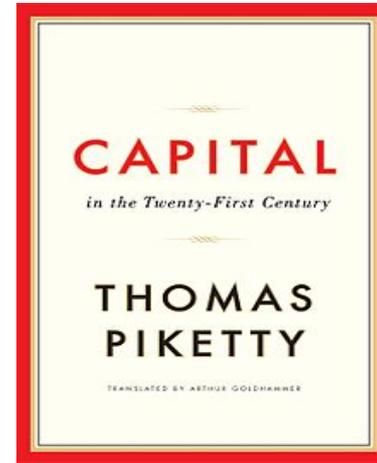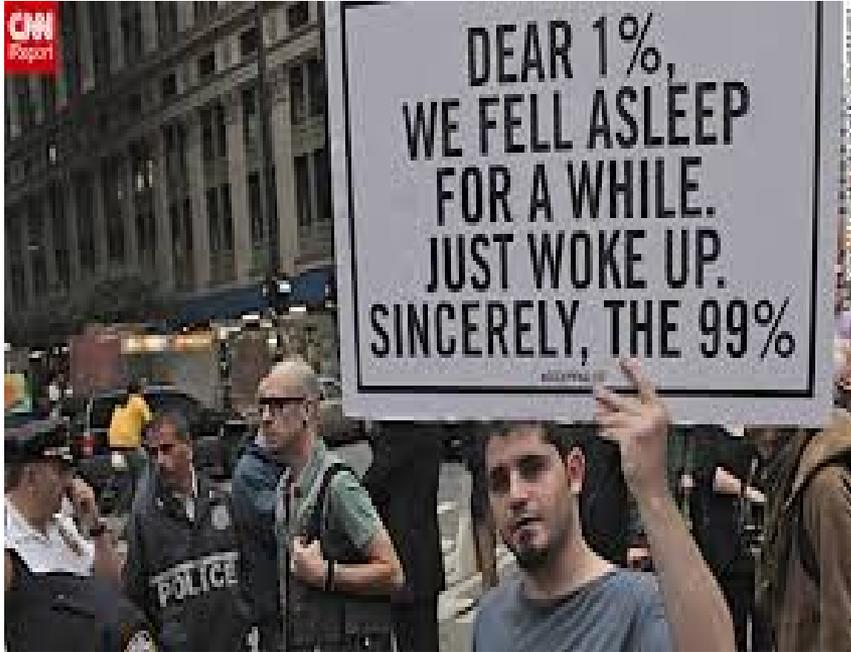# Tackling Inequality through Employee Ownership: prospects and challenges

Gabriel Burdin

IPSA Annual Conference 2016, Dublin
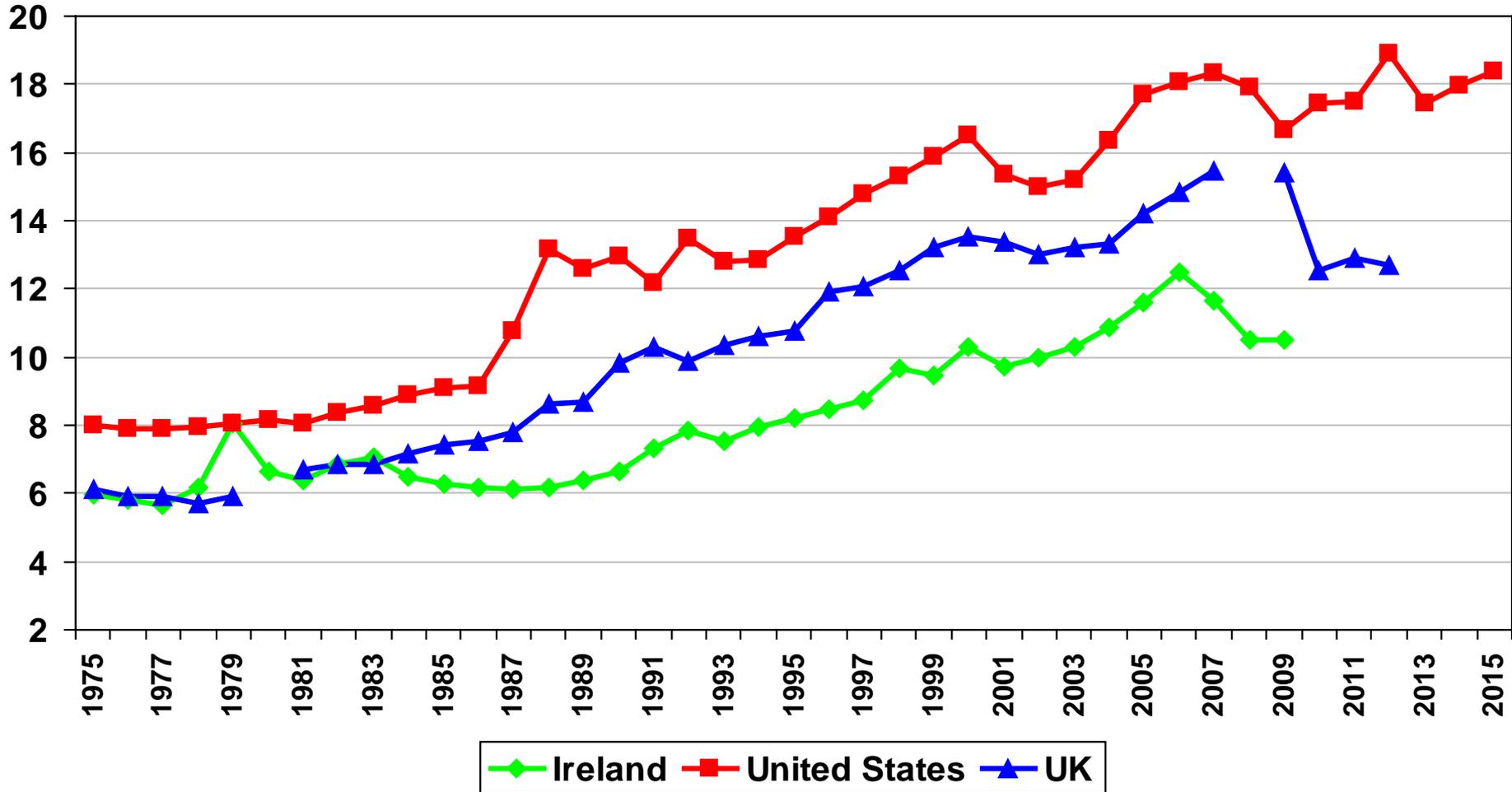
Inequality is back on the scene

Word cloud, UCL's new first year students, 2016

Source: CORE Project

Top 1% Income Share: US, UK, Ireland

Source: The World Wealth and Income Database

Policy debate focused on taxation, but role of employee participation in corporate governance/ownership is becoming increasingly recognised

"(…) I tend to devote too much attention to progressive taxation and too little attention to a number of other important institutional evolutions, such as the development of alternative forms of property arrangements and participatory governance. (…) increased financial transparency can help to develop new forms of governance (for instance it can facilitate more worker involvement in company boards)" (Piketty, 2014, BJS: p755).

Employee participation: Control/Ownership

Why Employee Ownership may help in reducing pay inequality?

- Median voter equilibrium (Kremer, 1997)
  - If the median member is less productive than the average (few voters are top performers), the majority can gain by reducing compensation differences relative to differences in productivity

- Employee Ownership may help to curb excessive (non-competitive) executive compensation within firms. Drivers of CEOs pay? (productivity, luck, rent-seeking).

- Employee-owned firms rely more heavily on teamwork and horizontal cooperation. Greater pay equality may be optimal in such contexts.

- Equal sharing rule a a simple focal point (Hansmann, 1996).
  - Using a political process to decide on a more complex compensation scheme would be time-consuming and divisive for all involved (Hansmann, 1996).

- Inequality-averse managers-workers may be self-selected into employee owned firms.

What does the evidence tell us?

- Mondragon Cooperatives (Basque Country):
    - Strict rules limiting wage differentials among members (Dow, 2003). Initially, the highest wage was constrained to be no more than three times the lowest wage (increased to six times in 1987).
    - Despite recent changes, managers still earn substantially less than in the outside market.

- Italian Cooperatives:
    - Bartlett et al. (1992) provided comparative evidence of worker cooperatives and conventional firms in north-central Italy.
    - Wage differentials in the coops "sharply compressed" compared to conventional firms.

- Plywood Cooperatives (United States):
    - Craig and Pencavel (1995) observed lower wage differentials in worker coops than in conventional plywood firms in the U.S. Pacific Northwest

Uruguayan Worker Cooperatives

- *"Equality under threat by the talented: evidence from worker-managed firms"* (2016: The Economic Journal)

- Research questions:
    - Do worker cooperatives actually exhibit a more compressed compensation structure than conventional firms?
    - Are high-ability members in worker coops more likely (than other members) to exit?

- Data:
    - Administrative records from social security (January 1997 to July 2009)
    - Matched organization-worker data for the entire population of WCs
    - Sample of workers employed in conventional firms

Wage inequality is lower among WC members than among employees in conventional sector: Gini inequality index
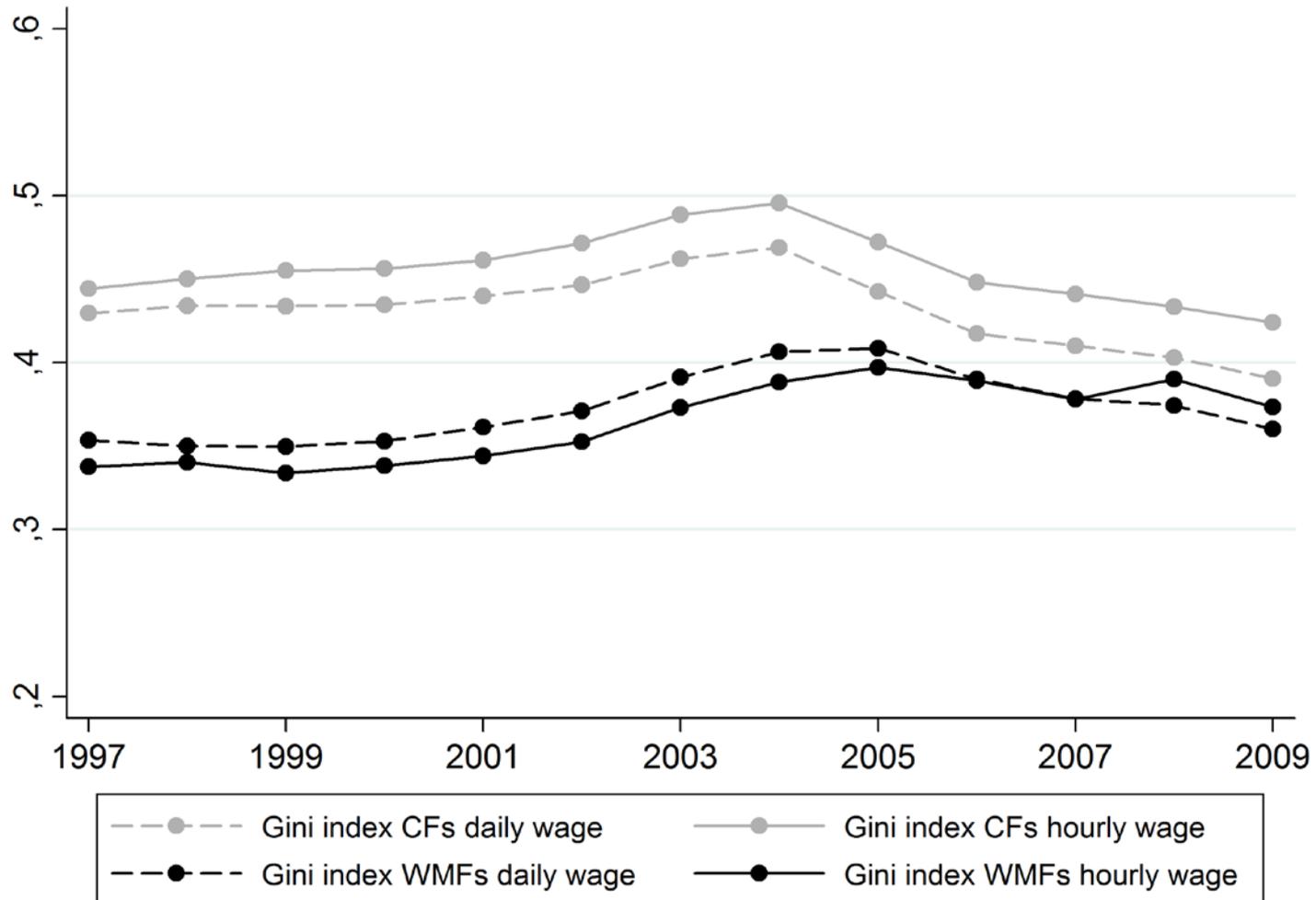
Source: Burdin (2016)

The Median Voter at work: Mean-to-median compensation ratio in WCs and conventional firms
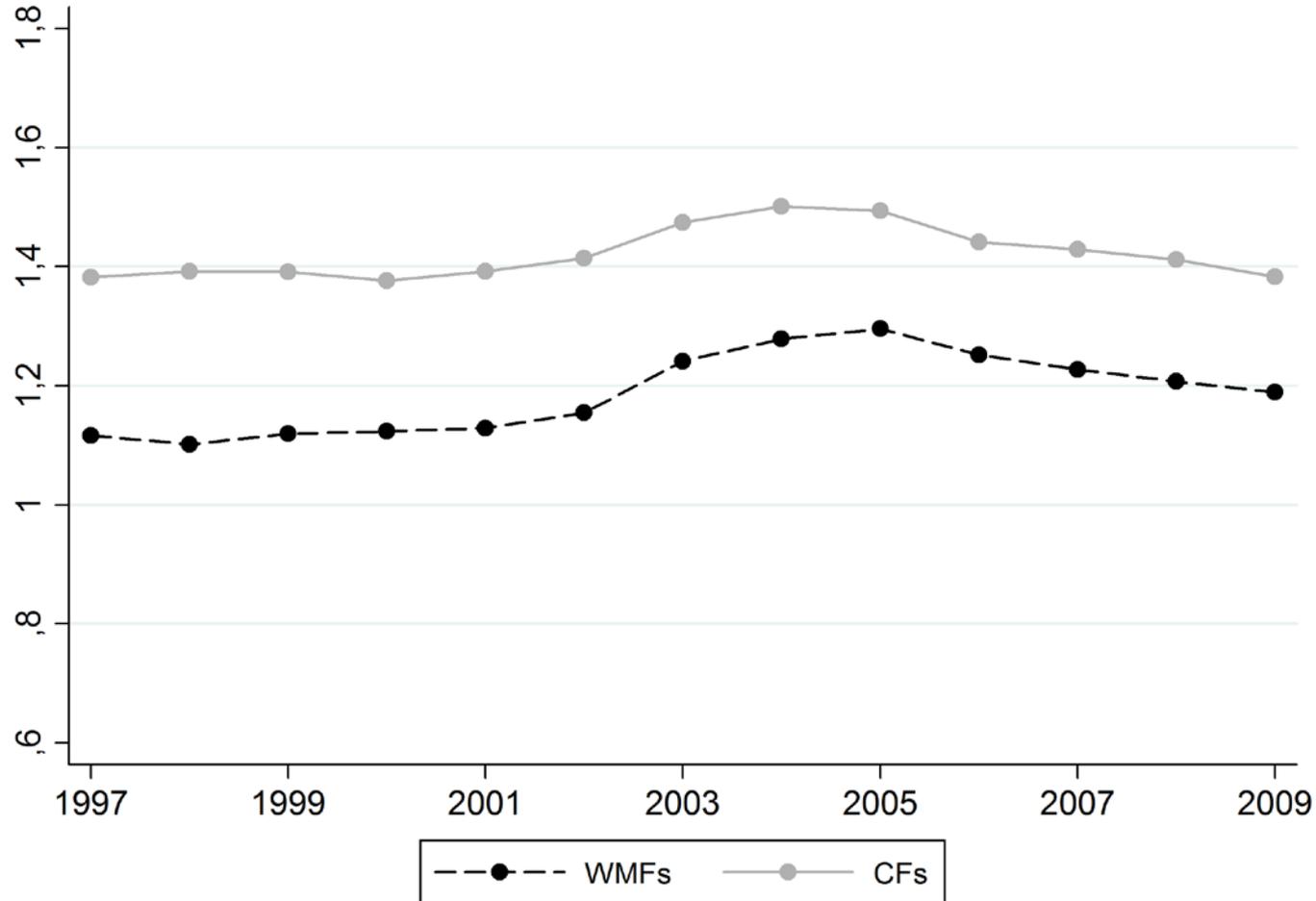
Source: Burdin (2016)

Worker coops' members enjoy a small wage premium compared to similar workers employed in CFs

TABLE I
WAGE GAP BETWEEN WORKERS EMPLOYED IN WMFs AND CFs

|	Pooled OLS	FE	FE	FE	FE
	(1)	(2)	(3)	(4)	(5)
Coop	0.055**	0.027*	0.028*	0.092**	0.091**
	(0.011)	(0.015)	(0.016)	(0.038)	(0.038)
Female	-0.230***				
	(0.005)				
Age	0.060***	0.210***	0.212***	0.212***	0.211***
	(0.001)	(0.002)	(0.002)	(0.002)	(0.002)
Age Squared	-0.001***	-0.001***	-0.001***	-0.001***	-0.001***
	(0.000)	(0.000)	(0.000)	(0.000)	(0.000)
Tenure	0.047***	0.032***	0.030***	0.030***	0.030***
	(0.001)	(0.001)	(0.001)	(0.001)	(0.001)
Tenure Squared	-0.001***	-0.001***	-0.001***	-0.001***	-0.001***
	(0.000)	(0.000)	(0.000)	(0.000)	(0.000)
Firm size (in logs)	0.153***	0.122***	0.099***	0.100***	0.099***
	(0.001)	(0.001)	(0.002)	(0.002)	(0.002)
Year fixed effects	Yes	Yes	Yes	Yes	Yes
Industry fixed effects	Yes	Yes	Yes	Yes	Yes
Observations	5,264,811	5,264,811	3,533,031	3,445,097	3,445,097

Notes: The dependent variable is the log of daily wage. Column (1) reports Pooled OLS estimates. Columns (2)-(5) report panel data fixed effects estimates.. Estimates reported in Column (3)-(5) exclude workers employed in micro-enterprises (<6 workers). Estimates in Column (4)-(5) compare employees in CFs with members in WMFs (nonmembers are excluded). All estimates include a set of 13 year and 6 industry dummies. Estimates in Column (5) also include sectoral-specific year fixed effects. Standard errors clustered at the individual level. * significant at 10%; ** significant at 5%; *** significant at 1%

Low-wage members of WC benefit disproportionally. Wage penalty for top earners.

	2009			
	q20	q40	q60	q80
Coop	0.160***	0.114***	0.059***	−0.039***
	(0.008)	(0.005)	(0.005)	(0.006)
Age	0.031***	0.038***	0.045***	0.065***
	(0.001)	(0.001)	(0.001)	(0.001)
Age squared	−0.001***	−0.001***	−0.001***	−0.001***
	(0.000)	(0.000)	(0.000)	(0.000)
Female	−0.202***	−0.211***	−0.240***	−0.263***
	(0.002)	(0.002)	(0.002)	(0.003)
Tenure	0.038***	0.044***	0.048***	0.049***
	(0.000)	(0.000)	(0.000)	(0.001)
Tenure squared	−0.001***	−0.001***	−0.001***	−0.001***
	(0.000)	(0.000)	(0.000)	(0.000)
Firm size	0.106***	0.107***	0.112***	0.122***
	(0.001)	(0.001)	(0.001)	(0.001)
Test of interquantile Differences				
20th = 40th	[.000]			
20th = 80th	[.000]			
40th = 80th		[.000]		
Observations	492,771	492,771	492,771	492,771

Notes: The dependent variable is the log of daily wages. The *Coop* dummy variable is set equal to 1 only for workers employed in a PC. Firm size is measured as the log of total employment in each firm. All estimates include six industry dummies. Bootstrapped standard errors (reported in parentheses) are based on 200 replications. *** significant at 1%.

Brain drain effect: Hazard of voluntary separation for high-wage members is significantly higher compared to low-wage members


Fig IIIc. Members in WMFs. Kaplan-Meier survival estimate
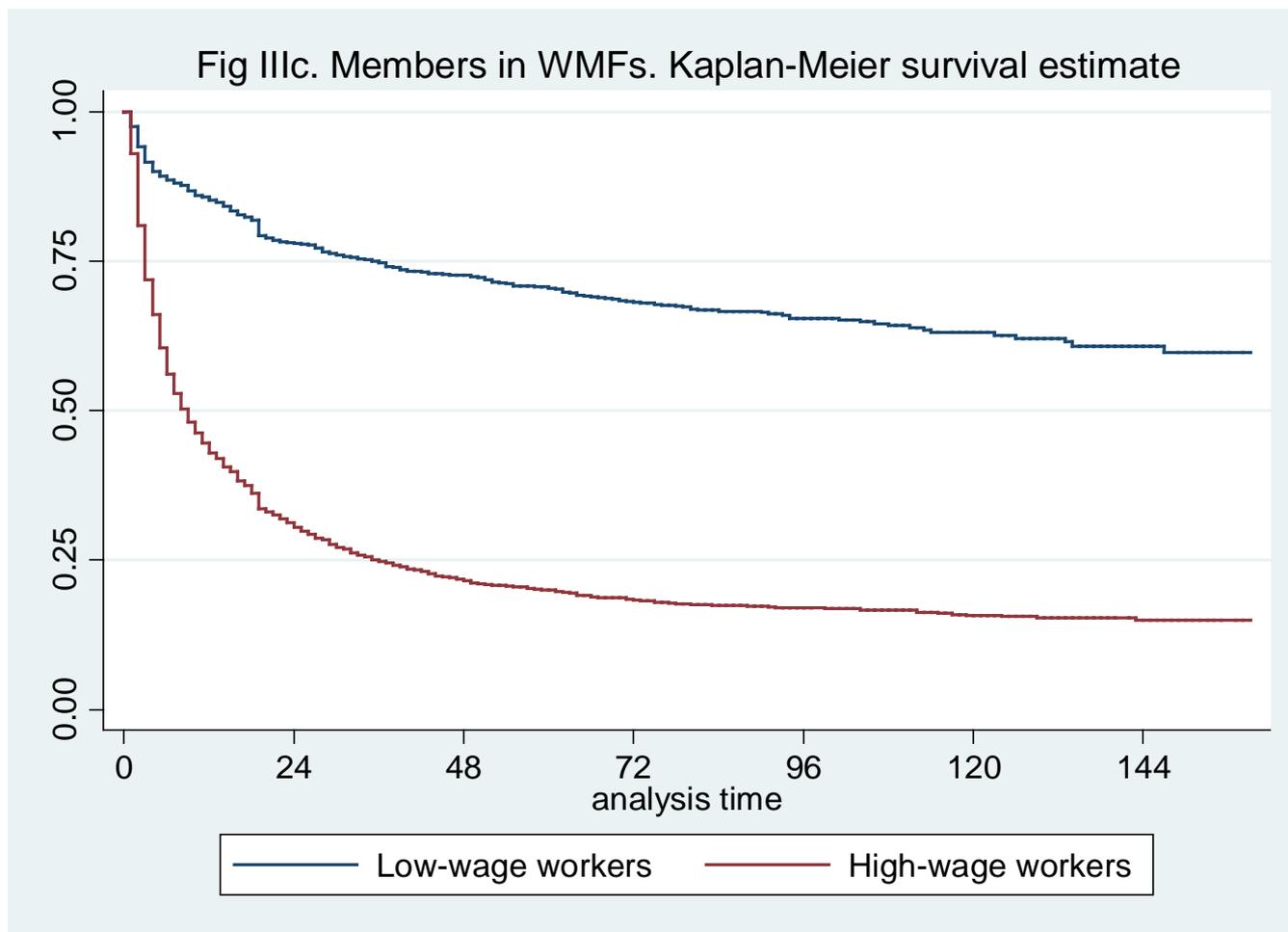
# Pay equality may also entail benefits for employee-owned firms

- It is not clear whether inequality maps into organizational performance. Employee-owned firms perform as well as (or even better than) conventional firms in many contexts (Burdin, 2014; Perotin, 2014).

- Efficiency losses due to inferior management should be compared with potential gains in shop-floor labour effort regulation. Low-wage workers may be highly motivated. (Ben Ner, 1988).

- Inequality may increase perceptions of unfairness among workers, eroding workplace cooperation and increasing the scope for rent-seeking activities within firms (Lazear, 1989; Levine, 1991; Milgrom and Roberts, 1990).

- People care about absolute and relative income. Pay comparisons within organizations reduce the job satisfaction for workers at the bottom of the wage distribution (Card et al., 2012)

Complementarity between EO & other policy tools
EO can help deal with intra-firm inequality, but pay inequality is mainly a between-firm phenomenon
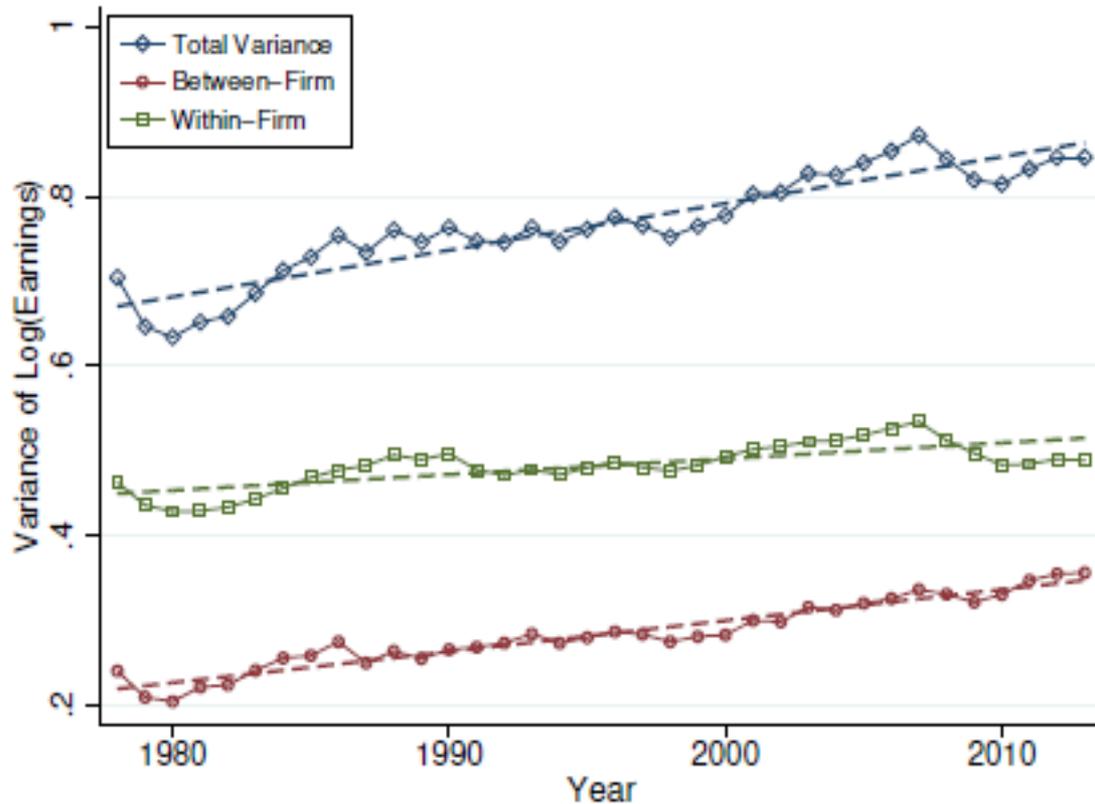

Since a system of syndicalist factories would involve great inequalities of income among workers in different factories (with different amounts of capital per worker and different profitability), it is difficult to see why people who favor certain egalitarian end-state patterns think this a suitable realization of their vision.
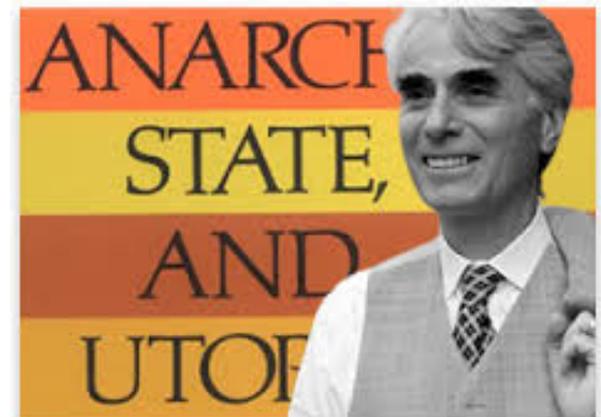
Source: Song et al (2016)

Final remarks

- His work has been crucial for understanding the role of asset ownership and how the allocation of control rights over firms is driven by efficiency considerations.

- Employee ownership may be an optimal property arrangement, particularly when investments in firm-specific human capital (skills, organizational culture, etc) are relatively important.

- Ownership protects workers against arbitrary use and abuse of authority (firm-specific skills prevent labour mobility).

- Employee Ownership should be part of the policy toolkit to redistribute wealth and income: it strongly benefits low-wage workers.

- But in some contexts equality is not a free lunch. EO firms face a trade-off between its counter-productive effects (brain drain) and its benefits (greater workplace cooperation and motivation).
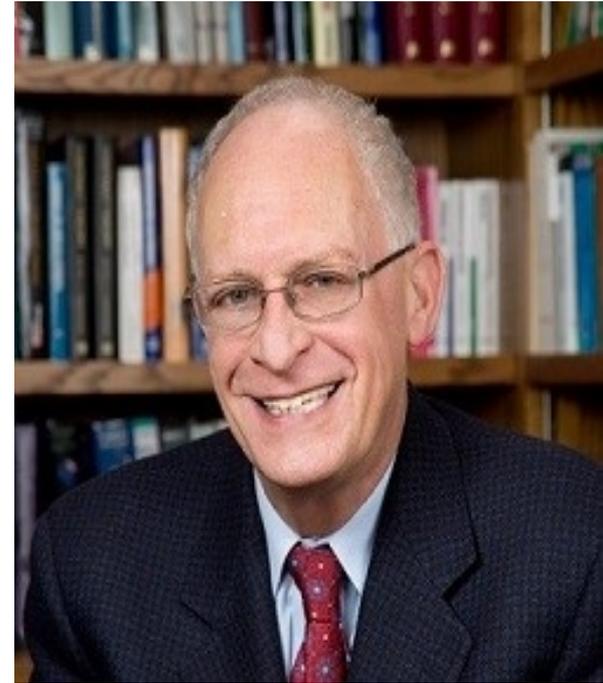
Oliver Hart
Nobel Prize in Economics 2016

Thank you !