of the firm's stock owned by employees – is strongly and positively related to productivity. However, comparative studies that contrast employee owned and non-employee owned business are less conclusive – indicating either a positive employee ownership effect or no significant difference in productivity between the groups [14, 19, 20].

Researchers point out that employee involvement appears to heighten the positive impact of employee ownership on productivity. In general, it is difficult to verify the influence of ownership on product and process innovation using statistical methods. However qualitative evidence indicates that employees in employee owned organisations feel more empowered to adopt changes to their tasks, roles, and routines, which could positively influence innovation. A study of the John Lewis Partnership shows a correlation between employee ownership, open information flows, high wages – all factors that are positively associated with high productivity and innovation [21].

### 3.2.1 Stephens Scown LLP



Company Overview: Based in St Austell and Truro, Stephens Scown is a full-service law firm. It specialises in industries that are the mainstay of the economy in the South West region – food and drink, tourism, mining, and green energy. It also offers services aimed at individuals such as home moves, separation, and employment disputes. In 2017, Stephens Scown reported profits of £6.2million on a turnover of £19.2million.

Employee Ownership: In 2016, the firm decided to go down the employee ownership route. All employees become ‘members’ of the company after a probationary period. Each co-owner member has a right to an equal share of the profit. The firm has adapted a Trust model and put in place an EBT. In 2017, Stephens Scown was voted by The Sunday Times as one the UK’s top companies to work for.

The decision to become employee owned was incremental. In 2012, as the revenues and profits stagnated, the partners recognised the need for transformation. As part of change plan, the firm first worked on cultivating employee engagement and as employees started taking more initiative, to develop new and existing client business. The firm thereafter took the bold step of becoming the first employee owned legal services firm in the UK. Christian Wilson, partner at Stephens Scown, told the Inquiry: “...the firm at that time wasn’t really going in a particularly significant direction. There was a feeling that it was underperforming; that there were things that just weren’t quite right. There was a look at the culture of the business, both in terms of the partners and all employees, and a recognition that actually things needed to change. And so, the first shift was in respect of culture, just changing the way that people behaved around each other. Having made those changes the idea of bringing in employees

for part ownership was a sort of logical progression. It was a bit of a radical one, because it just doesn't really happen with law firms. We've learnt there are an awful lot of obstacles in the way. However, there was a feeling among a number of individuals, and within the partnership that this would be a good thing, that it would put some power into the hands of the employees."

Improvement in productivity: Since it started the journey to employee ownership, the firm has grown its revenues by nearly 90%. In 2012, Stephens Scown reported a turnover of £11.3million, and as it became fully employee owned in 2016 – the firm reported a turnover of £17.8million, which increased to £19.2million in 2017. The operating profits have experienced a similar upward trajectory growing from £3.3million in 2012, to £6.2million in 2017. The company told the

Inquiry: "The performance of our firm has outstripped virtually every other firm of an equivalent size to us, our growth level over the last couple of years - as

- ✓ *Revenues have gone up by 90% since the beginning of the transition*
- ✓ *Profits have nearly doubled*
- ✓ *Employee feel empowered to make efficiencies in their roles*

we've transitioned towards employee ownership with attention to efficiencies, to wasted costs, electricity, paper use and things like that – [is] having an impact on the bottom line"

### **3.3 Long-term orientation**

EOBs appear to take more of a long-term approach to investment and growth than conventional ones. One factor may be employees' greater willingness to work harder and forgo short-term rewards in the interest of the organisation's long-term growth and survivability.

Long-term orientation is often a reflection of business resilience. During a crisis, companies with low resilience are more likely to subordinate decisions to immediate survival needs than more resilient counterparts. Research evidence from the UK suggests that employee owned firms are generally more resilient than non-employee firms [6]. Their resilience is not only financial, but also organisational. During a crisis employee owned are less likely to lay off workers, and more likely to maintain a long-term orientation when making decisions. Recent research also suggests that employee owned firms who offer employees the opportunity to increase their stake during financial crisis are viewed as organisationally more resilient by capital markets [8].

EOBs view the absence of external shareholders as an enabler for their long-term orientation in decision-making. Elements of the employee ownership culture, most notably trust and transparency, are also vital in generating wide support for decisions that reduce short-term financial rewards and increase investment in long-term growth.

### 3.3.1 Case of Symology



Company Overview: Formed in 1983 in Caddington, Luton, Symology develops and supplies a range of integrated software solutions for the management of infrastructure assets, including highways, land and property, bridges and structures, public lighting, and distribution networks.

The firm's customer base is primarily UK local authorities, utilities and private contractors. In 2017, Symology employed 107 people and reported turnover of £6.6 million.

Employee Ownership: ; In 2002 following several years of sustained growth, Symology embarked on the first steps of employee ownership by setting up an Enterprise Management Incentive (EMI) scheme. This allowed employees to own shares in the company, and actively participate in the operation of the company.

The EMI helped recruitment, retention and development of highly skilled employees. In 2014, the owners and directors of Symology sought to secure the long-term independence and integrity of the company and created an employee-owned majority shareholding.

The Trust is governed by a mixture of directly elected management and employee representatives, a number of whom sit on the Board. This approach ensures that there is employee representation on the Board, and a clear channel of communication between the Board and the employees. It also facilitates continuity of the company-wide teamwork approach that Symology's customers see as central to the provision of successful services.

Mike Barlett, Symology's managing director, told the Inquiry: "We devolve a lot of responsibility down to individuals; we have a mantra in our company of 'local decisions for local people'. It's not departmental heads or senior managers making most of the decisions; it's the person doing the task that makes most of the decisions. Obviously, there's governance in place and [employees] can raise things up the chain. But if every single decision has to keep going up three or four tiers - you are wasting time. By giving [employees] responsibility I think that makes it interesting for them because they tend to have an ownership of that task". He added: "I think as a small and medium sized company we can react very quickly because there isn't an external shareholder to go to; it's the board or people who work for the company. So board meetings tend to be spears in the ground

on a regular basis to review things. You don't have to wait for the next quarterly board meeting in that position, you can go to management meetings and they just happen."

Long Term Orientation: Being employee owned has shielded Symology from pressures to deliver short-term profitability. Instead, the firm has allocated resources towards research and development - developing cutting edge asset management systems. The long-term orientation in turn has ensured deep client relationships, without the

✓ *Protection from short-term profit motives helps build long-term orientation*

need to divert substantial resources into marketing and sales.

"I think our mantra and our board requirement is for us to deliver great software and services to our customers. Forever really, there's no timeframe, no five-year plan, no ten- year plan, we just want to do it forever because we think we can do it better than our competitors, not because of the way we write software, but because of the way we do business with them. So, it really is about achieving that, it's about delivering sustainable growth because if the growth is not sustainable we're not going to be able to do it forever."

Employee ownership has enabled Symology to attract and retain employees. "I think it [employee ownership] is a factor. We are thirty miles outside of London, so recruiting can be an issue. There is the bright lights of London with much higher salaries; we can't compete with those, but we can sell all the soft factors like employee bonuses which are nice, and actually can be in cash. It can be the sense of responsibility and joining in. You are trying to give people the impression that they're...not just coming for a job, but they are coming to be part of something that's going to go somewhere.."

### 3.3.2 Case of Turley Associates



Company Overview: Founded in 1983, Turley Associates has a network of 12 planning offices across the UK. In 2017, Turley employed 220 people and reported operating profits of £2.5 million on a turnover of £22.1 million.

Employee Ownership: Turley became employee owned in 2001 and is currently 100% employee owned. The decision to convert was taken to protect the long-term future of the firm as an independent entity, and against accountants' advice at that time.

"There were an awful lot of conversations that took place around that time to get people on board, and to really think about the future...financial reward wasn't one of their main motivators for becoming employee owned; it just wasn't in that equation. At the time, their accounting firm advised them... [that] there are other ways to make a lot more money. They chose not to do that which was fascinating, but at the same time very rewarding for the individuals that did stay around to see how that's helped lots of other people within the company."

Employee ownership has allowed Turley to undergo a behavioural shift. "Our approach is attribute-based so we make the attributes of the company visible on the website. So right from hiring new co-owners, they can see what we're about, and also I suppose de-select if they think 'that's not me'. We then follow that process from there in terms of induction. If you see somebody not displaying those attributes, then you call them out about it - because that is actually going to affect the team and its productivity. So it has been a process of cultural change over time. But I think that's a result of us being employee owned that we've been able to change, and that to me, in terms of culture change, is quite quick."



Long-Term Orientation:

Co-owners take keen interest in the long-term

✓ *Stewardship and long-term thinking are part of the employee ownership mind-set*

health of Turley. “Stewardship is something that’s really important for us, for everybody in the business. It’s not just for the four directors, it’s actually for all co-owners to take responsibility and care for the resources of the company. A good example of that was two years ago [when] we launched our new company business strategy, ‘Freedom to Flourish’. We consulted with all co-owners on the future of the company; we asked for their thoughts and suggestions about what’s important to them for the future. There were about 185 responses out of 220 which I don’t think is too bad., We were able to take in some of those thoughts and suggestions and include them in the company business strategy.”

The firm has also paid attention to mechanisms which speed up decisions. For instance, to ensure that leadership delegates to co-owners, the firm has a group called ‘realisers’ who are there to ask the right questions, make sure that actions are taking the organisation in the right directions, and support different people within the business who are trying to get things done.

Turley told the Inquiry that transparency was important: “So when it comes to financial information, it is very transparent, open for all, because we don’t want there to be any surprises at the end of the year, and also for people to know that they can impact the financials if they know what they are so they can make a difference in terms of the profit which is then shared....

The strategic leadership team and the operational leadership team have an open-door policy when they meet. We have a gathering once a month and anyone can join or participate in the meeting. We have a ‘Please Disturb’ sign up on the door, and people [still] pop in

which is great. A summary from those discussions is placed on the intranet, with a chat forum so that people can ask questions if they weren't able to attend... and somebody from that team has to respond."

As a result, Turley co-owners feel they can

✓ *17% reduction in costs*

influence or change those financials by doing things differently: "One of the points we noticed was the central costs were quite high so we talked to our co-owners about that and that has driven a 17% reduction in our costs - a big saving."

"I would say it is also about reinvestment in the company as well. So part of it is about reward, but also part of the profit is used to reinvest and actually make the company a better place – [and] remain competitive. People really value that as well, and again that is all very transparent."

### 3.4 Broader performance objectives

As with other models of business, employee owned companies are motivated by profit.

✓ *Employee owned businesses have different performance yardsticks – beyond profit maximisation*

However, it is the case that profit alone, or profit maximisation, are not normally the only objectives of EOBs. A core difference is that these businesses consider profit as an enabler, and not the purpose of the company. In essence, this is a different way of thinking about performance of the business.

This mind-set has implications when it comes to measuring performance. A significant number of businesses reported that they do not have very detailed measures of performance, apart from aggregated measures such as profits and productivity - which is most

often measured for the entire business, not per employee. The lack of obsessive focus on financial outcomes, common amongst comparable businesses – as pointed out by executives who have moved from non-EOBs – suggests that management attention is more evenly spread across performance factors that many other companies ignore.

Most Inquiry participants highlight an employee ownership culture as central to their success. Even if they feel that the economic logic of productivity and growth is sound, they are on the lookout for potential conflicts with the ethos of being employee owned. Thus, the respondents consistently said that they would forego financial results if it means compromising the culture.

#### **3.4.1 Case of Scott Bader**



Company Overview: Formed in 1921 by Ernst Bader, Scott Bader is a global chemical company with manufacturing subsidiaries in France, South Africa, Dubai and Croatia, and sales offices worldwide. Employing over 600 people, in 2016 reported an operating profit of £9m on a turnover of £180m. The company generates 62% of its sales from Europe with the UK its largest single national market, representing 24% of global sales.

Employee Ownership: Until 1951, Scott Bader was family-owned. Influenced by events surrounding the Second World War, the founder set about transferring the ownership of Scott Bader to the workforce with a view to transforming the company into a collectively organised Commonwealth (wealth-in-common). As a result, the shares of the company were transferred to Scott Bader Commonwealth Limited, a company limited by guarantee and a registered charity, thereby creating a common trusteeship company.

Employees become ‘Members of The Commonwealth’, and as such become ‘trustees-in-common’ of the company assets. The company aspires for each generation to ensure the ongoing success of the organisation so that future generations can benefit from its continued existence.

Culture and Performance: Scott Bader’s culture is shaped by its ownership structure. Having no external shareholders allows the company to prioritise values and guiding principles set out by its founder. The Inquiry heard that there is strong commitment to developing a governance structure that involves employees across the group in its strategic direction. To avoid being inward looking, the board includes external experts, there to provide insights, and exercise oversight over the company’s performance.

The business has three governance bodies. One is the ‘Commonwealth Board’ and it is organised with guardian trustees who are external people, as well as members’ representative of the company, who are employees of the company. The role of this Commonwealth Board is to make sure Scott Bader stays true to the original ideas of its founder and is not betraying the original ethos, if you wish. Additionally, there is a Group Board which is conventional in structure with external directors as well as members from the staff and three members of the executive leadership team. The third group is called the ‘Members Assembly’ and comprises of twelve employees representing the different parts of the world Scott Bader is involved with. Employees are able to exercise significant influence: “They are the ones who are actually the ultimate decision makers on key decisions, such as the employment of the CEO, and even the

✓ *Employee engagement, achieved by involving employees in strategic decisions, is at the heart of employee ownership.*

appointment of the chairman. If we make an acquisition, if we make a joint venture, if we are to close a plant, let's say, they would have the final say to say yes or no. We agree or disagree, and if it is agreed then we have to go on the business side, go back to the drawing board and find another solution and that's how it works"

Senior leadership in Scott Bader is convinced that being employee owned cultivates creative tension and releases high performance at leadership level. The managing director told the Inquiry: "There are probably more demands on the leadership to perform as leaders rather than managers when you are an employee owned organisation. Coming from the mainstream big businesses around the globe, I can definitely see the difference, and that can be painful. But I think it is a healthy pain at the end of the day, so that's the key point for me."

"It's in the process, and that starts for me [with] the leadership. They need to embrace this idea that as a boss you are better off when the ideas are not coming from you, and therefore you have to use your experience to ask good questions, and get the collective intelligence together, rather than thinking, 'Okay I've been there so I know'. You may know, but there are maybe better ideas out there that you need to be able to collect."

### **3.4.2 Case of Childbase Partnership**



Company Overview: Founded in 1989 as a family business Childbase Partnership is now a 100 percent employee owned company. It currently employs over 1600 people and has 41 day-nurseries. In 2017, it reported operating profits of £3.6 million on a turnover of £46.7

million. In 2017, it was rated as the eighth in the UK by the Sunday Times 100 'Best Companies to Work For'.

Overview of Employee Ownership: The founding Thompson family was convinced that to safeguard the future of Childbase as a sustainable independent firm, where employees are happy, engaged and motivated, Childbase needed to follow the employee ownership path. This journey started in 2000 with a 'Save and Buy' share scheme, and a 'Buy one get one free' share incentive. Working under the banner 'We all contribute, we all benefit,' Childbase became 100 percent owned by employees in 2017. One in four of its nurseries are rated "outstanding" by Ofsted, compared with an industry average of one in 50.

Culture, Leadership and Performance: As of January 2018, Childbase was the only employee owned early years child care provider in the UK. Since the sector is also marked by high employee turnover, creating a culture where employees contribute and engage is a challenging task. The company's governance structured has helped create a partnership culture, where employees act as stewards of the company.

Childbase has a 42-member partnership council of elected representatives from each of the nurseries. Their approval is sought on all major strategic decisions, such as the purchase of new nurseries. As the partnership council routines became embedded, Childbase leadership has created several conduits for engaging employees. It regularly holds lunches with the senior team for small groups of employees. The company has also invested in a mobile app, where staff from nurseries not only get information related to important issues but can also provide input into the decision-making process. Employees are given paid leave to support local charities and

community projects and recognised and rewarded for their efforts as volunteers.

The managing director commented, “There will be some decisions we take as an executive team..... and our job then is to persuade the partnership council that that is the right decision. The partnership council is really important to us in passing the message. So if you ask, what does our governance model mean to me? It means having absolute clarity over what the goals and the vision of the organisation are, and how they are communicated. They can go through the partnership representative in the nursery, they can go through the council, directly to us or they can feed back through the app ideas and we will make sure that we say ‘You said, we did’ becomes part of the vision.”

Recent surveys conducted by Childbase show 96% of staff believed, first of all, that

✓ *Rewards for performance are often equitable in employee owned businesses*

ownership has made a difference to their productivity. Leaders at Childbase believe that profit distribution in the form of dividends needs to be equitable and not based on position. The managing director explained why: “This is quite an interesting one because although we have been on this journey for 17 years, this is the critical point where we are actually going to pay a dividend to everybody. I drove that [decision] it would be equally shared and immediately someone said, ‘Well what about the senior people?’ I said ‘no, no, we’re not talking about salaries, we’re talking about the combined effort of everybody. That was my light bulb moment. I’m suddenly not in the commercial sector anymore, not in the public sector, I’m actually in an employee owned business and it really resonated with me.”

## 4 Impact on standards of corporate governance

In principle, employee ownership appears to offer Government some important ways to address their concern about the state of

✓ *Standards of corporate governance improve as a result of new governance practices as well as employees' genuine interest in understanding the operations of their own business*

corporate governance. As many observers have pointed out, a longstanding problem with corporate governance is the gulf between shareholders and management. Increasingly, shareholders – especially smaller shareholders - have little or no influence on how the business operates, ability to question management decisions and expect appropriate answers, or have any significant say board decisions. In contrast, employee ownership – by design - puts the co-owner shareholder right in the centre of governance.

Evidence collected by the Inquiry suggests employee ownership establishes high standards of corporate governance. Although the mechanisms vary, employee owned companies share a propensity to produce high levels of transparency and encourage co-owners to question management and expect answers. In this section we review the evidence on the impact of employee ownership on various aspects of corporate governance.

### 4.1 Better corporate governance

Employee ownership tends to install high standards of corporate governance by encouraging transparency, knowledge sharing, scrutiny and challenge, and multiple ways for co-owners to make their voice as shareholders heard. While corporate governance good



practice of this kind is not exclusive to employee owned business, evidence suggest that employee ownership makes it much more likely and much more likely to last.

A common observation from the oral hearings was that the improvement in the standards of governance in EOBs was not just a result of structural set-ups such as councils or committees. It also reflects an ethos that starts to shape governance when employees own the business.

For instance, many conventional businesses establish some kind of council to review major decisions taken by management on specific topics. But it's rare for such councils to have all the information they need to question boards and management fully, to probe, challenge or expect rapid, frank answers.

In contrast, the Inquiry found that consultative or representative councils in employee owned companies tended to benefit from a high degree of information disclosure and were generally encouraged and empowered to scrutinise management decision making effectively. EOBs often go through a steep learning curve when designing a governance structure that suits their context. This usually involves updating governance processes in line with their preferred approach to sharing information, improving reporting requirements, increasing response speed, and expanding autonomy in decision making. In a number of instances respondents discussed how practices were discontinued or replaced with other practices that were deemed more meaningful. This highlights the fact that there is no single 'template' of governance that works for every employee owned business.

#### 4.1.1 Case of Useful Simple Trust

Company overview: Useful Simple is set up as an Employee Benefit Trust (EBT) and is a group of companies with expertise in engineering, design, architecture and communication. Their objective is to “improve the human environment by delivering useful, simple outcomes that are beautiful and good”. Their group includes engineers, architects, designers, consultants, and communications specialists. The Trust has 56 employees and its annual turnover in the most recent year was £7m.

Employee ownership: The Trust founding directors transferred to employee ownership ten years ago and like a number of EOBs the transition was heavily influenced by the founders’ principles. A company representative told the Inquiry: “... they [founding directors] were saying “what’s the future for business ownership?” It just seemed wrong that everyone was putting in all these efforts and doing all these fantastic projects collaboratively, but the rewards aren’t there for everyone.”

Looking to the future, the founding directors felt that employee ownership could prevent the fragmentation that often bedevils professional firms as they diversify and in becoming employee owned, demonstrated that they were willing to several years to recover their equity. “We had a simple metric where 50% of our profits was retained in the business, 25% was distributed to staff and 25% was distributed to the original founders” as part of the 15-year deal. “Basically, they took a bet on the future of the business because they believed in what they’d built, and they weren’t about to [let it] disappear”.

Corporate governance: The Useful Simple Trust's corporate governance structures are based on openness and transparency. As reported by the representative: "As we've grown, and put more structure in place, having more formal boards, more formal lines of reporting and that sort of thing... the employee ownership has actually secured the culture.... it is recognised that there are benefits in everyone knowing what's going on and being involved in the decision-making process throughout. So, as we've grown and got more professional as a business, [we] had to put a structure in, it has actually kept us in line, kept our culture strong."

The willingness to question decisions is not directed upwards only at managers but applies horizontally among employees as well. "... we trust our employees, we trust our fellow owners. People are allowed to make decisions, whether that's to spend money or to spend time on things. And what happens is, somebody will see them doing something, going 'Are you quite sure about that?'... Everyone is looking out for everyone else and looking out for the business."

The physical layout of the work space in Useful Simple Trust is unusual and plays an important role in encouraging participation. "...everyone sits in the same open office, every single person is approachable, whether that's one of our junior engineers who happens to be one of our trustees, or one of our senior directors who sits on a couple of the boards. The impact of this openness and inclusion in decision-making processes is a clear sense of ownership and involvement. "We are an open book company and every couple of months everyone knows all the numbers, exactly what's going on. Anyone can ask to see anything at any time... people have this sense of [their] own company, 'it's my piece of work, it's my project I'm working on and it's my company, so the decisions I make on a daily basis affects things and they can see that link all the way through.'"

#### 4.1.2 Case of 3BM



Company overview: 3BM is a local government spinout founded in 2013. Since then, it has grown from a staff of 40 with just under £3m turnover, to employing over 100 people and a turnover of £14m. 3BM was created with a social purpose – providing specialist services to schools and strategic consultancy to public and private sector clients.

Employee ownership: 3BM has a hybrid ownership model, with an EBT owning a majority (75.1%) of the equity and a private sector partner, selected in open competition, owning the balance. The managing director describe how forming 3BM was a significant challenge: “...when we first spun out, taking three different councils and four sets of terms and conditions together, they gave us a blank piece of paper to work from and we had great fun creating our own values, learning what employee ownership means.”

Corporate governance overview: At the top of the corporate governance structure, a Trust board sets the strategic direction and holds the shares on behalf of the staff group. The Trust has three members of the senior leadership team, two members of the employee committee and two non-executive members (the Chair and an advisor). Below this, a management board runs day-to-day operations and finances. It has three non-executive members, three members of the leadership team, two employee representatives and a representative from the Trust's partner organisation. Employees originally had only one seat on each of these boards, but this has been increased to give employees more voice. “So they have two people now on each board and they are able to say exactly what they want.

They have their own agenda item to discuss any issues that they feel the board needs to be aware of.”

Finally, there is an employee committee that meets every six weeks: “...they double-check and provide feedback to the limited board and the Trust board on what partners are feeling... What we don’t want is me standing there saying ‘this is really good’ and my employee groups are sitting there not able to contradict that”. The end result of this layered structure is that “...in effect, our leadership team is accountable to three sets of corporate governance structures.”

Better corporate governance: An early experience with a strategic decision that went wrong provided a lesson in the importance of heeding the voice of the employee owners. “I should have listened to the employee committee [more] at the time because it was a big mistake we made as a leadership team; an example of not using corporate governance in the right way... So, we have had to reflect back as a business on that. Now what we try to do is make sure there is general consensus about what we’re doing. .... I mean a genuine consensus where people have debated the options.”

Management has grown to trust employees and actively seeks their opinion. “...if we’re not sure at a Trust board whether that’s the right thing to do, we will consult

- ✓ *The right level of corporate governance is achieved over time and through an openness to learn*
- ✓ *Employee owned business consistently show the capability to learn and update their governance processes*

with all partners. It’s their business, they have a voice and we have to listen to that. That’s a scary concept in a non-employee owned world, but in a world where you trust each other and ask questions, you get some very sensible answers back. The best answers we get within our

business are from the collective, because 104 people are far cleverer than five or six or seven.

## 4.2 Importance of transparent reporting

Inquiry witnesses told panel members that governance standards in employee owned firms are heavily dependent on transparency and that the nature of employee ownership makes it harder for companies to default on transparency. Transparency in reporting is most usually achieved through regular disclosure of extensive information about the performance of the business. Evidence also suggests that whilst employee owned companies determine what level and detail of information to share, this often mirrors the obligations seen in PLCs to disclose extensive information to their [external] shareholders. However, an equally important motive for EOBs' is the obvious conviction that such disclosure adds to co-owner motivation and engagement. In other words, the business benefits directly from being transparent.

Transparency in reporting practices is a hallmark of most employee owned business. We discuss how these practices have evolved in the following two cases.

### 4.2.1 Case of David Narro Associates

david narro associates



Company overview: David Narro Associates is a structural and civil engineering consultancy. It operates in the UK and currently has 50 employees with an annual turnover in the region of £2.8m.

Employee ownership: For many years, David Narro Associates was privately owned company, but in 2014 the business moved to a Trust

model of employee ownership and currently, 20% of the firm's equity is held by employees in this way.

The move to employee ownership was described by a representative as entirely due to the owner's values as "...someone who wants to continue what [was] built up over many years and doesn't just want to see it taken over by someone faceless who will decimate it." The transition was facilitated by legal advice, aided by lessons from the successful experiences of other firms in the sector: "We held back from pushing the button on employee ownership because we knew there were further advantages tax-wise in the offing, in one of the next budgets." (This comment refers to the Finance Act 2014 legislation which offers a financial incentive for the transition to an Employee Ownership Trust (EOT)).

Corporate governance overview: With staff numbers and turnover doubling over the past two and a half years a sharper focus on corporate governance was needed.

What sets employee ownership apart from other ownership models is the duality of inclusion in, and contribution to, corporate governance. Employees as shareholders are included in a process that sets the company's strategy, objectives, and the growth plan, but they also have an opportunity to contribute to it. Such involvement often leads to a feeling of a genuine sense of ownership in the business that is usually not seen in non-EOBs.

The values of David Narro Associates play a major role in shaping how the organisation communicates.

✓ *Transparent reporting gives employees the information to ask questions*

Employees as a matter of course are kept up-to-date with company finances; continuing a culture of openness that pre-dates,

and is enhanced by, the move to employee ownership. However, the transition to reporting under employee ownership was not entirely smooth. The business faced an early challenge in transparency and accessible reporting when insufficient understanding of how EOBs were set up delayed production of the financial accounts. The company has now addressed this problem: “Employees get a set of accounts prior to the AGM so that they can ask questions and interrogate them... I’m very keen on being as open as possible, we have been for years and [the founder] had been even before he started thinking about employee ownership.”

For David Narrow the impact of adopting an employee ownership model has been very positive. “I just think the benefits are there for everyone to see. We have all been able to buy into the firm, there are benefits, there are bonuses available, and the company is forward looking and trying to promote self-governance.”

The following case of a much larger firm reinforces the connection between good governance and openness.

#### **4.2.2 Case of Agilisys Holding**



Company overview: Agilisys is one of the UK’s larger EOBs. A digital technology provider to the public and private sectors, the business was co-founded by two entrepreneurs in the late 1990s. It now employs over 1,500 staff and has an annual turnover of £145m.

Employee ownership: The company moved to EOT status in 2015, partly for succession reasons, and partly as a growth strategy. Encouraged by the publication of the Nuttall Review in 2012, a representative at the Inquiry reported that the founders “...were interested in rewarding and creating some value for the employees



who had helped build the business to that point. They themselves...had created a number of different organisations and wanted to release some equity from the business in order to reinvest in those other organisations. They were able to see value out of the [EOT] and reinvest in different businesses.”

The move to EOT allowed the founders to keep 43% of the equity, with the remainder going to the employees. As one participant in the Inquiry put it: “...our co-founders didn’t want to fully exit the business. They are still interested in helping to shape and direct the organisation....”

Corporate governance overview: Governance structures were considered reasonably good prior to employee ownership. However, changes were nevertheless made to reflect the new ownership structure. “What we created and what I see as a positive investment is a more organised structure around our employee engagement, and the way we had to report information to our employees. The creation of what we call the engagement board [who meet] twice a year, where the trustees and the senior team are slightly more accountable to the employees... has actually been a positive way of creating some sort of champions in the organisation.”

In addition, two internal trustees (a co-founder and the chief executive) are balanced by three external trustees, whose “...role is very much to make sure we stick to the principles of the EOT - for the benefit of current and future employees.”

More transparent and accessible reporting: Reporting mechanisms in place prior to the EOT move have been augmented in order to address the continued, active, involvement of the co-founders in the business. “...they originally would make all the decisions, but there’s now a change to that; there are external trustees who will hold them to account over the principles”. In essence the move to an employee

ownership model has entailed the opening up of reporting, and more consultative decision making.

A core element of being more transparent and accessible is communication. Since becoming employee owned there has been a tangible change in how this issue is addressed. "...without the move to ownership... we wouldn't have had some of the engagement and communication mechanisms we've got now. Not that we couldn't have done [before] but we just traditionally didn't, and in some ways the move to employee ownership - because it is almost mandated as part of the EOT - [has] helped us make that evolutionary change and to communicate more effectively."

The respondent from Agilisys reports that these changes have improved employees' sense of ownership and their understanding of the business, and also provide a mechanism for voice where employees can contribute to the firm's running. "What we've seen - definitely different around the governance and the employee voice - is the dynamic, and a better understanding, of the organisation coming from the employees, and some challenges, and ideas and suggestions, coming through that become enacted by the senior team."

### 4.3 Better engagement with employees

Beyond the requirements of reporting, EOBs are more likely to engage

✓ *Employees tend to be more engaged with the business when they have better information*

employees in the governance of the firm because they are co-owners, and in return employees demonstrate greater willingness to contribute to improving the organisation. High levels of knowledge sharing have the same effect.

In this section we turn our attention to two cases that have shown significant improvement in employees' engagement with their jobs, and the organisation after the move to employee ownership.

#### **4.3.1 Case of City HealthCare Partnership**

##### **City Health Care Partnership CIC**

a co-owned business

Company overview: Hull-based City Health Care Partnership CIC was formed in 2010 as a spin-off from the NHS. It employs almost 2,000 staff and provides a wide range of health and care services across 70 sites. Growing at approximately 6% each year the company declared year on year profits but as a community interest company (CIC), surplus profits are reinvested in the business and the community.

Employee ownership: The equity of the firm is today 100% owned by the employees, but takeover of ownership by employees developed gradually. When the company first formed, staff could opt to become co-owners by purchasing a £1 share. More recently, the company formulated an opt-out system whereby employees on permanent contracts automatically become shareholders. The policy has been positively received and about 75% of employees are co-owners.

Corporate governance overview: The services that City Health Care provides require complex governance structures to oversee NHS regulated, and health-sensitive areas, such as clinical governance, patient safety and quality of care. However, an executive board, including elected employee representatives, oversees both clinical and corporate governance. One representative sits on the audit board, and another on the executive board with full voting rights. Further employee voice and representation is expressed via a co-owner committee, which also serves as a vehicle for transparency and

accountability. The whole approach to governance differs dramatically from how things worked in the NHS.

As reported by an Inquiry participant, “In terms of transparency, at the co-owner forum the finance director goes along and gives all the financial figures; they [the employee representatives] can ask the chief executive any questions. The co-owner forum must also take on board feedback from the employee survey. The survey results go to the forum, as do the “action plans that are developed by the staff...the directors will be held to account if they are not implemented.”

The move to employee ownership has changed attitudes to individual accountability. Employees are encouraged to be open about the problems that arise under their watch. Learning from errors is considered more effective than threats of disciplinary actions. “I think one of [the] changes [in our] culture is that of being open, so staff aren’t afraid...to raise an issue if they’ve done anything wrong. So, I would say that incident reporting has gone up, which is good for us; we want it to go up because we want to know where things are going wrong, so we can learn from it...”

A clear change that came about as a result of the transfer to employee ownership is management’s investment in leadership and commitment to supporting staff. “...when we were in the NHS we didn’t do ‘Investors in People’ or anything like that... our organisation has [now] gone from Bronze to Silver to Gold pretty quickly and a lot of the things have become outstanding.”

Impact on employees: Employee ownership has substantially improved employee satisfaction at City Health Care Partnership. The passion and commitment of the leadership was crucial. “...the chief exec is a nurse and...his passion and his commitment drives these shareholders.

There is evidence to suggest that better employee engagement creates a 'peer effect', which improves governance. In other words, co-owners will often self-regulate by holding each other to account.

#### **4.3.2 Case of Mike Stoane Lighting**

MIKE **STOANE** LIGHTING

Company overview: Mike Stoane Lighting is a founder-owned manufacturing business based in Scotland. It has grown from employing seven staff to now having 55 employees and a turnover in excess of £3m.

Employee ownership: The Company moved to employee ownership in 2014 when the founder exited the business. Like many founders who want to protect their legacy, and are passionate about keeping jobs in the region, a representative at the Inquiry reported, "... [the founder] wanted to leave the business with the jobs intact; he didn't want to sell up and have the business broken into pieces and so he used employee ownership as a method to do that." As a result, there is an EOT, with 65% of the company held by employees, with 25% of the equity retained by the founder.

Corporate governance overview: the representative reported that prior to employee ownership, the company didn't have any formal governance structures. "... employee ownership forced us to address that, forced us to sit down and say how are we going to be structured..." The new governance structure is based around a set of legal documents - a Trust deed, a shareholder agreement and a letter of wishes from the founder. "We then transcribed that into a kind of handbook which goes out to all staff which outlines how decisions are made and things on more of a day-to-day basis."

Formal employee participation includes two employee representatives; one sits on the board but is not a director, and the other is a trustee. However, there are rigorous mechanisms for reporting to the owners with corresponding increase in accountability. “We are bound to report back to shareholders, which includes the beneficiaries of the Trust...the directors have a responsibility to report back quarterly and a shareholder newsletter goes to our external shareholders and also to our employees, and we hold board meetings quarterly.” This has caused a shift in management focus, with the board very aware that they now need to reflect the views and concerns of staff.

Impact on employees: Employees’ new sense of ownership has generated a greater sense of involvement: “I do think that people feel they own the business and a large number – not everybody, but a large number of our staff - feel very strongly that we should be accountable to them and are very interested in the structure of the business, [and] in the future of the business.” This has had strong impact on employees’ levels of engagement and involvement, not just in their day-to-day work, but in the business as a whole.

The business has encouraged employee engagement by initiating a process of jointly agreeing

✓ *Employees, across levels, show genuine interest and care in understanding the business dynamics*

on aims and values. The panel were told the benefits of undertaking this piece of work, “If it comes from people’s own hearts, what they believe is good for the business, then that’s way more powerful than anything you can instruct people to do. Especially as some of the things that they’ve said that they expect from each other are things that as a leader of a company you probably wouldn’t feel you could

ask people to do; but people's peers can ask them to do - it's quite incredible".

## **4.4 Impact on well-being and health**

Stress and its impact on workplace health are of increasing concern in today's organisations. There is evidence to suggest that employee ownership reduces work related stress and thus positively impacts on employees' well-being. The case of Make Architects highlights well-being as an important factor in employee-owned business success.

### **4.4.1 Case of Make Architects**



Company overview: Make Architects is an international, award-winning architecture practice. Founded by Ken Shuttleworth in 2004, the practice has grown to over 160 people across studios in London, Sydney and Hong Kong. The most recent turnover of the firm was over £23 million.

Overview of employee ownership: All of the equity of the firm is held in an EBT, a departure from the ownership model used by most architectural firms. The explicit purpose is to share profits made by the company more equitably than in a traditional partnership model. Make was spared the challenge of converting from a partnership model to employee ownership and the HR director noted, "We were set up as employee owned so it is more about our culture from the very beginning".

Assessing well-being: As in many other EOBs, the management style at Make Architects focuses on people as much as the business. "We don't measure productivity, but we do things like client questionnaires

and employee engagement surveys and [other] things... What we tend to focus on...individuals - the positive relationships that they have with each other - but also externally with clients, that's how we measure ourselves". The company believes shifting the focus of assessment from financial objectives to relationships has a positive effect on employee wellbeing.

Employees at Make Architects also work long hours, but employees are able to discuss the issue openly and change practices as need. "There is a whole big debate internally about time sheets, and how much time we add but we're open about it, and we ask for suggestions of how we can stop it."

Another source of conflict between management and employees in many

✓ *Employee well-being often improves in employee owned businesses due to the focus on relationships*

organisations is managers having to monitor employees' day-to-day spending decisions. The profit-sharing approach at Make creates a framework that encourages employees to decide on spending without the threat of punitive oversight from management. The Penal were told that, "We don't have shares that we give to employees, we're all partners and everybody gets the same percentage of what they've earned in that year when the profit is given out, people do see the impact of it". Encouraging employees to make decisions about spending in a more mature way avoids the stress and uncertainty that often results from micro-managing. For instance, the company encourages employees to "...just think, if you are flying over to the Sydney office, and you fly business class, that's actually coming out of yours and your colleagues pocket."

Culture: At Make managing well-being is strengthened because of the culture of trust and ownership. As was repeatedly emphasized during



the Inquiry, the culture at EOBs also has an impact on roles, and role definition of employees, that adds to the sense of belonging, ownership, and overall well-being at the firm. In some instances, there are subtle benchmarks possible in practices across companies. The HR head recounts one such benchmark “... at a Future Leaders workshop session [with other firms] ... one of the sessions was about presentation skills. We sent 10 of our guys along; there were about 70 there... [The instructor] asked the question who is actually client facing and hardly anybody in the room put their hand up. But all the Makers, who were cross-levels, put their hands up because we don’t hide. Just because they’re a student, or just done an undergrad, we don’t hide them at the back doing the doing at the machine. They’re out there, they’re talking to clients and getting involved in it as well. That’s something I think puts us aside from different architectural practices”.

#### 4.5 Impact on fairness

The culture of openness in EOBs is arguably central to the creation of a fairer workplace. The research

✓ *Employees have a stronger sense of fairness and equity in employee owned businesses*

evidence supports the narrative of the participants at the oral hearing that employees in employee owned firms have greater sense of fairness in a variety of areas such as remuneration, rewards across levels, and workload. The evidence from the oral hearings is also in line with the TUC principles for Employee Share Ownership Schemes. Employee owned firms tend to distribute reward on a more equitable basis than most conventional companies. A recently published survey of US workers conducted by the National Center for Employee

Ownership, reports that employee owners' income from wages is 33% higher compared to non-employee owners; this holds true at all wage levels. The impact of better reward sharing is even clearer at the household level – with the median household wealth of employee owners being 92% higher than non-employee-owners [22].

Research shows that in addition to more equal distribution of financial benefits, EOBs tend to have fewer inequalities in terms of power, status and perks. All these factors appear to contribute strongly towards higher employee retention. [23].

Employees in employee-owned businesses also have higher levels of discretion over the way they work, and show a greater propensity to interact with, and help, their co-workers [24]. This reduces conflict and promotes cooperation.

As an example, in time of crisis employees in employee-owned businesses often seem to be willing to forgo short-term benefits for the long term survival of the firm. The following case illustrates this point.

#### **4.5.1 Case of Woollard and Henry Engineering**



Company overview: Papermakers Woollard and Henry was established in 1878 and now employs 69 people and has a turnover of £4.9 million.

Overview of employee ownership: 100% of the equity in Woollard and Henry is owned by employees and held in two Trusts, one being used for the distribution of shares to current employees. All employees are given shares after six months employment and can purchase more through a share incentive program. The company became employee owned in 2002, following a crisis caused by the illness of the previous owner.

Resilience in crisis: Woollard and Henry measures performance using metrics such as cash flow and margins. They benchmark the company against global competitors and attribute their strong performance to their products and their employee ownership.

The Inquiry heard that strongly embedding employee ownership has been crucial to attaining high levels of performance. “Every week we will try and have a meeting with employees, all employees. We will shut down and we’ll talk about cash; we’ll talk about opportunities coming in; we’ll talk about problems, talk about sales and all these kind of things, so we do spend a lot of time trying to get people engaged. People understand a lot more about the company and why we’re trying to drive it. This provides a number of advantages. For example, most companies will have wage negotiations. We’ll actually set out targets at the beginning of the year so people know what we are trying to drive to. I’ve not really had a wage negotiation in the 15 years that I’ve been here because people know if the company is doing well we will pay. But if the company is not doing so well, they understand the business well enough to say, ‘you know, we’re not pushing for pay increases and things like that’”.

✓ *Often employee owned businesses do have to enter into wage negotiations as there is greater parity between employees*

## **4.6 Impact on employee commitment**

Evidence suggests that transitioning to employee ownership also have an impact on the commitment of employees to their jobs as well as to the organisation. As the following case illustrates:

#### 4.6.1 Case of Tullis Russell Group



Company overview: Tullis Russell is a 170-year-old coating and papers company with 190 employees and a turnover of £40 million.

Overview of employee ownership and governance: Tullis Russell became employee owned in 1985, with 95% of its equity held in a Trust. Corporate governance at Tullis Russell is based on a plc model, and the practices that are pervasive today date back to the days when the firm was much larger. Currently, the firm has about 100 employees in the UK, and a similar number of employees in Korea. There are two management boards for each of the companies; [and] they report to a group board. There is also the employee ownership board. Each local management board has employee representation on the board.

Culture of openness: The MD of the firm, who joined the firm after considerable experience in non-employee owned business, remarks on the striking difference between his previous experience and what he has come to see at Tullis Russell. "In a plc, the shareholders aren't employees, so you are not actually accountable - the employees aren't holding the executives to account, it's the shareholders, and at the annual general meeting they may hold them to account... [At Tullis Russell] we also have an annual general meeting; we have a question time session where every one of the employees sits in front of the board and asks them any question they want for a whole afternoon. They have to answer the questions truthfully, and it is recorded and videoed, and put on the internet. So, they can go back and see exactly how the questions were answered -- they have to really take ownership...They [the management] get really tough questions right down to how much are you being paid, and they have to answer them". When employee have the right to ask questions, and expect an

answer, the management becomes “... very accountable very quickly”. The MD highlights that this culture is enabled by the processes that make the company’s accounts more open to inspection. “I think the level of transparency that you do have in a business in terms of every month you tell them the P&L, the cash in the bank, the core data, means you are held accountable because they have that data at their fingertips to hold you accountable, and then they have the ability at the executive level to vote you off the board if they feel you are not doing a good job”.

Employees’ commitment:

A consistent theme across a number of cases during the Inquiry was the change in employee commitment when they

✓ *The investment in sharing information, answering questions, and more governance pays off as employees tend to show greater commitment at the time of execution*

have access to more information, expect honest analysis from management, and experience involvement in key decisions of the firm. As in most employee owned business, Tullis Russell often “seeks approval from our employees to take forward major capital investment plans, and strategic plans. That consultation process has to go through and they have the right to veto it over a certain level of turnover or capital investment. So yes, there is very much a more direct involvement in the business and [employees] have to be well briefed to make those decisions”.

It is clear that the management team has to invest more time interacting with, and often convincing, employees about decisions – But as the MD points out, this has a longer-term payoff because it increases employees’ commitment to the implementation of the plan. “I have been in a plc, and I’ve also been in a co-operative environment, and they are different. But I think here it is actually better because I’d

far rather be dealing with employees than some corporate people to be honest. It's [also] a more refreshing environment to be in because you are actually dealing with the people who will execute the plan. If you get their buy-in, it makes the actual deployment of that plan a lot easier. So for me it has been a more positive experience as a senior manager in the business than in a plc, or within the structure of a huge American corporation which is very prescriptive in what you can do, or can't do".

An important indicator of employee engagement is the level of absenteeism. It is also an important contributor to performance. Research on absenteeism in employee owned business shows that while absenteeism declines with increasing employee ownership, the benefit from this decline can be offset by a greater tendency of employees to legitimise their absenteeism [25, 26]. In a study on absenteeism in French firms that had different profit-sharing and employee share ownership schemes running in parallel, researchers find that while all types of schemes are associated with statistically significant reductions in absenteeism, using only employee share ownership scheme led to a reduction of absenteeism by approximately 14%, while the using profit sharing and employee share ownership together led to a reduction of approximately 11%, and the use of profit-sharing alone reduced absence by approximately 7% [27].

A central question is how does this commitment transfer to new employees, especially millennials, who may not have the same shared values? We find that a number of EOBs are cautious in their process of selecting new employees.

## 4.7 Impact on employee retention

A recent US-based survey reports that the median tenure of employees in EOBs is 5.2 years, compared to 3.4 years for the non-EOBs [22]. Similar results have been reported across economies: a Spanish study shows that employee with a stake in the business are more likely to remain with the business [12].

Retaining talent is always a challenge in competitive industries, and in markets where talent is hard to attract. While retention rates vary significantly across industries and markets, the evidence suggests that employee owned business tend to have better retention rates than non-EOBs.

This could be due to a variety of reasons. Research shows that employee ownership, most often through ESOPs, has been widely used as tools for retention, especially for top talents and senior managers. UK research that examines this issue is not extensive, but evidence indicates a clear positive relationship between ownership and retention that is supported by studies in other countries. This effect is clearer in sectors that traditionally have high employee turnover, limited supply of labour, or shortage of skills.

Results from a large survey-based study shows that employees are less

✓ *Higher commitment from employees translates to better retention*

likely to leave when they expect substantial financial benefits from their company's share ownership. Retention rates also appear to rise when the company's management is highly committed to the principles of employee ownership, and when top management maintains extensive communications with employees [28].

Organisations that experience high labour turnover, also experience disruption and loss of talent and expertise. Studies with US

based firms show that EOBs who combine financial rewards with greater perceived influence on decision making produce more employee commitment and job satisfaction, which in turn increases retention rates [29].

#### **4.8 Higher levels of scrutiny by employees**

One of the changes that often accompanies a transition into employee ownership is the increasing employee interest and stronger voice in the operations of the business. Employee shareholders are reportedly keen to know about how decisions are made, why a course of action was chosen over others, and to contribute to the decision-making process. Overall, the panel heard that this results in greater scrutiny of management decisions.

On the one hand increased scrutiny can strengthen corporate governance as employees who are also shareholders now hold the management accountable. However, increased accountability is not without its challenges. For instance, for managers working at a firm without a culture of openness, or for employees unaccustomed to questioning management, coping with wider accountability is often difficult. Furthermore, increased scrutiny and questioning management, can take more time.

EOBs interviewed appear well aware of these pitfalls. A number of participants, especially from newly employee owned firms, highlighted the importance of learning and experimentation – indicating deliberate willingness to try new processes, assess their effectiveness, and change how things work. The following case of PB design and planning highlights this transition.



#### 4.8.1 Case of PB Design and Planning



Company overview: Based in Clevedon, Somerset,

PB Design and Planning is in the power equipment business. The company employs 56 people and has a turnover of close to £8 million.

Employee ownership and corporate governance: PB Design and Planning became employee owned in 2015 with 100% of the equity owned by employees and held in a Trust. The Trust will shortly have two directors, two employee trustee directors, and two external trustees.

The structure underlines management's commitment to openness and involving employee shareholders in the process of scrutiny and oversight.

Decision making and scrutiny: When asked if employee ownership has changed the level of scrutiny in the company, and the decision making culture more generally, the respondent noted "Yes, without a doubt. I think we were responsible, [and] fairly governed, but certainly being employee owned pushes us that much further. It is certainly setting up structures that employees have a way in which they can challenge the situation". In terms of operations, the employee representatives meet with the managing director once every two months to "... thrash out the various items that they have selected to go on that agenda".

Importantly, executive management have the authority in this set-up to make operational decisions. But they are answerable to trustees,

✓ *Better governance is accompanied by greater scrutiny, which may require significant change management effort if managers are new to the employee ownership model*

and the wider co-owner workforce for their decisions. Several witnesses to the Inquiry confirmed that this consultative approach could take more time. Almost without exception they appear to believe better decisions result.

Convincing long-time employees about the advantages of co-owner scrutiny can be difficult. “We’re a manufacturing company; that tends to have a certain culture as well. So for them [managers] it was about power in a way. [But] power has now been devolved...they can be questioned and that wasn’t happening before... We were going to do employee ownership for many reasons but [increased oversight of management decisions] was certainly one of the positive things we felt could help us to move on in terms of management development. Two years on, it’s just starting to make a difference”. On balance as the respondent points out “... employee ownership without a doubt is more challenging but it enables much closer scrutiny”.

#### **4.9 A people-centered management outlook**

Putting people at the centre of the organization is widely seen as crucial to superior business performance. EOBs are by no means the only organizations that are people-centered, but the relationship between employee ownership and management orientation is arguably more explicit in employee owned businesses. The relationship is most apparent in greater focus on training, health, and safety issues [30] that may bear greater fruit in EOBs because worker participation in the design of relevant programs [31].

Research shows that businesses that added communication, training, and participation are more likely to report performance gains. But investments in these areas are likely to decline when companies face economic threats. Research suggests that EOBs tend to buck this trend. It shows that majority employee owned companies are less

likely to cut back on these programs when facing economic threats, which in turn may account for why employee owned firms are more likely to perform relatively better in times of crisis [32].

Research also suggests that a people-centered management outlook may predate transition to employee ownership, and that it may facilitate the transition: We have evidence that companies that are employee centered are more likely to become employee owned. In the following case of ADP architects we illustrate this point – namely, that EOBs with an environment that is conducive for high employee performance often build on a culture that is people centered prior to transition.

#### **4.9.1 Case of ADP Architecture Ltd**



Company overview: ADP Architecture is a firm of architects and landscape architects who specialise in the education, health and commercial sectors. The company has 120 employees with revenues of close to £8 million. The practice is more than 50 years old.

Employee ownership: ADP Architecture became employee owned in 2016, for primarily succession and growth planning reasons. 75% of the equity is owned by employees and is held in an Employee Ownership Trust. The previous partners still own 25% of the equity and comprise of 5% of the workforce. There are plans for the Trust to gradually acquire the remaining 25% of shares. This would conclude a transition that is firmly rooted in the culture of the company before it became employee owned. “The culture we had was very employee orientated anyway. We have been an ‘Investor in People’ since the beginning, and we recently achieved the gold standard for that. We

are very employee orientated and we felt that culturally a move to employee ownership would be relatively easy for us; it wouldn't be too difficult for the staff.

Different management approach: Employees are at the heart of most EOBs. But arguably, this is particularly true for professional services companies like ADP. For this company being employee owned after being in business for more than 50 years held great promise for further growth because it unlocks the value and potential in people that is at the heart of its operations. As the MD points out "... because the people that lead our business are our project directors, our client managers if you like. In order to grow you have to have enough client managers to deal with a growing number of clients. ..In the past, as a partnership, traditionally the partner [as an equity holder] does that... If we wanted to grow, we don't want those constraints that people have to have capital in the business to do that; they can just be an employee - the same as anyone else. So that means we can promote people within the organisation to client management role without them having to contribute capital, and to have an equal status. Also, if we need to, we can bring in people from the outside who can contribute capital so it allows us to grow our client base with our client managers without the constraints of direct ownership".

✓ *Significant investments go into the development of employees in employee owned businesses*

In essence, an employee ownership structure provides the necessary opportunities to reward performance more equally, involve people in decision making of the firm, and redefines the role of the top management team away from a command and control setup.

Research has long noted that employee ownership fosters a different orientation towards participation of employees in decision

making. A UK study finds that employees' participation in decision-making generates stronger sense of employee ownership than stock ownership. The study also shows that employee's feelings of ownership is associated with higher levels of commitment and satisfaction [33]. A US based study provides further evidence that ownership programs are positively linked to greater participation in decisions, higher quality supervision, better treatment of employees, more training, higher pay and benefits, greater job security, and higher job satisfaction [34]. Research also indicates that owners tend to have higher quality of work, with fewer complaints, and yet perform a similar quantity of work [35].

This reorientation is bound to have an impact on the role of top management teams. Researchers have concluded that one of the reasons for higher employee engagement at EOBs is top management is often more likely to seek employees' input in strategic decision making. Thus, when setting the strategic direction for the firm top management is also more likely to encourage and take note of feedback from operations [6, 36].

#### **4.10 Impact on attracting millennials**

Much has been written about the millennial generation over the past decade [37, 38, 39]. Millennials constitute a large and growing share of the labour force. Attracting millennials is therefore crucial for the future of any business. Research shows that millennials place particular importance on finding meaning in their work – they are not as motivated by remuneration as previous generations. For the millennials, meaningful work is not only to be found in the tasks they are assigned, but also in the expectations that the company they work for is socially responsible. Beyond that, millennials are also strongly

mindful of career progression and hence are attracted to organizations that offer training and development.

EOBs are well placed to offer millennials work that is meaningful and training and career development. Although the inquiry did not specifically deal with attracting millennials it provided considerable evidence to suggest EOBs sought out individuals who are attracted to businesses that pursue responsible growth, reward employees equitably, develop talent, and make them stakeholders. The trend is illustrated in the following case which shows how EOBs actively seek out prospective employees who have this value set.

Research shows that employee ownership increases employee involvement – defined as participation of employees in goal setting, planning, and decisions that influence work practices. Employee involvement increases employee performance motivation, and thus is competitively important. A study of Spanish shop floor workers that examined the extent to which employee ownership influences employee involvement found that workers with a stake in the business are more likely to identify with the business, and more likely to actively seek greater efficiencies by cutting costs, thereby raising productivity and improving quality. However, performance motivation in EOBs may not be strictly due to self-motivation. Employees achieve the productivity gains in part by monitoring the work of their colleagues – another strong indicator of employee involvement [40].

Empirical studies of employee ownership usually rely on interviews, surveys, and indirect indicators. Testing the ‘mind set’ of employee ownership is difficult using this data. Research has begun to use experimental designs - the gold standard in science in general and social psychology in particular - to examine the employee ownership mind set [41]. A recent experimental study shows that participants who are exposed to the principles of employee-owned

firms exhibit higher productivity at the tasks that were assigned to them. This suggests that employee owned business may inculcate an employee ownership mind-set that creates more efficient designs of production, reduces waste, and improves coordination with other employees, or parts of the business.

An important factor that often attracts new recruits – especially millennials, to choose employee owned business

✓ *Employee owned business look for cultural fit with new employees and report that millennials often identify with their ethos*

over other businesses is the greater sense of autonomy in EOBs. Employee autonomy is related to, but distinct from, employee involvement. Employee autonomy is the extent to which employees can control their work, and the discretion that they are allowed to have when dealing with suppliers and customers.

Studies suggest that compared to non-EOBs, employee owned firms tend to allow non-managerial employees greater autonomy. A quantitative study of US firms finds that workers in employee owned firms often influence the firm's economic performance by innovating around work processes related to new products and marketing [10]. Top management willingness to allow employees the autonomy to adopt changes can be crucial for performance. Where non-managerial employees are included in ownership schemes, research shows a clear statistical relationship between ownership and productivity if the employees are accorded greater autonomy in decision making. In contrast, if the ownership schemes are confined to managerial staff, i.e. it excludes non-managerial employees, the positive relationship between autonomy and productivity no longer exists [42].

The following case from the oral hearing describes some of the organisational dynamics that enables EOBs to position themselves as preferred employers for many millennials.

#### 4.10.1 Case of Cambridge Weight Plan



Company overview: Cambridge Weight Plan (formerly Cambridge Diet), was launched in 1984, employs 204 full time staff and has revenues of just over £40 million. It sells products to independent Cambridge consultants, who then sell on to individuals.

Overview of employee ownership: In 2009 the then owners decided they wanted to retire from the business but protect its culture and ethos and legacy. They themselves had bought out the business from diet's inventor, but by 2009 it had grown too big for another management buy-out. So in 2010, 49% of the shares moved into a Trust, a bank loan was obtained and the company became employee owned – with the MD remaining one of the owners. The employees took on a second loan in 2014 for the rest of the shares, and it was at this point that the company became fully employee owned.

Recruitment and development: Cambridge Weight Plan actively promotes its employee ownership model to attract future employees. As the head of HR points out "... from our experience attitude is more important sometimes than ability". Employee ownership affects attitude, which in turn is more likely to deliver results: "... you can always teach people a job but if they have a positive attitude, and they are willing to learn and willing to develop, that's worked well for us". The firm told the Inquiry: "... We sell employee ownership as part of



our recruitment package. Some of them will come to interview and ask what that means in more detail. We talk about our culture and what it is in terms of our core values within the business. We've noted now in terms of recruitment that a lot of millennials are quite keen on working for an employee owned business - that's something that we've picked up in terms of what makes this business different to one down the road".

The company feels that being employee owned and highlighting it in its recruitment package can be an advantage in a highly competitive recruitment market. "We advertise... [that] we're an employee owned business, and as a result of being an employee owned business these are the benefits of working in an employee owned organisation. 'You have a voice; you are accountable' etc., so we do sell that. Currently the market is quite competitive, even for an employee owned business. When you are looking to recruit, getting good people is quite challenging and so selling that benefit to people has worked for us".

Apart from hiring top talent, the company also invests heavily in developing talent inside the firm. "We tend to spot talent within the organisation, people that we see have potential for the future. We invest a lot in terms of training and developing them, and we also look at succession because we know at some point some people will be looking to retire. So, we are quite upfront in trying to do that; we are very proactive in doing that in our organisation".

## **5 Employee ownership as a route to business succession**

Based on the evidence it received, the Inquiry has concluded that employee ownership has a major role to play in business succession.

The Inquiry noted that:

- UK businesses tend to handle the challenge of succession poorly, with many viable companies damaged as a result
- A growing number of companies now appear to see employee ownership as a viable succession option
- There is extremely low awareness of the employee ownership option among owners, advisers such as accountants, and the financial sector

A number of witnesses told the Inquiry that their move to employee ownership was motivated by lack of attractive and suitable alternatives. One common alternative, i.e. a trade sale, was frequently rejected because in the opinion of a number of business owners who participated in the oral hearings, it can so often lead to the breaking up the business, relocation of jobs, and even shutting down of operations. Owners tended to see a trade sale as a more financially lucrative option – certainly in the short term – but less attractive when their concerns were more about concerned the future of the employees, the legacy of the business, or commitment to the workforce of local community.

Andrew Lane from Union Industries told the Inquiry: “They [the family owners] had no direct line of succession, so really in the traditional world a sale was the only real option of what to do with this business... So, they [the family owners] went to the degree of employing somebody to find a buyer, and a buyer was found, and due

diligence occurred. [However], the meetings got intense. As it got more intense, words like integration and relocation started getting into the dialogue. For our former owners there came a moment where they thought, 'it's going, we're going to lose it' and the 'we' isn't just them [the owners], the 'we' was the family that had built that business over 40 or more years". The Inquiry heard a number of similar accounts. Owners often appeared to take the view that the employees who had helped build the company were as much contributors to the success of the business as themselves.

This strong sense of shared success is crucial to how the owners seem to see the future of the business: "So they had invested themselves in it, but they were also very conscious that the workforce, many of whom were long serving employees, also built it. They didn't do it on their own, there was a family that had created this business and, if they weren't careful, its identity, all that made it special and unique, would evaporate; it would be assimilated into another organisation. They did not want that".

As in the case of Union Industries, many business owners appear to have 'stumbled' upon employee ownership. "It was a discovery because it's not well known enough as a proper realistic honest transition vehicle for business owners to exit. I don't understand it because it is actually the perfect way to do it - in many, many ways". Even though some respondents reported that they became aware of employee ownership during succession - i.e. when they were actively looking for options, and even then, mostly by chance – there is consensus that the Finance Act 2014 has had a significant influence in bringing the option of an Employee Ownership Trust (EOT) into the mainstream. Notwithstanding greater awareness of employee ownership as an option for owners that wish to exit their business, lack of succession planning, especially among SMEs (more than 60% of

SMEs are estimated not to have a succession plan), is a major barrier to the uptake of employee ownership.

Employee ownership may become less attractive if an owner wants to exit the business and ‘cash in’ quickly. The Inquiry heard that a typical financial requirement in an employee buy-out is what’s often termed a ‘patient vendor’ – an owner who is happy to be repaid for their stake over a period.

## 5.1 Awareness and uptake in succession planning

Evidence provided to the inquiry suggests that awareness about employee ownership is

✓ *The Finance Act 2014 has improved awareness of employee ownership as an option in succession planning*

improving, but from a very low base. A number of respondents identified the Finance Act 2014 as a key event in bringing employee ownership more mainstream. Furthermore, through the work of organisations such as EOA, as well as the support for transition by devolved governments in Wales and Scotland, there is growing access to the employee buy-out expertise owners need.

For instance, as Simon Mounsey from Agilisys Ltd. points out “The co-founders had been looking at different succession options for a while, and really none of them quite suited what they were looking for. Then the Nuttall Review [2012] came out and the associated legislative changes [Finance Act 2014] came through on that, and it was the package of all of those things that became really attractive to them. I would say they were interested in rewarding and creating some value for the employees who had helped build the business to that point”.

Furthermore, the Employee Ownership Association Annual conference is a significant propagator of the model.

✓ *The Employee Ownership Association is a central source of knowledge about employee ownership*

As Steve Bonnick, founder of Toucan Computing Ltd states “I founded the business over 20 years ago. We have got very stable staff, very low staff turnover, we’ve got about 25 staff. For many years I’ve been trying to look at ways of permanently tying the staff in. They did receive bonuses, quite substantial bonuses for many of those 20 years, but I wanted to tie them in better. I looked at all sorts of models, and they were all far too complicated or they had downsides to them. Then [using] the power of Google, I came across EOA and went on their conference, and it all just suddenly started to fit into place and went from there”.

As one of the panel members from the oral hearing observed about the greater awareness “...Post-2012, as I think we heard from [a participating firm] the changes in tax law are raising awareness. We heard a presentation on the finance at 2014 Changes and so there is a new generation that are coming to this because they’ve heard about it; because of the coalition government’s efforts, and the Employee Ownership Association’s efforts to promote it.”

The Chief executive of Wise Investment, part of The Oak Investment Partnership was formed in 1992 and became employee owned in 2013, Alex Rae told the Inquiry: “The original founder looked at various options and felt that employee ownership resonated with his views of how to manage the business for the staff and our clients. So it became 51% employee owned on day one, and then it’s another 5% every year, so we’re now 66% employee owned and it will be 100% in another seven years”.

A number of witnesses stressed the importance of speaking to businesses who have gone through an employee buy-out and learning from their experience. This awareness is changing the calculus of succession for many firms where founders are contemplating exit.

## 5.2 Owners' values a key determinant of transition

Not surprisingly, the decision to transition to employee ownership is strongly influenced by the objectives of the departing owner. A common pattern across evidence to the Inquiry was owners wanting to achieve various non-financial objectives as part of the transition. This could include any of:

- Rewarding employees who had been part of the 'journey' to build the business
- Keeping jobs in the region and community
- Protecting the culture of the company
- Protecting the owner's sense of a legacy; sometimes referred to as 'the name over the door' feeling

Importantly, owners questioned by the Inquiry seemed to feel buy-outs could anyway meet both their individual financial needs and non-financial objectives like the ones above.

David Heslop, the MD of ADP Architecture told the Inquiry: "...We established the EOT and 75% of the shares were

✓ *Owners often choose employee ownership as an alternate to an exit via a trade sale to preserve their legacy*

transferred to the EOT. The reason we didn't do 100% was that we

wanted to tie in the six original owners; we didn't want them disappearing off immediately. The arrangement is that they own the shares until they reach their retirement age, at which point they are bought back by the EOT. In the fullness of time it will become 100% employee owned. That's the only reason why we didn't go to 100% immediately because we just wanted to make sure that nobody cashed in and went off."

Some employee ownership transfers are the result of an owner gifting all or part of the equity to the business. One such case is Classic Motor Cars, setup in 1993 by an enthusiast and entrepreneur called Peter Newmark. Mike Roe, the current Managing Director told the Inquiry: "So we arrived at the point where Peter decided he wanted to start to step back. Because he didn't particularly need the money, and he had had quite skilled people with him for many, many years (some of the skills within the business take years to learn). Bridgenorth is particularly an engineering area, Wolverhampton, Telford, it's where they [Skilled engineers] were. He wanted to retain the skills, wanted to give something back to the people that had built the business with him. He thought, 'what can I do?' So he gifted 61% of his shares to the employees, and really that's how we've come to be where we are".

## **6 Impact on communities and regions**

Organisations that are employee owned are not only concerned with creating economic value for shareholders, but also with contributing to the communities and regions in which they are located. The evidence gathered during the Inquiry shows that EOBs view their engagement with the community as an integral part of their identity. The values that employee ownership fosters encourage employee and management

to make decisions with the potential impact on the community in mind to an extent not usually observed in non-EOBs.

Overall, there is clear evidence to show that employee owned business have a positive influence on the communities and regions where they operate. We find that this influence is exerted both indirectly and directly. EOBs create well-paying jobs in the communities in which they operate. They also develop skills and talent and contribute significant financial and human resources that are crucial to the development of the community. In this section, we first review the evidence for indirect influence on regional development that is a result of the organisational practices of EOBs followed by the direct contributions made by employee and management of EOBs.

## **6.1 Impact on job creation in local communities**

Mergers and acquisitions that lead to corporate restructuring, layoffs, and closure of plants pose a threat to the economic livelihood and social fabric of communities and regions. The buying and selling of corporate assets is often indifferent to the impact on the wider society. By design, EOBs are significantly less likely to be sold to outside owners. A study of U.S. public companies using matched samples of companies with and without employee ownership shows that companies with employee ownership stakes were more likely to remain independent [43]. Secure in the knowledge that they are less likely to be the target of acquisition by other firms, EOBs are able to build stronger and more stable relationship with stakeholders. Inquiry participants repeatedly noted that greater customer confidence in the continuing independence of EOBs customers was a positive factor in their ability to build long-term mutually beneficial business relationships.



The evidence gathered during the Inquiry supports the view that employee-owned businesses take local job creation very seriously. The evidence showed that EOBs worked to fill positions with local candidates and went to considerable length to retain these jobs in the face of economic pressures. The importance of recruiting locally was a consistent, and passionate, theme during the Inquiry, especially in hearings at Edinburgh, Cardiff, and Manchester. The following cases of Gripple and Swann-Morton from Yorkshire exemplify the commitment of EOBs to invest in creating high quality local jobs.

#### 6.1.1 Case of Gripple



Overview: Sheffield based Gripple sells wire joining and tensioning systems and has operations in a number of international locations. Formed in 2011, the company has over 550 employees worldwide and its most recent annual turnover was over £50m.

Gripple's strategy is guided by the parent company GLIDE, which stands for Growth Led Innovation Driven Employee Company Limited, through the Articles of Association of GLIDE companies. The articles set out Gripple's aspiration to achieve an annual turnover growth of 10% and 25% from products that are less than 4 years old.

Brief history of employee ownership: The Company converted to employee ownership in the mid-1990s with the founder intent on securing his legacy and protecting the interests and future of the employees. There is 100% uptake in ownership as the contract of employment stipulates that employees are obliged to buy shares after working in the business for one year. Shares are held via a Trust, the vehicle by which the founder and vice-chair can gift their privately held shares. The Trust currently owns 20-25% of the equity, but this has

been growing over a 10-year period with more shares being gifted annually. These shares have been designated 'permanent shares' and can never be sold. Further protections have been put in place to preserve the legacy, allowing the Trust to exercise a right to prevent the break-up of companies for the sole purpose of profit.

Community engagement: Investing in the region and the local community is at the core of Gripple's identity as a company. The company has a significant commitment to working with the local community, describing this engagement as "part of who we are". GLIDE makes a contribution of 1% of budgeted profits to charitable causes, and the promotion and support of employee ownership in the wider economy. Community engagement extends to the company's international sites. Regular activities include donating a percentage of company profits to charity, and in the spirit of the company's culture, developing innovative ways of raising money for worthy causes. These activities are managed by an internal charities team that organize activities and provide teams of people when needed.

Employment security: The importance of keeping jobs in the UK is a consistent theme among EOBs. Gripple is no exception. The company prides itself on its ability to retain staff, and attributes much of its success to the engagement and sense of empowerment that come with employee ownership. It also highlights the benefits to communities of low labour turnover – not only in delivering stable incomes that allow families to plan for the long term, but in terms of providing a stable tax base for local authorities.

Long-term jobs: There is a strong emphasis on growth and turnover at Gripple, but this does not mean that the company's

✓ *Employee owned businesses show a clear focus on creating and preserving high quality long-term jobs that are rooted locally in their regions*

chief concern is meeting targets. “I think we have an overriding responsibility to try and create and sustain a business for the long term”, said one witness who spoke on behalf of Gripple during the Inquiry, “we realise that part of our responsibility is to continue to grow and continue to innovate and change and evolve and invest, and we do so because we are custodians of the business, we hope for two, three, four generations down...”. Taking a long-term view of the business, however, does not mean avoiding risk. In fact, Gripple argues that innovating and taking risks is part of its responsibility to employees, and to the community at large. Contrary to expectations, Gripple argues that employee ownership makes risk taking easier because the articles of association prevents selling the business. Protected from the threat of takeover pressures Gripple can focus on taking long term risks that generate growth and jobs – benefiting the community as well as future generations of employees.

#### **6.1.2 Case of Swann-Morton**



Overview: Swann-Morton specializes makes surgical and industrial blades and exports 70% of output to over 80 countries worldwide. It has 410 employees and turnover close to £30m with a profit of £2.7m.

Brief history of employee ownership: During the mid-1940's, the founders of, motivated by a concern for the workforce, and wishing to secure the future independence of the company, gave 50% of the shares to the employees, and placed the remaining 50% in a charitable Trust. The EBT was created in 1965 and the charitable Trust in 1974.

Engagement with the community: The Swann-Morton culture is inclusive; it does not make hard and fast distinctions between its

responsibilities to employees and the community. The EBT for example, helps local charities and sponsors students as well as other community activities. Commitment to keeping jobs in the community is strong. The company tries to keep manufacturing jobs as close to home as possible. Regional interests figure strongly in decision making that affect employment. As one Swann-Morton participant in the Inquiry put it: The way we see it, "...if you can make it in Sheffield let's make it in Sheffield, if we can make it in Yorkshire let's make it in Yorkshire, if we can make it in England, let's make it in England."

Employment security: Swann-Morton makes employee retention a virtue out of necessity. Secure employment encourages workers' commitment to quality and acquisition of new skills. This in turn reinforces Swann-Morton reputation as high-quality providers of surgical and industrial blades. As one Inquiry participant from the company noted: "We find that people that start with us, generally someone that's been with us 18

✓ *The focus on creating local jobs may often come at a higher short-term cost*

months, two years, will stick, they'll stay and be with us... we've got 44 years' service awards this year, 25 years' service is quite normal...".

Long-term orientation: EOBs often appear to defy conventional wisdom when it comes to dealing with growth. The Inquiry heard that they are particularly resistant to the kind of short-term growth pressures that govern public companies. A participant in the Inquiry from Swann-Morton commented: "The question I get often is why don't you diversify, why don't you grow? What I say to them is one of our main goals is to provide good quality employment for 400 odd people and their families for a long time. If we stay at 400 people and 30 million turnover for the next ten years, I don't care".

## 6.2 Impact on regional resilience

Communities and regions flourish when businesses make a conscious effort to recruit and train locally. A survey of US based employee owned business finds that employee-owned firms create jobs three times faster than their conventional counterparts [44]. During the economic crisis of 2007/08, studies show that firms that offer employee stock options were also more likely to retain more employees providing further support that employee owned business tend to create more long-term jobs [45].

There is considerable research evidence that employee ownership enhances the ability of firms to create employment in low-opportunity communities, both urban and rural. This body of work finds that this effect is also associated with community development – an objective not commonly provided by conventionally organised firms. [46]. Furthermore, research in specific sectors such as tourism, show that the employee ownership model has a positive socio-economic impact on the development of new business models such as sustainable tourism [33].

### 6.2.1 Case of Shawston



Overview: Shawston is a distributor of steel tubes, fittings, valves and pipe supports to contractors at UK building sites. The company has a staff of 120 employees and annual turnover of £17 million.

Brief history of employee ownership: Shawston has been in partial employee ownership since a management buy-in in 2000, but in 2015 it moved to a direct employee ownership model. By the end of 2017 the company plans for the employee stake in the equity to reach 100%.

Internal resilience through greater employee engagement: Studies consistently show that employee ownership leads to higher employee engagement. But these studies rarely capture how employee engagement increases as companies make a transition to full employee ownership. The evidence provided by Shawston provides

fine grained detail of the process. Participants spoke of employee engagement following ownership as a “journey” in which some employees are in the middle, moderately engaged

- ✓ *90% of decisions are in the hands of employees*
- ✓ *Takes time and trust to build this engagement*
- ✓ *Impact on a number of measures including hard measures like 10% reduction in costs*

category, while a few are highly engaged. To encourage more employees to become fully engaged, the company is using consultants to discuss shareholder roles, and involve employees more closely in decision making. A Shawston participant indicated that 90% of the decisions are in the hands of the employees, but to get employees to accept this takes explaining and some negotiating upfront.

Long term orientation – Shawston sees over concentration on growth as reducing flexibility. The alternative, breaking up the company into units, and spinning some units out is also rejected. Ultimately, the company has decided to remain an SME, in order to keep the “family feeling”, and take advantage of the fast decision making that their size makes possible.

- ✓ *Employee owned businesses prioritise investments in developing world class skills as well as promoting industries such as high-quality manufacturing in their region*

An unexpected growth challenge facing Shawston is whether to outsource some work. On the one hand, outsourcing has certain advantages, and is consistent with keeping the company at a certain size. Yet, Shawston feels that outsourcing may not be in keeping with the employee ownership ethos. Ultimately, the company prefers to vertically integrate, creating jobs in the community and region in which it operates. As one Shawston participant puts it “You don’t do employee ownership and import everything. What you look at is how many jobs you have created. Instead of importing from China, you buy the machinery and take the trouble to manufacture the inputs yourself. Ultimately, you save sea freight, avoid import tariffs and currency fluctuations. More importantly, you guarantee in-house demand and the jobs that go with it”.

Impact on community resilience: The oral testimony repeatedly brought up the theme of employee owned companies embedded in their local regions and making decisions that benefitted the wider community. Shawston is investing in education, with particular attention to training future leaders locally. The Inquiry heard that:

“...the Manchester heritage is crucially important...So we’ve started to look at MMU [Manchester Metropolitan University]. For example, [we] put one of our bright young guys through an MBA... We go to the local community to research [apprenticeship] ...Suddenly you find out about the apprenticeship levy. ..We can put one of our guys in at £2700 to come away with a business and management degree. So...actually it’s trying to then keep the local guys to be future leaders in the business, but also recruit from people who may be studying already at local universities, whether that be in Sheffield, Manchester, Liverpool, Leeds, wherever. So very much you’re looking in your local community a lot more and with a bit more intent than you would have done without being employee owned.”

### 6.2.2 Case of Mott MacDonald



Company overview: Mott MacDonald is a global engineering, management and development consultancy company with 16,000 FTE employees operating from 180 principal offices in 50 countries. Turnover in 2016 was £1.5bn.

Brief history of employee ownership: Mott MacDonald converted to employee ownership in 1987. Planning for growth made employee ownership 'the right thing to do'. Ownership is a hybrid model where 100% of the equity is owned by employees either directly or through a Trust. Direct owners who have bought shares account for 20% and are rewarded according to how many shares they own. The remaining 80% is owned through a Trust, which effectively holds shares on behalf of employees who are not direct owners, paying them a 'dividend'.

Employee ownership contribution to resilience of regional economies: Consistent with creating and keeping jobs in the region, EOBs contribute significantly to the ability of a region to recover from crises or from economic downturns. There is evidence to show that investment decisions by EOBs are strongly influenced by regional interests, rather than being determined solely by the economic interests of the firm. For Mott MacDonald employee ownership and engagement with the community are inseparable. This company is keen to promote the employee ownership model, believing that it is good for "our employees, our clients, and the communities we work in".

Long-term orientation: Employee ownership also allows the company to resist takeover attempts and avoid asset stripping, to instead focus



on sustainability, organic growth and the long-term benefits for the company and its employees. The contrast with PLCs is emphasized. "...in the Plc world...They know what's important out there to many of our competitors and it's financial performance. That is what drives them. Yes, all of these other things are important, because they need to have clients, they need to have staff, they need to attract and keep staff and so on... I think that we are driven by innovation, by having great people...great business with clients, good clients, great client relationships. We have all of that and it delivers to us financial performance. So the difference is that we put all of our effort into that side of things whilst monitoring and managing the financial performance to the side."

### **6.3 Impact on commitment to community development**

Employee owned businesses contribute to the development of the community directly and indirectly. Being deeply embedded in the community is often the result of the company's history, but at times it is central to the organization's identity. As the next two short cases illustrate:

#### **6.3.1 Case of Hayes Davidson**

The logo for HayesDavidson, featuring the company name in a bold, orange, sans-serif font. The text is positioned to the right of the section header and above a thin horizontal line.

Company overview: HayesDavidson is a small visualisation company, specialising in architecture and the built environment. It was founded in the late 1980s and currently has 21 employees.

Brief history of employee ownership: An EOT was set up in 2015 as a result of a succession plan. Employees own 100% of the equity and

are all partners. The transition to EOT from an LLP model has fundamentally changed decision-making or corporate governance.

Community development: HayesDavidson supports and encourages charitable giving, with the team regularly undertaking fundraising activities. The studio also donates to a wide range of worthy causes. “...there seems to be a real sense of charity...and this is something I’ve noticed recently, maybe it is the ownership effect but there is a sense of ‘can we do something for charity? Can we do this or that? Or if we do that we could do that and that would be really good’...It’s just that feeling that they want to do something, and whether this is the case I don’t know, but if you get more people feeling involved and inclusive you’re bound to generate more conversations about the greater good, maybe”.

### 6.3.2 Case of Remploy



Company overview: Remploy is an employability service that helps disabled people find and maintain sustainable employment and careers. It has been in operation since 1946 and at the time of the oral hearing in 2017 it employed over 700 people across the UK.

Brief history of employee ownership: Until 2015, the Remploy was wholly government owned. When it was sold, an employee ownership element was part of the sale expectations and process. Remploy was bought by a global consultancy which holds 80% of the shares with the remaining 20% are held by the employees in an EBT.

Community engagement: Remploy is another employee owned company with a strong ethos of charitable giving. “...we’ve had two

dividend payments so far...we receive 50% of the profit that comes to the EBT, 50% of the profit is distributed to charities that we all vote on, and we have given £50,000 this year to Cancer Research as our UK partner, and each department and team also has a budget to donate to charities of their own choice.”

This focus on contributing to the community may be a consequence of the nature of the sector and the way in which staff are selected. “...the employee ownership element is very much focused around our mission and values and it has really kept that at the core of our business. We recruit on values and behaviours, we don’t recruit for experience or qualifications...Essentially we support disabled and disadvantaged people into work, so we genuinely transform lives and that focus on why do we do what we do, it’s not to tick a box...I have worked for a number of private sector organisations and I’ve never seen an organisation as focused around how we do it and why we do it, rather than just how much money is it going to make”.

## **7 Comments on employee ownership trade-offs and tensions**

Thus far we have focused on clear and consistent themes that emerged during the Inquiry. However, the evidence also suggests that employee ownership also demands trade-offs and can inevitably create organisational and managerial tensions. These trade-offs and tensions are sometimes viewed as problems but can also be sources of creativity and innovation for new practices.

Decision making: The culture of decision making in most EOBs is governed by the values of transparency and participation. There is evidence to suggest that these values can sometimes prolong the decision-making process and may result in greater risk aversion than privately owned firms. But the Inquiry has also heard about the upside of this approach.

For instance, Mike Haigh, MD of Mott MacDonald points out “... our model is that we are collegiate... in our thinking. I think that means that when we make decisions we get real buy in, they tend to be well accepted decisions that people have been engaged with so they are easier to implement, and I think it makes for a very sustainable solid kind of business. ... It can slow down the decision making so I think what you need to do is you need to have a business that recognises that that's potentially a negative thing and mitigates for it”.

Scaling-up: Some participants expressed caution about rapid growth or using debt to expand operations, even when the business is financially sound. Although respondents viewed profits and growth as important for the long-term health of the business and its employees – many expressed a reluctance to pursue profits and growth if this posed

risks to the culture of the organisation. However, some of the EOBs seem to have successfully tackled this dilemma; scaling up rapidly, often through debt financing, while at the same time investing the resources needed to strengthen their employee ownership culture.

As Peter Holland, Chief Executive of the OPM Group told the Inquiry: "... I think there is a live debate in the organisation about how big we want to be... some people are happy with the scale that we are, they like the size that we are, they don't necessarily want us to get very much bigger. The board and obviously our investors think that we probably do need to be bigger... [However] the cultural bit means that [there will] probably be more of a tension and a debate within the organisation... if you had a more hierarchical and top-down driven corporate governance structure. So we debate this perhaps more than I would like but that is perhaps not a bad thing because actually it means that people understand why we are doing what we're doing".

## **8 Comments on barriers to expanding employee ownership**

We believe the following trends of the current economic environment are useful when considering further policy interventions to promote employee ownership. First, there is an increasing move towards services in the economy. The UK economy is increasingly shifting from manufacturing to services. The change involves the development of firms with greater focus on human capital through the recruitment, development, and retention of talent – all of which are positively influenced by models of employee ownership. Second, increasing economic turbulence, and therefore increasing uncertainty due to economic crises and Brexit calls for the development of more resilient businesses and communities – both of which are better supported by employee ownership models. Finally, there is increasing focus on corporate governance – especially greater emphasis on good practices by management teams. There is evidence to suggest that EOBs are better and more responsibly governed. This suggests that promotion of employee ownership and its values could have positively influence corporate governance.

While the evidence also identified some of the barriers to expanding employee ownership, in the recent years, there has been significant progress in promoting employee ownership. In 2012, The Nuttall Review [1] presented three main areas of policy intervention in support for employee ownership. These are (a) Raising awareness (b) Increasing resources available to support employee ownership and (c) Reducing the complexity of employee ownership. We find there has been progress along all three recommendations.

The Finance Act 2014: For employee ownership to spread, the most significant policy update is the introduction of tax exemptions for

companies owned by an EOT. The Finance Act 2014, Schedule 37, introduces three new tax reliefs to promote employee ownership. Employees of firms under direct employee ownership i.e. if the employer offers its employees company shares, already enjoy tax benefits such as not paying Income Tax or National Insurance on the value of the shares. The update in the Finance Act 2014, Schedule 37, puts employee Trust ownership on a par with the tax advantages enjoyed by direct employee share ownership.

We find that political interest in employee ownership is also growing. Over the past decades, successive governments have promoted different types of employee share ownership schemes; most notably Approved Profit Sharing (1979), the now discontinued Share Incentive Plan (2000) and policies to promote employee ownership, for example, Qualifying Employee Share Trust (1989) and more recently The Finance Act (2014). These initiatives have been accompanied by growing awareness, as well as increasing political support, for employee ownership (See for instance the Ownership Commission 2012, Hunt Review on Mutuals, 2014, and successive parliamentary group inquiries on the wider topic of employee ownership).

### **8.1 Points of transition to employee ownership**

The Employee Ownership Association notes that transition to employee ownership typically happens in one of the following scenarios:

- Business succession or ownership succession – private owners, such as an entrepreneur or family business, decide to sell to their workforce. The most typical route into employee ownership. From the oral hearings we find that there has been a significant increase in the awareness of transitioning to

employee ownership as a succession route, but clearly more work needs to be done

- Growth and Expansion: Partners, owners, or managers might decide to broaden ownership to cover most or all employees, reflecting the need to attract, retain and motivate talented people
- Public Service Spin-Outs: Sometimes called 'mutuals', these newly created businesses including social enterprises and community interest companies delivering public services may choose an employee led or owned solution as part of their structure
- Start Ups – as in the case of John Lewis, Arup Group or Scott Bader, the founder of a business opts for employee ownership at the outset of the business or later
- Insolvency or closure threat – employee buy-outs can prove an effective route to recovery for businesses that might otherwise fail

The main limitations and hurdles to expansion as identified by participants at the oral hearings are as follows:

## **8.2 Limited professional advisory support**

While on the one hand general awareness of the importance of seeking quality advice is increasing, and the cost of search for professional advice is coming down - largely due to the internet, word-of-mouth recommendations, and through the work of organisations such as EOA as well as the devolved governments in Wales and Scotland that provide subsidised support for the transition – there is persistent concern about the limited supply of high quality professional advisors. As a panellist pointed out: "...The level of knowledge of



EOTs is still woefully low amongst the professional advisory community at large. Sadly, that's the challenge for this entire sector, to get that option considered alongside trade sale and alongside sale to private equity". The issue is essentially the limited number of high quality advisors. "...it is a monumental step that is being taken, and it is one of those things where you really do need to have good advice. It is simply accessing that advice and having sufficient really good advisors out there that I think is one of the current problems. We will all agree that the advisors we had.... were excellent, but actually we're not talking about dozens and dozens out there"

The quality of advice came up as a strong theme in the discussion on transitioning. "...my big concern is that the advice that people get when they are thinking about becoming employee owned from a financial perspective is not good enough, so I don't think EOBs are getting sufficiently good [at] what I call corporate finance advice. There are very few of us around who can provide the advice in terms of what is right for the business. It's fine for the telling owners to go into a vendor finance model, but that may or may not be right for the business. So my concern is that the business gets the right financial advice alongside the legal advice"

### **8.3 Limited organisational readiness support**

The evidence indicates the need to better understand and develop organisational and leadership skills for managing EOBs prior to transition. In most instances, respondents making the transition rely on advice from a variety of sources such as EOA, owners who have gone through a similar transition, or employees who have prior experience of working in EOBs. Or they learn through trial and error. As one respondent notes "...you wouldn't get somebody who has done

say, a GCSE in Accountancy to advise you on tax implications, you would go to professional help – and I think people who are experts in transition, or in change or of organisational structure, who can help you navigate your way through. The challenges that you are going to face. Supported by access to other businesses that have been through this, the combination of that will be quite dynamic in helping organisations prepare and embrace the changes that they’re going to face”.

#### **8.4 Limited curricula in education**

Awareness about employee ownership in the labour market is low partly due to absence of the topic in higher education and business school curricula. This is most evident during recruitment of graduates. Although there is positive interest from millennials who often identify with the ethos of being employee owned, lack of knowledge often hampers recruitment. As a respondent points out “...we run businesses that are going to be maintained by the millennial generation, and the millennial generation are interested in very different things than our generations... our millennials in our business were very clear what they wanted: They wanted a voice, they wanted to be listened to, they want to be trained and developed. They don’t care about salaries; it’s not their number one thing any longer. Too many times business looks at things from a different perspective. They’re [millennials] wanting the things that employee ownership and a governance structure that listens and responds [offers]. I think that’s the really important message isn’t it? [To] listen and respond.”

## 9 Concluding remarks

The evidence of the impact of employee ownership on performance is overwhelmingly positive. The clearest evidence is for smaller firms, firms with larger employee ownership stakes, and in studies over longer time horizons. Employee owned firms tend to be more productive, have higher employee engagement along factors like rewards sharing, job satisfaction, organisational commitment, and motivation – which is reflected in higher retention and lower absenteeism. Employee owned business are more resilient in crises and appear to have a positive impact in the wider community. This evidence has salience in the current economic climate.

The UK economy is increasingly shifting from manufacturing to services. The increasing shift involves the development of firms with greater focus on human capital through the attraction, development, and retention of talent – all of which are positively influenced by models of employee ownership.

Increasing uncertainty due to economic crises and Brexit calls for the development of more resilient businesses and communities – both of which are better supported by employee ownership models. While the general awareness of employee ownership models is improving, complexities involved in transitioning appears to be a significant hurdle. This can be more actively addressed through the combined work of policy makers and employee ownership champions in generating awareness, providing incentives, and creating best practices.

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## Appendix I: List of contributors

3BM Ltd	Classic Motor Cars
4-consulting	Community Dental Services
A G Parfett & Sons Ltd	Computer Application Service
Aber Instruments	Cooperative Development Scotland
Accord Energy Solutions	Co-operatives UK
ADP Architecture Ltd	Co-ownership Solutions LLP
Agilisys Ltd	CSH Surrey
Alfa Leisureplex Group	Cubiks Group Ltd
Allied Irish Bank	Cullinan Studio
Aquascot Ltd	David Narro Associates
ARUP	Donald Insall Associates
Barnard & Westwood	EA Gibson Shipbrokers
Baxendale	Eden Nuclear & Environment
Bennetts Associates	Employee Owners Group
Black Light	Flowstore Systems Limited
BPR Architects	Golder Associates Corporation
Broomfield & Alexander Limited	Gripple
Cambridge Weight Plan	Hayes Davidson
Camlab Ltd	InSync Technology
Capital for Colleagues	J Gadd Associates
Castlefield	John Lewis Partnership
Childbase Partnership	Leading Lives
City Healthcare Partnership CIC	Lloyds Bank
Clarke Nicklin LLP	Loosemore Solicitors
	Make Ltd
	Mike Stoane Lighting

Mishcon de Reya LLP	Stride Treglown
MJP Architects	Swann Morton
Mooncup Ltd	Symology
Mott MacDonald	TateHindle Ltd
Network ROI	Team Medical Devices Limited
Noble Grossart Limited	The Gateway Dental Practice
Novograf	The Homebuilding Centre Limited T/A The
OPM	National Self Build & Renovation Centre
PB Design & Planning	The RM2 Partnership
Pett Franklin	The Useful Simple Trust
Pollitt & Partners Limited	Tibbalds Planning & Urban Design
Postlethwaite Solicitors	TLT Solicitors
Prospects	Toucan Computing
Quintessa	Tregroes Waffle Bakery Ltd
Remploy	Tullis Russell
Rinova Ltd	Turley Associates
Rowlinson Knitwear	Union Industries
RSM	Unity Trust Bank
Saxton Bamfylde	Wales Co-operative Centre
School Trends	Wales Finance Investments
Scott & Fyfe	WCF Ltd
Scott Bader	Wessex Eagle T/A Eagle Plant
Shakespeare Martineau	Wise Group
Shawston Holdings Ltd	Woollard & Henry
Skye Instruments	Wrigleys Solicitors
Steer Davies Gleaves	
Stephens Scowns LLP	

## Appendix II: Number of participants at oral hearings by topics

	London	Birmingham	Manchester	Wales	Scotland
Performance & productivity	10	3	4	3	3
Corporate governance	12	3	3	4	3
Business succession & growth	7	3	3	3	4
Advisors	6	3	3	4	3

*Note: Some participants have provided evidence to more than one topic*

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Prof Joseph Lampel, Eddie Davies Professor of Enterprise and Innovation Management at Alliance Manchester Business School, University of Manchester. His work with Ajay Bhalla on the economic performance of UK employee-owned businesses, has been funded by John Lewis Partnership, and the UK Department for Business, Innovation, and Skills and has been extensively used to encourage employee ownership in UK.



**Dr Aneesh Banerjee**, Lecturer in Management, Cass Business School, City, University of London. His research is in technology, innovation management, and employee ownership.



**Prof Ajay Bhalla**, Professor of Global Innovation and Family Business at Cass Business School, City, University of London. He and Joseph Lampel have a long-standing collaboration on researching employee ownership.