SCOTLAND's ECONOMIC FUTURE POST-2014

SUBMISSION FROM *STRENGTHENING DEMOCRACY* PROGRAMME

This response relates to the '*Welfare and equality'* and the *'Scotland at home and abroad'* themes identified in the call for evidence.

About Strengthening Democracy

In 2013, the Strengthening Democracy programme hosted a series of international workshops in Scotland, funded by the Scottish Universities Insight Institute. Invited participants from practice, policy and academic backgrounds met over the year to share experiences, research and ideas and to deliberate on how we can strengthen democracy in our workplaces and communities. The programme identified a need for Scotland to introduce an **Employee Right-to-Buy.**

Redistribution of wealth and income

While the redistribution of land through collective ownership continues to be seen by the Scottish Government as a direct route to community development and wealth, other assets, such as business organisations, have not been considered as means to redistribute wealth and income. Yet the evidence is apparent that employee owned organisations spread wealth more widely (perhaps the only non-fiscal way to counter rising inequality), and are more resilient and innovative than conventionally owned businesses (McQuaid 2013). Such local businesses can often be essential to community resilience. For example, they have a powerful local economic multiplier effect that is lacking in companies with absentee owners.

Redistributive effects

An employee-owned company has a greater redistributive effect than a conventionally structured company.

The wealth created is not extracted from the community to distant financial institutions, but is divided between being invested in the business and distributed to local families.

The **local economic multiplier** is massive.

Economic Multiplier: John Lewis vs. Marks and Spencer.

The most recent figures from employee-owned John Lewis Partnership and from Marks and Spencer are revealing. They are very similar in size (JLP £9.5 billion sales, M&S £10 billion; JLP 84,000 people, M&S 81,000 [note that the employee-owned company has, typically, created more jobs for the same turnover]) JLP distributed £210 million to the employees, which went out with no transaction cost, the same percent of salary to every employee. This made a difference to 84,000 or so families, who paid their tax and spent the cash on ordinary things, lifting the local economy in every area where there is a store. By contrast, M&S paid out £268 million, which went overwhelmingly to City institutions, many of whom have sophisticated ways of avoiding paying tax; it will have incurred very significant transactions costs in the form of fees to the people who run these institutions; and it will largely have been 'invested' in hedge funds, derivative contracts and similarly unproductive instruments. The effect on the local economy will have been pretty well zero, as also on child poverty. Since this is a low-paid industry, that is a relevant point: the JLP effect was positive on child poverty, but not M&S. Almost certainly less tax was paid from the larger distribution from M&S than was paid on the lower sum from JLP.

Economic Multiplier: Tullis Russell

While Tullis Russell had always done well in family ownership, on completion of its employee buyout in 1994 its productivity took off, and it is still going strong in employee ownership as 9 out of 10 Scottish paper mills have closed.

Economic Multiplier: Woollard & Henry

In 2002 Woollard and Henry's owner announced that it was closing, but an employee buyout transformed its destiny, bring a string of innovations, entering new markets, winning a prestigious export award and multiplying its profit at least tenfold in ten years to some £750,000, most of which is reinvested with the rest distributed as substantial profit shares for its employees, who spend the money mainly in the local community.

Where there are clusters of employee-owned businesses, they produce a positive effect on community **welfare**, with numerous positive knock-on effects. A pilot study (Erdal 1999) in Italy, partly replicated in Spain (Gago and Freundlich 2013), suggests that as well as better educational performance, lower domestic violence, wider and more supportive social networks and greater support for local government and for charities, people live longer. (This latter observation was checked with the John Lewis Partnership pension fund, whose actuaries identified the same effect among their retirees).

The people tend to become more **active citizens**, using the participative skills learned and confidence developed at work. This has a direct positive effect on participation in the community at multiple levels. The best research on this was done in Canada at the large Algoma steel plant employee buyout (Broad and Savory-Gordon 2006), which supported the claims that where employees are given a democratic voice they carry these participatory skills and attitudes into other walks of life.

Economically, a large body of studies from the 1987 study of ESOPs by the US General Accounting Office (GAO 1987) to ‘Shared Capitalism at Work’, the latest authoritative book by Harvard and Rutgers economists (Kruse et al 2011) shows that employee owned companies, by comparison with matched conventional companies:

- promote **equality** through a real and local sharing of resources and benefits
- do more training and education
- retain wealth within local areas (the shareholders are the employees of the business)
- spread wealth more widely across social strata

- are rated more highly for service by customers
- are more productive
- create more jobs
- sustain the jobs better through recessions

In **human** terms, people working in employee-owned businesses:

- stay longer
- understand business better
- learn skills of participation
- gain confidence in participation
- find work fulfilling to a greater extent (and frustrating to a much lower extent)

(e.g. Broad and Savory-Gordon 2006; Matrix, 2010; Lampel et al 2010)

So even if there is no formal mechanism for making a company serve the local community, an employee-owned company, just in the normal course of business, has multiple positive effects.

Scotland at home and abroad

Employee right to buy legislation for companies in administration has applied in Spain since the mid 1980s (Sociedades Laborales, see Jensen 2011), and they have successfully rescued many hundreds of businesses and thousands of jobs – particularly in rural areas. In Italy, the Marcora Law, introduced in 1985 "has both funding powers and the ability to target support when nine or more workers are facing redundancy as a result of bankruptcy, business sale or offshoring the legal right to bid to buy out the business, with a matching state investment of up to three times the workers' own investment" (Foster & Leonard, 2013).

Policy Relevance

1. We suggest an **Employee Right-to-Buy** where there is a business which,
   *is being sold, on the market, or in administration
   *plays an important role in a community (either as a major employer, or providing a significant service to the community)
   *will act to preserve communities in which the business/organisation is situated.
2. The market for companies is a very well established market: buying and selling companies takes place all the time.
3. The specific form of buyout, the all-employee buyout using a trust (Employee Benefit Trust) for all the employees, has been widely and increasingly used and is quite simple to complete. Scottish examples include Tullis Russell, West Highland Free Press, Clansman Dynamics, Woollard and Henry, Highland Home Carers, Page & Park Architects, and Stewartry Care.
4. Employee owned organisations are demonstrably more resilient and innovative than conventionally owned businesses. Simply expecting accountants and lawyers to promote this model has, over many years, proved ineffective in growing the sector. It requires legislation.

5. There is no legal reason why a local community and an employee-community could not jointly own a community anchor business. The business would still be held in trust for the benefit of the community of place and community of interest.
6. Current employee-owned organisations (including Clansman Dynamics and Baxendale), have a clause in their Trust Deeds which specifies that should the employees ever vote to sell the business, then the assets of the trust, on winding up, are gifted to charity. There are two main routes that are commonly used in employee owned companies:

i. The Employee benefit Trust has as one of its beneficiaries a charity – either named specifically, described by location or purpose or left entirely open to the discretion of the trustees, but rarely so open that the funds can be directed to a charity of questionable track record.

ii. The granting of an option to acquire shares to a body, which might be a specific charity or other organisation. The option being exercised at nil or nominal cost and only on specific events such as a sale of the business (John Alexander, Director, Baxendale)

Both of the above are appropriate instruments to avoid employees thinking of the shares in the company held for collective benefit as being something they can sell for short term personal gain. Using this model in an Employee-Community Right-to-Buy would mean any buy-out could not be resold for profit. If a fund, along the lines of the Scottish Land Fund for community buy-outs, were in the future to become available we suggest that this fund becomes the legal recipient of the proceeds of any sale, thus allowing the money to be reinvested in employee-community buy-outs.

Employee-owned companies not only have hugely important redistributive effect, but also generate growth and promote welfare for those involved, and for their communities. To the extent that sufficient powers rest with the Scottish Government, an **Employee Right-to-Buy** policy should be pursued.

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January 2014