Creating an Ownership Culture

One distributor's experience in building a self-starting corporate culture

The author of this article, the 20-year owner and CEO of a seal distribution company, talks about the rewards and challenges in transforming the culture of his company to one where the employees took ownership and went beyond their normal daily activities to do what is best for the company.

By Larry Goode

I once had the pleasure of hearing Retired General Arnold Schwartzkopf speak on the topic of leadership. To paraphrase, leadership is getting others to do what they would not ordinarily do, voluntarily. In an ownership culture, employees voluntarily do activities they would not normally be expected to perform.

In visiting hundreds of companies, I have observed wildly different corporate cultures. It doesn't take long in a visit to sense a strict authoritarian rule or, at the opposite spectrum, a 'whatever works' mentality. Occasionally, after several visits, I will see employees, especially those on the lower echelon, take on more responsibility and accountability for actions outside their traditional job description. I call that an "Ownership Culture."

Defining an Ownership Culture

What is an Ownership Culture? My definition: when employees conduct themselves at work in a manner that demonstrates individual motivation to go beyond their normal daily activities to do what is best for the company.

What's the payback to creating an ownership culture? It is a return on investment that is both tangible and intangible. In an ownership culture, I would argue that employee:

- Retention is higher, lowering recruitment and training costs.
- Attitude is better. A happy employee makes for happy customers.
- Commitment/buy-in is higher, which leads to ...
- Higher productivity. The ESOP Association publishes a variety of studies citing sales per employee are almost 9 percent higher in ESOP companies versus non-ESOP, and that the rate of return is 2.7 percent higher.

Let me speak from a more personal perspective. As a longtime member of its industry trade association, R.T. Dygert regularly participated in their annual benchmarking studies. Almost consistently, our sales per employee were 75 percent to 100 percent higher than average. A variety of factors can contribute to that disparity, such as market/product segment or geography, but I would argue that at least one component of that success was our ownership culture.

Laying the Groundwork

Where do you start to create an ownership culture? This may sound overly simplistic, but this attitude must start from the top. The CEO or president must first buy into the potential benefits and be willing to accept a change in how they operate.

They must be willing to let go of strong, authoritarian rule and transition from dictator (no matter how benevolent) to a more "equal among equals" leadership role. Top leadership must adopt more of a "we, not I" and "work with, not for" style of management.

There are certain management basics that need to be in place first. Clearly written job descriptions help employees understand minimum expectations. There should be departmental and individual goals and responsibilities developed and evaluated on a regular basis. Finally, and this may be a departure for many, owners need to solicit ideas for company and individual improvement *from the bottom up*. This is the first building block to an ownership culture.

You must demonstrate respect all the way down the line. It is easy for the sales group to seem more important than the receiving department, but the challenge of a leader is to raise the self-perceived value of all groups and make them understand they are important to the success of the company.

I made a regular effort to elevate the importance of the lowest-compensated department in the company – the warehouse group. I would frequently tell them that their work in correctly picking and packing our product was our last chance to look good to our customers. I would emphasize that it didn't matter how good a spec our salesperson got our customer to adopt, or that our customer service group correctly entered an order, if the parts going out the door weren't the right part or quantity.

continued on the next page

If you would like to share management experiences and best practices with your peers, please contact Editor Lindsay Konzak at lindsay@mdm.com or 303-443-5060.

Another exercise I did periodically was to chart or list all the elements that went into the "perfect order." I would make a point of including several steps from each department. Was the part spec'd appropriately, did the correct item get entered into the sales order, did the packing list reflect the correct quantity, and did the invoice show the agreed-upon price? By the time we finished compiling even a short list of all the elements, there were usually at least 20-30 steps to the perfect order. I would emphasize that just one error made the order imperfect.

Sharing Financials

To foster an ownership culture, you need to share critical financial information with the troops. For many closely held companies, this will be a major departure from the traditional "keep the info close to the chest" mentality. Open Book Management is self-descriptive – you open the income statement and balance sheet to the employees, and invest time in helping them understand the financial workings of the company.

There are judicious ways to do this and still keep certain information confidential. I conducted quarterly meetings where, in my PowerPoint presentation, I would share sales, gross margin, expenses and net pre-tax information from the income statement and inventory, receivables and debt data from the balance sheet. In some areas, this was done at a summary level, and I did not share individual compensation data or my owner's equity.

I showed and more importantly explained the various ratios (turns, DSO, quick and acid test, productivity, etc.) and charted trends to show progress or lack thereof. I made a point to discuss debt to emphasize (indirectly and politely) that when I took what seemed to be an expensive trip, or drove an above-average car, that it was my hide on the line if the bank called the loan.

One interesting demonstration I would do at least once a year was the "Take away the pennies" exercise. I would show a pro forma income statement for the company with all data shown in both dollars and as a percent of sales. I would also show a balance sheet and show major changes in receivables or inventory in the same way. Then, I would put 100 pennies on a table and designate an employee to subtract pennies from the pile as I directed. First, take away 65 pennies for the cost of the goods we sold. I then asked how many were left and (fortunately) most employees responded 35. I then said take away 20 pennies for salaries … 3 pennies for utilities … you get the point. Finally, when we were through the major expenses, there would be 8 – 10 pennies left, and I would remind them to take another 4 – 5 away for taxes, leaving usually just 3 – 5 left on the table.

I would ask them if they thought that was what I as the owner put in my pocket and most would say yes.

Generally, our inventory and receivables would have gone up, and I would then explain that profits were different than cash. I would then tell them the change in assets was equal to 6 minus 7 pennies and would they please take 7 pennies off the table. You can imagine the shocked expression when they said there weren't that many pennies. Light bulbs went on about the responsibility and risk of ownership.

Do all employees understand or even appreciate the effort? I will admit that there were more than a few blank stares. My guesstimate was that about 30 percent really understood what I was saying, about 40 percent semi-understood and the rest didn't have a clue. But it was the effort to be both accountable and transparent that mattered.

Performance Measures

To reinforce the ownership culture, you need to emphasize this on a regular basis; one method I encourage is to have quarterly company meetings. Central to the meetings I conducted was a discussion of the performance measures mentioned above, but I used these meetings for other activities as well. As we were an ISO company, we collected customer comments every quarter (ISO requires feedback) and I made a point of reading 6 – 10 of the most praiseworthy ones and led applause of the recognized employees.

We also had an Employee of the Quarter award which was typically based on peer nominations and again, I led the cheers for the winner. Finally, we had a quarterly "Brite Ideas" award for the best employee suggestion submitted. The point is that the more often employees were recognized, the more our ownership culture reinforced the importance of their commitment and contributions.

These were some of the most anticipated parts of the quarterly meeting: even when your employees try to act like they don't care what you think, they do.

Empowering Employees

If you are trying to create an ownership culture, you need to become a hands-off manager. Ownership without empowerment negates the benefit; you want employees to be self-starters.

Does that mean you have a plane entirely on autopilot? Absolutely not, but you need to learn not to intervene unless there is a problem. You need to allow a certain amount of risk-taking, without retaliation and within reason. Be prepared to allow a few things to go awry, coach on how to improve the next time, and reinforce the successes. You need to encourage people below you to make decisions on their own and not try to pass the buck up the line.

My managers knew that when they approached me with a problem that I was going to ask them what their solution was before I gave my input.

Profit-Sharing

Variable pay is a topic in its own right, and probably best addressed in a separate article. However, one principle I believed in regarding ownership was to put your money where your mouth was. We had a quarterly profit-sharing plan based on a percent of net pretax profit for the quarter that was distributed to all the employees; also, if we hit a certain threshold, there was an additional bonus.

The individual share determination I used is lengthy, but suffice it to say the bonus checks were much-anticipated. Equally important was that we posted the monthly sales and profit figures so all could see the progress. As a result, none of the managers needed to encourage sales, customer service or warehouse employees to make the last-minute push to get products out the door.

ESOP and Phantom Stock Plans

ESOP it is the ultimate ownership enabler. An ESOP is a qualified retirement plan whereby shares in the company are granted on an annual basis to the employees based on tenure and individual compensation.

There are also significant capital gains tax advantages for the majority owner who establishes the plan. Part of the ESOP process requires an annual valuation of the company shares, and this process examines all phases (management depth, sales and marketing, operational efficiencies) of the company's performance.

I found this 'report card' a useful tool to communicate to the employee/owners how we could collectively improve the company, and hence our ownership share.

If implementing an ESOP is too daunting a process to the majority owner, a similar approach that does not actually transfer shares, but does reinforce ownership, is the concept of phantom stock.

Phantom stock differs from ESOP in several ways, but the main areas are that it is not a qualified retirement plan, and therefore subject to less IRS and D.O.L. scrutiny, and is reserved for only the top managers. Phantom stock is also usually tied to specific, annual key performance measures attained by the recipient, as opposed to the ESOP, which is based solely on companywide performance.

Signs of an Ownership Culture

How do you know you have achieved a culture of ownership? Unfortunately, this is more of a journey rather than a destination, or rather like defining pornography – I can't describe it, but I sure recognize it when I see it.

I can give an example of what I saw in my company that told me I had created the right culture. We had just hired a new warehouse worker from a temp agency on a temp-to-hire trial. Late one afternoon, a rush order came from customer service that had to go that day, and it landed in the hands of the temp. He walked through the warehouse fuming about that #^&*@#T customer that delayed his departure. I can't tell you how proud I was to hear one of the longer-term workers pull the temp aside and tell him "that customer pays for our profit-sharing." Maybe not surprisingly, that temp worker didn't last long with us.

Another time my wife and I were coming home from dinner at about 9 on a cold winter night, and I stopped by the office to pick up a file to work on at home.

To my surprise, one of our customer service reps who had been on vacation for 10 days was at her desk clearing things for the next day so she wouldn't be backlogged when the phones started ringing. Priceless.

Is creating an ownership culture worth the effort? I can only tell you that in 20 years of 'walking the walk', I've had …

- Warehouse employees (and others) tell me they want to be 'lifers' at the company, to the extent that they moved closer to the office to shorten commute times
- Average tenure increase consistently.
- Exceeded industry benchmarks in productivity.
- Employees bring friends and family into the company – the ultimate referral.

Larry Goode served for 20 years as CEO and owner of seal distributor R.T. Dygert International, and now is the president of Goode Advisors Inc. He can be reached at larry.goode@goodeadvisors.com.