

OWNING THE WORK · CHAPTER FIVE

A Bakery's Arithmetic

Chapter Five of Owning the Work

Ammanuel Santa Anna

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THE LICENCE

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Chapter Five of Owning the Work. The whole book, with every chapter, is at business.hautelumiere.life/library/owning-the-work (DOI https://doi.org/10.5281/zenodo.23988988).

A NOTE BEFORE YOU READ

This work is offered for education and leadership development. It is not legal, financial, accounting, investment, medical or psychological advice; take the advice of a qualified professional who knows your circumstances. Companies and events are described from the public record as the author understands it; characterisations are the author's analysis. Examples are illustrative, and no particular outcome is promised to any reader.

ABSTRACT

The ovens at a regional bakery are lit at four. By six the first vans are loaded for the cafés and grocers on the morning route, and by nine the owner is at a small desk above the packing floor with a pencil and last year's accounts. She is sixty-one. She has no children who want the business, two offers from larger competitors on the desk, and a question she has been circling for a year: whether the people downstairs could own it. She is a composite, built for teaching, and so is her bakery. Every figure that describes the firm in this chapter was set by the writer to be plausible and round enough to follow; none describes a real company. Every figure that describes the research comes from a cited, published source, and the notes give each one. The point of putting the two side by side is the one Ammanuel Santa Anna makes about this whole field in his notes on finance: "This isn't naive idealism—it's systems theory with a balance sheet." A balance sheet is what this chapter is for.

CHAPTER FIVE

A Bakery's Arithmetic

Four in the morning

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Chapters 2 to 4 set out where the idea came from, where it goes wrong and how the house reads it. This one works a case. It begins with the published figures, read with their limits, then turns to the bakery.

What the strongest figures say

Four bodies of evidence carry most of the weight in this field, and each answers a slightly different question.

Profit sharing and productivity. Douglas Kruse surveyed 500 American public companies and joined the survey to panel data on corporate performance. Controlling for other influences, he found that adopting profit sharing "is found to be associated with average productivity increases of 4-5%, with no subsequent positive or negative trend," and that the increase was larger for small companies and for cash plans.[42] He was candid about the limit: there was "no evidence on the mechanisms" by which profit sharing works. The finding is an average across public companies; it cannot tell any single firm what will happen to it.

Profit sharing and jobs in a downturn. In an earlier study of 2,976 publicly traded companies between 1971 and 1985, Kruse tested an idea of the economist Martin Weitzman: that firms whose pay moves with profit

should keep more people employed when times are hard. In manufacturing, when the unemployment rate rose by one point, firms in which all employees took part in a profit-sharing pension plan saw a 2.0 percent fall in employment, against 3.1 percent for firms without profit sharing. Outside manufacturing, he found no significant difference.[43] The second half of that result matters as much as the first.

Participation of every kind. Chris Doucouliagos combined 43 published studies in a meta-analysis in 1995. He found that profit sharing, worker ownership and worker participation in decision making were all positively associated with productivity, that mandated codetermination laws were negatively associated with it, and that every correlation was stronger in firms owned and controlled by their workers than in conventional firms that had adopted participation schemes.[44]

Employee ownership and firm performance. Ernest O'Boyle, Pankaj Patel and Erik Gonzalez-Mulé combined 102 samples representing 56,984 firms in 2016. They found that employee ownership has "a small, but positive and statistically significant relation to firm performance," with an average corrected correlation of 0.04 (a very small effect in the conventions of the field), that the effect held across public and private firms and across firm sizes, that it had grown in more recent studies, that studies from outside the United States reported stronger effects, and that they found "little to no evidence of publication bias."[45]

The fair summary is plain. The association between sharing and performance is positive, consistent and modest. A reader looking for proof that ownership transforms firms will not find it here. A reader looking for evidence that broad sharing does no harm to performance and often does some good will find it in abundance.

The bakery as it stands

Now the composite. The owner's accounts, as the writer has set them, show the following for a normal year.

- Employees: 140, of whom 96 work in production and dispatch and 44 in drivers, sales and the office.
- Total payroll: $7,840,000, an average of $56,000 a person.
- Revenue: $21,000,000.
- Pre-tax profit: $1,400,000, which is 6.7 percent of revenue.
- Current sharing: none, beyond a discretionary Christmas bonus averaging $300 a person, or $42,000 in total.

The Ownership Inventory from Chapter 2, completed for this firm, would show a single arrangement, the bonus, held by everyone, worth very little, and withdrawable at will. Part B of the inventory would show that only the owner and her accountant see the full accounts.

The Risk and Voice Check from Chapter 3 would show three things worth noting. The unit is small enough to see: the night bakers, the dispatch team and the drivers each know one another's work. Fixed wages are at the local market. And there is no information or voice at all.

Read through Chapter 4's lens, that last line is the important one. Whatever plan the owner chooses, it will land in a structure where attention still faces outward, because no one downstairs can see what the business earns.

Step one: the numbers on the wall

Following the order Chapter 4 suggested, the first move costs almost nothing. The owner begins posting four figures by the clocking-in machine each month: sales against the same month last year, waste as a share of flour bought, on-time deliveries, and pre-tax profit for the year to date.

The finer point is choosing figures that people can affect and that move often enough to be watched. Waste and on-time deliveries change weekly and respond to what happens on the floor. Profit does not move weekly, but leaving it off the wall would tell everyone that the real number is a secret. Santa Anna is clear that this part is the hard one: "Designing such measurement systems is among the most important — and most difficult — practical challenges the movement faces."[46]

The owner also starts a monthly half hour in which anyone may ask about the figures. The first two sessions are quiet. The third is not. A driver asks why on-time deliveries fall every Monday, and the dispatch lead explains that the Monday flour delivery arrives late and holds up the first bake. Nobody in the office had connected the two. The owner moves the flour order to Saturday at no cost. It is a small thing, and it is exactly the kind of thing Chapter 4 predicted: a sensing organ the firm did not know it had, reporting for the first time because someone asked it to. In the composite, nothing else about the firm has changed yet, and nobody owns anything new.

Step two: a profit share, worked in full

Six months later the owner introduces profit sharing. The design, all of it set by the writer for this composite, is as follows.

The pool. Ten percent of pre-tax profit, paid in cash twice a year. Kruse's 1993 finding that the productivity association was larger for cash plans and small firms is the reason for cash; it is a reason, not a guarantee.[42] In a normal year the pool is 10 percent of $1,400,000, which is $140,000. The Christmas bonus is folded into it, so the net new cost in a normal year is $140,000 less $42,000, or $98,000.

The split. Half the pool is shared equally among everyone employed for the full period; half is shared in proportion to pay. This answers the exclusion objection from Chapter 3: an equal floor means the night baker and the sales manager receive the same first share.

- Equal half: $70,000 divided by 140 people is $500 each.
- Pay-weighted half: $70,000 divided by a payroll of $7,840,000 is about 0.893 cents per dollar of pay. A baker earning $44,000 receives about $393; a manager earning $90,000 receives about $804.
- A baker's total share: $500 plus $393, about $893, or 2.0 percent of pay.
- A manager's total share: $500 plus $804, about $1,304, or 1.4 percent of pay.

The equal half makes the share a larger fraction of pay for lower earners. That is a design choice, not a law of nature, and the owner records why she made it.

A bad year. Suppose profit falls to $350,000. The pool is then $35,000: an equal half of $17,500, or $125 a person, plus a pay-weighted half of $17,500, which comes to about $98 for the baker. Her share falls from about $893 to about $223. The share falls by three quarters. Wages do not fall, because the share was added to market wages rather than carved out of them, which is the answer to the first objection in Chapter 3.

What the research would and would not predict

It is tempting at this point to multiply the published averages by the bakery's numbers. It is worth doing once, carefully, to see why the result must be held loosely.

Productivity. If the bakery's productivity rose by the 4 to 5 percent Kruse found on average in public companies, the gain would be large compared with a $98,000 net cost. But the bakery is not a public company, the finding is an association across firms rather than a forecast for one, and Kruse himself found no mechanism. The honest use of the figure is to say that the plan is not expected to harm performance and may help, not to put a number in a budget.

Jobs in a downturn. Kruse's 1991 result was for manufacturing, which a bakery broadly is. Applied naively to 140 people, a 2.0 percent fall rather than a 3.1 percent fall is the difference between about 2.8 and about 4.3 jobs for each point the local unemployment rate rises. That is roughly one and a half jobs. The figures come from firms in 1971 to 1985 with profit-sharing pension plans, not cash plans, so the comparison is illustrative only. What the study does support is the mechanism: when part of pay moves with profit, a firm has a way to absorb a bad year that does not run through redundancy.

Survival. Kurtulus and Kruse found an association between broad employee ownership and greater stability and survival through the recessions of 1999 to 2011.[47] That study concerns ownership, not profit sharing, and it leads to step three.

Step three: the question of succession

The owner's real question was never profit sharing. It was who will own the bakery when she stops.

The evidence on succession is thinner than the evidence on performance, and this chapter will not pretend otherwise. What can be said is structural. In the United States the instrument for a sale to employees is Kelso's ESOP, which can borrow to buy the owner's shares and repay the loan from the company's earnings. In the United Kingdom, since the Finance Act 2014, the employee ownership trust offers a simpler route with tax relief for the seller.[48] Both need lawyers, valuers and time. Neither should be designed from a book.

What a book can say is what the first two steps did. By the time the owner raises succession, the people downstairs have watched the numbers for a year and shared in them twice. The conversation about owning the firm is no longer abstract. Santa Anna's notes on cooperative ownership put the cost of this honestly: "Yes, it requires more conversation. But so does keeping a forest from burning."[41]

His book offers the question the owner should ask before any adviser is hired. In its reflection questions it invites the reader to imagine redesigning "one structural feature of your workplace or economic life" and specifies what that means: "not a policy or a perk, but an actual *structural* element."[49] A Christmas bonus is a perk. Numbers on a wall are a policy. Who owns the bakery is a structure.

What the owner said on the floor

Numbers do not introduce themselves. In the composite, the owner announced the profit share at the end of a Friday shift, standing on the packing floor rather than writing from upstairs, and what she said is worth setting down because the words carried as much of the design as the arithmetic did.

She began with the figures everyone had been watching on the wall for six months. "You have seen what we make in a normal month and in a bad one. From January, ten percent of the profit before tax is yours, paid in June and December." She then said what it would be in a normal year, $893 for a full-time baker, and what it would have been in the firm's worst year of the last five. She said it would come on top of wages and that wages would not be cut to pay for it. She said half of it would be the same for everyone, and why. And she said what it was not: "This is not ownership of the bakery. That is a bigger question, and I would like us to answer it together over the next two years."

Three questions came at once. A night baker asked whether part-timers were in; the owner said they would be in, pro rata to hours, and wrote it into the plan that week. A driver asked who would check the profit figure; she offered to have the accountant explain the accounts to anyone who wanted to come, and nine people did. The sales manager asked whether the equal half was fair to people who carried more responsibility; she said that the pay-weighted half answered that, that the split was a choice, and that it would be reviewed after a year with whoever wanted a say.

Each of those answers is a piece of the design that Chapter 3's objections called for. Part-timers answered the exclusion objection. An open explanation of the accounts answered the voice objection. A review of the split, with a date, answered the drift. None of them cost money. All of them were decided in public, which is what made them believable.

Santa Anna's notes on finance describe the alternative to principal-agent supervision in one phrase: "Decisions are made where information and impact intersect."[50] The packing floor on that Friday was such a place. The owner had the information; the people in front of her would feel the impact. The conversation that followed was the first in which both were present at once.

The finer points

A few lessons from working the case apply well beyond bakeries.

Price the plan at its net cost, not its gross. Most firms already spend something on discretionary rewards. Folding it in shows the true decision.

Decide the split in writing, with reasons. Every split favours someone. The record of why is what makes it fair.

Model the bad year before the good one. A plan that only works in good years is a bonus scheme. Show people what the share would have been in the firm's worst recent year.

Keep the share on top of the wage. This is the single most important protection for the household on the other side of the plan.

Treat succession as a third step, not a first. Information and a visible share build the relationship that ownership then formalises.

For a firm working out where the value it might share is actually made, the Alpha Papers' reading of the value chain is the right instrument. For the history of incentive plans tied to measured improvement rather than to profit, the lineage's gainsharing series covers the ground (*The Gain Was Always Shared*), and readers interested in what patient ownership does to a firm's horizon will find Colin Mayer's work in the series on patient capital (*The Long Clock*).

The bakery is a composite and its future is the writer's to imagine. In this telling, a year later, the owner is still at the small desk at nine. The difference is that the figures on her desk are also on the wall downstairs.

The Tool: The Shared Capitalism Readiness Sheet

Complete with your own figures. Where a figure is an estimate, mark it (e). Where it comes from the accounts, mark it (a).

1 · The firm

ITEM	FIGURE	SOURCE (A/E)
Employees		
Total payroll		
Average pay (payroll ÷ employees)		
Revenue		
Pre-tax profit, normal year		
Pre-tax profit, worst year of the last five		
Current discretionary rewards (bonuses etc.)		

2 · The numbers on the wall

- Four figures we will post monthly, each one that people can affect: 1 __ 2 _ *3 4* ___
- Date of the first monthly question session: _____

3 · The profit share

- Pool as a share of pre-tax profit: __ % → normal-year pool: $____
- Net new cost (pool less current discretionary rewards): $_____
- Split: equal __ % · pay-weighted ____ %
- Equal share per person: $_____ (equal part ÷ eligible employees)
- Pay-weighted rate: _____ cents per dollar of pay (pay-weighted part ÷ payroll × 100)
- Share for our lowest-paid full-time role: $__ = ____ % of pay
- Share for our highest-paid role: $__ = ____ % of pay
- Same three lines for the worst year: $__ · $_ · $___
- Is every share paid on top of a market wage? yes · no

4 · Succession (for owners considering a sale)

- Earliest year a sale might happen: _____
- Routes to explore with advisers: ESOP · employee ownership trust · cooperative conversion · other: _____
- Months of open numbers and shared profit we will have behind us before raising it: _____

5 · The one structural question

- The one structural feature of this workplace we would redesign, in a sentence: _____

A NOTE FROM THE HOUSE

The bakery's arithmetic is worked from its own accounts and the published evidence before anyone decides who should own what. A gainshare is often the first step on the same road: a share in a measured gain, with no change of ownership at all. Luminous Prosperity Inc. does this work inside organisations, and is paid as a share of the gain it helps find.

REQUEST A CONVERSATION

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