
OWNERSHIP CULTURE AND STRATEGIC ADAPTABILITY

Peter B. Thompson

University of Illinois at Chicago • Chicago, IL

Mark Shanley

University of Illinois at Chicago • Chicago, IL

Abigail McWilliams

University of Illinois at Chicago • Chicago, IL

ABSTRACT

Although abundant evidence demonstrates a positive relationship between employee ownership and firm performance, two questions remain unanswered: why does employee ownership fail to enhance the performance of some adopting firms, and what are the mechanisms by which employee ownership enhances performance? We argue that employee ownership has the potential to enable managers to shape organizational culture in support of firm strategy. In supporting firm strategy, employee ownership has the status of strategic choice. Further, to the extent that organizational culture is strategy-appropriate, it leads to competitive advantage by increasing the availability of resources, the serviceability of those resources to the firm, and flexibility in the allocation of resources to address competitive threats and opportunities. When managers of employee-owned firms are unable to create such a culture, the performance of their firms suffers as a result.

INTRODUCTION

Strategic management, often called ‘policy’ or nowadays simply ‘strategy’...includes those subjects which are of primary concern to senior management, or to anyone seeking reasons for the success and failure among organizations.

Rumelt, Schendel, and Teece (1991)

Why do employee-owned companies perform better, on average, than conventionally-owned companies? And why do some ESOP companies perform better than others?

Employee ownership, also called “shared capitalism” (SC), or “earned capitalism” (EC), a term that includes employee stock ownership plans (ESOPs) stock

purchase plans, profit- and gainsharing plans, and broad-based stock options (Kruse, Freeman, and Blasi (2010), is a management practice that has been utilized by firms for decades.¹

Partly a tool of corporate finance, and partly a tool of human resource management, ESOPs have become a small yet significant part of the economic landscape. Congress created the ESOP in the 1974 Employee Retirement Income Security Act (ERISA), which established the legal basis for ESOPs as a defined contribution retirement plan. Laws and regulations pertaining to ESOPs are regularly considered by Congress and reported in the press. During the last two decades, the number of ESOP firms has held steady at around 10,000 firms (NCEO, 2008).

ESOPs have a dual nature. On the one hand, they are a tool of corporate finance. For instance, the law permits the employee stock ownership trust (ESOT) to borrow money for the purpose of purchasing shares. As such it is a mechanism for raising capital or restructuring the balance sheet. And, they can be used to alter the governance structure of a company. However, as a tool of human resource management employee ownership has the potential to have a much greater impact on firm performance than do alterations to the right-hand side of the balance sheet. This is the basis of our discussion.

There have been a large number of studies attempting to show that EO activities “work” – that they have results that are beneficial to a firm’s overall results. A considerable body of empirical work has demonstrated a positive link between employee ownership and firm financial performance (to be discussed in detail below). Research has also demonstrated some positive effects of EO programs on individual attitudes and behavior (to be discussed in detail below). While both of these lines of research are promising, there is a gap in the theoretical basis of this work that limits its usefulness. Specifically, there is a need for a clearer delineation of the mechanisms by which EO programs work at the individual level in motivating employees and yet are seen as contributing to significant firm level performance outcomes.

Explanations tend to point vaguely at factors such as increased motivation, culture, information sharing, even a multi-period prisoner’s dilemma, but generally lack detail. To compound the deficiency, no theory of which we are aware addresses the question of exactly how individual-level outcomes produce firm-level outcomes.

 This gap in the research is due to scholars approaching the topic from different disciplines and from studying the ownership phenomenon from a single level of analysis.

¹For a typology of employee ownership, see Toscano, 1983; Ben-Ner and Jones, 1995.

²For details of the financial, tax, and other technical characteristics of an ESOP, Smiley, Gilbert, Binns, Ludwig, and Rosen (2007) present an excellent discussion.

Because an empirical demonstration of (a) multi-level linkage(s) would be a monumental undertaking, requiring the simultaneous collection of data from two levels of analysis—individual-level *and* firm-level—and from a large sample of firms, it is not surprising that this knowledge gap persists. To our knowledge, this multi-level feat has been attempted only rarely (Klein, 1987; Kruse, Freeman, and Blasi, 2010; Rosen, and Quarrey, 1987; Rosen, Klein, and Young, 1986). Practical obstacles such as collecting individual-level data from a large number of firms have to date limited researchers' progress in describing the complete causal chain linking these programs with corporate performance. As a consequence of the practical difficulties of uncovering causal mechanisms, the nature of those links remains a matter of speculation. The *employee ownership*→*individual outcomes*→*firm outcomes* linkage is a complex phenomenon that is not fully understood and not every study has shown a positive relationship (Kruse, Freeman, and Blasi, 2010).

BACKGROUND—EMPLOYEE OWNERSHIP RESEARCH

Employee ownership, whether realized in ESOPs or other forms, has been studied from multiple perspectives.² It has been treated extensively by political scientists (e.g., Al-Saigh, and Buera, 1990; Alperovitz, 1997; Bradley, 1986; Dugger, 1987; Gibson-Graham, 2003; Gunn, 2000; Howe, 1986; Miller, 2003; Mygind and Rock, 1993; Steinherr, 1978); philosophers (e.g., Mill, 1871, 1998; Miller, 2003) sociologists (e.g., Whyte, and Blasi, 1982, 1984); economists (e.g., Ben-Ner, 1988, Blinder, 1990; Doucouliagos, 1990, 1995; Fama, and Jensen, 1983; Kruse and Blasi, 1997; Kruse, Freeman, and Blasi, 2010; Vanek, 1976) legal scholars (e.g., Ellerman, 1984; Hansmann, 1990), and management scholars (e.g., Conte, and Svejnar, 1990; Klein, 1987; Pierce, and Rogers, 2003) Pierce, Kostova, and Dirks, 2001; Pierce, Rubinfeld, and Morgan, 1991; Rousseau, and Shperling, 2003).³

In addition, a vigorous practitioner literature extols the virtues of employee ownership (e.g., Brohawn, 1997; Gates, 1998; Quarrey, Blasi, and Rosen, 1986; Rosen, and Carberry, 2003; Rosen, and Rodgers, 2007, 2011; Rosen and Young, 1991; Rosen, Klein, and Young, 1986; Rosen, Case, and Staubus, 2005; Young, Rosen, and Carberry, 1995). The central question motivating the bulk of this work is the relationship between employee ownership and firm performance.

²The authors wish to thank the following for their helpful suggestions: Ginny Vanderslice, Corey Rosen, Anne-Laure Winkler, and Jack Veale. Thanks also to our anonymous reviewers for their insightful comments.

³There are several excellent reviews of the employee ownership / shared capitalism literature, including for example, Blasi, Conte and Kruse, 1992; Bonin, Jones and Putterman, 1993; Carberry, 2011; Freeman, 2007; Kruse and Blasi, 1997; and the introduction to the monograph by Kruse, Freeman, and Blasi, 2010).

Table 1
Employee Ownership Outcomes
Individual Level

Outcome	Authors
Satisfaction	Greenberg, 1980 Hammer, Stern and Gurdon, 1982 Long 1978a. 1978b, 1980, 1982 Kruse, 1984 Tucker, Nock and Toscano, 1989 Buchko, 1993 French and Rosenstein, 1984 Russell, Hochner, and Perry, 1979
Would Take the Same Job Again	Russell, Hochner, and Perry, 1979
Organizational Commitment / Identification	Hammer, Stern and & Gurdon, 1982 Keef 1994 Long 1978a. 1978b, 1980 Oliver, 1984 Rhodes and Steers, 1981 Russell, Hochner, and Perry, 1979 Long, 1982 Tucker, Nock and Toscano, 1989 French and Rosenstein, 1984 Oliver, 1990
Motivation, ESOP Satisfaction	Goldstein, 1978 Kruse, 1984 Long 1978a. 1978b, 1980 Rhodes and Steers, 1981 Russell, Hochner, and Perry, 1979 Long, 1982 Buchko, 1992, 1993 Klein and Hall, 1988 Rosen, Klein, and Young, 1986
Perceived and Desired Influence Under Employee Ownership	Goldstein, 1978 Hammer, Stern and & Gurdon, 1982 Kruse, 1984 Long, 1979, 1981, 1982 Rhodes and Steers, 1981 Russell, Hochner, and Perry, 1979 Sockell, 1985 Hammer and Stern, 1980

Table 1 (cont.)
Employee Ownership Outcomes
Firm Level

Turnover, Absenteeism, Tardiness, Injuries	Buchko, 1992, 1993 Hammer, Landau, and Stern 1981 Kruse, 1984 Rooney, 1992
Sales, and Sales per Employee	Bell and Kruse, 1995 Bloom, 1985 Dunbar and Kumbhakar, 1992 Kumbhakar and Dunbar, 1993 Kruse, 1988, 1992, 1993
Return on Assets, Market Return	Bell and Kruse, 1995 Conte, Blasi, Kruse, and Jampani, 1996 Park and Song, 1995 U. S. Gov't Accounting Office, 1986
Tobin's Q, Value Added	Bell and Kruse, 1995 Kruse, 1993
Profitability	Mitchell, Lewin, and Lawler, 1990 U. S. Gov't Accounting Office, 1986

EMPIRICAL EVIDENCE

Firms sponsoring employee stock ownership plans tend to perform, on average, better than non-ESOP firms. Empirical studies have overwhelmingly shown a link between ESOPs and positive firm performance. However, the nature of that relationship, namely the mechanisms whereby employee stock ownership enhances organizational outcomes, remains obscure, raising the question—"Can ESOPs be a source of sustainable competitive advantage?"

Studies at the firm level of analysis document an *employee ownership*→*performance* link, while individual-level studies tend to focus on the *employee ownership*→*positive attitudes* link. (The divide between the individual-level and the firm-level streams is evident in Table 1.) Moreover, ESOP research has also demonstrated that the linkage between ESOP firms and superior outcomes is especially strong when employee ownership is combined with participatory management (Kruse, Freeman, and Blasi, 2010; Quarrey, Blasi, and Rosen, 1986; Rosen, Klein, and Young, 1986). The assertion *that* employee ownership is associated with superior performance has been settled, although *how* it affects firm performance remains an open question.⁴ Firm-level outcomes associated with employee ownership include reduced turnover, absenteeism, tardiness and injuries, and increased

sales, sales per employee, return on assets, market return, Tobin's Q, value added and profitability. (See Table 1 for citations.) Individual level outcomes include satisfaction, organizational commitment, motivation, satisfaction with ESOP, increased perceived influence, and increased desired influence.

When the empirical research is considered as a whole it is reasonable to conclude that shared capital programs enhance or in some way facilitate individual-level outcomes that translate into positive organization-level outcomes. But—and this is an important qualification—even when taken together, the two streams of research can do no more than hint at a causal connection. This is because firm-level studies treat the firm as a black box, as they do not measure differences in inner processes that cause differences in performance. On the other hand, individual-level studies report differences between employees in employee-owned firms and employees in conventionally-owned firms, but do not measure the performance of those firms. (Some studies compare employee owners in a single firm with non-owners in the same firm (e.g., Long, 1978b). Nonetheless, in no study has the complete *employee ownership*→*individual differences*→*organizational outcomes* causal chain been observed or measured. It is essential that in order to show how interior processes lead to organizational outcomes, it is necessary to simultaneously observe and measure both internal processes and organizational outcomes across a sufficiently large set of firms. That is, it is necessary to conduct research at two levels of analysis. This point cannot be over-emphasized. As a consequence, our knowledge of the employee ownership phenomenon is incomplete and important questions remain unanswered:

(1) For instance, it is possible that the observed ownership→outcome relationship is spurious, that there is some third variable driving both performance and the creation of an ESOP. Candidates for this variable include the possibility that better-skilled managers are disposed to share returns with workers. Or, a particular management philosophy leads to both performance and employee ownership. Or, firms with some other form of competitive advantage wish to protect that advantage by linking employment with ownership.

(2) Alternatively, the linkage could be endogenous whereby better performing companies have the financial and human resources to implement an ESOP. (Setting up an ESOP is time-consuming and costly.)

⁴For example, Gary Becker and Richard Posner criticize the performance of ESOPs as stemming from their tax advantages to sponsoring firms rather than from their effects on workers and suggest that the rationale for such advantages is questionable given available evidence (Becker-Posner Blog, 4/08/07 - www.becker-posner-blog.com/2007/04/employee-ownership-through-esops-a-bad-bargain-becker.html).

(3) Another possibility is some serendipitous outcome resulting from an action taken for completely different reasons. For example, a few ESOPs have been created as a takeover defense, which could lead to the unexpected outcome of increased employee loyalty, motivation, and performance. Similar outcomes might devolve to a firm whose retiring owner, rather than cash out to an outsider, sells to the employees. There are a large number of reasons why firms institute ESOPs (See Table II), each with its own intended and unintended consequences.

Table 2
Reasons for Creating an ESOP

<ul style="list-style-type: none"> • provide an alternative to the fiscal responsibilities of a defined-benefit plan • provide an alternative to the fiscal responsibilities of another defined-contribution plan • raise capital for the firm more cheaply • repurchase stock • buy out minority or majority shareholders • or sell whole companies to employees • sell a company threatened with shut-down to its employees • or divest an unwanted division or subsidiary • defend against takeover or maximize internal control • carry out hostile or friendly takeovers by employees • give workers stock at no cost to the company • tax savings • defer compensation to increase cash flow • repurchase shares to increase leverage • cash out large shareholders without losing control • take a public company private • restructure right-hand side of balance sheet 	<ul style="list-style-type: none"> • finance a leveraged buyout of a public corporation • deduct employee dividends from corporate income • trade stock for wage or benefit concessions • develop a flexible compensation system • purchase life insurance for key executives or workers • resolve estate and estate-tax problems • use as a strategy in collective bargaining • increase the value and possibilities of charitable contributions • convert ownership of a proprietorship or partnership • refinance existing debt • finance acquisition of another company (Blasi, 1988), • restructure wages and benefits • institute pay-at-risk or variable pay • trade stock for wages • replace defined benefit plans • replace profit sharing plans.
--	---

Source: Blasi, (1988); Blasi & Kruse, (1991)

EXPLAINING ESOP PERFORMANCE

Surprisingly, none of the reasons listed in Table 2 have addressed the role that employee ownership might play in a firm's competitive strategy. The surprise is even more puzzling because instituting an ESOP is a major administrative undertaking.

Our novel contribution is the application of strategy theory to an unexamined phenomenon combined with an explanation of the performance results of employee-owned firms. Our main theme is that employee ownership programs in general and ESOPs in particular have the *potential* to be of strategic importance to firms in that they can render a company's existing culture more adaptable and capable of channeling employee motivation, effort, creativity, and buy-in to support overall firm results. Realizing competitive potential is not easy, which is why some ESOP firms do not perform well and eventually drop out of the ESOP population.

Here we propose a theoretical framework to guide empirical study of our two questions: "Why do employee-owned companies perform better, on average, than conventionally-owned companies?" And "Why do some ESOP companies perform better than other ESOP companies?" Answering these questions requires a framework that meets three criteria: it must be consistent with empirical observations, account for ownership phenomena at two levels of analysis and the interaction(s) between those levels, and be empirically testable.

FINDINGS SO FAR

To summarize the foregoing discussion of the studies listed in Table 1, at the individual level of analysis we know that:

1. employees who participate in an ESOP tend to be more satisfied than non-participants
2. employees who participate in ESOPs report greater motivation than non-participants.
3. the greater the portion of an employee's wealth that is invested in company stock the greater the employee's commitment and satisfaction

At the firm level of analysis we know that:

1. ESOP companies perform better, on average, than conventionally-owned companies
2. not all ESOP companies are high performers
3. ESOP companies that practice participatory management tend to perform better
4. ESOP firms are continuously created and terminated

These findings raise intriguing questions, while failing to explain the performance of ESOP companies. For instance, do individual-level satisfaction and motivation account for enhanced firm-level performance? What role does the size of an employee's stake in the firm play in firm performance? What accounts for the variance in firm performance across ESOP companies? What is the effect of participatory management—is it a moderator, mediator, or primary cause? Why are ESOPs continuously created and why do they disappear?

Motivation—individual level effects. One possible explanation for the superior performance of ESOPs is that employee ownership is an incentive that motivates workers to work harder, increasing efficiency. Criticisms of the assertion that employee ownership leads to productivity often rest on the observation that employee ownership is a reward system, and a group reward system at that. While it is true that there are (often substantial) financial rewards associated with ESOPs, the more important rewards are *intrinsic*. We address this point below.

Table 3 lists six practices recommend by Rosen and Rogers (2011) for building an ownership culture. Next to them, we have listed motivation theories that could explain why the component increases motivation. The list suggests that there appears to be ample theoretical support for increased motivation among employee owners. And, it is true that employees may be motivated by incentives—but to do what? Individual motivation alone is not enough to explain the effect of employee ownership on firm performance. Rather, the effects of an ESOP have been observed at both the firm level as well as the individual level so it is more likely the case that individual effort is directed not only toward each employee's individual goal, but also toward a single, firm-level goal. Put another way, having an emotional, psychological investment in the success of an ESOP has the potential to motivate an employee beyond her individual task(s) provided that individual motivation from an ESOP is linked to firm goals on account of the efforts of and messages from management.

Rosen and Rogers (2011) debunk the individual-level motivation explanation for firm performance with a numerical example: Assume that labor accounts for 30% of a firm's costs. Suppose further that about half the workers are fully engaged, and the other half are "incorrigibles," indisposed to work hard no matter what. How many more minutes of labor will the engaged workers contribute? Assuming they would work an additional 30 minutes, what effect would a 'powerful' incentive system have on costs? Only about one percent!

$$\begin{aligned}
 & 0.5 \text{ Percentage of engaged workers} \\
 \times & .067 \text{ Extra time worked i.e., from 7.5 hours to a full 8 hours} \\
 \times & .30 \text{ Percentage of operating costs owing to labor} \\
 = & 1.0\% \text{ Cost savings}
 \end{aligned}$$

Even more generous assumptions yield similarly unimpressive results. This example underscores the faulty logic of aggregating individual outcomes in order to explain a group outcome (Danserau and Cho, 2006; Kozlowski, and Klein, 2000; Rousseau, 1985).

The question now is: If a general increase in individuals' aggregate motivation is unlikely to have a meaningful effect on firm performance, what role does individual-level motivation play in firm performance? In other words, what are the processes by which these six components drive *organizational* outcomes? We must look for a mechanism by which individual activity (perception, attitude and behavior) engender firm-level results. Again, Rosen and Rodgers (2011) offer an answer: Rather than working harder, the effect of an ownership culture is to stimulate employee owners to "work smarter."

Table 3
Prescriptions for Creating an Ownership Culture

Components of an Ownership Culture	Possible Theoretical Explanation
<ul style="list-style-type: none"> • Level of ownership that is financially significant to employees 	<ul style="list-style-type: none"> • Expectancy Theory (Valence) • Two Factory Theory (Hygiene Factors)
<ul style="list-style-type: none"> • Understanding of the terms and conditions of the ownership plan 	<ul style="list-style-type: none"> • Expectancy Theory (Instrumentality) • Goal Setting Theory
<ul style="list-style-type: none"> • Skills training to increase effectiveness 	<ul style="list-style-type: none"> • Self Efficacy Theory • Path-Goal Theory
<ul style="list-style-type: none"> • Sharing financial and performance information with employees 	<ul style="list-style-type: none"> • Instrumentality (Expectancy Theory)
<ul style="list-style-type: none"> • Short-term financial incentives like profit-sharing and bonuses (in addition to the long-term benefits of stock ownership) 	<ul style="list-style-type: none"> • Reinforcement Theory
<ul style="list-style-type: none"> • Employees have structured, regular opportunities to have meaningful input into decisions concerning the work they do. 	<ul style="list-style-type: none"> • Voice • Job Characteristics Model (Feedback, Autonomy) • Two Factory Theory (Motivating Factors)

Source: Rosen and Rodgers, 2011

Ownership culture. The explanation most often given for the observed ownership→performance linkage is that these ESOPs create an *ownership culture* that contributes to superior performance. While this general conclusion is defensible, we believe along with others (Freeman, 2007; Kruse and Blasi, 1997; Kruse, Freeman, and Blasi, 2010) that it is overly simplistic to argue that the simple adoption of employee ownership programs or continuing stable levels of employee participation in those programs improve firm performance. The census of ESOPs, for example, is in dynamic equilibrium as existing ESOPs are terminated and new ones created (NCEO, 2008). This would be hard to predict from simple adoption rates and participation levels and suggests that other forces are needed to explain the linkage between employee ownership and firm performance. Meantime, the census changes continuously as firms terminate ESOPs and new ones are created.

The concept of an ownership culture may be best introduced with a thought experiment. The reader might want to contemplate something he or she owns—a car, a house, a prized work of art. You probably know how much you paid for your car, the mileage you have put on it, and when it is due for service. Likewise, you probably know the balance owed on your home mortgage, the amount of real estate taxes, and which repairs are needed. Yet, if you rent an apartment, how likely is it that you know the amount of real estate taxes? Consider another example: many travelers have had the experience of boarding a taxi at a strange airport and noticing its condition. If it is owned by the driver, it is likely to be clean, well maintained, and pleasant. Drivers who lease their cabs do not take such good care of the company's vehicle.

Property rights. Ownership consists of three property rights: knowledge pertaining to the object owned, control over the object, and the right to residuals (Rousseau and Shperling, 2003). Participants in an ESOP enjoy all three. As owners, they are entitled to increases (or decreases!) in the stock price, and to dividends. In ESOP companies practicing participatory management, employees can exert some degree of control. This is especially true when voting rights are passed through to employees.⁷ And finally, some, but not all, ESOP companies practice open book management (Case, 1995; Sockell, 1985) by sharing financial and operating information as a part of their “communication and participation” (C&P) programs (See below.). Employee owners, like independent taxi drivers, have a special relationship with their work.

⁷Technically, an employee stock ownership trust (ESOT) owns the employees' shares. Depending upon how the employee ownership Plan Document is written, the trustee(s) may vote those shares themselves or pass voting rights through to the employees.

Effective ownership culture and competitive advantage. Ownership culture can be a resource that leads to competitive advantage according to the VRIO theory developed by Barney (1991). According to this theory, competitive advantage is derived from the effective management of heterogeneous resources that are valuable (to the consumer), rare (not abundantly traded in markets), inimitable (not readily imitated) and which the organization is ready and able to exploit. Ownership culture is valuable, relatively rare and hard to imitate, so that with the correct organizational support such as effective strategic planning and excellent evaluation and control, management can create a more effective and efficient firm. Accordingly, we first present the mechanism by which an ESOP has the potential to lead to competitive advantage (See Figure 1), and then examine ESOPs within the VRIO framework.

Firm level. An ESOP by itself does not confer competitive advantage, as noted above. Instead, it must be managed deliberately to enhance existing culture—to nudge as it were firm-specific values, beliefs, and norms in support of the firm’s (changing) strategy. As the empirical research suggests, an ESOP must be combined with participation in order to produce superior firm results. Technically, an ESOP is a defined contribution benefit plan that provides employees with shares that they can cash in upon retirement. This has a cross-level effect of providing extrinsic rewards at the individual level. In addition to extrinsic, albeit deferred, rewards, an ESOP’s enhancing potential lies in combining it with “participation and communication programs” or their equivalent.

Individual level. Participation and communication programs encourage participation, cooperation, group identity, and other psychological states that are intrinsically satisfying. Two psychological states that are particularly important for the development of an ownership culture are *shared risk* and *commitment to group goals* (discussed below). The achievement of an uncertain goal to which all members of a group are committed is intrinsically satisfying, nowhere more evident than a sports team that has just won a challenging championship game. Intrinsic rewards do not pay the bills, but company stock on top of salaries, bonuses, wages and sometimes even profit sharing do pay the bills. Neither alone is enough to create an ownership culture.

Emergence⁸. But when extrinsic and intrinsic rewards are combined, they can foster an “ownership culture,” which may—if management is skilled enough—



Shared unit properties are presumed...to originate in individual...members’ experiences...and to converge among group members....In this way shared unit properties emerge as a consensual, collective aspect of the unit as a whole.” (Kozlowski and Klein, 2000: 30)

enable the company to make strategic changes more rapidly than the competition. Ownership alone is not sufficient to shape culture. And participation without ownership is nothing less than manipulation. The two together succeed because financial ownership makes the work of participation worthwhile to the employee. Information sharing, cooperation, mutual monitoring and similar norms—however intrinsically satisfying they may be—require extra effort, so must be reinforced with monetary rewards to have an effect on culture. With respect to ESOPs competitive advantage is not one thing, but rather a combination of financial ownership and psychological engagement applied to competitive threats and opportunities.

(V) Value creation. In order to be successful the content of a culture must be open to adaptation (Kotter, and Heskett, 1992). By its definition, firm culture has an inertial and conservative bias to it, since it represents the cumulative sense making activities of individuals regarding a firm's history. Further, "All too often, major organizational change occurs only when an organization is in serious trouble and is faced with complete failure." (Lawler, 1994: xxxv). The firm's culture must make sense out of past experiences with the firm, while also permitting the possibility of growth and adaptation. If the potential for growth and adaptation are not there, then the culture will be inertial and resistant to change, and the economic impact of the firm's culture will be one of increased rather than reduced implementation costs. Finally, the content of the culture should support the details of the firm's strategy and not be antagonistic to them. Each firm's culture is unique and there is no one best culture; therefore, culture is a heterogeneous resource in the Barney (1991) framework.

Any culture has the potential to be a source of competitive advantage in that certain core values and beliefs about how a company ought to conduct its business may be transformed into value-creating decisions and actions. An ownership culture has more value-creating potential than other cultures because it satisfies a higher order need, that is, the desire to help the firm prosper. An ESOP enables management to shape or change culture more effectively and more rapidly than would otherwise be possible in the absence of such a program. It amplifies management's influence and its ability to engage workers more deeply. The financial rewards that such programs offer to participants are complemented by the more intrinsic rewards that come from achieving performance goals within an ownership culture—rewards that include increased levels of job satisfaction, personal autonomy, and even organizational commitment (Buchko, 1993; Chiu, 2003; Klein, 1987; Klein and Hall, 1988). Besides focusing participant attention on firm goals, an ESOP has the capability to intensify the effect of culture on the willingness and ability of workers to ex-

ecute strategy. Value-creators include (1) increased efficiency in information sharing and processing and decision-making (Ben-Ner, 1988; Bonin, Jones, and Putterman, 1993); Conte and Svejnar, 1990; Young, Rosen, and Carberry, 1995; (2) increased self-monitoring while decreasing the need for supervision (Ben-Ner, 1988; Bonin, Jones, and Putterman, 1993; Conte, and Svejnar, 1990; Hansmann, 1990); and (3) increased cooperation among workers (FitzRoy and Kraft, 1987).

More important than the strength⁹ of a culture, though, is its adaptability (Kotter and Heskett, 1992). Because an ESOP aligns the (financial) interests of the firm with its employees, employees are more likely to be willing to change the way they do things to support new strategies in order to protect their emotional and financial investments—which they have paid for with their labor—as any entrepreneur or sole proprietor would do. In this lies the potential value of an ownership culture. However, employees' willingness to alter their behavior is conditioned upon whether they perceive that their effort will make a difference, and whether that difference will show up in their wallets (Lawler, 1994; Vroom, 1964). Accordingly, ESOP firms have the potential to deploy and redeploy those human resources quickly in order to adapt to changing conditions (Penrose, 1959). This is affected by the ability of an ESOP to facilitate cultural change more rapidly than the non-ESOP competition. An ESOP can accelerate cultural change when management is able to use it to demonstrate to the workforce that “the way we do things here” affects their interests for better or for worse as well as those of the company. In an ESOP those interests are linked or, more precisely, they are the same (Jensen and Meckling, 1976). This leads to our first two propositions regarding the value of ESOPs in supporting strategic change and flexibility.

Proposition 1(a): Changes in employee perceptions, attitudes, and behaviors occur more rapidly in ESOP firms supporting an ownership culture than in comparable non-ESOP firms.

Proposition 1(b): The time requirement for strategic change in an ESOP company is shorter than in comparable non-ESOP firms.

These changes in culture and improvements in flexibility make the ESOP valuable in the VRIO (Barney, 1991) sense.

(R) Rarity of effective ownership culture. As noted above, at any one time, there are about 10,000 ESOP concerns in the U. S. with employee stock ownership plans. This may not on first blush seem rare, but it does represent a very small

⁹The strength of culture may be measured by scores on the Organizational Culture Inventory (Cooke and Lafferty, 1987), or the Ownership Culture Survey (Mackin, Freundlich, Rodgers, and Kerr, 2012).

percentage of the firm population in the U.S. What is rarer is an effective ownership culture that depends on both the genesis and the management of the ESOP.

Reason for creating ESOP. Not all ESOPs are instituted with employee participation, the enhancement of human capital, etc., as primary concerns. Many are established to realize tax benefits, cash out a retiring owner, protect against a takeover, or for similar non-human capital (i.e., non-cultural) purposes (See Table 2). Accordingly, one could make the case that instituting an ESOP in order to foster an ownership culture is relatively rare. One could also argue that fostering an ownership culture requires a significant investment of firm resources, thereby reducing the number of firms for whom such an investment is affordable.

Further, rarity is a matter of degree—some things are scarcer than others. There is no one best ownership culture, but many. It is not a question of having one or not. Rather, it is a question of degree and of fit. Unlike a patent or a corner location, the fit between culture and strategy can vary between good and bad, along a lengthy continuum. Rarity lies in the quality of execution, which is itself, a heterogeneous resource.

Because ownership culture is heterogeneous, we expect differences in ownership culture, including how it is managed, to account for differences in ESOP performance. Therefore, companies in which building a strategy-supportive culture is not the primary purpose of the ESOP, we would expect no direct *ownership*→*performance* effect. Alternatively, in companies whose management aspires to use an ESOP as a complement or enhancement to its H R policies and practices, we would expect superior firm performance, except that because of the difficulty in creating an ownership culture, not all ESOPs are likely to succeed. This is because, as Barney (1991) pointed out, a “particular mix” of resources is required to implement a strategy.

Note that several measures of culture are on the market (e.g. Cooke and Lafferty, 1987) including one specifically tailored for employee-owned companies available from the National Center for Employee Ownership (Mackin, Freundlich, Rodgers, and Kerr, 2012). These measures are normative, so that the investigator can test his/her hypotheses by degree of deviation from the norm.

Proposition 2: Excluding ESOPs that were created solely for corporate finance or governance purposes, the failure to create a strategy-supportive “ownership culture” increases the likelihood of the failure of an ESOP.

Strength of culture. Most firms already have a culture (strong or weak), irrespective of the actions of managers, since the people in the firm will have some degree of shared values, beliefs, and norms of behavior. So it is not a question of

creating a new culture but of shaping a firm's existing culture. The first issue that managers must consider is whether the culture is supportive or not supportive of the firm's strategy because "culture constrains strategy" (Schein, 1985).

There must be sharing of knowledge, beliefs, and values so that the 'culture' is not just nominal and a mere conceptual artifact of aggregating a set of individuals. *Without a strong culture, shared capitalism programs like ESOPs are merely incentive programs that appeal to lower-order needs and are likely to lack strategic impact.*

Difficulty. An ownership culture is difficult to cultivate, but not impossible, which may also account for the extent to which it is rare. In addition to the host of ESOP advisors, attorneys, investment bankers, commercial bankers, and compensation firms, there are experienced and dedicated organization development consultants and other practitioners who stand ready to institute an ESOP, a participation and communication program (see below), or an ownership culture for their clients. So, ESOPs are to a certain degree off-the-shelf.

Participation and communication programs. Management can influence culture in support of firm strategies by fostering supportive institutions (such as ESOPs) and their related practices (Scott, 2008). By establishing clear and objective sets of rules and procedures that link firm goals and operations with employee incentives and compensation, employee ownership programs focus employee attention around core values and activities and link individuals and groups to the goals of the firm and to firm performance. Once established these programs persist and grow and in doing so become routine for employees, even taken for granted. This is the process of institutionalization (Aldrich, 1999: 48-49), as exemplified by the prescriptions in Table 3. As ESOPs become institutions, they provide an objective focus for individuals in the firm that strengthens the link between culture and strategy.

To sustain an ownership culture, many (but not all) ESOP companies invest considerable time and effort in their "participation and communication" programs. The intent of these programs is to shape perceptions and attitudes by increasing employee awareness and understanding of the ESOP of which they are the beneficiary. In addition to providing general information about ESOPs, some participation and communication programs are intensely firm-specific. In addition, many firms practice "open book management" (e.g., Case, 1995; Stack, 1994). These firms not only share financial information with employees, but also offer instruction to teach employees to read and understand financial information so that employees fully appreciate the benefits (and risks) of owning the company's stock. Their purpose is to create a clear "line of sight" between effort and reward (Lawler, 1995). Train-

ing often includes topics such as effective teamwork, leadership, decision-making, problem-solving, and effective communication.

Although participation and communication programs are as varied as the companies that sustain them, there are some commonalities. For example: sharing information, skill training, building awareness of and enthusiasm for the ESOP, emphasizing common interests, and participation in decision making. In addition, some ESOP sponsors choose to grant employees the right to vote their shares, thus giving them a role in governance. This leads to our next proposition.

Proposition 3: The greater the investment by an ESOP company in its “participation and communication” programs or the equivalent the stronger the ownership culture.

All of the requirements for an effective ownership structure make them indeed rare in the sense of the VRIO framework.

(I) Imperfect imitability of ownership culture. To be a source of sustainable competitive advantage, ownership culture must also be difficult to imitate. The difficulty of imitating an ownership culture comes from creating the incentives and personal satisfaction that come with ownership. No organizational structure short of ownership has been shown to create the same advantages as ownership on a broad or extended basis. This was the warning contained in Berle and Means' (1932) discussion of the separation of ownership and control and it remains a driving force behind entrepreneurship. Notwithstanding that employees may be attentive to their responsibilities and perform them diligently, it is still a big step from conscientious self-interest to commitment to organization performance. The failure to understand personal motivation and the lack of resources to create this link is what prevents firms from imitating an ownership culture to create parity with an effective ESOP. The hard part is to create an adaptive culture from an existing culture, not to create culture X *de novo*. When an entrepreneur creates a firm, he or she necessarily is obliged to create its culture from scratch (Schein, 1985). Rosen and Rogers (2011) do not envision that there is one perfect culture, anymore than there is one perfect strategy for winning an NBA championship. The coach must work with what s/he has.

(O) Organization of ownership culture. Finally, for an ownership culture to be a resource in the Barney (1991) sense, it must be managed effectively, that is, there must be appropriate organizational support. Therefore, we describe how exceptional ESOPS manage for competitive advantage.

¹¹Among managers of ESOP firms and practitioners like organization consultants who serve them, the term “participation and communication” has roughly the same meaning as corporate culture.

Multi-Level Effects. An ownership culture may be motivational at the level of the individual, and individual motivation is certainly a necessary condition, but it is not sufficient to explain firm performance. Having observed that the mere creation of an ESOP is insufficient to enhance firm performance, and that aggregate individual-level motivation has a only slight effect on firm performance, we have argued that the strategic effect of an ESOP is due to the creation of a culture of cooperation and mutual support—i.e., an “ownership culture” characterized by “working smarter.” Nonetheless, it is possible to create these conditions using conventional rewards and organization development efforts, and so they are not rare or inimitable. What sets an ownership culture apart is, well, ownership.¹¹ In an ESOP, this means owning an enterprise jointly, where all participants are exposed to the same risk, and it means that one’s job has effects beyond one’s area of responsibility.

In an ownership culture, effort is directed toward organizational goals *in addition to* individual goals. In a strong culture, values and norms are widely and deeply shared. Accordingly, employee owners embedded in a strong ownership culture value and engage in such value-creating behaviors as sharing information, mutual monitoring and support, proposing new ideas, making adjustments to work procedures quickly, embracing new work methods enthusiastically, and otherwise cooperating to make the ESOP a success. These cooperative behaviors are individually-generated and pervade the enterprise, and thus have a collective effect, not through aggregation but through synergy.

Shared risk. Shared risk is another individual-level factor contributing to firm outcomes. Analogous to shared deprivation (Tucker, Nock, and Toscano, 1989), shared risk is the perception—held by members of a group—that all are dependent upon each other to obtain individual outcomes. In extreme settings, such as armed combat, the rewards of mutual cooperation are highly desirable (survival) and the failure of mutual cooperation is catastrophic (death) (Van Der Dennen, 2005). In the same vein, an employee’s thinking might go along these lines: “I have skin in the game, which I could lose, but it is more than just my skin that’s at stake—because I know that my co-workers also have skin in the game, and I do not want to let them down.” In addition to imparting decision-making and communication skills to employees, communication and participation programs educate employees about the risks and rewards—with emphasis on the rewards, naturally—of employee ownership. In successful ESOP companies it is not unusual for employee owners to

¹² Several authors have proposed that psychological ownership, an individual level variable, is a factor in the functioning of employee-owned companies (e.g., Pierce, Rubinfeld and Morgan, 1991; Pierce and Rogers, 2003; Pierce, Kostova, and Dirks, 2001). To save space, we omit this point and leave it for future discussion.

enjoy substantial account balances, often exceeding \$100,000, for unskilled or semi-skilled work.

Higher-level effects should not be understood as the sum of all the individual risks added up into a total, but that each individual experiences the same risk. It is the global awareness that all are in it together that creates the higher-level effect.

Two factors. The rewards of an ESOP are twofold: financial and psychic. The genius of employee ownership is that it has the potential to satisfy both lower- and higher-order needs, as predicted by Herzberg's (1968) Two-Factor Theory. The financial rewards of an ESOP function as hygiene factors, while the social and psychological rewards function as motivators. The financial rewards of stock ownership, plus membership in a group pursuing a common goal, can be highly satisfying. It is workers' perceptions of the ESOP as a higher purpose that fosters an ownership culture that makes them "think like an owner."

The important difference between a conventional culture and an ownership culture is that in the former a worker need only concern him/herself with his/her own job. Choosing tasks and coordinating work in a conventionally-owned firm is the responsibility of management. Accordingly, failure in scheduling, coordinating, resource allocation, etc. is the fault of supervisors. But when the activities of a given worker are seen to affect everyone's outcome, the game changes. We are not referring to mere mutual monitoring. Rather, one worker's efforts can be perceived as part of a larger whole. One becomes aware of one's membership in a group serving a larger purpose. That kind of awareness can satisfy higher order needs such as affiliation (McClelland, 1985), relatedness and growth (Alderfer, 1972), self-actualization, esteem, and love (Maslow, 1943). The success of the ESOP itself becomes the overarching goal because it satisfies these higher order needs. An employee's individual tasks are demoted, as it were, to satisfying lower order needs. In an effective ownership culture, individual tasks are merely the means to a greater end: the success of the ESOP. In this way, workers' efforts are linked to a higher purpose, *existing at the level of the firm*. And so, the ESOP has the potential to create a workforce committed to making the company successful—a firm level outcome. It is this vision-driven commitment that has the potential to overcome the inertia that hampers strategic adaptability.

Because the financial rewards of an ESOP combined with the psychological benefits of participation and communication so thoroughly engage employees, we would expect such efforts to affect both individual-level and firm-level outcomes. This leads to the following propositions.

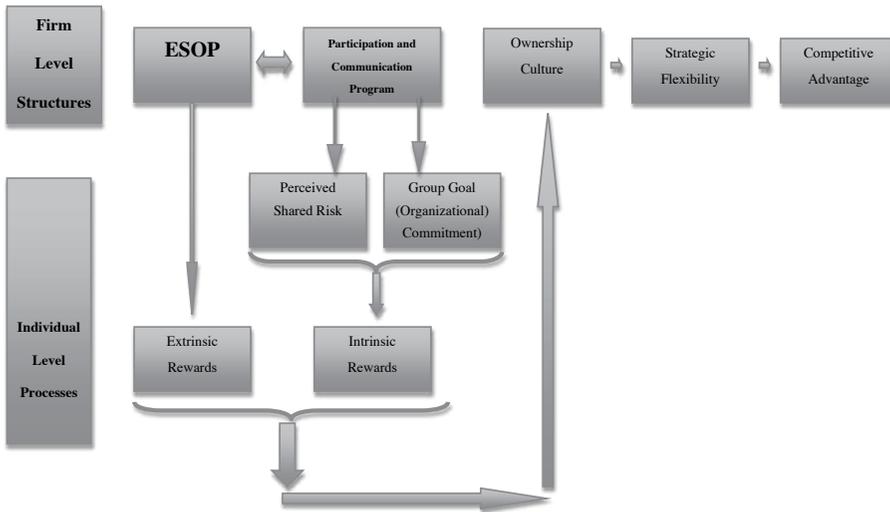
Proposition 4(a): *The greater the investment by a company in its “participation and communication” programs or the equivalent, the greater the individual-level awareness of shared risk and the greater the individual commitment to firm goals.*

Proposition 4(b): *The greater the individual-level perception of shared risk, ceteris paribus, the better the firm-level performance.*

Proposition 4(c): *The greater the individual-level perception of mutual commitment, ceteris paribus, the better the firm-level performance.*

In operationalizing these constructs, it is important to distinguish between individual level and organization-level phenomena. A survey item like “I have a significant amount of my wealth invested in the company” is an individual-level measure. In contrast, a firm-level measure of *others’* risk positions might read, “My co-workers have a significant amount of their wealth invested in the company.” If this procedure is followed, the average score will be a measure of a firm-level outcome, not an aggregation of individual-level outcomes.

Figure 1



The relationship of our propositions to each other are depicted graphically in Figure 1, and neatly summarize our main theme. An ESOP—a firm-level variable—can provide extrinsic rewards in the form of stock ownership. When combined with firm-level “participation and communication” programs an ESOP can create two

key perceptions—shared risk and groups goals—at the individual level. The feelings of sharing risk with co-workers while pursuing a group goal engenders intrinsic rewards. The combination of extrinsic and intrinsic rewards creates an ownership culture. Finally, an ownership culture increases a firm's flexibility to adapt to competitive opportunities and threats, and thereby achieve competitive advantage.

Taken together, we have outlined how an effective ownership culture within an ESOP can be valuable, rare, difficult to imitate and can be organized to create a competitive advantage. This explains why ESOPs have been shown, on average, to create superior performance. In addition, the difficulty of creating and managing an appropriate culture, with ESOPs as well as in other firms, explains why some ESOPs outperform others.

EXTENSIONS AND LIMITATIONS

Testing the propositions. Up to this point we have argued that an ownership culture can enable a company to achieve competitive advantage by making it more flexible and able to adapt to changing circumstances. Here, we offer suggestions for testing the propositions by focusing on the interrelationships among the relevant constructs. The processes we've discussed encompass two levels of analysis: individual and firm. Further, cause and effect travels along multiple pathways.

Multiple levels. The empiricist has a number of choices: Test

(1) the firm-level portion of the model i.e., propositions 1b, 2, and 3, showing the connection between the existence of an ESOP that is combined with a *communication and participation program*, with the effect of creating an ownership culture leading to strategic flexibility and *competitive advantage* (firm success).

A test showing large effect sizes at an acceptable level of alpha error would tend to support the principal claim that to have an ownership culture an ESOP firm must invest in its human capital through communication and participation programs, and that these create the culture that enables a firm to respond quickly to competitive opportunities and threats. Note, however, that this result would not confirm or disconfirm claims about employee perceptions, attitudes, or behaviors.

(2) the individual-level portion of the model, showing the effect of a communication and participation program on *perceived shared risk* and *organizational commitment* (together called intrinsic rewards), and combined with the ESOP's extrinsic (i.e., financial) *rewards*, contributes to an ownership culture.

A test showing large effect sizes at an acceptable level of alpha error would tend to indicate that the reason why communication and participation programs are

effective is that they alert employees to shared risk, and increase organizational commitment. Note also that this result would not confirm the effect of culture on strategic flexibility or competitive advantage.

(3) both levels together. (See discussion below.)

A test showing large effect sizes at an acceptable level of alpha error would tend to confirm the strategic flexibility argument *and* the propositions regarding the internal mechanisms driving the formation of an ownership culture.

(4) the between firm-level portion of the model by comparing ESOP firms with and without *communication and participation programs*.

A test showing large effect sizes at an acceptable level of alpha error would tend to confirm the important role communication and participation programs play in creating an ownership culture.

Pathways. The discussion above is based on the assumption that cause and effect can be detected by comparing the yes-or-no existence of communication programs and the strength or degree of attitudes. Alternatively, another way to study the effects of employee ownership on individuals and firms is to trace pathways among the variables (Edwards and Lambert, 2007). In the model in Figure 1, multiple paths emerge from the box labeled “*ESOP*” and converge on *ownership culture*, then on *flexibility* and competitive advantage. Given a large enough number of observations (See discussion below), it is possible to estimate path coefficients, test them, and draw conclusions about the fit of the model using structural equation techniques. If that is not feasible or desired, a researcher may wish to examine the strength of the mediators, i.e., those variables in between “*ESOP*” and *competitive advantage*.

Multi-level research. It is important to emphasize that empirical demonstration of a multilevel linkage would be a monumental undertaking, requiring the simultaneous collection of data from two levels of analysis—individual-level *and* firm-level—and from a large sample of firms. As noted above, overcoming this challenge has been a rarity. Notwithstanding the lack of sufficient resources, undaunted researchers continue to explore the ownership→performance link from a single level of analysis. Insofar as is practical, it would be well to investigate how cause and effect operate across level boundaries. Nonetheless, in order to fully understand the employee ownership phenomenon, multi-level data collection and analyses are the ideal. When impracticality is invincible, the researcher would do well to introduce control variables into the analysis such as tenure, level in organization, account balance, department, level of compensation, and performance appraisals. Cultural measures should not be omitted, but treated as an individual-level measure.

Equally important is avoiding aggregating individual-level data in an attempt to describe a firm level phenomenon (Danserau and Cho, 2006; Kozlowski and Klein, 2000; Rousseau, 1985). Note, however, that when an individual completes a paper-and-pencil questionnaire regarding his/her perception of an organization's culture, these data may be aggregated because each one is a *rating*, in the same way that the scores given by Olympic judges of gymnastics or diving are ratings of a single performance and may be combined.

Firm level. The place to begin is to document and measure the content of ownership cultures and then compare them with firm outcomes. This line of investigation faces the practical challenges discussed above. Fortunately, there are several measures of organizational culture available to organizational development practitioners from which scholars may choose. An interesting avenue of research would be to determine which of them more accurately predicts relative success of ESOP companies. Some publishers of measures of culture keep a databank against which ESOP companies may be compared, and the unique elements of an ownership culture highlighted. In the absence of quantitative measures, discussions of culture can hardly rise above speculation. Managers want to know what specific values, beliefs, norms, and behaviors they can count on to improve adaptability and ultimately, firm performance. And scholars are hard pressed to illuminate the connection between culture and firm performance without a reliable and valid measure thereof.

Another important avenue of research would be to examine the ways in which an ESOP is capable of coping with certain dilemmas related to the management of human resources. Coff, for example (1997, 1999) identifies the persistent threat of turnover, as well as three types of information dilemmas: (1) lack of relevant hiring information results in workers who do not fit the job (adverse selection), (2) motivation and moral hazard (i.e., an employee who shirks), or (3) ineffective management decision making (bounded rationality). Information dilemmas arise from two sources: the first source creating these information dilemmas is social complexity, which is a potential shortcoming of team production, where individual contributions are unobservable, and so increases the risk of shirking. The second source is causal ambiguity, that is, the difficulty of identifying those factors that contribute to an organization's performance. The fundamental question here is to what extent does an ESOP encompass the coping strategies proposed by Coff (retention, rent sharing, organizational design, and information strategies)?

One shortcoming of firm level research has been to make comparisons between companies matched according to size. As an analytical strategy, matching works only when the objects matched are identical in every respect, not just the

matching variable. To see why this is so, imagine two companies, one with an ESOP, the other without. Suppose Company E pursues a low-cost strategy in an industry with intense competition, while Company C pursues a differentiation strategy in an industry with moderate competition (Porter, 1980). Matching by size does not account for performance differences owing to strategy, the intensity of competition, and the multitude of other variables.¹²

Individual level. At the individual and group levels of analysis, theory and empirical evidence have barely cracked the lid on the black box concealing the inner workings of an ESOP company. In general, existing research has focused on attitudes and motivation—interesting, but not enough to lift the lid. To better understand what goes on at the individual level, we would like to know to what extent, if any, do individuals in ESOP firms differ from non-ESOP firms on such variables as organizational commitment, organizational identification, self-efficacy, risk preference, openness to experience, locus of control, or self-monitoring? If there are differences, do they account for differences in firm performance?

Shared risk as a management concept is novel. We have not developed it here due to space considerations. Yet the notion that employees respond to the knowledge of a shared fate has been around for a long time (Melville, 1851, 1981; Mill, 1871, 1998). Accordingly, it requires further theoretical development and empirical testing, especially the creation of operational measures. A good first step would be an ethnographic study across a variety of employee-owned and conventionally-owned firms. From people's stories, researchers could then develop a measure of individual-level risk perceptions and firm-level risk perceptions. Example: "My wealth is at risk here." "This is a risky place to work for all of us."

Although the Rosen and Rogers' (2011) example is convincing, it is based on a binary assumption: motivated vs. not motivated. Investigators might instead adopt the view that level of motivation is continuous rather than categorical and explore how level of motivation interacts with level of fatigue. It would be worth exploring the relation between worker output and degree of motivation. Output might vary proportionately. So questions like "How does level of motivation affect felt fatigue, and response to that fatigue?" might be appropriate.

Managerial implications. Because the causal mechanism is not well understood (Coff, 1997), ESOPs are risky and forming an ESOP remains a major strategic decision. It is the exceptional manager who is willing to depart from tried-and-true ownership structures. The initial costs of creating an ESOP represent a major invest-

¹²See Cook and Campbell (1979) and Shadish, Cook, and Campbell (2002) for a discussion of the dangers in using matching in quasi-experimental research.

ment for a small company and creation absorbs much management time and energy dealing with setting up the necessary legal, accounting, administrative and human resource processes. Third, ongoing maintenance requires continual investments of time and energy. Perhaps most importantly, though, is the challenge of managing an entity for which there is not much historical experience on which to draw—managers of ESOPs are still something of pioneers. Scholars can help by peering into the black box, as we have attempted to do here.

The adventurous manager can, however, rely on past experiences of successful managers by adopting these and other practices:

- Describe and measure existing culture and track changes over time
- Engage employees early in the process of planning to adopt an ESOP
- Invest in training, especially open book management, problem solving, conflict resolution and decision-making
- Make the financial rewards meaningful
- Have a plan for employees who do not care to participate
- Encourage information-sharing and create a mechanism for doing so, such as an internal wiki

Further research. We have discussed the processes by which an ownership culture can help an ESOP firm respond more quickly to strategic opportunities and threats. Yet, the effects of employee ownership are not limited to employees' perceptions, attitudes, and behaviors, or to culture; it is logical to expect that its effects pervade all aspects of an organization's functioning. A promising avenue of research is to explore the effect employee ownership might have on an organization's structure, or the problem of allocating resources among internal stakeholders. There are many questions to answer, for instance: How does employee ownership affect the ways a firm manages its workflow, budgeting, human resource management, marketing, and finance functions? As we have said, much is known about employee ownership, but there is much more to be learned.

SUMMARY AND CONCLUSION

Our purpose here has been to offer an explanation of why ESOP firms tend to perform, on average, better than conventionally-owned firms, and why some employee-owned firms tend to perform better than others. We conclude that employee ownership has the potential to *enhance* competitive capability and possibly make it sustainable by increasing the flexibility of the workforce in responding to environmental threats and opportunities quickly and cheaply, but requires proper management.

Empirical evidence indicates that an ESOP alone is not a sufficient condition for superior performance, but must be combined with participatory management. The common explanation, that increased motivation of employees is responsible for ESOP performance, is not sufficient because aggregate motivation is not a significant factor at the level of the firm. Instead, a more convincing explanation points to the process through which increased strategic flexibility occurs in an ownership culture. Strategic flexibility emerges from two conditions: *shared* risk combined with widespread perception of ESOP success as a *group* goal. This means that an employee perceives that the attainment of her individual goal is dependent upon every one attaining their goals, and that achieving firm success will provide psychic rewards in addition to material rewards. The two must occur together; neither condition is sufficient alone. When the two conditions are present they lead to cooperative behavior, efficiency, and strategic flexibility. When the common goal is achieved (higher stock price), individuals experience satisfaction of lower-order needs (wealth) and higher order needs (growth, esteem, self-actualization).

To answer our two questions we stipulated a framework that meets three criteria: it must be consistent with empirical observations, account for ownership phenomena at two levels of analysis and the *interaction(s)* between those levels, and be empirically testable. We have met those criteria: (1) The difficulty of creating an ownership culture accounts for the varied performance of ESOPs companies; and the necessity of combining financial rewards with group aspirations accounts for the superior performance of ESOPs over conventionally-owned companies. (2) Individual motivation is a necessary but not a sufficient condition for firm performance while shared purpose is also a necessary but insufficient condition. Further, it is necessary to combine the two. (3) With sufficient resources to measure individual-level perceptions and attitudes and match them with measures of firm performance, it is possible to test empirically our claims.

REFERENCES

- Al-Saigh, N. M. and Buera, A. M. (1990). Privatization in the arab world: Prerequisites for success. *International Review of Administrative Sciences*, 56, 125-135.
- Alderfer, C. P. (1972). *Existence, Relatedness, and Growth: Human Needs in Organizational Settings*. New York: Free Press.
- Aldrich, H. E. (1999). *Organizations Evolving*. Thousand Oaks, CA: Sage Publications.

- Alperovitz, G. (1997). The old socialist idea and the new century. *Peace Review*, 9, 41-48.
- Barney, J.B. (1991). Firm Resources and Sustained Competitive Advantage, *Journal of Management*, 17(1): 99-120.
- Bell, L. and Kruse, D. (1995). Evaluating ESOPs, profit sharing and gain sharing plans in U.S. industries; A report to the U. S. Department of Labor, Washington, D.C.: U.S. Department of Labor.
- Ben-Ner, A. (1988). The life cycle of worker-owned firms in market economies: A theoretical analysis. *Journal of Economic Behavior and Organization*, 10: 287-313.
- Ben-Ner, A. and Jones, D. C. (1995). Employee participation, ownership, and productivity: A theoretical framework. *Industrial Relations*, 34, 532-54.
- Berle, A.A. and Means, G.C. (1932). *The Modern Corporation and Private Property*, Harcourt, Brace and World, New York 1967.
- Blasi, J. R. (1988). *Employee ownership: Revolution or ripoff?* Cambridge, MA: Ballinger Publishing Company.
- Blasi, J., Conte, M. and Kruse, D. (1992). The new owners: Stock price performance for public companies with significant employee ownership. *Journal of Employee Ownership Law and Finance*, 4: 95-130.
- Blasi, J. R. and Kruse, D. L. (1991). *The new owners: The mass emergence of employee ownership in public companies and what it means for american business*. HarperBusiness.
- Blinder, A. S. (1990). Introduction. In Blinder, A. S. (Ed.) *Paying for productivity: A look at the evidence*. Washington, D. C.: The Brookings Institution.
- Bloom, N., Kretchmer, T., and Van Reenen, J. (2011). Are family friendly workplace practices a valuable firm resource? *Strategic Management Journal*, 32: 343-367.
- Bloom, S. M. (1985). *Employee Ownership and Firm Performance*. Unpublished doctoral dissertation, Department of Economics, Harvard University.
- Bonin, J. P., Jones, D. C. and Putterman, L. (1993) Theoretical and empirical studies of producer cooperatives: With the twain ever meet? *Journal of Economic Literature*, 31: 1290-1320.
- Bradley, K. (1986). Employee-ownership and economic decline in western industrial democracies. *Journal of Management Studies*, 23, 51-71.
- Brohawn, D. K. (1997). *Journey to an Ownership Culture: Insights from the ESOP Community*. Washington, D. C.: The ESOP Association and Scarecrow Press, Lanham MD & London.

- Buchko, A. A. (1992). Effects of employee ownership on employee attitudes: A test of three theoretical perspectives. *Work and Occupations*, 19, 59-78.
- Buchko, A. A. (1993). The effects of employee ownership on employee attitudes: An integrated causal model and path analysis. *Journal of Management Studies*, 30, 633-657.
- Carberry, E. J. (2011). *Employee Ownership and Shared Capitalism*. Urbana-Champaign, IL: University of Illinois at Urbana-Champaign, School of Labor and Employment Relations.
- Case, J. (1995). *Open-Book Management*. New York: HarperCollins Publishers.
- Chaplinsky, S. and Niehaus, G. (1990). The tax and distributional effects of leveraged ESOPs. *Financial Management* (Spring), 29-38.
- Chiu, W. C. K. (2003). Employee stock ownership plans and organizational integration among workers in the People's Republic of China. *Human Resource Management Review*, 13, 407-421.
- Coff, R. W. (1997). Human assets and management dilemmas: Coping with hazards on the road to resource-based theory. *Academy of Management Review*, 22, 374-402.
- Coff, R. W. (1999). When competitive advantage doesn't lead to performance: The resource-based view and stakeholder bargaining power. *Organizational Science*, 10, 119-133.
- Conte, M. A., Blasi, J. Kruse, D., and Jampani, R. (1996). Financial returns of public ESOP companies: Investor effects vs. manager effects. *Financial Analysts Journal*, July/August, 51-61.
- Conte, M. A. & Svejnar, J. (1990). Employee ownership plans. In Blinder, A. S. (Ed.) *Paying for productivity: A look at the evidence*. Washington, D. C.: The Brookings Institution.
- Cook, T. D., and Campbell, D. T. (1979). *Quasi-Experimentation: Design & Analysis Issues for Field Settings*. Boston: Houghton Mifflin Company.
- Cooke, R. A., & Lafferty, J. C. (1987). *Level V: Organizational Culture Inventory*. Plymouth, MI: Human Synergetics.
- Danserau, F. and Cho, J. (2006). Avoiding the "fallacy of the wrong level." *Group and Organization Management*, 31, 536-577.
- Doucouliaagos, C. (1990). Why capitalist firms outnumber labor-managed firms. *Review of Radical Political Economics*, 22: 44-67.
- Doucouliaagos, C. (1995). Institutional bias, risk, and workers' risk aversion. *Journal of Economic Issues*, 29: 1097-1118.

- Dugger, W. M. (1987). Democratic economic planning and worker ownership. *Journal of Economic Issues*, 21, 87-99.
- Dunbar, A. E. and Kumbhakar, S. C. (1992). An empirical investigation of the association of productivity with employee stock ownership plans. *Journal of the American Taxation Association*. 22-39.
- Ellerman, D. P. (1984). Theory of legal structure: Worker cooperatives. *Journal of Economic Issues*, 18: 861-891.
- Fama, E. F. and Jensen, M. C. (1983). Separation of ownership and control. *Journal of Law and Economics*, 26: 301-325.
- FitzRoy, F. R., and Kraft, K. (1987). Cooperation, productivity, and profit sharing. *Quarterly Journal of Economics*, 102: 23-35.
- Freeman, S. F. (2007). Effects of ESOP adoption and employee ownership: Thirty years of research and experience. University of Pennsylvania Organizational Dynamics Working Paper #07-01.
- French, J. L., and Rosenstein, J. (1984). Employee ownership, work attitudes, and power relationships, *Academy of Management Journal*, 27: 861-869.
- GAO (General Accounting Office). (1986). *Employee stock ownership plans: Benefits and costs of ESOP tax incentives for broadening stock ownership*. GAO-PEMD-87-8. Washington, DC: U. S. Government Printing Office.
- Gates, J. (1998). *The Ownership Solution: Toward a Shared Capitalism for the Twenty-First Century*. Reading, MA: Addison-Wesley.
- Gibson-Graham, J. K. (2003). Enabling ethical economies: Cooperativism and class. *Critical Sociology*, 29, 123-161.
- Goldstein, S. G. (1978). Employee share ownership and motivation. *Journal of Industrial Relations*, 20: 311-330.
- Greenberg, E. S. (1980). Participation in industrial decision-making and worker satisfaction: The case of producer cooperatives. *Social Science Quarterly*, 60: 551-569.
- Gunn, C. (2000). Markets against economic democracy. *Review of Radical Political Economics*, 32, 448-460.
- Hammer, T. H., Landau, J. C., and Stern, R. N. (1981). Absenteeism when workers have a voice: The case of employee ownership. *Journal of Applied Psychology*, 66: 561-573.
- Hammer, T., and Stern, R. (1980). Employee ownership: Implications for the organizational distribution of power. *Academy of Management Journal*, 23: 78-100.

- Hammer, T., Stern, R., and Gurdon, R. (1982). Worker ownership and attitudes toward participation. In F. Lindenfeld and J. Rothschild-Whitt (Eds.) *Workplace democracy and social change*. Boston: Porter Sargent Publishers.
- Hansmann, H. B. (1990). When does worker ownership work?: ESOPs, law firms, codetermination, and economic democracy. *The Yale Law Journal*, 99: 1749-1816.
- Herzberg, F. (1968). One more time: How do you motivate employees? *Harvard Business Review (January-February)* p. 56ff.
- Howe, C. (1986). The politics of class compromise in an international context: Considerations for a new strategy for labor. *Review of Radical Political Economics*, 18 1-22.
- Jensen, M. C. & Meckling, W. H. (1976). Theory of the firm: Managerial behavior, agency costs and ownership structure. *Journal of Financial Economics*, 3, 305-360.
- Keef, S. P. (1994). Employee share ownership and job attitudes: The effects of share sale. *Asia Pacific Journal of Management*, 11: 91-102.
- Klein, K. (1987). Employee stock ownership and employee attitudes: A test of three models. *Journal of Applied Psychology*, 72: 319-332.
- Klein, K. J. and Hall, R. J. (1988). Correlates of employee satisfaction with stock ownership: Who likes an ESOP most? *Journal of Applied Psychology*, 73: 630-638.
- Kotter, J. P. and Heskett, J. L. (1992). *Corporate Culture and Performance*. New York: The Free Press.
- Kozlowski, S. W. J. and Klein, K. J. (2000). A multilevel approach to theory and research in organizations. In Kozlowski, S. W. J. and Klein, K. J. (Eds.) *Multilevel Theory, Research, and Methods in Organizations*. San Francisco: Jossey-Bass.
- Kruse, D. (1984). *Employee ownership and employee attitudes: Two case studies*. Norwood, PA: Norwood Editions.
- Kruse, D. (1988). *Essays on profit sharing and unemployment*. Unpublished doctoral dissertation, Department of Economics, Harvard University.
- Kruse, D. (1992). Profit sharing and productivity: Microeconomic evidence from the United States. *Economic Journal*, 102: 24-36.
- Kruse, D. (1993). Profit sharing: Does it make a difference? *Kalamazoo, MI*: W. E. Upjohn Institute for Employment Research.

- Kruse, D. L. and Blasi, J. R. (1997). Employee ownership, employee attitudes, and firm performance: A review of the evidence. In *Handbook of Human Resource Management*. Mitchell, D. J. B., Lewin, D. and Zaidi, M. (Eds.) Greenwich, CT: JAI Press.
- Kruse, D., Freeman, R. and Blasi, J. (2010). *Shared Capitalism at Work: Employee Ownership, Profit and Gain Sharing, and Broad Based Stock Options*. Chicago: University of Chicago Press.
- Kumbhakar, S. C. and Dunbar, A. E. (1993). The elusive ESOP- productivity link. *Journal of Public Economics*, 52, 273-283.
- Lawler, E. (1995). The new pay: A strategic approach, *Compensation and Benefits Review*, 27, 14-22.
- Lawler, E. E. (1994). *Motivation in Work Organizations*. San Francisco: Jossey-Bass.
- Long, R. J. (1978a). The effects of employee ownership on organizational identification, employee job attitudes, and organizational performance: A tentative framework and empirical findings. *Human Relations*, 31: 29-48.
- Long, R. J. (1978b). The relative effects of share ownership vs. control on job attitudes in an employee-owned company. *Human Relations*, 31: 753-763.
- Long, R. J. (1979). Desires for and patterns of worker participation in decision making after conversion to employee ownership. *Academy of Management Journal*, 22: 611-617.
- Long, R. J. (1980). Job attitudes and organizational performance under employee ownership. *Academy of Management Journal*, 23: 726-737
- Long, R. J. (1981). The effects of formal employee participation in ownership and decision making on perceived and desired patterns of organizational influence: A longitudinal study. *Human Relations*, 10: 847-876
- Long, R. J. (1982). Worker ownership and job attitudes: A field study. *Industrial Relations*, 21: 196-215.
- Mackin, C., Freundlich, F., Rodgers, L., and Kerr, C. (2012). *Ownership Culture Survey*. Oakland, CA: National Center for Employee Ownership.
- Maslow, A. H. (1943). A theory of human motivation. *Psychological Review*, (July) 370-396.
- McClelland, D. (1985). *Human Motivation*. New York: Scott Foresman.
- Melville, H. (1851, 1981). *Moby-Dick, or, The Whale*. Berkeley: University of California Press.
- Mill, J. S. (1871, 1998). *Principles of Political Economy*. New York: Oxford Press.

- Miller, D. E. 2003 Mill's 'socialism.' *Politics, philosophy and economics*, 2, 231-238.
- Mitchell, D. J. B., Lewin D. & Lawler, E. E. (1990). Alternative pay systems, firm performance and productivity. In A. S. Blinder (Ed.) *Paying for Productivity: A look at the evidence*. Washington, D. C. Brookings Institution.
- Mygind, N. and Rock, C. P. (1993). Financial participation and the democratization of work. *Economic and Industrial Democracy*, 14, 163-183.
- (NCEO) National Center for Employee Ownership (2008). *Employee Ownership Report*, 28: 5.
- Oliver, N. (1984). An examination of organizational commitment in six workers' cooperatives in Scotland. *Human Relations*, 37: 29-46.
- Oliver, N. (1990). Work rewards, work values, and organizational commitment in an employee-owned firm: Evidence from the U.K. *Human Relations*, 43: 513-526.
- Park, S., and Song, M. H. (1995). Employee stock ownership plans, firm performance, and monitoring by outside blockholders. *Financial Management*, 24: 52-65.
- Penrose, E. T. (1959). *The Theory of the Growth of the Firm*. Oxford: Basil Blackwell.
- Pierce, J. L. and Rogers, L. (2003). The psychology of ownership and worker-owner productivity. *Group Organization Management*, 29: 588-613.
- Pierce, J. L., Kostova, T., and Dirks, K. T. (2001). Toward a theory of psychological ownership in organizations. *Academy of Management Review*, 26: 298-310.
- Pierce, J. L., Rubenfeld, S. A., and Morgan, S. (1991). Employee ownership: A conceptual model of process and effects. *Academy of Management Review*, 16: 121-144.
- Porter, M. (1980). *Competitive Strategy*. New York: The Free Press.
- Quarrey, M. Blasi, J. and Rosen, C. (1986). *Taking Stock: Employee Ownership at Work*. Cambridge, MA: Ballinger Publishing Company.
- Rhodes, S. R. and Steers, R. M. (1981). Conventional vs. worker-owned organizations. *Human Relations*, 34: 1013-1035.
- Rooney, P. (1992). Employee ownership and worker participation: Effects on health and safety. *Economic Letters*, 39: 323-328.
- Rosen, C. and Carberry, E. (2003). *Ownership Management: Building A Culture of Lasting Innovation*. Oakland, CA: The National Center for Employee Ownership.
- Rosen, C. and Quarrey, M. (1987). How well is employee ownership working? *Harvard Business Review*, Sept/Oct, 126-129.

- Rosen, C. and Rodgers, L. (2007). *The Ownership Edge: How Employee Ownership Can Make Good Companies Great*. Oakland, CA: The National Center for Employee Ownership.
- Rosen, C. and Rodgers, L. (2011). *Fundamentals of Ownership Culture: Practical Ideas for Creating a Great Ownership Company*. Oakland, CA: National Center for Employee Ownership.
- Rosen, C. and Young, K. (1991). *Understanding Employee Ownership*. Ithaca: ILRR Press.
- Rosen, C. M., Klein, K. J., and Young, K. M. (1986). *Employee Ownership in America; The Equity Solution*. Lexington, MA: Lexington Books.
- Rosen, C., Case, J. and Staubus, M. (2005). *Equity: Why Employee Ownership is Good for Business*. Boston: Harvard Business School Press.
- Rousseau, D. M. (1985). Issues of level in organizational research: Multi-level and cross-level perspectives. *Research in Organizational Behavior*, 7, 1-37.
- Rousseau, D. M. and Shperling, Z. (2003). Pieces of the action: Ownership and the changing employment relationship. *Academy of Management Review* 28, 553-570.
- Rumelt, R. P., Schendel, D. and Teece, D. J. (1991). Strategic management and economics. *Strategic Management Journal*, 12: 5-29.
- Russell, R., Hochner, A. and Perry, S. E. (1979). Participation, influence and worker-ownership. *Industrial Relations*, 18: 330-341.
- Schein, E. H. (1985). *Organizational Culture and Leadership: A Dynamic View*. San Francisco: Jossey-Bass, Inc.
- Scholes, M. S., and Wolfson, M. A. (1990). Employee stock ownership plans and corporate restructuring: Myths and realities. *Financial Management*, 19, 12-28.
- Scott, W. R. (2008). *Institutions and Organizations: Ideas and Interests*. Los Angeles: SAGE Publications.
- Shadish, W. R., Cook, T. D., and Campbell, D. T. (2002). *Experimental and Quasi-Experimental Designs for Generalized Causal Inference*. Boston: Houghton Mifflin Company.
- Smiley, R. W., Gilbert, R. J., Binns, D. M., Ludwig, R. L., and Rosen, C. M. (2007). *Employee Stock Ownership Plans: ESOP Planning, Financing, Implementation, Law and Taxation*. San Diego. Beyster Institute at the Rady School of Management, University of California at San Diego.
- Sockell, D. (1985). Attitudes, behavior, and employee ownership, some preliminary data. *Industrial Relations*, 24:130-138.

- Stack, J. (1994). *The Great Game of Business*. New York: Crown Publishing Group.
- Steinherr, A. (1978). The labor-managed economy: A survey of the economics literature. *Annals of Public and Co-operative Economy*, 24, 129-148.
- Toscano, D. J. (1983). Toward a typology of employee ownership. *Human Relations*, 7, 581-602.
- Tucker, J., Nock, S. L., and Toscano, D. (1989). Employee ownership and perceptions of work. *Work and Occupations*, 16: 26-42.
- U. S. General Accounting Office. (1986). *Employee stock ownership plans: Benefits and costs of ESOP tax incentives for broadening stock ownership*. GAO-PEMD-87-8. Washington, DC: U. S. Government Printing Office.
- Van Der Dennen, J. M. G. (2005). *Peace Review: A Journal of Social Justice*, 17, 81-89.
- Vanek, J. (1976). *Uncertainty and the investment decision under labor-management and their social efficiency implications*. In *Collected Essays on Self-Management*, Ithaca, NY: Cornell University Press.
- Vroom, V. H. (1964). *Work and Motivation*. New York: John Wiley & Sons.
- Whyte, W. F. and Blasi, J. R. (1982). Worker ownership, participation and control: A theoretical model. *Policy Sciences*, 14: 137-163.
- Whyte, W. F. and Blasi, J. R. (1984). Employee ownership and the future of unions. *Annals of the American Association of Political and Social Science*, 473: 128-140.
- Young, K. M., Rosen, C., and Carberry, E. J. (1995). *Theory O: Creating an Ownership Style of Management*. Oakland, CA: The National Center for Employee Ownership.

BIOGRAPHICAL SKETCH OF AUTHORS

Peter Thompson is an Assistant Clinical Professor in the College of Business Administration at the University of Illinois at Chicago. Prior to his academic career, he spent 12 years in the banking industry, including The Northern Trust, and the Capital Markets Group at The First National Bank of Chicago, now J. P. Morgan Chase. He holds degrees from Temple University, Northwestern University, and The University of Illinois at Chicago.

Mark Shanley is a Professor of Management and Associate Dean at the College of Business Administration of the University of Illinois at Chicago. He received his Ph.D. from the University of Pennsylvania and has taught at the University of

Chicago, Northwestern University, and Purdue University. He is a member of the Editorial Board for *Strategic Management Journal*. His research interests include strategic groups, mergers and acquisitions, strategic alliances, and healthcare strategy.

Abigail McWilliams is Professor of Strategic Management at the University of Illinois-Chicago. She earned a BS in Business and an MA and PhD in Economics from The Ohio State University. Her research interests include Corporate Social Responsibility, Methodology, Strategic Management and Strategic Human Resource Management. She has published extensively in leading management journals over the last 25 years and is co-editor of *The Oxford Handbook of Corporate Social Responsibility*, 2008.