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**Article**

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Thomas Steger, Ronald Hartz\*

## **The Power of Participation? Power Relations and Processes in Employee-owned Companies\*\***

Introducing employee participation in a company can be expected to change the power relations and the power processes within the organization. This is particularly true when the majority ownership of a company moves into the hand of its employees. Drawing on three case studies of East German companies this paper describes how the introduction of employee ownership interrelates with power relations and processes in the company. Moreover, some overarching patterns were derived from the analysis finally resulting in seven propositions about how employee ownership and power are linked to each other.

### **Die Macht der Partizipation? Machtbeziehungen und Machtprozesse in Mitarbeiterkapitalbeteiligungs-Unternehmen**

Die Einführung von Mitarbeiterkapitalbeteiligung in einem Unternehmen lässt in der Regel auch die Machtverhältnisse und Machtprozesse innerhalb der Organisation nicht unberührt. Das gilt insbesondere in jenen Fällen, wo die Mehrheit der Unternehmensanteile in die Hände der Mitarbeiter übergeht. Auf der Grundlage von drei Fallstudien in ostdeutschen Unternehmen wird beschrieben, in welchem Interaktionsverhältnis die Einführung von Mitarbeiterkapitalbeteiligung und die Machtverhältnisse und -strukturen in den betroffenen Unternehmen stehen. Darüber hinaus werden firmenübergreifende Muster herausgearbeitet, die in sieben Thesen über das Verhältnis zwischen Mitarbeiterkapitalbeteiligung und Macht münden.

Key words: **Employee Ownership, Employee-owned Company, Power, Small and Medium-sized Enterprises, Company Crisis, East Germany**

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## 1. Introduction

Introducing employee participation in a company may be expected to change the power relations and the power processes within the organization. As participation usually results in a certain gain in power for the employees, other actors, e.g. the middle management, may be threatened by a loss of power. This is particularly true if the (majority) ownership of a company moves into the hand of its employees creating an employee-owned company (EOC) (Voß et al. 2003; Stracke et al. 2007).

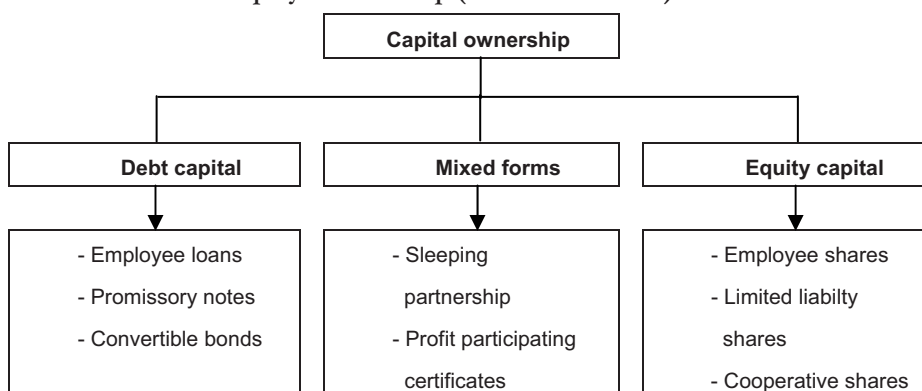
In spite of a few studies in this context (e.g. Hammer/Stern 1980; French/Rosenstein 1984), the process and character of the power relations in and around EOCs are still largely unexplored. This holds particularly true for the context of Germany where this kind of companies is still quite rare (AGP/GIZ 2007; Bellmann/Möller 2006). Moreover, we do know little about the impact of the particular framework in which employee ownership (EO) is introduced on those relations which can be expected to differ considerably between different countries and economic systems (Schuler/Rogovsky 1998; Poutsma et al. 2003), but also according to different situations in the company life cycle (Pajunen 2006).

This constitutes the starting point of our paper. It draws on three case studies of East German companies that tried to escape bankruptcy by means of introducing considerable EO. A broad range of data from qualitative interviews, company visits, company documents, and media articles were analysed following the case study methodology introduced by Eisenhardt (1989). It will be described how those companies managed their (economic) crisis and the hence resulting conflicts. We particularly highlight how and to what extent the introduction of employee ownership is driven by and shapes power relations and processes in the companies. Seven overarching propositions are derived from the analysis providing a more general picture of how employee ownership and power are linked with each other.

## 2. Literature review

The use of EO dates back to the first half of the 19<sup>th</sup> century (Fiedler-Winter 2000; Gaugler 2002). Since then, a broad range of different forms and models have been developed (Table 1).

**Table 1: Forms of employee ownership (cf. Voß et al. 2003)**



We need to note, however, that recent (positive) data about the spread of EO in Western industrialized countries are first of all influenced by a limited number of big companies (Jones/Kato 1993; Poutsma/de Nijs 2003; Mathieu 2006) where EO has hardly led to a considerable increase of participation or even a shift of power in favour of employees (Hyman/Mason 1995). Meanwhile, EO can play an important role in small and medium-sized enterprises (SMEs) (Steger 2008), though the percentage of companies engaged here is still fairly limited, which holds particularly true for Germany (AGP/GIZ 2007; Bellmann/Möller 2006).

### ***2.1 EO and power – a general perspective***

Although Niehues (1994, 59) states a “fundamental democratic orientation” within EOCs the rights and interests of different actors herein must generally be considered somehow diffuse (Dunn/Daily 1991) not at last due to the “double role” of employees as shareholders and stakeholders at once. Moreover, as Bartkus (1997) notes, some fundamental differences between the motivation and objectives of different actors regarding the introduction of EO do regularly occur and, in case of a lack of transparency, may lead to severe conflicts.

From the *management* perspective, one can differentiate between an idealistic and an instrumental approach to EO (Hyman/Mason 1995). The idealistic approach, on the one hand, is connected with prominent examples of charismatic entrepreneurs and philanthropists (e.g. Ernst Abbe, Ernest Bader). EO herein is primarily introduced with respect to a humanistic world-view intended to share the company wealth with all company members. Consequently, the number of examples for this approach is fairly limited. The instrumental approach, on the other hand, is much more widespread. Here, EO is considered to function as a legitimation of the shareholder value ideology to a certain degree (Hyman/Mason 1995). So, it is aimed to stabilize and foster the position of management (Prasnikar/Gregoric 2002; Wright et al. 2002).

From the *employee* perspective, given the indirect form of democracy that is constitutive for most EOCs, it seems necessary to renounce to a certain extent on accomplishing individual interests (Hardwig/Jäger 1991). Instead special focus lies on the development and organization of the company organs (Niehues 1994) and of special arrangements with management (Wright et al. 2002). Empirical evidence was found for employees’ awareness of those needs: They understand themselves more like investors than like owners (French/Rosenstein 1984) and do not automatically claim for more participation based on share ownership (Hammer/Stern 1980). It was even found that the higher the financial engagement of the individual employee, the more he/she is willing to delegate power to the management (Hammer/Stern 1980).

Nevertheless, this does not imply that power relations and processes would definitively remain unchanged: Several common conflicts, namely employee dismissals or profit sharing, will become considerably altered by EO (Buck et al. 2003; Rousseau/Shperling 2003). As a consequence, problem solving mechanisms need to be reshaped (Hardwig/Jäger 1991). Kuvaas (2003) also notes that the perceived fairness of the EO introduction would affect the future development of the whole concept. Kaarsemaker and Poutsma (2006) even urge that, in order to make the EO successful, the whole human resource management should represent the EO philosophy.

From the perspective of *unions*, finally, several authors point out that EO does not necessarily include a drop of union power (Lajtaj 1997; Rock/Klinedienst 1997; Vaughan-Whitehead 1997). However, in cases where unions show an ambivalent or adversarial attitude towards EO they risk to be only partly included in the discussion and introduction process (Kozarzewski/Woodward 2001). This is even aggravated when obvious conflicts between different unions regarding EO exist (Pendleton/Poutsma 2004).

## ***2.2 EO and power – a German perspective***

Our knowledge about EO and power originates from a broad range of different countries and regions and, thus, reflects rather different cultural and institutional frameworks making it difficult to transfer this knowledge. So, this section is dedicated to Germany that must be considered peculiar in several respects: The German co-determination system developed during the last five decades provides the employees with a fairly strong position on different institutional levels (national, branch, company, firm, and individual level) (FitzRoy/Kraft 1987; Fiedler-Winter 2000; Stracke et al. 2007). This may be perceived a supportive background for the spread of EO models; however, it may also become a strong competitor for EO or just make it look dispensable.

Consequently, the interplay of EO and employee co-determination has been widely debated in the German context. On the one hand, Hebestreit (2000) denies a positive impact of EO on co-determination and Lezius (2006) even warns of mixing the two aspects. On the other hand, several authors point to the positive effects of participative structures (e.g. co-determination culture, works councils) on the performance of EOCs (FitzRoy/Kraft 1995; Zwick 2004; Kauls 2006; Stracke et al. 2007). Some recent process studies show that a well balanced interplay between employee participation and EO is a crucial factor (Steger 2008). This may be due to the above described particular German framework which makes it little promising to introduce EO as a means to oppose the well institutionalised system of employee co-determination.

Regarding the position of works councils, Eschenbach et al. (1999) found that they were usually included early in the process of EO introduction, much earlier than unions were. The latter fact was said to be due to the often ambivalent position of unions, be it with respect to blue-collar (good) versus white-collar (bad) ownership (Kabst et al. 2006) or with respect to the inter-union disagreement about EO (Stracke et al. 2007).

## ***2.3 EO in company crises***

It is widely unquestioned that crisis-induced EOCs, i.e. companies introducing EO in order to rescue the firm from bankruptcy and to secure employment, constitute a special case within the context of our topic. Nevertheless, crises usually mark some key events of the company history and, thus, can be considered highly valuable for the analysis of the EO–power interplay in general and the influence and contributions of different stakeholder groups in particular (Pajunen 2006).

Pointing to the “double risk” of employees of losing both their job and their investment, several authors warn of taking EO as a remedy for struggling firms (Eschenbach et al. 1999; Kauls 2006). Therefore, it is not surprising, that the performance of this kind of projects reported in literature is ambiguous. Mygind (2002) describes five Latvian cases with crisis-induced EOCs of which three ended in liquidation soon. In the German context, both successful cases (e.g. Fiedler-Winter 2000; Latscher et al. 2003; Thaller 2007) as well as failing ones (e.g. K  ppler 1995) were reported. Pfuller (2003) even stressed that in the East German privatization process the majority of EOCs would have been firms in crisis while the Treuhandanstalt, i.e. the East German privatization agency, tended to sell the promising firms to external investors.

Regarding power relations in the company stories mentioned above, it turns out that balancing the interests of different actors and agreeing on a common strategy to be pursued has been a crucial aspect in both successful as well as unsuccessful EOCs (Pfuller 2003, Thaller 2007).

It is to note that all those studies failed to address the power topic in more detail. Before doing that, we need to develop an analytical framework in order to conceptually build a base for our further considerations.

### 3. EO and power – An analytical framework

Although power in organization and management has a long tradition within the field of organization and management theory (e.g. Vigoda-Gadot/Drory 2006; Fleming/Spicer 2007), discussions of power in and of organizations are not common to the mainstream of literature (Greenwood/Hinings 2002, Clegg et al. 2006). The research on EO can be interpreted as part of that deficit.

For our framework, we refer to the classic definition by Max Weber who perceives power as “the probability that one actor in a social relationship will be in a position to carry out his will despite resistance, regardless of the basis on which this probability rests” (Weber 1978, p.53). Thus, power is always a kind of social relation, not necessarily conflict driven, based on an indefinite number of means and a will, i.e. the interests of persons or groups (e.g. Nienh  ser 2003). Consequently, any power analysis has to deal with at least three questions (e.g. Neuberger 1995, Schirmer 2000, Morgan 2006):

- Which players or actors can be identified?
- What are their interests?
- How is power used to overt (or to cover) conflicts and to assert specific interests?

The triad and interrelation of actors (“Who?”), interests (“Why?”), and power usage (“How?”) can serve as a basic framework for the following case studies. In addition, it makes sense to differ between active and passive players in order to identify the drivers of the power game (Hinings/Greenwood 1988).

Furthermore, to enrich the picture of EO and power it is useful to differentiate between three types of power, i.e. to subdivide the third question. Etzioni (1964) made a useful distinction between coercive, utilitarian, and normative *types of power*. Coercive power means to force someone to comply with one’s will. Utilitarian power is based on a system of reward or punishment. Normative power rests on the beliefs



of someone that individuals, groups or organizations have the right to govern his or her behaviour. By this differentiation, Etzioni points to the hidden side of power, the “deep structure politics” that shape the everyday “wheeling and dealing” in organizations (Frost/Egri 1991).

Moreover, we adopt Hardy’s (1994) three dimensions of power, which allows us to separate the *dominant directions of political performance* and the corresponding actions. With reference to Lukes (1974), Hardy distinguishes between the control and management of resources, the control of processes and, finally, the control of legitimacy. The first two dimensions emphasise the influence of resources and the establishing of rules on decision-making processes. The third dimension of power refers to the “management of meaning” (Pfeffer 1981).

In sum, beside the exploration of *players*, their *status* and *interests* we will seek for different *types of power* (Etzioni) as well as the *dominant directions of political performance* (Hardy) to obtain a complex picture of EO and power.

#### 4. Methodology

A qualitative case study design was employed to understand how EO impacted on power relations and power processes within three SMEs. We followed the suggestions made by Kathleen Eisenhardt (1989) regarding how to gain theoretical insights from case study analysis. This model proceeds with eight steps:

1) *Getting started*: Our basic research question is ‘*How do power relations and processes in companies look like and may develop with the adoption and consolidation of employee ownership?*’

2) *Selecting cases*: This was done through theoretical, not random sampling. We searched for companies that share some particular characteristics: Firstly, they are all medium-sized enterprises in which EO can get an influential position. Secondly, they all introduced EO as a means to rescue the company from bankruptcy. So, they share a common situative background. Thirdly, they all belong to or are connected with the mechanical engineering branch. Even Educator is mainly engaged in professional technical education and acts as an important supplier for the local industry companies. Moreover, they are all situated in the region of Chemnitz, a highly traditional industry area of East Germany that underwent deep transformation throughout the past 18 years. So, they share a common institutional background.

Besides, the three companies show some fairly different development paths and, thus, provide us with some variation about how EO may proceed over time.

**Table 2: Characteristics of the case companies**

	<b>Toolcom</b>	<b>Educator</b>	<b>Metalcorp</b>
<b>Founding date</b>	1852	1991	1845
<b>Employees (2006)</b>	150	50	65
<b>Branch</b>	Mechanical engineering	Professional education	Metal processing
<b>Introduction of EO</b>	1996	2001	2005
<b>Model</b>	Limited liability shares	Limited liability shares	Sleeping partnership
<b>Size of EO</b>	100% ⇒ 39% (2006-) (ca. 100 employees)	100% ⇒ 0% (2004-) (ca. 17 employees)	ca. 35%  (ca. 25 employees)

3) *Crafting instruments and protocols*: In our study we used some diverse data collection methods. First of all, we conducted some qualitative interviews that were based on a flexible guideline with both members of the company management and employees. Where possible, we also included some members of the company works council. Besides the interviews we had some informal talks with various company representatives as well as with some local experts (e.g. politicians, union representatives). Regarding observations some company visits were made. Moreover, we used some diverse archival data, such as company documents or reports from the local media.

As suggested by several authors (e.g. Pettigrew 1988) we used some multiple investigator teams for data collection. These included different researchers from the department as well as advanced students.

4) *Entering the field*: The data collection of our study was not limited to a distinctively fixed period but rather often overlapped with data analysis which is strongly recommended by the literature (e.g. Glaser/Strauss 1967). This enabled us, on the one hand, to remain close to the field data and, on the other hand, to flexibly deepen our comprehension of the cases.

5) *Analyzing data*: This phase consisted of two parts. Firstly, the within-case analysis of each company case resulted in the detailed descriptions to be found in chapter 5 of this paper. Subsequently, some cross-case patterns were searched with the help of diverse categories and dimensions (e.g. the ones emanating from our basic analytical framework described in chapter 3).

6) *Shaping hypotheses*: We then tried to formulate a few overarching propositions concluding the main findings of our data analysis. Those propositions are presented in chapter 6.

7) *Enfolding literature*: In order to not become deprived from the existing knowledge of the field, we tried to contrast our results with the existing literature. Consequently, each proposition in chapter 6 is accompanied by a short discussion.

8) *Reaching closure*: Given the deficit of in-depth studies about power relations and power processes in EOCs we assume that it is too early to reach closure here. This final step, therefore, could be a main challenge for further investigations.

## 5. Case studies

In this section the three company cases are described in detail. This description is guided by our analytical framework introduced above. Moreover, to further structure the stories and to make them easier for the readers to follow, we distinguished three phases – (a) adoption, (b) consolidation, and (c) modification of EO.

### 5.1 Toolcom

After the fall of the Berlin Wall in 1989 and the subsequent start of the transformation process in the former GDR, Toolcom, a highly traditional drill machine manufacturer, became independent from the combine structure. However, it was not fortunate with its investor(s) and mother company(s): It was involved with several crises of large West German companies and, as a result, Toolcom became insolvent in March 1996.

(a) *Adoption of EO*: The insolvency left Toolcom with a veritable vacuum. Disappointment, frustration and a lack of orientation were omnipresent in the company. In



this moment the works council of Toolcom (supported by the local union) took the initiative, i.e. it became an active player. They developed a concept to rescue the company from bankruptcy by transferring it into an employee-owned company. The interests were twofold: to rescue the company as well as their jobs and to prevent some further questionable investors from entering the firm. The company management supported this process as good as they could. Simultaneously, the employees physically occupied the firm plant in order to safeguard the company property. So, the strong support of the large majority of employees for the activities of the works council was obvious. All this provided the employee representatives, predominantly the works council, with a kind of first-mover advantage.

The works council used this situation to form a broadly based supporting network for Toolcom including the insolvency administrator, some local politicians, the local labour agency, a prominent local lawyer and a well-known accountant. Finally, the Saxon government also assured assistance. All this helped the works council to build up legitimacy and to put through its ideas of EO in the company concept: 100 employees should get 1 company share each at a prize of 10'000 DM which created 1 Mio. DM postulated by the house bank as precondition for its engagement. So, in autumn 1996 the newly founded EOC could be started.

*(b) Consolidation of EO:* The works council who always declared to aim for rescuing the firm and for securing employment decided not to take a double role but to remain the representative body of all employees, be they owners or not. Consequently, it renounced on demanding the key position in the new company but freely agreed to step back and leave room for two professional managers – one long-standing manager from GDR times and one newly hired West German.

This kind of modest reluctance was also the dominant attitude among the company workforce. So, the employee-owners of Toolcom delegated their competencies to a newly founded supervisory council (Beirat) consisting of four externals (prominent local personalities) and three employee representatives. It was moreover agreed that no dividends should be paid as long as the company did not reach a minimum equity capital rate of 30% but a market-oriented interest rate was calculated (but not paid out). Any further extras were prohibited from the beginning, e.g. no employee could receive more than just one share.

This was mainly due to the fact that a large majority of employees have a long tenure with Toolcom and so feel strongly committed with the company in general and with the founding myth of the EOCs ('We did it to rescue our company') in particular.

„You feel that you possess a part of the firm (...) that you are an employee or an owner of a company well-known worldwide. (...) You can proudly speak it out. And this is positively acknowledged.” (White-collar employee)

Consequently, there is also a certain readiness to make sacrifices in favour of the company's wealth.

“The commitment of our employees with the company is so highly developed that they rather engage in convincing their union that they want not to receive more money than convincing me that they want to receive more.” (CEO)

When the EOC started in the autumn of 1996 only 13 employees could receive a working contract while all others remained in unemployment. Thanks to a wealthy company development little by little some more employees were hired again and in mid-1997 all owners were back on board.

In spite of (or exactly because of) its modest power use the works council of Toolcom preserved its strong position throughout the consolidation process. It can be described as a kind of moral authority that is unquestioned by the management too and, by this, executes a high extent of normative power.

Although the dominant company culture of Toolcom has not come into crisis and the employees could profit from a continuous satisfying development of the firm some ambiguous patterns occurred among the employee-owners in time. The double function (employee and owner) created a dilemma between egalitarianism (no difference between owners and non-owners) and elitism (wish to be honoured for his/her sacrifices).

“I should feel more from the fact that I gave some money to that. This would surely help me with certain decisions if the connection between my share and the company were closer.” (White-collar employee)

Moreover, regarding the future of the company, another dilemma occurred between a somehow conservative attitude (‘we did it alone in the past and, so, we will remain independent for the future!’) and the more pragmatic conviction that new requirements will call for new solutions.

**Table 3: Power related aspects in the case of Toolcom**

	<i>Status</i> (Hinings/ Greenwood 1988)	<i>Interest</i>	<i>Action</i>	<i>Type of power</i> (Etzioni 1964)	<i>Form of political performance</i> (Hardy 1994)
<b>(a) Adoption of EO</b>					
<b>Works council</b>	Active	EO implementation, rescue of company	Coalition building	Normative	Control of legitimacy
<b>Local union</b>	Active	Support of works council	Coalition building	Normative	
<b>Employees</b>	Active	Rescue of company	Plant occupation	Coercive and normative	Control of resources
<b>Company management</b>	Rather active	Rescue of company	Coalition building	Normative	
<b>(b) Consolidation of EO</b>					
<b>Works council</b>	Active	Consolidation of company	Delegation of power to professional managers	Normative	Control of legitimacy
<b>Employees</b>	Active	Consolidation of company	Delegation of power to supervisory council	Normative	Control of resources
<b>(c) Modification of EO</b>					
<b>House bank</b>	Active	Risk reduction	Ultimatum to accept external investor	Utilitarian	Control of resources
<b>Employees</b>	Rather active	Beware EO	Resistance to several proposed investors	Normative	Control of resources and legitimacy

*(c) Modification of EO:* It was Toolcom's growing need for capital to finance its future growth that led the firm into another crisis from mid of the 2000s on. The house-bank, in order to limit their risks, became increasingly suspicious against the unusual idea of EO and forced the company management to find an external investor to take over the company. In opposition, the large majority of employee-owners acknowledged the need to adopt a strategic investor but they resisted to completely abandon the EOC or to accept an investor who did not seem to fit with the company's culture and tradition. The conflict culminated when the house bank issued an ultimatum to the company and, by this, demonstrated its control of crucial resources. Finally in December 2006 the company management found a Dutch investment company that agreed to take over 61% of the equity capital, to guarantee the future financial needs and to accept a considerable minority stake with the employees.

Although, the future development of Toolcom is by no means clear, the current power structures can be considered as the result of the company's recent history characterized by the works council (and the majority of employees) balancing between decisive activity and modest restraint in order to secure the endurance of the company community as well as the employment.

Table 3 summarizes the development of EO in the case of Toolcom against the background of our analytical framework.

## **5.2 Educator**

Educator was founded in 1991 on the basis of the training centre of a large combine. It developed fairly well in the following years. However, due to formal mistakes of the management it lost its charitable status in 2001 which resulted in a demand for the return of money by the local tax agency amounting to several millions DM and, thus, in immediate insolvency of the firm.

*(a) Adoption of EO:* This left Educator in a situation of high uncertainty and a lack of leadership since the former management was taken fully responsible for the crisis and, therefore, was completely de-legitimated. In this moment, the company's works council (supported by the local union) took the initiative. They both stated that the foundation of an EOC, according to the model of Toolcom, would be the only way out. This proposal was widely accepted by the company's employees. Consequently, the works council took the lead. In order to secure the financial resources by a bank loan, 17 employees were found ready to pay 1500 DM each for their share. Moreover, the works council formed a broad based local supporting network in order to strengthen its legitimacy. The old management was forced to leave the company. In face of a lack of successors, the very engaged head of the works council, in agreement with the union leader, took over the position of the CEO.

*(b) Consolidation of EO:* Similar to the structure of Toolcom, a special supervisory council (with a majority of external local personalities) administering the employees' ownership competencies was founded. The other strong actor turned out to become the newly established CEO.

Although only eight employees could immediately enter the new EOC, the new strategy remained widely unquestioned, due to confidence in the new management but also a certain mental inertia.

“We do not have this self-confidence here as the West Germans do. This knowledge, that you must do something for your own, that you have to care about and that you can’t just sit there – somebody presents something to us and we all agree...” (White-collar employee)

However, in spite of the successful development of the firm, more and more employees who had not really actively pursued the concept of EO also felt a certain dilemma due to their double role (employee and owner). This problem was even found among works council members.

“Additionally, I was a works council member and, moreover, a member of the supervisory council... Sometimes I did not even know: who am I in the end? That’s why I think that this does not really work because the interests are too different from each other.” (White-collar employee)

The key conflict with Educator during those years was the increasing alienation between the supervisory council and the top management. On the one hand, the former more and more tried to instrumentalize the company for their own targets. For instance the local union leader wanted to present Educator as a role model for the 35-hours-week in East Germany and, by this, to exert normative power. This was strictly rejected by the company management. On the other hand, the latter openly wanted to attract a strategic investor which was not approved by the majority of the supervisory council.

**Table 4: Power related aspects in the case of Educator**

	<i>Status</i> (Hinings/ Greenwood 1988)	<i>Interest</i>	<i>Action</i>	<i>Type of power</i> (Etzioni 1964)	<i>Form of political performance</i> (Hardy 1994)
<b>(a) Adoption of EO</b>					
<b>Works council</b>	Active	EO implementation	Coalition building	Normative	Control of legitimacy
<b>Local union</b>	Active	Support of works council	Coalition building	Normative	
<b>Employees</b>	Passive	Preservation of employment	Not observable	(Compliance)	
<b>(b) Consolidation of EO</b>					
<b>Company management</b>	Active	Consolidation of company	Stabilization of their power position	Normative and utilitarian	Control of legitimacy and process
<b>Works council</b>	Rather passive	Consolidation of company	Delegation of power to (new) CEO	(Compliance)	
<b>Employees</b>	Rather passive	Not observable	Delegation of power to supervisory council	(Compliance)	
<b>(c) Modification of EO</b>					
<b>CEO</b>	Active	Attract external investors	Dismissal of supervisory council	Coercive	Control of process
<b>Supervisory council</b>	Rather active	Use of company as role model	Public relations	Normative	Control of legitimacy
<b>Employees</b>	Rather passive	Not observable	Acceptance of management’s strategy	(Compliance)	

(c) *Modification of EO*: In the end, the CEO used his power position and released a “*revolt*” (CEO): Without information to the supervisory council, he invited an owners’ general assembly, received a clear vote to dismiss the supervisory council and to sell the majority of shares to an external investor with whom he already agreed about all details before. So, the CEO exerted coercive power and, by this, managed to gain control over the current process. For most employees EO was not really a matter dear to their heart but more a temporary solution. So, they had no problem to follow the CEO’s new strategy and to re-abandon the EOC.

The resulting power structure is undoubtedly characterized by the new investor who possesses 75% of the shares. Though the CEO and two of his executives holding the remaining 25% kept a certain power and, moreover, were guaranteed that all strategic decisions would be taken consensually. Moreover, the management got rid of both potential conflicts with any supervising council and opposite activities from any employee-owners.

Table 4 summarizes the most important power related aspects of this case.

### 5.3 *Metalcorp*

After the end of the GDR in 1990 Metalcorp, whose roots date back to the mid 19<sup>th</sup> century, was re-privatized. Having been fairly successful throughout the early years, Metalcorp ran into a deep crisis in the late 1990s due to some severe strategic management mistakes and, finally, had to announce insolvency in 2002. Although the employees continued to work profitably under the control of the insolvency administrator, no potential investor could be found.

(a) *Adoption of EO*: In 2005, five leading executives decided to fill out this vacuum and to take over the firm. Due to their limited financial resources and pressured by the house bank, the idea occurred to set up a sleeping partnership including the company’s workforce. With respect to the wealthy development of the firm and thanks to the confidence in their executives this plan was approved by a broad majority of employees. Moreover, the management also demonstrated a high time pressure. By this, they exerted coercive power in order to gain control of the current process.

“All this was rather helter-skelter. We had only limited time when this was introduced. So we were taken a bit by surprise. And we have been fairly credulous because we did not know all the legal things, what will be, and we were not able to check this. So we did it, more or less, since it was proposed...” (Blue-collar employee)

25 employees paid a total of 70’000 € and agreed to receive, with the sleeping partnership, some information rights but no participation or co-determination rights. The only real incentive was a guaranteed interest rate well beyond market conditions. Interestingly, the works council perceives itself in a more traditional manner: Since it did not understand the suggested concept as a key task to be broadly discussed it remained rather passive during this process.

“Indeed, these people were fairly restraint in this matter...” (CEO)

As a consequence, there was no critical voice questioning the activities of the management. Thus, forming a larger supporting network to secure legitimacy was not necessary for them.

(b) *Consolidation of EO*: The management used this situation and its powerful position to gain dominance over the company. The financial input from the sleeping partnership backed their position. One of the five founding owners was also appointed head of the sleeping partnership. Consequently, they demonstrated a leadership style that was strongly top-down oriented in order to control the processes. Information flows, also regarding the investment of the sleeping partnership, were very limited. Given the highly attractive interest rate for the employees the management perceives the sleeping partnership as a mere utilitarian exchange relationship. All in all, they seemed not to give high priority to this matter.

“Once per year we have the duty to pay the interest and we will do this. But we do the information together with the whole company. I think all other employees who are not owners of the sleeping partnership also need to be informed and so we do that for all together.” (Head of the sleeping partnership)

Moreover, during the interviews some members of the top management made some rather contradicting accounts, e.g. regarding the safety level of the sleeping partnership’s capital (e.g. “*absolutely safe*” vs. “*risk capital*”). The lack of negative feedback from the employee side was perceived by the management as an indicator of the high level of confidence.

Although it is too early to decide about the success of the management’s strategy the company figures are rather ambivalent. On the one hand, the most current productivity rate increases (8-10%) are rather promising. On the other hand, however, the equity rate of Metalcorp (8.6%) is fairly worrying. Nevertheless the first interest instalment has been paid and so everything seems to be okay...

Table 5 summarizes the most important power related aspects of this case.

**Table 5: Power related aspects in the case of Metalcorp**

	<i>Status</i> (Hinings/ Greenwood 1988)	<i>Interest</i>	<i>Action</i>	<i>Type of power</i> (Etzioni 1964)	<i>Form of political performance</i> (Hardy 1994)
<b>(a) Adoption of EO</b>					
<b>Company management</b>	Active	Take over company	Enforcement to install EO	Coercive	Control of process and legitimacy
<b>House bank</b>	Active	Risk reduction	Enforcement to financial investment	Utilitarian	Control of resources
<b>Employees</b>	Rather passive	Preservation of employment, ROI	Acceptance of EO (sleeping partnership)	(Compliance)	
<b>Works council</b>	Passive	Not observable	Not observable	(Compliance)	
<b>(b) Consolidation of EO</b>					
<b>Company management</b>	Active	Consolidation of company	Information	Utilitarian	Control of process and legitimacy
<b>Employees</b>	Passive	ROI	Not observable	(Compliance)	



## 6. Propositions and discussion

Taking the three cases together some overarching findings can be identified that will be concluded and discussed hereafter in seven propositions:

Proposition 1: Severe crisis situations often lead to a power vacuum providing a 'window of opportunity' for the actors included. This does particularly advantage those actors with well developed social skills.

In all of our three cases the insolvency of the company created a veritable vacuum situation with widespread uncertainty often connected with frustration and helplessness. However this problematic situation also provided a great opportunity for actors who demonstrated to be initiative, decisive and sometimes even aggressive, confirming the more general picture designed by Pajunen (2006): The works council (Toolcom), the head of the works council (Educator) and the five management executives (Metalcorp) could use this situation to gain a remarkable power position. The cases demonstrate the importance of creating coalitions (Schirmer 2000) in order to control processes and to strengthen legitimacy.

Proposition 2: The modus of power delegation from the employee-owners to the management determines whether and how the formers will be compensated by the latter.

Not surprising and consistent with earlier studies (e.g. Hammer/Stern 1980, Hardwig/Jäger 1991), in all three companies the employee-owners delegated a remarkable amount of their power to the company management. However, the modi of power delegation were rather different and had some distinctive consequences. So, we need to focus on *how* power was delegated (Wright et al. 2002) rather than *whether* it is delegated or not.

The works council and the employee owners of Toolcom freely decided to delegate part of their power to the management. Consequently, they got compensated through a high moral status for the works council and a strongly developed, long-standing employee oriented policy of the company management. Meanwhile the employee-owners of Educator and Metalcorp took a rather passive role and did hardly feel powerful in any moment of the whole process. The power that they (theoretically) possessed was appropriated in both cases by the new bosses. Both sides implicitly took this process for granted and, consequently, a potential compensation was not a matter here. In more general terms, the mere possession of resources does not imply its usage. It is rather shaped by the management of processes and meaning (Lukes 1974; Hardy 1994).

Proposition 3: The self-perception of the employee-owners is crucial for their role taking and, thus, considerably impacts on the further development of the EOC.

The way the employee-owners see themselves in the context of an EOC is a complex and, to some extent, problematic topic. Against the background of the three case studies observed it became clear that there are some important impacts from this on the development process of the EOC. It is necessary to distinguish between active and passive owners: With the active owners (of Toolcom and Educator) some patterns of

ambivalence (e.g. the dilemma between egalitarianism and elitism) or some specific role conflicts (e.g. of works council members sitting on the supervisory council) occurred. Those conflicts tended to undermine the broad based support for the idea of EO and, thus, for the EOC in the long run. With the passive owners of Metalcorp, no real employee-owner self-perception could be found. Be it due to a lack of information, to a lack of interest or to a broad confidence in management (or a combination of all that) it seems highly problematic to speak of EO in this case. From the power perspective, moreover, it is to note that the management of meaning by the dominant actors may considerably shape the self-perception of the other actors.

Proposition 4: Against the German institutional framework EO and employee co-determination can hardly be separated from each other. Consequently, the introduction of EO in German SMEs will shape the further development of the firm-level co-determination as well as the respective power structures.

Our three cases have highlighted that in the particular German context EO lead to some very specific situations that challenge the co-determination arrangements in the company, independently of how they look like. This is obviously in line with earlier findings (e.g. Kauls 2006; Steger 2008). On the one hand, in all three cases the employee-owners face some dilemmas between their role as an employee (in a company with institutionalized co-determination) and their role as a co-owner of the company. On the other hand, in all three cases the works council, as the key institution of German firm-level co-determination, had to decide about what position they should take vis-à-vis of the EO.

The respective solutions were rather different: The works council of Toolcom decided to step back from its active power position in order to continue their task as the representative organ of all employees (owners and not-owners). The works council of Educator (or better said: the head of it) took the opportunity to change the sides and to shift to the top management which subsequently created some new dilemmas. The works council of Metalcorp did not perceive the introduction of EO as a situation to take position and, so, behaved rather passively.

With both actors, employees and works councils, it became obvious that unclear or diffuse rights and role definitions even aggravate the conflicts and dilemmas which was already found within rather different institutional frameworks (Dunn/Daily 1991; Bartkus 1997).

Proposition 5: Crisis-induced EOCs do not necessarily imply an increase of workplace democracy. Often it works merely as a means to consolidate certain organizational actors' power position.

Only in the case of Toolcom the adoption of EO led to a remarkable increase of power on the side of the employees and their representatives (here: the works council). Notably they even managed to keep their strong position over the following years. Although more workplace democracy may was an initial target of the EOC with Educator, it turned out quickly that only the head of the works council as the new CEO could profit of it. With Metalcorp, it was clear from the beginning that an empowerment of employees was not the target but rather the consolidation of the management

buy-out. The sleeping partnership was a mere financial exchange – capital against interest – and works as a good example for the earlier mentioned investor role model (French/Rosenstein 1984). Moreover, it was demonstrated how EO may be used to legitimate and foster the management's position (Prasnikar/Gregoric 2002).

Proposition 6: EOCs have a fairly short half-life. Moreover, there are some indicators of path dependency in the long run.

Given the high complexity of EOCs it seems obvious that their long-term stability is lower than with "normal" SMEs. The power relations and structures, as could be seen in all three cases, are rather volatile. New challenges in the environment demand for new solutions which may include a fundamental modification or even the abandonment of EO. This can be seen even in the case of Toolcom where EO is strongly rooted in the company culture. After ten years the company would not have survived without accepting an external investor and abandoning the employee majority ownership. With Educator this process went on even more quickly which may be due to the perception of the EOC as an exceptional measure. The EO in Metalcorp is still fairly young, but we can already identify some problematic aspects that question the long-term existence of this model.

Although the limited number of cases does not allow us to postulate a clear-cut path dependency a process of three phases, as introduced above, well adapts to our three cases: (a) The *adoption* phase is characterized by euphoria, pioneering spirit and some strong trust relations. (b) During the *consolidation* phase the EOC has to be implemented and integrated into the company's daily business. Moreover, some first conflicts have to be endured and resolved. (c) In the *modification* phase some alternative ways become more widely discussed which, finally, leads to complete abandonment of EO or to the transfer of the existing EOC into a new form.

Proposition 7: Given the inner logic of Western capitalism the success of EOCs sooner or later leads to its own destruction or transformation.

The capitalist logic that strongly interrelates success and growth sooner or later leads most EOCs into a dilemma. On the one hand, the need to grow will demand for some additional capital that is usually limited among employee-owners and forces them to open up the company for external investors. This became obvious in the case of Toolcom and (partly) of Educator.

On the other hand, to renounce on this classic path would imply to keep the company in a well shielded niche and, implicitly or explicitly, to opt for a logic of the "solidaric economy" (Altvater/Seckler 2006), e.g. according to the model of co-operatives (e.g. Hettlage 1987). This idea, however, does also include several caveats, for instance the development and organization of the company organs and the rules of power distribution (Hardwig/Jäger 1991; Niehues 1994). Moreover, it will be challenged by the opposition of powerful actors (e.g. the house bank of Toolcom) who exert normative power in order to prevent any organizational models that run counter to the dominant system logic disseminated and supported by the public discourse (Hartz/Steger 2004).

## 7. Conclusions

The analysis of power relations and processes in EOCs is undoubtedly in deficit. This paper should have pointed out that introducing a power perspective and closing this gap can provide us with interesting new insights that help for a better and deeper understanding of the nature and development of EOCs.

In *theoretical terms*, it was particularly highlighted that several processes in and around EOCs can not be explained by an economic logic alone. It must be rather perceived as highly interwoven with numerous aspects of power. We pointed to the importance of power vacuums (and their use by different actors), of the distinctive modus of power delegation (not just of power delegation per se), or of the value and pay-back of financial and emotional investments made by several actors. Moreover, it is to note that the role of the institutional framework became clearly visible in different respects, namely regarding the interplay of EO and the German employee co-determination or the development path (and particularly the path logic) of EOCs against the background of the economic system.

With regards to *practical implications* we can mention three points: First, our paper made it obvious that the introduction of EO indeed can make a positive impact and may even be used as an instrument to rescue the company from bankruptcy. This is widely independent from whether EO was chosen predominantly from a normative (e.g. Toolcom) or from a utilitarian perspective (e.g. Educator). Secondly, if employees and employee representatives manage to adapt to the specific circumstances they can benefit from the introduction of EO as well. So, employees in general as well as works councils and unions in particular are well advised to take a more active role regarding this topic. Thirdly, any introduction of EO ought to take into consideration the different strands of power as well as the institutional background. This implies to give up a purely utilitarian view on those processes.

Nevertheless, we need to remark some *limitations* of our paper as well. Although the case study analysis pursued here provided us with some deeper insights it is just based on three company cases of crisis-induced EO in East German SMEs. They need to be treated as rather specific stories and their findings ought to be transferred to other contexts only with great care. Moreover, we are still far from reaching theoretical closure in this topic but some further research efforts are definitively needed.

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