



E.F. Schumacher
Small is
Beautiful
Economics as if
People Mattered

Chapter 19

New Patterns of Ownership

A Lonergan Institute Seminar

St Anselm's Abbey

From Schumacher:

“The conventional view serves to protect us from the painful job of thinking.”

— **John Kenneth Galbraith**

“J. K. Galbraith has spoken of private affluence and public squalor. It is significant that he referred to the United States, reputedly, and in accordance with conventional measurements, the richest country in the world. How could there be public squalor in the richest country, and, in fact, much more of it than in many other countries whose Gross National Product, adjusted for size of population, is markedly smaller? If economic growth to the present American level has been unable to get rid of public squalor - or, maybe, has even been accompanied by its increase - how could one reasonably expect that further 'growth' would mitigate or remove it?”

What are our initial thoughts on Schumacher's starting premise?



From Schumacher:

"...for under private ownership every bit of wealth, as it arises, is immediately and automatically privately appropriated. The public authorities have hardly any income of their own and are reduced to extracting from the pockets of their citizens monies which the citizens consider to be rightfully their own. Not surprisingly, this leads to an endless battle of wits between tax collectors and citizens, in which the rich, with the help of highly paid tax experts, normally do very much better than the poor. In an effort to stop 'loopholes' the tax laws become ever more complicated and the demand for - and therefore the income of - tax consultants becomes ever larger. As the taxpayers feel that some- thing they have earned is being taken away from them, they not only try to exploit every possibility of legal tax avoidance, not to mention practices of illegal tax evasion, they also raise an insistent cry in favor of the curtailment of public expenditure."

The Tax Collectors by Quentin Massys (1466-1530)

From Schumacher:



Private Wealth, Public Squalor: America's Dilemma

“There is no way out of this dilemma unless the need for public expenditure is recognized in the structure of ownership of the means of production. It is not merely a question of public squalor, such as the squalor of many mental homes, of prisons, and of countless other publicly maintained services and institutions; this is the negative side of the problem. The positive side arises where large amounts of public funds have been and are being spent on what is generally called the 'infrastructure', and the benefits go largely to private enterprise free of charge.”

From Schumacher:



“All the educational, medical, and research institutions in any society, whether rich or poor, bestow incalculable benefits upon private enterprise - benefits for which private enterprise does not pay directly as a matter of course, but only indirectly by way of taxes, which, as already mentioned, are resisted, resented, campaigned against, and often skillfully avoided.”

Tax payment to a lord, illumination on parchment, ca. 1490

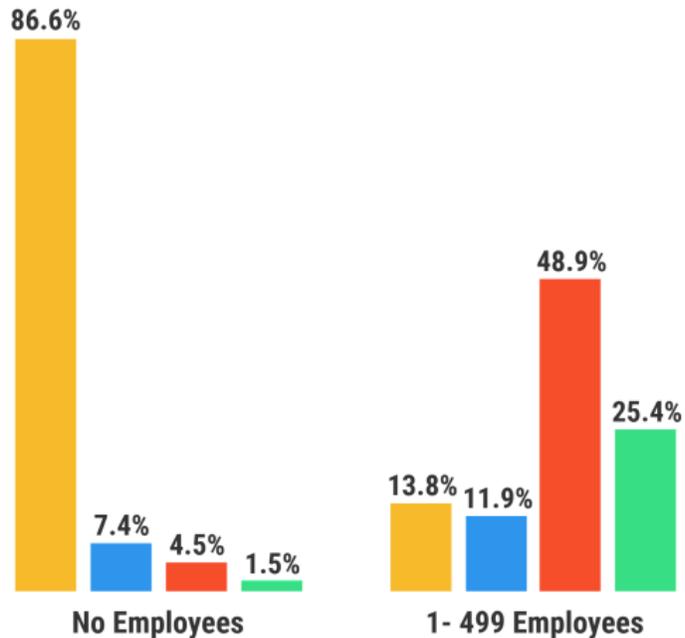
From Schumacher:



“Private enterprise claims that its profits are being earned by its own efforts, and that a substantial part of them is then taxed away by public authorities. This is not a correct reflection of the truth - generally speaking. The truth is that a large part of the costs of private enterprise has been borne by the public authorities - because they pay for the infrastructure and that the profits of private enterprise therefore greatly over- state its achievement.”

U.S. Small Businesses by Legal Structure

● Sole Proprietor ● Partnership ● S Corp ● C corp



(c) 2020, Small Business Trends Data source: SBA

From Schumacher:

“I shall therefore now present two examples of how the structure of ownership can - or could - be changed so as to meet the two fundamental criticisms made above. The first example is of a medium-sized firm which is actually operating on a reformed basis of ownership. The second example is a speculative plan of how the structure of ownership of large-scale firms could be re-formed.”

Example 1: The Scott Bader Commonwealth



Eugene Delacroix. Liberty Leading The People, 1830. Louvre Museum, public domain.

He decided to introduce 'revolutionary changes' in his firm, 'based on a philosophy which attempts to fit industry to human needs'. 'The problem was twofold: (1) how to organize or combine a - maximum sense of freedom, happiness and human dignity in our firm without loss of profitability, and (2) to do this by ways and means that could be generally acceptable to the private sector of industry.

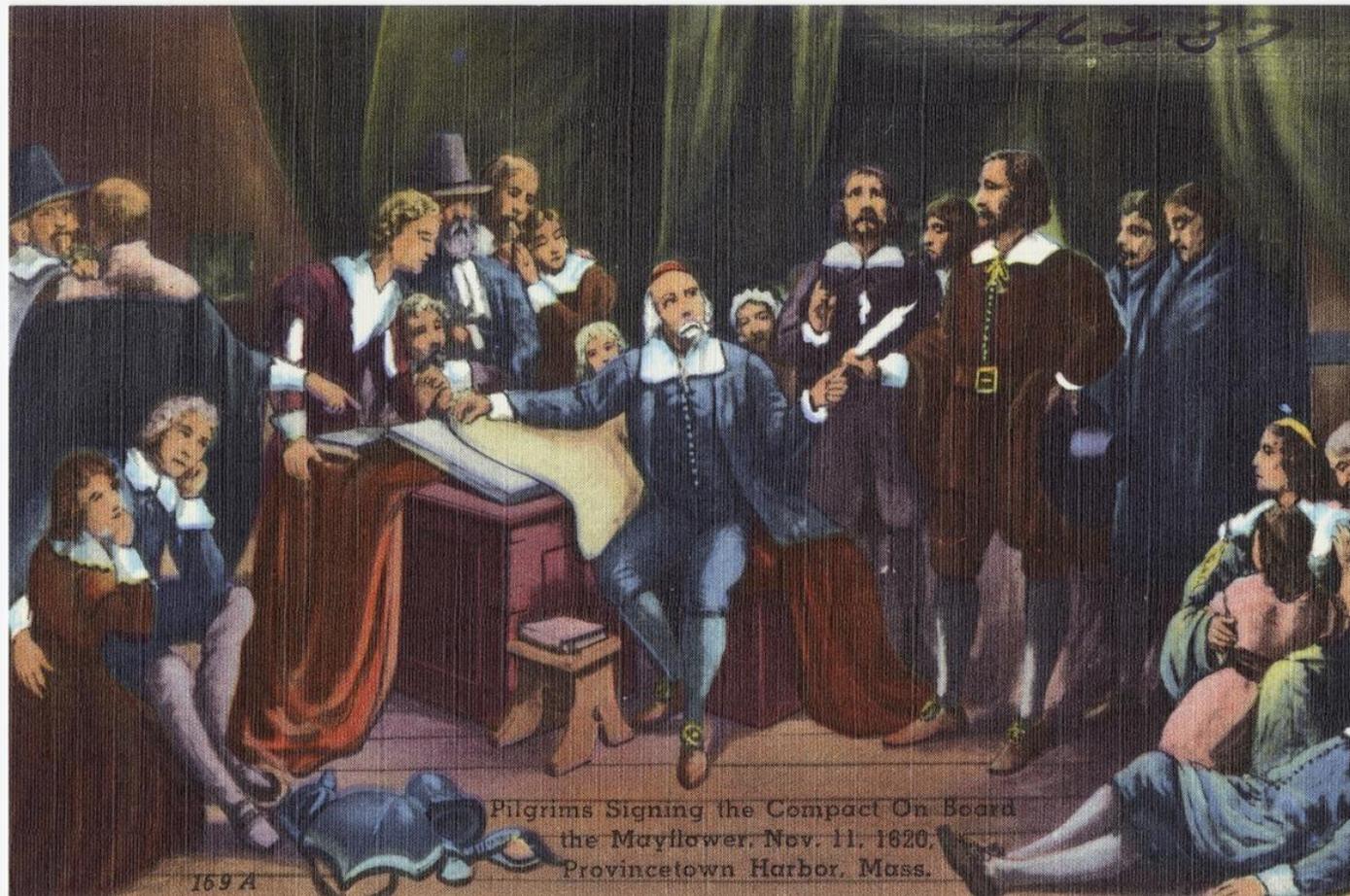


Seal of the Commonwealth of Virginia

The Scott Bader Commonwealth

“Mr. Bader realized at once that no decisive changes could be made without two things: first, a transformation of ownership - mere profit-sharing, which he had practiced from the very start, was not enough; and, second, the voluntary acceptance of certain self-denying ordinances. To achieve the first, he set up the Scott Bader Commonwealth in which he vested (in two steps: ninety per cent in 1951 and the remaining ten per cent in 1963) the ownership of his firm, Scott Bader Co Ltd. To implement the second, he agreed with his new partners, that is to say, the members of the Commonwealth, his former employees, to establish a constitution not only to define the distribution of the 'bundle of powers' which private ownership implies, but also to impose the following restrictions on the firm's freedom of action.”

The Scott Bader Commonwealth



Pilgrims Signing the Compact On Board
the Mayflower, Nov. 11, 1620,
Provincetown Harbor, Mass.

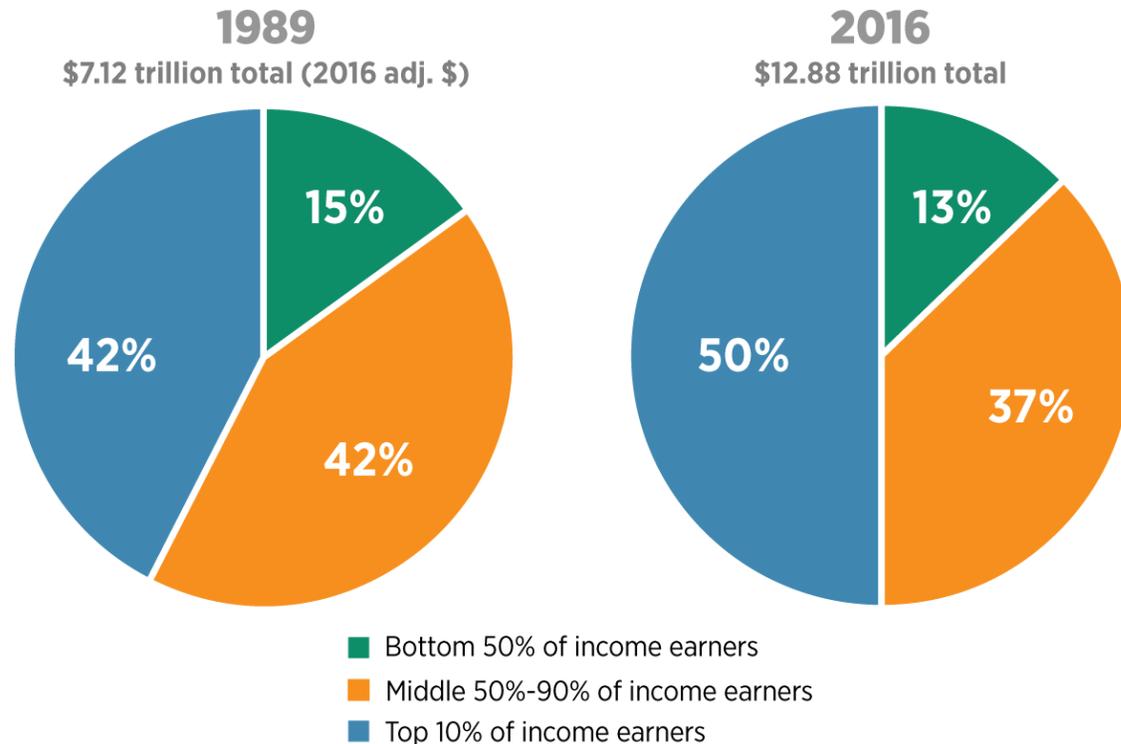
*Pilgrims signing the compact on board the Mayflower, Nov 11, 1620,
Provincetown Harbor, Mass.*

“First, the firm shall remain an undertaking of limited size, so that every person in it can embrace it in his mind and imagination. It shall not grow beyond 350 persons or thereabouts. If circumstances appear to demand growth beyond this limit, they shall be met by helping to set up new, fully independent units organized along the lines of the Scott Bader Commonwealth.”

The Scott Bader Commonwealth

Income Distribution (Pre-tax)

How U.S. earners' shares of the total household income pie have changed

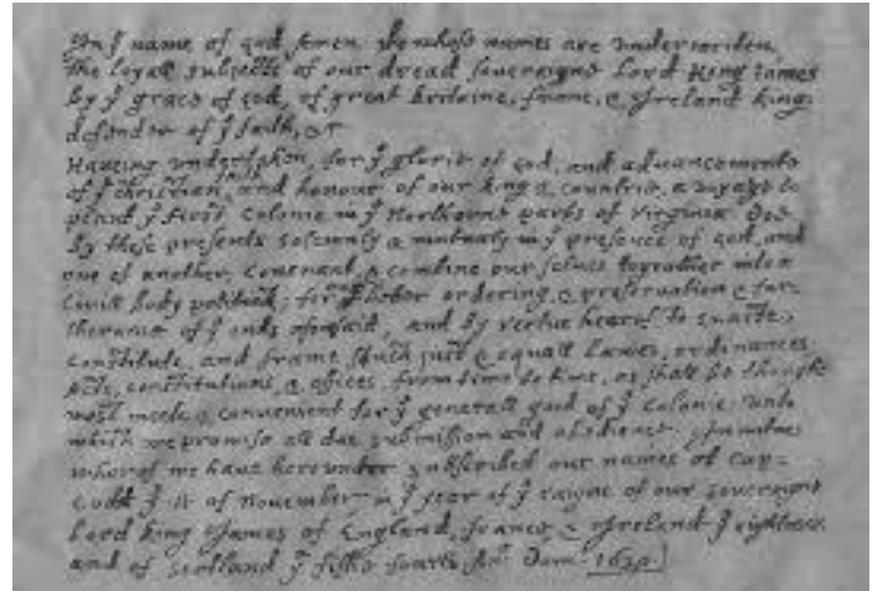


■ FEDERAL RESERVE BANK OF ST. LOUIS

"Second, remuneration for work within the organization shall not vary, as between the lowest paid and the highest paid, irrespective of age, sex, function or experience, beyond a range of 1:7, before tax."

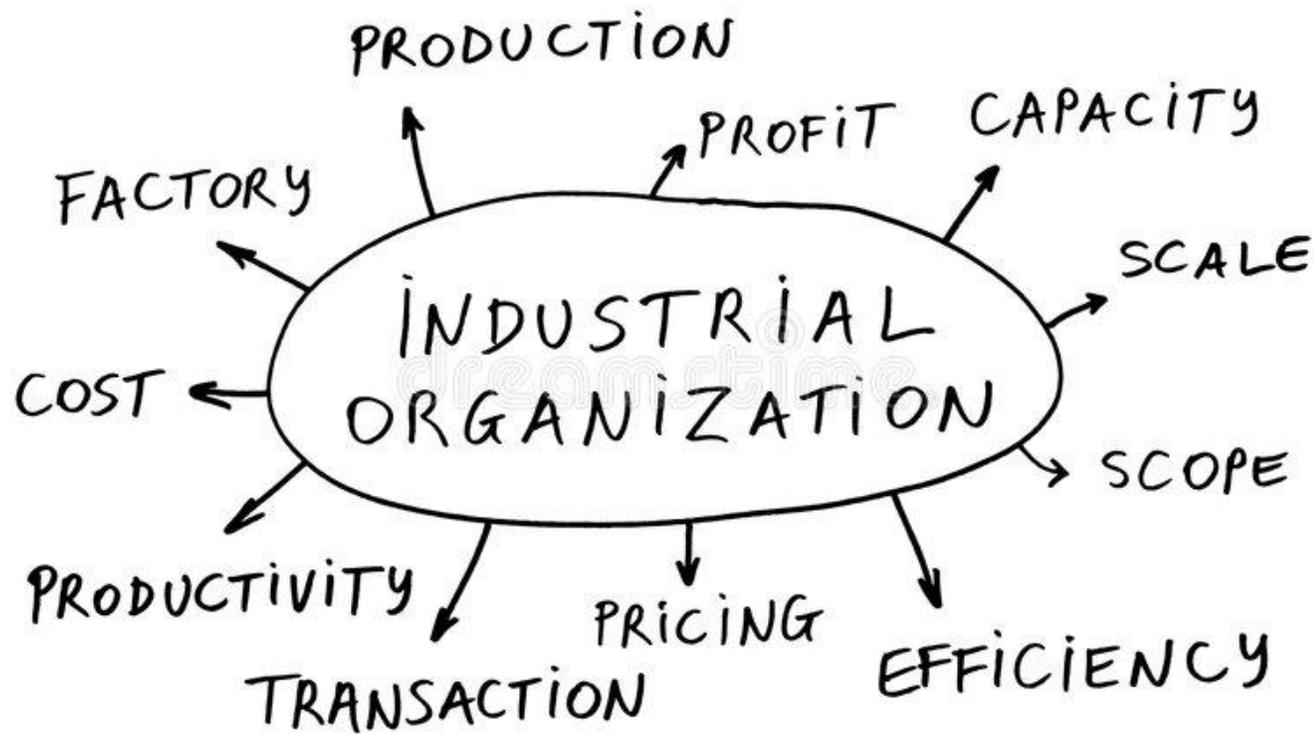
The Scott Bader Commonwealth

“Third, as the members of the Commonwealth are partners and not employees, they cannot be dismissed by their co-partners for any reason other than gross personal misconduct. They can, of course, leave voluntarily at any time, giving due notice. Fourth, the Board of Directors of the firm, Scott Bader Co Ltd, shall be fully accountable to the Commonwealth. Under the rules laid down in the Constitution, the Commonwealth has the right and duty to confirm or withdraw the appointment of directors and also to agree their level of remuneration. Fifth, not more than forty per cent of the net profits of Scott Bader Co Ltd shall be appropriated by the Commonwealth - a minimum of sixty per cent being retained for taxation and for self-finance within Scott Bader Co Ltd - and the Commonwealth shall devote one-half of the appropriated profits to the payment of bonuses to those working within the operating company and the other half to charitable purposes outside the Scott Bader organization. And finally, none of the products of Scott Bader Co Ltd shall be sold to customers who are known to use them for war related purposes.”



The Mayflower Compact

The Scott Bader Commonwealth

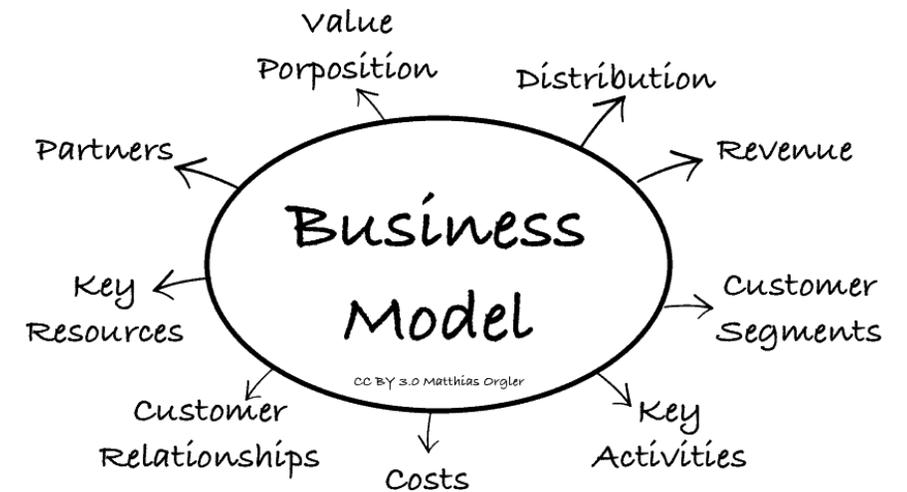


"In other words, the Bader 'system' overcomes the reductionism of the private ownership system and uses industrial organization as a servant of man, instead of allowing it to use men simply as means to the enrichment of the owners of capital."

The Scott Bader Commonwealth

“The Commonwealth, accordingly, recognized that the tasks of a business organization in society are not simply to make profits and to maximize profits and to grow and to become powerful: the Commonwealth recognized four tasks, all of equal importance:

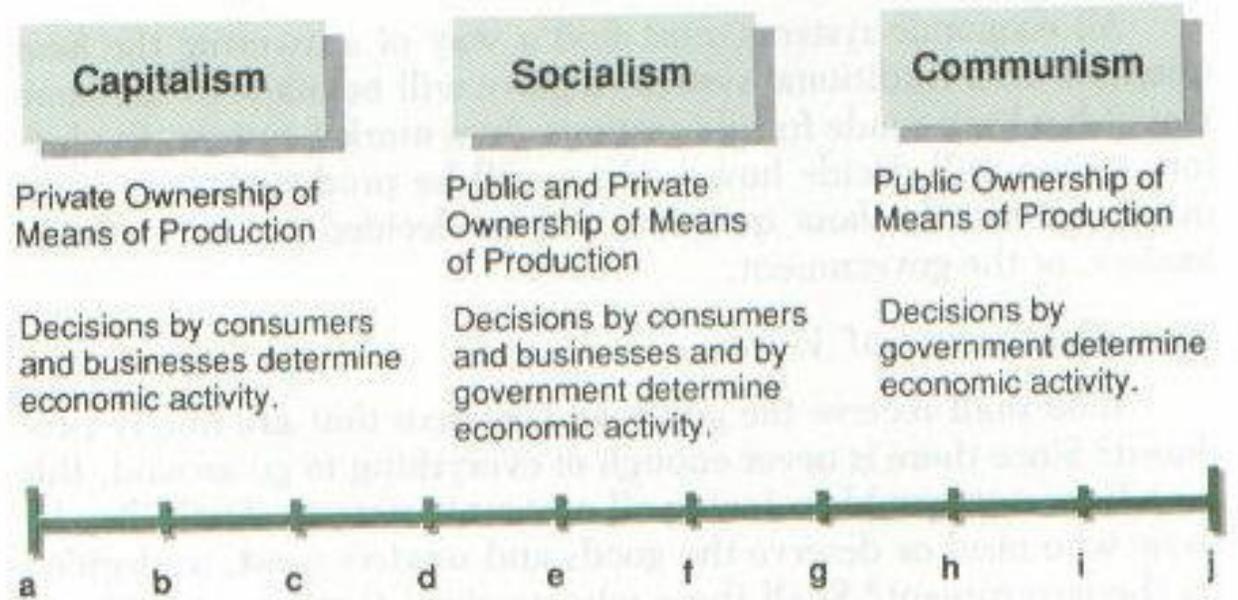
- (A) The economic task: to secure orders which can be designed, made, and serviced in such a manner as to make a profit.
- (B) The technical task: to enable marketing to secure profitable orders by keeping them supplied with up-to-date product design.
- (C) The social task to provide members of the company with opportunities for satisfaction and development through their participation in the working community
- (D) The political task: to encourage other men and women to change society by offering them an example by being economically healthy and socially responsible.”



What is the right way to organize a business?

New Methods of Socialization

“There appear to be three major choices for a society in which economic affairs necessarily absorb major attention - the choice between private ownership of the means of production and, alternatively, various types of public or collectivized ownership: the choice between a market economy and various arrangements of 'planning'; and the choice between 'freedom' and 'totalitarianism'.”



New Methods of Socialization

The eight possible cases, as regards the three choices I have mentioned, are as follows:

- Case 1 Freedom Market Economy Private Ownership
- Case 2 Freedom Planning Private Ownership
- Case 3 Freedom Market Economy Collectivized Ownership
- Case 4 Freedom Planning Collectivized Ownership
- Case 5 Totalitarianism Market Economy Private Ownership
- Case 6 Totalitarianism Planning Private Ownership
- Case 7 Totalitarianism Market Economy Collectivized Ownership
- Case 8 Totalitarianism Planning Collectivized Ownership



New Methods of Socialization

"I have already argued that private enterprise in a so-called advanced society derives very large benefits from the infrastructure - both visible and invisible - which such a society has built up through public expenditure. But the public hand, although it defrays a considerable part of the cost of private enterprise, does not directly participate in its profits; all these profits are initially privately appropriated, and the public hand then has to try to cover its own financial requirements by extracting a part of these profits from private pockets. The modern businessman never tires of claiming and complaining that, to a large extent, he 'works for the state', that the state is his partner, inasmuch as profit taxes absorb a substantial part of what he believes to be really due to him alone, or to his shareholders. This suggests that the public share of private profits - in other words, the company profits taxes - might just as well be converted into a public share of the equity of private business - in any case as far as large-scale enterprises are concerned."



New Methods of Socialization

For the following exposition I postulate that the public hand should receive one-half of the distributed profits of large-scale private enterprise, and that it should obtain this share not by means of profit taxes but by means of a fifty per cent ownership of the equity of such enterprises.

1. To begin with, the minimum size of enterprises to be included in the scheme must be defined. Since every business loses its private and personal character and becomes, in fact, a public enterprise once the number of its employees rises above a certain limit, minimum size is probably best defined in terms of persons employed. In special cases it may be necessary to define size in terms of capital employed or turnover.
2. All enterprises attaining this minimum size - or exceeding it already - must be joint-stock companies.
3. It would be desirable to transform all shares of these companies into no-par shares after the American pattern.
4. The number of shares issued, including preference shares and any other pieces of paper which represent equity should be doubled by the issue of an equivalent number of new shares, these new shares to be held by 'the public hand' so that for every privately held old share one new share with identical rights will be held publicly.

Public entitled to



of distributed profits of publicly traded corporations obtained not through taxation but through



ownership of the equity of those enterprises.

New Methods of Socialization

- Under a scheme along these lines, no question of 'compensation' would arise, because there would be no expropriation in the strict sense of the word, but only a conversion of the public hand's right to levy profit taxes into a direct participation in the economic assets from the use of which taxable profits are obtained. This conversion would be an explicit recognition of the undoubted fact that a major role in the creation of 'private' economic wealth is in any case played by the public hand, that is to say, by non-capitalist social forces, and that the assets created by the public contribution should be recognized as public, and not private, property. The questions that would immediately arise may be divided into three groups. First, what precisely is meant by the 'public hand'? Where are the newly issued shares to be placed and who is to be the representative of the 'public hand' in this context? Second, what rights of ownership should possession of these new shares carry? And, third, questions relating to the transition from the existing system to the new, to the treatment of inter

No-par value stock is issued **without a par value**. The **value of no-par value stocks** is determined by the price investors are willing to pay on the open market. The advantage of **no-par value stock** is that companies can then issue **stock** at higher prices in future offerings.

New Methods of Socialization

"I therefore turn to the second set of questions. In principle, the rights associated with ownership can always be divided into two groups - managerial rights and pecuniary rights."

Bundles of Rights

Each stick represents a separate, distinct ownership right:

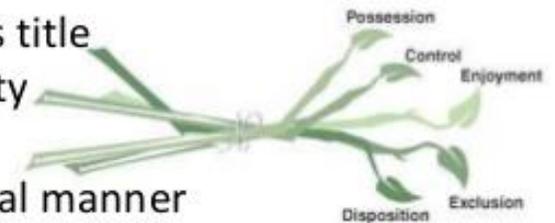
Possession: Owned by whomever holds title

Control: Controls the use of the property

Exclusion: Others can be excluded

Enjoyment: Use the property in any legal manner

Disposition: Sell, rent or transfer ownership



From Schumacher:

"I am convinced that, in normal circumstances, nothing would be gained and a great deal lost if a 'public hand' were to interfere with or restrict the freedom of action and the fullness of responsibility of the existing business managements. The 'private' managers of the enterprises should therefore remain fully in charge, while the managerial rights of the public half-share should remain dormant, unless and until special circumstances arise. That is to say, the publicly-held shares would normally carry no voting rights but only the right to information and observation. The 'public hand' would be entitled to place an observer - or several - on the Board of Directors of an enterprise, but the observer would not normally have any powers of decision. Only if the observer felt that the public interest demanded interference with the activities of the existing management, could he apply to a special court to have the dormant voting rights activated. A prima facie case in favor of interference would have to be established in front of the court, which would then activate the publicly-held voting rights for a limited period. In this way, the managerial rights of ownership associated with the new, publicly-owned equity shares would normally remain a mere possibility in the background and could become a reality only as a result of certain specific, formal, and public steps having been taken by the 'public hand'. And even when in exceptional cases these steps have been taken and the voting rights of the publicly-owned shares have been activated, the new situation would persist only for a short time, so that there should be no doubt as to what was to be considered a normal or an abnormal division of functions."

CHARACTERISTICS

Public Sector

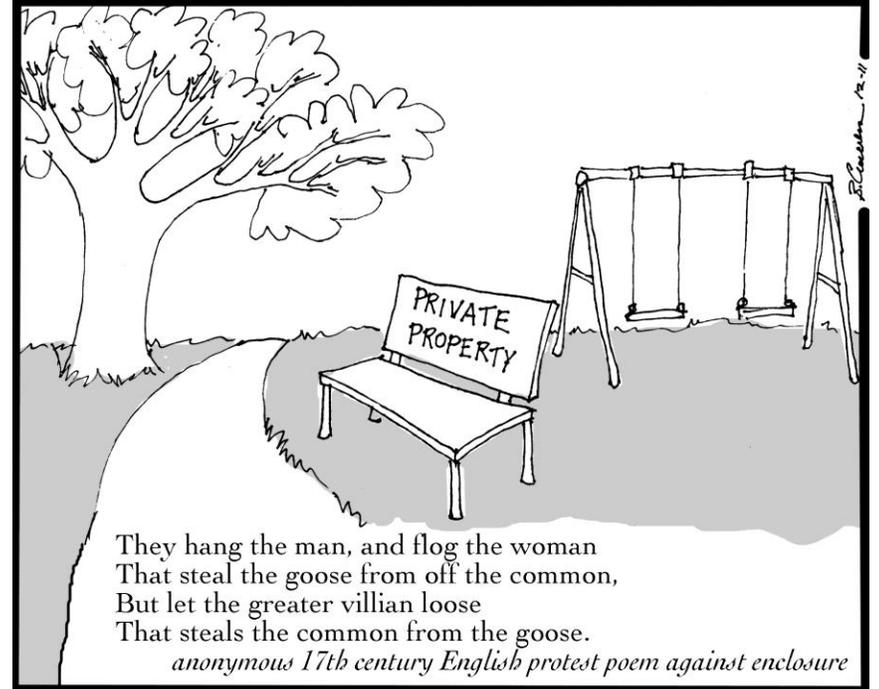
- ▶ State Ownership
- ▶ State Control
- ▶ State Financing
- ▶ Socio-economic objectives
- ▶ Public Accountability

Private Sector

- ▶ Private Ownership
- ▶ Private Management
- ▶ Private Financing
- ▶ Profit objective
- ▶ Private Accountability

From Schumacher

“Having thus briefly sketched the rights and duties associated with the new shares, we can now return to the question of personnel. The general aim of the scheme is to integrate large-scale business enterprises as closely as possible with their social surroundings, and this aim must govern also our solution of the personnel question. The exercise of the pecuniary and managerial rights and duties arising from industrial ownership should certainly be kept out of party-political controversy. At the same time, it should not fall to civil servants, who have been appointed for quite different purposes. I suggest, therefore, that it should belong to a special body of citizens which, for the purpose of this exposition, I shall call the 'Social Council'. This body should be formed locally along broadly fixed lines without political electioneering and without the assistance of any governmental authority, as follows: one-quarter of council members to be nominated by the local trade unions; one-quarter, by local professional associations; and one-quarter to be drawn from local residents in a manner similar to that employed for the selection of persons for jury service. Members would be appointed for, say, five years, with one-fifth of the membership retiring each year.”



From Schumacher:

“The above proposals may be taken as nothing more than an exercise in the art of 'constitution-making'. Such a scheme would be perfectly feasible; it would restructure large-scale industrial ownership without revolution, expropriation, centralization, or the substitution of bureaucratic ponderousness for private flexibility. It could be introduced in an experimental and evolutionary manner - by starting with the biggest enterprises and gradually working down the scale, until it was felt that the public interest had been given sufficient weight in the citadels of business enterprise. All the indications are that the present structure of large-scale industrial enterprise, in spite of heavy taxation and an endless proliferation of legislation, is not conducive to the public welfare.”



Declaration of Independence, Trumbull



THE END



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