ALASKA LEGISLATURE SPECIAL COMMITTEE / SUBJECT FILES 8672

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combination. If you want all three of those goals or an additional one, maybe what you want to do is bring it up when we get to combination.

MR. MOTLEY: All right, I'll wait -- I'll hold off until after we finish the combination.

MS. FLEISCHER: I still don't understand how you'll get regional decisions reflected under community development. I think that people will have some priorities in their own communities that somehow have to be reflected and I don't understand how that ---

MR. GALLAGHER: You don't think it can be accomplished with some sort of sectoral -- say the Natives want teachers housing, and then you do that through Alaska Housing Finance, you don't think that can be accomplished.

MS. FLEISCHER: Do you want to put -- repeat what we've said under development under community development.

MR. GALLAGHER: I think we have it up there.

MS. FLEISCHER: Okay, then spell it out for me. The board made up of representatives from different agencies?

MR. GALLAGHER: No, let's say you have one agency handling housing and another one small business loans.

MS. FLEISCHER: Then how does a particular village get their priorities ---

MR. RHODE: They would approach that existing State agency to put a loan together and offer it to the Permanent

Fund.

MR. LOVE: In response to Mr. Barnes' comment that he thinks the citizens board would be able to perform the function of giving the input of what a particular community wants out of it since we've got these guys elected from the Senatorial Districts, I think the problem with that the citizens advisory board is given two jobs. One is to decide their priorities as to whether or not the Fund should -- let's use these existing things, trust, development and community development. Now, let's say you're a community and the guy that got elected ran on a real strong platform of development and that was it. He was opposed, let's say, to putting a lot of dough into community development or the trust account. Let's say he was successful to a degree that they're still going to put some money into development, that may not be the person who is best equipped to represent the wishes of that particular community. He may have done a pretty good job in saying this is our priority in terms of how we want the Permanent Fund invested, but he may not be the most sensitive person as far as that community is concerned in terms of community development. I'm not thrilled with Price Waterhouse's idea of a 32-member citizen committee meeting once a year. I would like written down on the board, regional advisory committees to the central management of the Permanent Fund about the types of community development they want as part of the structure.

MR. LOVE: Also, I think we should also ---

MR. WOHLSFORTH: Jamie wait a minute. Others may have some thoughts now and the time is short. You have really had ample time. Does anyone have any other comments on this subject before we turn the board over?

MS. FLEISCHER: Can we add veto to that because of what Mr. Barnes said, and I do think the people should have the right to veto a particular project if it isn't right for that particular region.

MR. EDENSO: Should we have a general election to get some kind of development done?

MS. FLEISCHER: I don't think we should ram something through because it is good for the State if it is not good for the region.

MR. GALLAGHER: A community development loan is a pretty small loan and it only affects --- If you are talking about a bigger development project, then it would fall over here. But if you are talking about a housing loan in Bethel, I don't want them to vote on every housing loan. The very fact that you do a development loan, you've got to go out and get input from the community. That is the only way you can do it. If you're going to have a utility system, the city council has got to decide they want a utility loan.

MS. FLEISCHER: In other words, you are saying it is already ---

MR. GALLAGHER: It is implicit when you talk about community development.

MR. EDENSO: Why don't we add to a 5th one under community development loan, why don't we say city councils and managers and boroughs and combined assemblies. Those are structures that we could conceivably deal with.

MR. WOHLSFORTH: I think you get to a point where you really don't like the philosophy of a development loan and you get to this point. Admit it if you don't like it.

MS FLEISCHER: If you're talking about me, I do like the idea but I want to make sure that somehow the structure is set up so people have a real say as to what happenes to them.

MR. GALLAGHER: We all agree with that.

MR. CRAWFORD: Mr. Chairman, I would like to ask Dennis a question. Do you feel that this recommendation you have come up with is applicable to the four alternatives that we've had? Is it a management system that can be accepted ---

MR. MOTLEY: If you are asking my opinion, yes.

MR. WOHLSFORTH: Maybe we can get on with that. Is that the board's decision?

MR. MOTLEY: What we tried to do in the approach was to approach it as a businessman's decision if each one of us was given a million dollars or a billion dollars or whatever and try to work out managerial decisions on how you're going to structure this thing. You can go on for an eternity talking

about various structures. You could have them decentralized where you would have everybody in the whole State of Alaska working on this thing, the bureaurocacy involved would be so great you'd never get anything done. Starting off here at the top, using the Department of Revenue for openers. Commissioner of Revenue. Over here in this block will be the Deputy Commissioner and we have Deputy Commissioners of the Treasury. I'm taking a line off of that because of the fact the Department of Revenue has already got short term vehicles, people working down there in governmental investments in Treasuries and CD's or deposits in the bank, we thought that working off of this particular Department of Revenue which is in charge of handling money for the State of Alaska. Over here a totally separate group of people, i.e., a president -- or start from the top, Chairman of the Board, president, vice president and so on. The same structure as the banks. When a bank such as Bob Barnes, or the NB of A or the First National -- have a working staff and the Chairman of the Board and the president and these various officers, depending on the amount of work to be developed and this will depend on whether or not we are just going to go to savings or whether we are going to development or community loan and whatnot. The larger it is the more staff you're going to have. Over here and totally separate from any other entity -- we have this box, and we have a staff of people. For example, you decide to go just into a savings account, you

might get one person, i.e., a money manager from Outside which will invest in CD's or governments or whatever we have. We think that they should have a board of directors. We selected, and this is something open for discussion, 12 people. The 12 people are broken down into groups of 3. The top group would be in power for 4 years. The next group is 3 years, 2 years and 1 year. By structuring it like this you are going to alleviate potential possibilities of turning this thing into a political football because of the fact this particular individual up here will be in office, either elected or appointed, for 4 years, Governor Hammond is going to be there for 2 years, or maybe another 6 years. But each one of these individuals will keep moving on so there will be no direct conflict by the board of directors who, in fact, will be the people -- the board of directors will be responsible to these people here. These people can hire or fire these individuals depending on the performance of what they are doing with the Fund.

We suggested that these 12 people be selected, 6 from the administrative group, the governor's group, and 6 from the legislative group. Those particular individuals would be chosen such as the way the commission board or the board of realtors is chosen. Divide the State into five different sections and a particular individual comes out of each one of those areas to make up the board of realtors, to make all the decisions in the real estate area. Now, this particular group

up here is expanded to whatever the demands are going to be. If you decide every step is going to go into development, general development of the State of Alaska, needless to say this particular board is going to have to be much more large in size. If you elect just to put it in savings, probably one small business manager and one-quarter of one percent in the Lower 48 to invest in various savings accounts, Treasuries, or whatever. Just an individual, maybe out of the Revenue Department. But this way, you have totally alleviated the thing from the political atmosphere. This particular board could treat just as a business assignment. Take the money and make it go.

Now, as far as the structure of these people are concerned, this has to go on to a later date because the people of the State of Alaska or the legislature will have to decide what kind of vehicle they are going to want. If they want a combination of savings account, general development or community. That could be called maybe Alaska General Development Corporation or it could be called something else that the Price Waterhouse people and the White Weld people come up with. That is something the legislature itself is going to have to decide and that will be the proportionate or amount of money for each area that you are going to want to go into. At least by keeping this concept, working management, they can immediately take over the responsibility.

MR. BARNES: I think you need a tie-breaker on your

board, either 11 or 13.

MR. MOTLEY: 13 we'll say, or some odd number. The question was asked, how is the policy decision made up here. The policy decision would come -- let's assume that after this Committee and the legislature have come to an agreement, 1/3 into development, 1/3 into local community areas and 1/3 into savings. This policy would be handed to this group of people by the legislature, these people would be responsible -- if they didn't they'd get fired and put in new people. By putting in the kind of staff, you can go out and hire the best in the United States to be the president of the board and so on, so you have the best banking expertise.

These particular individuals will be six from the legislature, six from the administrative department.

MR. FREER: The six from the administrative side, do you contemplate they would be existing employees of the State or would they be from the public sector.

MR. MOTLEY: From the public sector.

MR. FREER: Would they be fulltime paid employees?

MR. MOTLEY: Our suggestion was that the governor would select six people, again using the real estate's board concept, divided into 5 different sections. Try to pick people out of each one of the sections so each one of the sections in the State of Alaska has representation. The same with the legislative people over here, they would choose their people

from the various areas of Alaska so that the whole State is represented to help make these decisions.

MR. FREER: Are they voluntary, or are they paid?

MR. MOTLEY: We believe that they should be on a voluntary basis. These people up here, this board of directors, working board of directors are going to be paid very handsome amounts of money. These people over here will be supervising to make sure that your policies, whatever the legislature chooses, is carried out. And if it isn't carried out, you remove the board of directors and put in a new board of directors.

MR. WOHLSFORTH: Mr. Gallagher has to leave but we might as well continued with any questions on this.

MR. BARNES: It is very similar to the Price Waterhouse model. You are using the legislature as the citizens board. And you are setting up an operating board and it sets up management which is pretty much what Price Waterhouse has said. Doesn't it strike you that it is fairly similar?

MR. MOTLEY: We felt that it was a little bit more workable from the standpoint that it is more clear cut and less bureaurocacy involved so far as getting those decisions out. And it also gives more attention to these particular individuals who are up here. If they don't carry out these policies that have been selected, these 12 people are going to elect to fire them. It's just like over at your shop, if you don't carry out

the policies of your board, the decision of the board, you aren't going to be there any more.

MR. WOHLSFORTH: Any other discussion before Sterling has to take off?

MR. LOVE: Two comments. First I am wondering when we're going to address different ways of things to do with the earnings. As we have community development, development and trust funds, I think we ought to have -- that the goal is to redistribute the wealth.

MR. GALLAGHER: If your goal is to redistribute the wealth, how ---

MR. LOVE: I would like us to take a look at possible ways of distributing it. There will be prosperity in the State brought about by the revenues, who is going to get the most of it? Who is going to become wealthy and who is going to remain poor? I'm not saying we should discuss it right now, but I think those are some things we are going to have to discuss.

MR. GALLAGHER: The third week in December is the next meeting.

MR. MOTLEY: Is there a possibility to move it forward just one week?

MR. EDENSO: Jim Rhodes and I have talked at some length about the next meeting. Due to travel schedules and time of the day, time of the year, holidays and everything, it looks as though the third week of December is probably the best.

And probably if we could have another 2-day meeting. I think we pretty well filled up two days this time, so December 17 and 18th. But that is only open to the Committee. If the Committee decides that is a bad time, then let's hear some other suggestions.

MR. MOTLEY: Would it conflict very much with the Department of Revenue if we had it sometime between the 6th and the 10th, which is the second week in December?

MR. LOVE: I would like to see us meeting again in the month of November, even if we don't have a -- because I think this has been very fruitful.

MR. [illegible]: If we could have some work committees in November and come back and look at organization and structure.

MR. LOVE: This has been very helpful to me in getting a clearer picture. I would like to the committee as a whole meet sometime in November and pursue the discussion we started today. Maybe just for a day.

MR. WOHLSFORTH: I wonder if it came to a vote how we would feel about some subcommittee work. I think you resisted it very strongly at the last meeting.

MS. FLEISCHER: No, we didn't, we asked for it.

MR. EDENSO: If we are going to hold a meeting that soon, I would like some ideas, or at least a better idea of what we are going to attack or address at that meeting.

MR. LOVE: I would like us to talk about the two things I mentioned previously. Distribution of earnings from the Fund and the effect of the investment policies on either concentration of wealth --- Secondly, I think we should have some additional presentations, if we could, by the consultants giving us a background on present State loan programs and maybe something relative to the activities of the Native Corporations.

MR. RHODE: I think to take each one of these areas we have discussed today, the three different separate goals and start looking at how an organization under that would be structured.

MR. : You might break down into subcomittees on the basis of the three sets of structures, and in each case focusing on what kind of governing board. What any of them be elected or not. Would you have professional managers that are appointed by an executive officer.

MR. WOHLSFORTH: The idea of subcommittees makes worlds of sense. These are expensive meetings when you consider the number of people who are being brought in from throughout the State.

MR. LOVE: What kind of subcommittees do you want?

MR. WOHLSFORTH: I think Jim had a suggestion on that.

MR. RHODE: According to the three things.

MR. LOVE: I don't think one on the savings account.

MR. RHODE: Probably not, but on the other two.

MR. LOVE: Community development and development.

MR. RHODE: I think that allows people who have strong ideas in one area or the other to concentrate on them.

MR. LOVE: Just work sessions and whoever shows up becomes the subcommittee.

MR. RHODE: Have a work session and then at the next formal meeting in December.

MR. LOVE: Let's have a couple of work sessions on those two subcategories that you mentioned sometime in November, and just those who are interested in those particular areas make up the subcommittees

MS. FLEISCHER: Could you ask the consultants to come up with some ideas on the structure based on these alternatives.

MR. RHODE: You have the structure in front of you. I think it is a relatively simple one. In my judgment, every issue that you have to face is laid out in the paper by Price Waterhouse or White Weld.

MS. FLEISCHER: I don't think it is very workable.

MR. : One is simple and one is complex. If the complex one or the goals demand complexity, then it is variations on a theme that Price Waterhouse has suggested. The questions are, should the citizens board be elected or appointed, should it be -- should the citizens and the governors board be merged into a single board. Should the governor be given guidelines as to how he designates his people. Then the next

level is operation as opposed to management and a control.

MS. FLEISCHER: I guess what I wanted to know is whether we could have some help on the implications of the variations on the theme.

MR. CRAWFORD: I think it is going to be very difficult for us to come up with any kind of concensus on a structural entity until we get the answers from the AG so far as the constitutional questions.

MR. WOHLSFORTH: It might be helpful if we do have an interim meeting and the young AG's assigned to the problem could advise us at least -- give some preliminary views and that would lead us a little bit farther down the line. I doubt very much if we could get a definitive yes, no answer very quickly,if at all. On the 17th and 18th, is that agreeable for the next full board meeting.

MR. EDENSO: There is some difficulty with that whole week.

MR. MOTLEY: How about the 3d and the 4th of December.

MR. WOHLSFORTH: Will somebody move that? If no objection, so ordered.

MR. EDENSO: A subcommittee meeting on the 19th and 20th has been suggested.

MR. RHODE: Does the Committee available at this work session or not?_

MR. WOHLSFORTH: 19th and 20th for a workshop, December

3 and 4th for the regular meeting. May I have a motion to adjourn?

MS. FLEISCHER: So moved.

(MEETING ADJOURNED AT 1:50 P.M. NOVEMBER 6)

SCOMM

#9:41

DECENTRALIZING THE AMERICAN ECONOMY

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Our recent bicentennial has focused national attention on the changes wrought by 200 years of American development. Unfortunately, that attention did not extend to one of the most important changes; the general transfer of power from small and local institutions to larger and more remote ones. What was once a highly decentralized social and economic system has become much more centralized. Our own control over important decisions--decisions affecting our personal and family lives, our communities, our jobs and our work opportunities--has increasingly been eroded.

This is nowhere more obvious than in economic life. For example, the 500 biggest American firms produce over three-quarters of all American goods and services, and employ a similar proportion of the work force, despite the fact that they are only one-fifieth of one percent of all businesses. Our industrial system consists of a handful of very large firms and a great many comparatively tiny ones. Because of this, economic life tends to be dominated by the action of a few large firms, which are themselves controlled by a relatively small group. This is not a radical statement; top management personnel, who make the critical decisions, constitute a very small percentage of the total work force.

Present Concerns

These large firms are coming increasingly under attack; disclosures of inappropriate acts appear regularly. Lockheed, Gulf and many more have been heavily involved in unethical practices both here and abroad; many others have tacitly admitted to discriminatory behavior. Even where proof is hard to get, grave suspicions are the order of the day; "The energy crisis was

engineered by big oil to increase their profits," or "Multinationals are replacing American jobs with foreign ones." As a matter of fact, practically nobody is really satisfied with the present situation.

The underlying concerns fall roughly into three different categories or schools of thought. The first includes those who see a system of large firms as the appropriate response to the vase and varied demands for goods and services characteristic of modern economics; in their view, large size is not only the efficient production means, but also the most effective economic agent for furthering social goals. Not surprisingly, this includes most people associated with "big business." The second group comprises those who see large firms as necessary evils; necessary because of the demands of highly developed economies and the requirements of modern technology, but bad (inappropriate) in terms of their impact on the distribution of rewards, opportunity, and power. John Kenneth Galbraith is perhaps this camp's most eloquent spokesman, but the same feeling underlies the considerable bipartisan support that rises in discussions of controls on prices, wages, profits, and employment. Economic liberals tend to fall into this camp. The third group essentially takes it for granted that large size is not primarily a consequence of economic or technological necessity, but is rather a reflection of the concentrated power characteristic of societies permitting private ownership of production resources and the private accumulation of great wealth. This, in general, is the radical position.

These three groups have different goals, different degrees of interest in changing the system, and have in mind different mechanisms for change. The first, believing in the virtues of big business, would like to reduce "government interference" and thereby bring the system closer to classical free enterprise ideals. The second, which is probably closest to the present main stream, sees no other option but to make the best of a bad job, supporting the large firms of which it disapproves in principle, but hedging them all around with

controls, which become an unfortunate necessity. The third wishes either to break up the large firms and to modify the economic framework to eliminate any future possibility of private ownership of the means to production, or alternatively, to nationalize them forthwith.

These "solutions" are no more satisfactory than the problems they wish to attack. The first two are flatly wrong in asserting either the value or the necessity of very large firms, as I will show below. The first group also errs in stressing the virtues of private enterprise; they are real and important, but they simply do not result from a system dominated by very large firms. And the second group is attacking problems of overcentralization by developing even more centralized mechanisms, a strategy akin to fighting for peace; anyone who thinks it can work should take a look at the British economy. As for the third group, transfering control from "private" to "public" hands (those words mean different things to different people) simply shifts power from one small group to another. This is clearly demonstrated by the general experience of most nations putting those principles into practice (for example, in the socialist bloc).

The plain fact of the matter is that the major proposals being put forward today are simply inadequate to the job that needs to be done. And yet that job is probably more important even than these remarks suggest. It is not merely a matter of fine tuning. The need to develop real alternatives is pressing, because our present economic arrangement is defective in several <u>fundamental</u> respects. First, effective and timely coordination is difficult or impossible. We continue to "discover," for example, that our plans and programs do not always work as intended and indeed, that they often produce entirely the wrong results. Second, it is wasteful of resources; costs continue to increase without equivalent benefits. It takes more and more merely

to stand still, as we see from the combination of high inflation and deteriorating results. Third, it is unresponsive to the needs of our society. The economic system and its components only exist to serve social functions. They cannot be justified otherwise. Yet increasingly, these large organizations--firms and governments alike--operate in terms of their own priorities. They are simply too remote from the ultimate results of their actions and too big to respond adequately even if they were in closer contact.

Finally, the present arrangement is downright destructive in two important ways. For one thing, it tends to swamp local economic life. As the tides of economic change sweep across the country (and the world) they leave prosperity in some towns and some regions and destruction in others. But even the prosperity is temporary; at the moment, New England is down and the sunbelt is up. Or look at New York City: its present situation was unthinkable as little as a decade ago. These effects are not aberrations. Rather, they are entirely normal, because the present arrangement makes it both appropriate and necessary that some places prosper while other do not. Plants are moved, products shift, market orientations are altered, and economies change. Under those circumstances, people lose jobs and towns, areas and regions are hurt, sometimes fatally.

Second, our present economic arrangements do not and cannot offer most people rewarding and dignified work. Although this applies most particularly to blue-collar and clerical work, it is increasingly true of managers and professionals as well. This generates enormous human and social costs by reducing mental and physical health and it contributes directly to the lagging productivity that has lately become characteristic of American industry. Most importantly, peoples' capacities, skills and competence cannot be developed without opportunities for their exercise. And these are available only to a small fraction of our citizens.

This is always a tragedy. But it is especially tragic in the United States, with its extraordinarily fruitful and well-developed economy in a richly-endowed social and physical environment. That good fortune permits us much more flexibility and a greater possible range of options. Societies that literally cannot feed their citizens--and there are many such societies--have to deal with those basic problems first. (This is no excuse for repressive governments; there are always some options).

Happily, a real alternative is available in America; one that is particularly consistent with the American historical experience. I am referring to a return to traditional American decentralist principles, and in particular to decentralizing our economic system by simultaneously moving to reduce the size of large firms and distributing control over them more broadly. I would like to show first, that smaller firms need not be less effective and indeed that in important ways they would be more effective; second, that alternative arrangements for redistributing control are both available and valuable in their own right; and third, that their advantages are enhanced by combining both these approaches.

Some Important Distinctions

Before developing my argument, let me clarify a few important points. First, an economic system is not merely a collection of firms. It includes consumption units (households, families, and individuals), and production and distribution units (firms), all operating within a legal and political framework establishing the range of legitimate action open to them. In the U.S., key elements of that framework include private ownership, freedom of enterprise, and markets in labor, capital, physical assets, and knowledge. This is important because changes can be made through any or all of those avenues. Substantial changes may even require attention to all of them, and particularly to the "rules of the game."

Firms--especially large ones--are themselves complex entities. In particular, they are very different from plants or individual business establishments (factories, stores, motels, etc.) which are their basic operating units and which produce goods or offer services at particular locations. In contrast, a firm is a legal or operating entity, controlled and owned by some particular person or group and often owning and controlling in its turn any number of individual plants or establishments. This is the central fact about large firms; they consist in every case of a whole cluster of separate facilities, whether plants, offices, laboratories, or distribution outlets, under central control. The classic firm of economic theory, which owns and operates a single plant or establishment, is actually what we now call "small business." The whole issue of size for this reason becomes confused with issues of control or ownership, which are of very different characters. Since our measures of size are usually related to firms, then the very same plant or retail store shifts in classification from "small" business to "large" depending on whether it is owned independently or by an international firm a curious and unsatisfactory situation.

Finally, size itself can be measured in very different ways--number of employees, dollar volume of sales, and value of assets owned are probably the three most common. Each is useful for particular purposes. Since my major focus is related to the relationship between individuals or groups, and organizations of different types, it makes sense in general to measure size by employment.

Size is also technically different from scale. Whereas measures of size are absolute--numbers of employees, dollars or whatever--scale is a measure of relative size. The scale of a firm, for example, might be specified as twice as many employees, 70 percent of sales, or 25 percent more assets than

some standard of reference. In practice, they are often used more-or-less interchangeably.

The Anatomy of American Industry

I would like to start by briefly describing the size and character of American industry now. The size distribution of American firms is shown for all industry in Figure 1 and for manufacturing industry only in Figure 2. Although those figures are for 1967 (the last year for which comprehensive and detailed statistics are available), there has certainly been no marked change since. One thing stands out at once; the mean number of employees/establishment never gets very large, especially if the top category is dropped. Companies tend to grow not by increasing the size of their individual production units or plants, but by bringing new units of roughly comparable size under their control. Moreover, much of this growth is accomplished by acquiring existing firms, or product lines, rather than by developing new ones from scratch (see John M. Blair, Economic Concentration, NY: Harcourt Brace, Jovanovich, 1972). Note also that manufacturing companies, which overall account for only 10.9 percent of all companies with employees, account for 70.4 percent of all those employing more than 1,000. Clearly, although problems of large size exist in all business sectors, they are most evident in manufacturing.

Even so, the separate units are surprisingly small; mean employment per operating establishment in 1967 was only 52.5 persons. To some extent, that is the result of a large number of tiny businesses still classified as manufacturers. However, even if these figures are pulled apart, it can be shown that most plants are still of moderate size. American multi-unit firms (those controlling more than one establishment) comprise only about 4.3 percent of the total American manufacturing companies, although they own 16 percent of all plants and contain over 74 percent of total manufacturing employment.

Figure 1

DISTRIBUTION OF EMPLOYMENT BY ESTABLISHMENT AND COMPANY

ALL BUSINESS

	Companies	Establishments/ Company*	Employment/ Establishment
All companies (with at least 1 employee)	2,326,703	1.18	15.20
Companies with 1-99 employees	2,292,680	1.05	6.94
Companies with 100-999 employees	31,353	3.86	60.50
Companies with 1,000-9,999 employees	2,306	36.00	75.6
Companies with 10,000-99,999 employees	346	352.80	68.0
Companies with over 100,000 employees	18	855.60	213.0

*An establishment is a business unit at a single physical location which produces or distributes goods or services for sale, usually in a particular line of activity.

Source: General Report on Industrial Organization, 1967, Vol. I, Government Printing Office, Washington, D.C., 1972.

Figure 2

DISTRIBUTION OF EMPLOYMENT BY ESTABLISHMENT AND COMPANY

MANUFACTURING INDUSTRY ONLY

	Companies	Establishments/ Company*	Employment/ Establishment
All companies (with at least 1 employee)	253,498	1.61	52.5
Companies with 1-99 employees	234,923	1.02	14.5
Companies with 100-999 employees	16,694	2.31	107.0
Companies with 1,000-9,999 employees	1,593	23.60	119.0
Companies with 10,000-99,999 employees	273	312.00	77.3
Companies with over 100,000 employees	15	398.00	452.0

Source: General Report on Industrial Organization, 1967, Vol. I, Government Printing Office, Washington, D.C., 1972.

These are the giants of American industry, and here, if anywhere, we expect to find large plants. Yet the separate plants owned and operated by these firms employed only 203 people on the average. Moreover, if a very few industries such as automobiles, defense systems, and large electrical machinery were excluded, the mean employment figure drops to about 100. I do not deny the existence of many very large plants. I do deny that they are typical; the size of plants is very different from the size of firms. American industry is therefore quite concentrated so far as control (firms) is concerned, but is still remarkably dispersed, small scale and unconcentrated so far as production (plants and establishments) is concerned.

Size and Decentralization

Much more attention has been paid to the size and concentration of firms than to that of plants or establishments. Most discussion never even mentions the distinction. This has led to a general confusion between the two very different issues of control or ownership, and size. And this has led in turn to a parallel confusion between decentralization, or distribution of control, and options for the effective arrangement and use of resources. In fact, each has an important effect on the other, though each can also be profitably explored separately.

Reducing the size of large firms would itself be a step toward decentralization for a very simple reason: it would result in more units of more comparable size, among which control could be distributed. However, there is obviously some limit below which we would not wish to go for it would mean the loss of the qualities that make such organizations valuable in the first place. A totally "atomized" economy, with no firm employing more than, say, 10 persons would be inefficient, wasteful of resources, and in general unable to provide adequately for society's economic needs. The question is: What are the limits of useful reduction of firm size? It is also perfectly possible to imagine

an economy containing no firms above some moderate size (say, 500 employees) but in which those firms were each closely controlled by a single entrepreneur/owner. This would be an economy decentralized in one sense (no market concentration) but not another (not, that is, with respect to employees, customers, or neighbors). The question here is: What are the consequences of decentralizing by only reducing size of firm?

Conversely, the economy could continue to be dominated by very large firms but ones over which control was distributed quite broadly. This could be done in many different ways. One alternative exists in West Germany (and increasingly in Scandinavia) where the principle of co-determination assures laborers of formal representation on the managing board of the firm. Firms could also be organized along principles of broad-based worker (meaning all employees) control, as in Yugoslavia. Or again, control could be shared with groups outside the firm itself, whether consumers, suppliers, members of plant communities, or even a governmental agency acting as representative to the public (as is the case, for example, with AT&T). And this by no means exhausts the options. The question is: What difference do these differences make?

The Effects of Size

Since the effects of size are probably clearest, let me start by exploring that one first. My own detailed studies (and others) concerning the relationship between the size of economic units and their ability to utilize resources effectively unequivocably deny the routine assertion of large firms that their great size is necessary. The usual argument is based on economies of scale; that is, the principle that some costs become relatively smaller as the size of the operation increases. For example, the cost of producing, say, ten identical chairs per week may be $100 per chair. If production could be expanded to 100 of the same chairs per week, the cost would drop considerably; say to $50 apiece.

Let me say at once that there is no doubt that such economies of scale exist and that they are important. But most of the obvious ones are related to the size of plant or establishment, and not to size of firms. The tables presented earlier show conclusively that most plants are not very large. The great majority are within the Commerce Department's definition of "small business." And if larger plants were required to gain those economies, the firms that own and construct them would certainly build larger ones.

The real issue therefore hinges on the possible economies to be gained by operating many plants under a single organizational umbrella. Most studies are in basic agreement here. In general multi-unit operation is not more economical than single-unit firms operating an equivalent facility (I have reviewed and summarized the evidence in Size, Efficiency, and Community Enterprise). The most comprehensive economic treatment of this question was recently carried out in depth on 20 industries by F. M. Scherer and associates (The Economics of Multi-plant Operation, Harvard, 1975). Their conclusions were mixed, but even where they found evidence for multi-plant economies of scale, they were typically of the order of only a few percent.

However, the nature of their data and procedures do not allow us to put much confidence in them; the authors themselves noted many mitigating factors. Even if the figures are taken at face value, they are well within the range where "business practice" can make more of a difference. Furthermore, and I will expand on this below, economies from scale in such functions as research or finance or in specialized skills, can be gained by other means than ownership. For example, separate specialized firms can offer such services: this is now widely true for computer facilities. Cooperative or other shared activities can provide adequate scale for other purposes; for example, small Swiss firms pool credit and financial resources. Or again, industry and trade

associations are common devices to gain economies in promotion, training, and standardization of products.

There are also important diseconomies of scale (costs that increase with size). For example, both the generation of new ideas and their applications are more common in small firms than in large. This is often particularly clear in market-concentrated industries, where major technical developments tend to come from smaller, more peripheral firms (See J. Jewkes et al, The Sources of Invention, 2nd ed., W.W. Norton, 1969). Similarly, small firms are more responsive to environmental, social, and economic changes, because they can perceive them more accurately (being less insulated from them) and because they can respond to them faster (just as a small ship can be maneuvered vastly more easily than a large one). In short, smaller firms can "track" social changes and consumer needs much better than can large ones. This is the central factor in John Kenneth Galbraith's sustained critique of mainstream economics (The New Industrial State, Houghton-Mifflin, 1967). And in fact, is is related to the most fundamental source of diseconomies of scale, rapidly increasing costs of coordination as organizations become larger. There is also a substantial human cost. As size increases, worker satisfaction and mental health decrease, and strikes, physical injury, and sabotage increase. (See the report of the Special Task Force of HEW, Work in America, MIT Press, 1973.)

Many large firms attempt to minimize these problems by decentralizing their decision-making as much as possible. Although this is certainly useful, it is not and cannot be equivalent to fully independent units, and in principle can only gain a fraction of the benefits. To the extent that there is central control, it will reduce flexibility. If there is not, then common control is not needed. Finally, many of these diseconomies, such as those involving long-term loss of human resource potential, and those related to less constructive or downright destructive behaviors will not show up in

economic calculations such as those carried out by Scherer.

All this leads to an important conclusion. A large fraction of existing manufacturing capacity operated under the control or ownership of multi-unit firms could be converted to independent operation without loss of economic effectiveness, and with some probably gains. In other words, this is an issue of control and not one of size. Since it could be done, actions leading to this end should certainly be encouraged, since our economy, without the present proportion of multi-plant firms, would be far less concentrated than is the case at present. For similar reasons, business and individual opportunity would increase; wealth, power, and income would tend to become more equitably distributed; and government regulation of business could be greatly reduced.

That leads to the second question; How far could such a decentralization or divestiture be carried without creating efficiency problems of its own? In other words, how big do plants have to be to take advantage of real economies of scale in particular industries? Previous work on this topic has led to extremely inconsistent results. Recently a colleague and I carried out a new series of calculations by making detailed comparisons of successive government censuses of manufacturing industries (at four or five year intervals) to determine the size of new plants entering particular markets. These markets were those described by so-called four-digit Standard Industrial Classifications, which are moderately precise (see B. Stein and M. Hodax, Competitive Scale in Manufacturing--The Case of Consumer Goods, Center for Community Economic Development, 1976). Specifically, we determined the minimum size of plants entering the 100 such markets for manufactured consumer goods between 1963 and 1967. In effect, we estimated the smallest (by employee-size) plants thought by business people to be effective in the marketplace. Using other data, we also estimated the capital requirements of such plants and the necessary consumer market (numbers of average consumers) needed to support them.

The results are as follows.

1. Almost 70 percent of these industries could use plants with less than 250 employees; 44 percent of them need less than 100 employees.
2. If automobile-related products are excluded (eg, cars, petroleum products, tires), 71 percent of all consumer goods (by value) could be locally produced for an area containing 1 million persons. Twenty percent could be produced even for a market of 200,000.
3. In about 70 percent of the 100 industries, these minimum plants would need a capital investment of less than $1 million.

I should also add that there is no reason to assume that these figures represent a real minimum. On the contrary, if our practice and technology were oriented toward smaller rather than larger units, fully effective and competitive firms could enter the market at considerably smaller sizes even than those identified by this procedure, which reflects current practice. Size, per se, can be reduced substantially without losing effectiveness and even with some gains.

Alternatives for Decentralization

I will now turn to the organizational and institutional alternatives that could modify the distribution of control, whatever the size of the units. There are many variations in detail. They can be grouped according to whether they attempt to decentralize by redistributing control within firms, outside firms, neither, or both. These four possibilities are shown schematically in Figure 1.

In the usual case, every firm is associated with one or more persons whose financial benefits and costs are directly linked to the fortunes of the firm. Such persons usually exercise control and are known as owners. The axis "Control Within the Firm", differentiates arrangements in which only the

Control Outside the Firm

Control Within the Firm	Minimum Distribution	Extended Distribution
Minimum Distribution	Quadrant 1: Entrepreneurial Firms Partnerships Shareholder Corporations	Quadrant 2: Community Development Corporations Consumer Cooperatives Government Firms
Extended Distribution	Quadrant 3: Firms with Codetermination Worker-Owned Firms Producer Cooperatives Communities of Work	Quadrant 4: Israeli Kibbutzim Intentional Community-based Firms Yugoslavian Firms

Figure 1

Decentralist Alternatives

"owners" have legal rights of control (Minimum Distribution) from those in which others within the firms, such as employees, also have control rights (Extended Distribution). The qualification "legal" is strictly necessary; many owners as a matter of good practice or good conscience elect to share their own control with others. But if it rests on the owners' whim, which can be taken away as readily as it is given, it is not equivalent to legally shared control. The category "Control Outside the Firm" similarly differentiates legal arrangements that offer some control to external persons or groups (Extended Distribution) from those that do not (Minimum Distribution).

Quadrant 1

This quadrant describes entrepreneurial firms, partnerships, and shareholder corporations. To the extent that shareholder's fortunes are tied to those of the firm, they are by my definition owners even though they may in other ways be outside it. Indeed, the legal mechanism permitting widespread share ownership of a corporation serves precisely to encourage owners to put the firm's interest above all other potentially conflicting interests. Some external influence is always necessary--one is otherwise dealing with a species of dictatorship. In this quadrant, that is provided by the exceedingly indirect means of the market. But this is fundamentally different in character from the sort of control or influence that can be thoughtfully and deliberately applied to the firm by persons or groups legally entitled to do so.

This is the markets' greatest strength and greatest weakness. Its impact cannot readily be deliberately withheld, nor can it be deliberately increased by the action of an individual or firm. Where it is thought to be functioning inappropriately, the government must step in one way or another. Indeed, there can be no such thing as a market system unless the government and the legal system provide rules and agreements by which all participants abide. Since these influences are still indirect, so far as particular firms

are concerned, it is still fair to say that in quadrant 1, control is closely limited to owners. In this case, a decentralized system exists to the extent that the market functions in its classic competitive mode, or it does not, to the extent that market distortions exist.

The conditions necessary for a perfect market are well-known, stringent, and nowhere observed in practice. In the present U.S. economy, the chief source of distortions is the extremely skewed size distribution of firms described above, and the consequent concentration and market power held by the giants among them. As this becomes evident, the government introduces new mechanisms, or redefines old ones, to restore what is thought to be a proper balance. But this generally has unintended and inevitable side effects and it is not always clear that the cure is better than the disease.

Quadrant 1

This quadrant basically includes firms that operate internally much as do the conventional enterprises in quadrant 1, but that add control by outsiders. These firms are of three types; community development corporations (CDC's), consumer cooperatives (coop's) and enterprises under government control, whether exercised directly by the state (socialist firms), directly by a subordinate political unit (municipal firms) or merely regulated closely by political agencies (regulated firms, such as AT&T or public utilities in general). Although these differ in detail, they are based on a common structural arrangement that justifies putting them all into one category. In the final analysis, they share a theory.

They all assume that the conventionally accepted arrangement of an enterprise--that is, by a system of hierarchical control and a chain of command--is most appropriate for operational purposes, but that the market as it exists is disadvantageous. That in turn can be divided into two views; one, th

market defects prevent appropriate outcomes (and therefore must be modified deliberately) or two, that an alternative arrangement produces better results in some way than would the market, even if perfect. In the first case, the external control is used as a corrective of the existing market, whereas in the second, it is a deliberate distortion of it. Holders of the former view see the results of the market as the best that can be achieved, while to holders of the latter view, this is not true.

On this basis, regulated firms wish to achieve market outcomes (regulation is clearly supposed to be corrective); all others in this quadrant believe that market results need modification. Regulated firms are therefore more like the enterprises of quadrant 1; they are based on minimum possible interference with the market, that interference being designed to produced outcomes consistent with a perfect market. Since the issues I am exploring here are more sharply focused in the other alternatives, and since no one ever seems satisfied with the results of regulatory mechanisms, I will drop them for this discussion.

The fully-fledged members of quadrant 2 wish to decentralize by giving legal rights to special groups of persons outside the firm. Coops empower the firms' customers, CDC's empower members of the community in which the firm does business, and socialist or municipal firms empower citizens of the appropriate political jurisdiction. These, at least, are the theoretical results. In all too many cases, the potential benefits of these arrangements (assuming for the moment that they exist) are not in fact realized. Socialist or municipal firms, for example, often give power only to those persons already politically influential. And in practice there is much overlap among these different types of firms; consumers, local residents, and citizens might be substantially the same group of people, depending on the enterprise in question. This is not to suggest that the difference is not important; the rationale for choosing one or another of those differs profoundly. In the limit, however, an organization providing goods or services for people who <u>by definition</u> are

customers because they are also residents and citizens is a political rather than a economic entity.

Quadrant 3

This quadrant basically contains the alternatives built around employee participation. Decentralization here is internal; those who are directly involved in operation of the firm are seen as appropriately involved in its control, although the mechanisms vary. As a common position, I should say that these alternatives are based on theories exactly opposite to those of quadrant 2. Alternatives in quadrant 3 seek minimum external interference with a firm's independence and autonomy, but believe that the internal organization of the firms should differ from the classic entrepreneurial or managerial model.

There are essentially three variants here. In order of increasing involvement of employees in the decision-making apparatus, they are; codetermination (worker-employee representative on the firms' board of directors), worker-owned firms or producer coops in a free enterprise market environment, and communities of work (of which the Scott Bader Commonwealth in England is perhaps the outstanding example). Codetermination, which has been applied most extensively in very large firms, shares control at arm's length, so to speak; day-to-day and shop-floor decisions tend to be made along conventional lines. Scott Bader, on the other hand, attempts to transform the very nature of the firm to make it less of an isolated job-related, 9-5 entity and more an integrated part of people's total lives, in the process changing also the relationships among "employees" (who become instead "members") and the nature of internal decision-making.

Quadrant 4

Quadrant 4 finally, includes those firms attempting to distribute

control much more broadly both within and without the firm itself. This is the only group in which decentralization is thought to require changing both the internal decision-making structure of the firm and its relationship to its external environment. Fully-fledged examples include kibbutzim, Yugoslavian worker-owned firms (which differ in very important ways from the western or American variant because ownership has a different meaning) and enterprises operated by and as a part of intentional communities (many of which exist in the U.S.).

Operationally, such firms offer people more than one means of formal influence over the firm's actions. In the kibbutz, or in intentional communities in general, all workers have access to control because they are workers. But they are also members of the community itself, and are entitled to some control over the enterprise for that reason as well. Moreover, because these alternatives are rooted in philosophical principles that see many defective results from hierarchy, bureaucracy and unevenly distributed expertise, such firms tend to develop special mechanisms to reduce those while keeping their desirable effects. For example, regular rotation of work roles is one such device.

Such firms also call attention to issues that must be considered in any discussion of alternative economic organizations; namely, the relationship between the principles underlying the alternative itself and the society in which it operates. As I noted earlier, an economic system consists of operating and consumption units and a legal/political framework that permits and supports certain things as against others. Conventional firms in the U.S. are effective in part because they are consistent with and reinforced by that framework. Different alternatives inevitably face pressures and problems as a direct result of their inconsistency with the framework; because they need to make a variety of adjustments, their results are in part due to those adjustments

or inconsistencies and are not necessarily inherent in the alternative. American intentional communities that operate enterprises should not be expected to match the results of kibbutzim in Israel, where they are socially supported. Similarly, American worker-owned firms should not be expected to duplicate the effects of the Yugoslavian system, where all firms must operate according to common principles.

The Effects of Size on Decentralist Alternatives

I have already extensively discussed certain effects of size on the firms in quadrant 1. As far as the effect on the potential for decentralization is concerned, there is little to add. Decreasing the size of large firms is important because it increases the numbers of competitors (reduces concentration) while simultaneously reducing the existing great disparities in size (and market power) as between firms. This properly speaking, is an issue of relative size--that is, scale--particularly in terms of existing market capacity and competing production units.

In quadrant 2, size enters in a different way; the relevant measure is the membership of the particular group with which control is being shared; customers, community members, or citizens. As these groups become larger, the effect of the sharing of control becomes increasingly small until, beyond a certain not very large point, it ceases to have much meaning for most people. An exactly similar argument applies to shareholders of quadrant I corporations. As a device for sharing control (decentralizing), it decays rapidly with size; as a device for sharing financial returns, it can be infinitely expanded. The difference is crucial; it is unfortunately much easier to offer people participation financially than in terms of power and control.

The effect of size on the quadrant 3 variants is clear. Co-determination, though readily applicable to any size of firm, offers relatively less personal

involvement for individual workers as size increases. The same issues arise as in any representative system; the larger the numbers, the less the individual influence, save for the inevitable small (elite) group that becomes more central. Neither of the other variants has been applied to firms of more than a few hundred persons, and thoughtful members of such groups, as well as theoreticians viewing them, agree that their benefits could not readily, if at all, be gained beyond that. Indeed, Scott Bader made the specific decision to split off a new entity rather than grow. Some of the American worker-owned firms, have, with growth, shown one of the potential problems. They have developed two distinct classes; an elite group of worker-owners and a secondary group of employee-workers with distinctly less influence. In quadrant 3, then, absolute numbers of people contained in the enterprise work force is the relevant measure.

As to the effects of size on the quadrant 4 alternatives, they combine those in quadrants 2 and 3 and are, accordingly, doubly important. Well-developed institutions of this type have invariably spent considerable time and energy on this issue. All observations indicate that where size is allowed to increase beyond a certain very modest point, the difficulty of living up to these principles becomes correspondingly great. The effect of size is compounded; it enters both in numbers of workers and in relation to the size of the larger unit of which the firm is an integral part (community or political body).

It follows that all possible variants function more effectively (that is, achieve more of their objectives) if their size, measured appropriately, is relatively small. This is not at all surprising; political theorists have long recognized the enormous effects of size on participation. And the classical political alternatives designed to deal with that problem are being applied to the economic or industrial sphere as well. Representative methods can certainly help; to the extent that control is distributed among interest

groups or important social units rather than individuals, somewhat larger numbers can be effectively accomodated. But this obviously involves trade-offs as well. An effective system for broadly distributing control will invariably need to combine direct participation with representative methods.

No matter how these variations are arranged, however, the critical point is this. Larger size is never beneficial so far as distribution of control is concerned. The fact that smaller enterprise size is fully consistent with effective operation means that all of the options explored become more accessible rather than less. It is technically feasible to decentralize the economic system, and there are many ways to do it.

A Decentralized American Economy

I would like to shift my focus now, and explore some specific principles that derive in part from the foregoing, or are consistent with them, but that draw on a wider range of experience. The alternatives mentioned have all been tried out in different places, and there exists much information on their impact and effectiveness. Similarly, the issues they raise, like those raised by the whole subject of decentralization, have been discussed extensively in theoretical terms and in an attempt to devise larger generalizations. Thus, we do not lack a basis for offering serious suggestions.

There seem to me two basic principles that need to be followed; each of them suggests many subordinate propositions. The first principle is this: any decentralist or power-sharing thrust--if that is really desired--must necessarily involve a strongly pluralist orientation. No single solution nor unique device or arrangement can possibly survive as a decentralist mechanism. Organizations in general, and firms in particular, are characterized by limited goals: it is the main source of their strengths. And people attached only to such groups become committed to those goals and those organizations,

in part because they offer their members the only source of rewards and power accessible to them. Yet we know that that single-minded dedication is an important source of the corrupting character of too much power. What is good for General Motors--or nearly anything else--is seen to be good for the country. This is not the result of evil or calculating people, but of structural limitations.

The solution is simple. Separate units of all kinds should be kept as small as possible, and people should be able to participate in meaningful roles (again, that requires smaller units) in a wide variety of institutions. Everyone should be able in principle to exert some personal influence, or to make his/her voice heard in many arenas. This is not to say that all will always, or even generally, be active; rather, it says that access to personal influence must be ready-at-hand and the mechanisms must be kept lubricated. The best guarantee against too great power wielded by any single group or entity is provided by a rich variety of options through which other people can express other views and gain influence. Thus competition in the most healthy sense of the word is an essential part of any effective decentralist system, but it is competition that always offers people a chance to learn and a place to turn.

On the other hand, it is important not to lose sight of the value of the dedication and commitment that people can bring to a social group or organization, especially when they identify strongly with it. This is a matter of balance; it would be just as much of an error to allow too little chance for people to concentrate their energy and attention as the opposite. That is why I stress access to channels for participation and influence rather than its uniform presence. People will make the choices themselves if the alternatives are visible, accessible, and real. But once again, this requires

relatively small and flexible structures and institutions; it is simply less flexible if giant organizations--firms or political unite--are dominant.

Overall, this sort of pluralist and influence balancing strategy offers important functional advantages for society. Indeed, if it did not, it would not be worth proposing, since every social alternative needs to be evaluated in terms of its impact on the three central types of social goals; those concerning operation, distribution, and integration. This sort of decentralist economic strategy would contribute positively in each of those categories.

Operational goals address the effectiveness of the economic system itself; the extent to which it provides goods and services when and where they are desired, and does so with minimum waste of resources. It has always been recognized that smaller sized units, even without other reforms, respond more flexibly, more rapidly, and more appropriately to shifting demands and needs. They also provide for location, style, and product variety (making more of the things people want and less that they don't). Such a system maintains flexibility by providing a rich variety of alternatives in economic life; alternatives, moreover, that are closely enough linked to their customers to enable rapid adjustment to environmental or international changes. A widely-ranging pluralist system of smaller firms would offer at least at the margin a means to modify other arrangements. Economists have pointed out--indeed, it is the central feature of mainstream theory--that competition need not be uniform; it need only exist to set boundaries (hence, at the margin) beyond which still less competitive behavior will result in replacement of that supplier by another. The conventional reason that this does not occur routinely is that larger (less ideal) firms are said to be needed for reasons of technical efficiency and to gain economies of scale. Yet as I have shown, this is simply not true. We can have the advantages of smaller firms, and we can have them without these assumed costs.

Distributional goals concern the ways that benefits and costs are spread across society. Smaller sized economic units, supported by institutional reform, would provide a more appropriate distribution of opportunities, rewards, and costs. Our present system tends to restrict many of the benefits to relatively few people, while spreading the costs among many. (See, for example, C. Jencks, Inequality, NY: Basic Books, 1972; and L. Thurow, Generating Inequality, NY: Basic Books, 1975). Since distributional issues concern not only direct economic rewards and costs but also opportunity to be influential, or to share power and control, these smaller and more decentralized alternatives result in broader distribution of these by definition.

Integration goals concern the relationship among different elements of society; no social order can function effectively unless its component parts are reasonably congruent and mutually supportive. In this sense, smaller firms and modified institutions would offer two important benefits that our present arrangement lacks. First, a smaller-sized enterprise offers employees a greater sense of the whole and provides for a more human scale of effort, in which people can take pride by seeing the value of their contribution. (See E. F. Schumacher, Small is Beautiful, NY: Harper and Row, 1972). Second, on a larger scale, such a system provides a more appropriate balance among economic, political and social institutions, and reduces the danger from the (virtually certain) misuse of power by large firms. This contributes to a healthier world order. (See H. Kohr, The Breakdown of Nations, NY: Reinhold, 1959.) Moreover, this would also go far towards eliminating the problem I mentioned earlier; the present overdependence of individuals, communities, and regions on one firm or organization.

These desirable changes can only be brought about by attending to the second basic principle. It is not enough merely to reduce the size of some large firms; they will simple become enlarged over time unless the legal and

institutional "rules of the game" are simultaneously changed. They must be made consistent with the revised, decentralist system instead of, as now, supporting and in fact generating a system of large firms. The present outcome is not an accident; it is the specific result of legal arrangements and governmental actions that have existed to this point. There are many appropriate modifications; let me suggest a few.

It is important to move towards mechanisms to provide much more open and public access to the internal operating data of firms in general, and especially those operating more than one unit or in more than one economic sector. The argument that this would destroy competition by giving away "industrial secrets" is nonsense. On the contrary, it would markedly enhance competition by showing precisely where effort could profitably be expended, by forcing firms to increase their effectiveness steadily, and by reducing their ability to hide ineffectiveness or unprofitability in one area in the profits of another.

At the same time, it is essential to modify present anti-trust legislation and its interpretation to permit (indeed to support) certain kinds of inter-firm efforts that are presently ruled out by the threat of government action. Most of the real benefits that do seem associated with size-access to capital, certain kinds of research and development, etc.--are perfectly accessible through limited collaboration of smaller units, such as are used in Switzerland (a country extremely strongly oriented towards decentralist principles) to provide credit for small firms by enabling each to draw on the potential value of all. Similarly, arrangements could be and should be devised that would provide community-based worker-controlled or cooperative enterprises with more access to support and capital, and with more flexible legal bases on which to operate. As it is, they tend to be seen as somehow anti-American, despite their deep roots in our early traditions, and it is much more difficult for them to gain access to resources or to use the same

mechanisms available for more conventional or entrepreneurial firms. For example, it has been virtually impossible for "collectives" to get loans or loan guarantees from the Small Business Administration.

I want to underline the most important point of all; that is, the notion of limited collaboration among independent firms. Virtually every advantage of scale beyond those associated with individual establishments can be gained by association for that specific purpose. It is not necessary that the separate units be under common ownership or control. Yet that is the conventional and in some ways the easiest means for such collaboration in the U.S. We desperately need new mechanisms and institutions to support limited association. The major oil companies have been vigorously arguing that they need to be big to explore new sources of oil; an offshore drill unit can easily cost $750. million. But several firms could form a limited association for this purpose, with the costs or benefits to be shared, and with the resulting petroleum (if any) to be refined and marketed separately. Indeed, such consortiums are perfectly common for larger ventures (eg, the Alaskan pipeline); they could readily be much more generally used.

Divestiture proceedings launched by the government under the provisions of anti-trust legislation should also specifically set out to make sure of two things; one, that the units divested are fully capable of independent operation (that is, that they are not stripped of key people, functions, and facilities) and two, that they in fact be operated independently and not merely purchased by some other multi-unit firm, as is often the case now. Large firms in general and multi-unit firms in particular should have to prove very specifically the advantages that would follow from their aquisition of another firm or establishment. Conversely, it would be particularly helpful to support aquisition of these divestitures by community groups, worker organizations, or consumer cooperatives, both legally and by providing access to credit and capital.

This would be helpful in another sense as well. One of the fundamental characteristics of the market is that production units are organized whereas consumption units are not (that is, the ultimate consumption units, household or individuals). And to that extent, the production side of the market inevitably has power not matched by the consumption side. Smaller firms reduce this disproportion, but in the local decision whether to buy or not, options are still restricted because, as economists well know, even very small firms gain monopoly power from their local and specialized character.. New sorts of firms whose control is shared by consumers in one form or another would offer a corrective alternative.

These are some of the steps that could lead to a much more decentralized economic system; one that, in my view, would be superior to our present one in terms of its efficiency, its equitable distribution of rewards and opportunities, its flexibility for the future, and its resistance to becoming a source of too great power for any one group. Perhaps most importantly, it would offer more people more alternatives--for work, for rewards, for goods and services, and most of all, for full participation in society. Surely lack of that is the most corrosive of all social ills.

What is proposed here is entirely consistent with American values, and all of it could be carried out by small steps. No sudden nor complete shift in public or legal attitudes is called for. And I believe that such a thrust would be supported very widely by the American people as it became obvious that it benefits the many, and costs only a few.

STATEMENT

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Before the Senate Select Committee on Small Business December 2, 1975

I am pleased to comment in connection with the Small Business Committee's hearings on "The Role of Small Business in Our Society." I am especially pleased by the Committee's express interest in the relationship of small business to American communities, American ideals and values, and the quality of American life. I say that because ordinarily, the phrase "small business" is taken to refer merely to a quantitatively distinct subcategory of business in general. On this assumption, considerable attention is paid to size and scale and their relationship to economic efficiency and market opportunity. Policies are devised in compensation for the presumed disadvantages of small size, and government agencies and offices arise to direct and monitor the resulting programs. Useful though this may all be, it has less than the desired impact because it ultimately rests on a misconception. Small business differs not quantitatively but qualitatively from business in general.

Small business in reality refers to a fundamentally different sort of economic system--one comprising economic entities and relationships with distinctive qualities lacking in the giant firms at the core of our present economy. Although size of firm is one dimension differentiating these two economic orders, it is far from the only one. Indeed, it is in some ways the least fundamental. What, after all, is a large firm?

In virtually every case, it consists of a whole cluster of separate facilities, whether plants, offices, laboratories, or distribution points, under unitary control. The classic firm of economic theory, a single plant or establishment owned and operated by some person or group, is in actuality the essence of what we now call "small business." The issues of size and control are therefore confounded, and it is essential to consider both in any discussion of either small or large business. The very same plant or retail store in a community, depending on whether it is owned by a local entrepreneur or an international conglomerate, shifts from classification as "small" business to "large". However, since that does not change the establishment, we may well ask what difference the distinction makes and to whom.

Grossly speaking, five categories of persons and groups are affected by every firm's activities: society at large, the local communities of operation, customers, employees, and controlling beneficiaries. Since each of these is in some way affected by changes in the size of the firm and its control structure, government must decide among the conflicting benefits and costs that alternative arrangements entail, and adjust the rules of the game to provide what is thought to be a fair and proper balance among them. I firmly believe that the present set of rules is seriously distorted by this standard on two accounts. First, there is a widespread (and incorrect) presumption that large size is necessary for productive efficiency, from which it follows that the special virtues of small business must be subsidized. Second, existing regulations essentially fail to give

adequate consideration to the costs and benefits of alternative means for distributing control over firms, even though these have a marked impact on both social and individual welfare.

Taking size first, some facts may put the matter in perspective. I restrict my remarks to manufacturing, both because that is the sector in which economies of scale are most important and because my own work has focused on it. American manufacturing units are surprisingly small; mean employment per establishment in 1972 was only 43.8 persons. To some extent, that is the result of a large number of tiny businesses still classified as manufacturers. However, even if these figures are disaggregated, most plants are of modest size. American multi-unit firms comprise only about 3 percent of the total number of American companies, although they own 16 percent of all plants and contain 73 percent of total manufacturing employment. These are the giants of American industry, and here, if anywhere, we can expect to find large plants. Yet the separate manufacturing establishments owned and operated by these firms employed only 203 people on the average, and that figure, by the nature of the data, is probably exaggerated. Moreover, if plants in a very few industries such as automobiles, defense systems, and large electrical machinery are excluded, the mean employment figure drops to about 100. I do not deny the existence of many very large plants. I do deny that they are typical; the size of <u>plants</u> is very different from the size of <u>firms</u>.

Of course, economies of scale do exist. However, my own extensive survey and the great majority of studies carried out by others, including

agents of the Congress, show clearly that these economies are generally achieved in individual plants of modest size. The exceptions are the large assembly-line operations to which I have already referred. The more critical issue, therefore, concerns possible economies to be gained by operating more than one efficient size plant; that is, in multi-plant or conglomerate firms. Here also most studies are in basic agreement. In most cases multi-unit firms are not more economical than single-unit firms operating an equivalent facility. Furthermore, economies from scale of such functions as development or finance, or in specialized skills, can be gained by other means as well. For example, separate firms can offer such services; this is now widely true for computer facilities. Cooperatives or other shared activities can provide more than adequate scale for other purposes; small Swiss firms pool credit and financial resources. Or again, industry and trade associations are common devices to gain economies of promotion, training, and standardization.

There are also diseconomies of scale. For example, both the generation of innovations and their application are more effective in small firms than in large. This effect is often particularly marked in concentrated industries, where major technical developments tend to come from smaller, peripheral firms. Similarly, small firms are more responsive to environmental, social, and economic changes, both in accuracy of perception and response to it. This capacity, which is important to national purpose, is related to the most fundamental source of diseconomies; larger firms acquire rapidly increasing costs of coordination. As information needs to flow further and across more junctions, it becomes both less accurate and less timely. There is also a substantial human cost. Available data indicate clearly

that as size increases, worker satisfaction and mental health decrease, and strikes, physical injury, and sabotage increase. Many large firms attempt to minimize these problems by decentralizing as much decision-making as possible. Although this is useful, it is not equivalent to fully independent units and in principle can only gain a fraction of the benefits.

In light of this it is natural to seek figures on the actual size of plant necessary to exhaust economies of scale in particular industries. Previous work in this direction has led to extremely inconsistent results. Recently a colleague (Mark Hodax) and I carried out a new series of calculations utilizing detailed comparisons of successive Censuses of Manufactures to determine the size of new plants entering particular markets characterized by four-digit Standard Industrial Classifications, which are moderately precise. Specifically, we determined the minimum size of plants entering 100 manufactured consumer goods markets between 1963 and 1967. In effect, our procedure estimates the smallest employment-size plants thought by business to be viable in the marketplace. Using other data, we have also estimated the capital asset requirements of such plants and the necessary consumer market or numbers of average consumers needed to justify them. The results are as follows.

1. Almost 70 percent of these industries involved entry plants with fewer than 250 employees; 44 percent required fewer than 100 employees.
2. If automobile-related products are excluded, about 71 percent of all consumer goods by value could be

produced for a market of 1 million persons. Twenty percent could be produced even for a population of 200,000.

3. Correspondingly, about 70 percent of the 100 industries require a capital investment in plant of less than $1 million.

These data suggest an important conclusion. A large fraction of existing manufacturing capacity operated under the control of multi-unit firms could be converted to independent operation in the market without loss of economic effectiveness, and with possible gain. Although this is an issue essentially of control rather than size, I certainly do not suggest it as a strategy. It is not feasible, and the short-term results would be disastrous. However, there is every reason to encourage individual actions of that sort, since an economy with a smaller proportion of multi-plant firms would be far less concentrated than our present one; business and individual opportunity would increase; wealth, power, and income would all be more equitably distributed; and government regulation of business could be greatly reduced. Policies for this purpose can be devised. I will offer some tentative suggestions later.

I wish also to call attention to the fact that the plant sizes resulting from these calculations are in general well within the category of small business as defined by the Small Business Administration. This applies not only to the minimum entry sizes computed for consumer goods but also to the mean size already existing in multi-plant firms. Although I have not carried out the detailed calculation, it is certain that a considerable share of present manufacturing already takes place in plants

more consistent with small business than large, a fact masked by confounding size of firm, size of plant, and issues of control. The very phrase, "small business", therefore, creates in the mind an exceptionally misleading image. Such units are substantial and complex, and contain adequate capacity to carry out most of the economic functions of American society.

So much for size and effectiveness. As to control, I have already noted that the data on multi-plant firms make it clear that in many or most cases, unitary control is not necessary to gain what small economies of multi-plant scale exist and that, indeed, it may generate diseconomies of its own. In short, efficiency is certainly not the main drive to growth, although American values and traditions make it mandatory that big business claim greater efficiency, because it has no other acceptable reason for existence. In consequence, large industry devotes much energy to rhetorical demonstrations of its economic effectiveness.

In reality, large firms exist for quite different but persuasive reasons that explain why their size tends to increase, and why so many persons, groups, and institutions prefer to associate with them. First, large firms have power and visibility, in which employees, suppliers, and customers all wish to share, since they are thought to confer status and other social benefits. For this reason, people will pay a premium, even explicitly, to gain them. Second, power provides security. Employees feel more secure than they would in smaller enterprises, whether efficient or not. Indeed, from an individual point of view, efficiency is irrevelant. What is relevant is income, position, and continued assurance of both. This both requires and helps firms to accumulate

power above that characteristic of a competitive market. This power in turn becomes the basis of large firms' impact both on the market and on society in general.

The tendency to grow also derives in part directly from a particular form of limited control. Incremental benefits from growth, particularly financial, can be captured in most firms by the few people (owners or managers) who exercise control over the distribution of those benefits. If those few people can gain a dollar of additional income or a step up the Fortune 500 ladder, on incremental sales of a million dollars, it is worth their while to do so, even though it represents an extremely inefficient use of resources. So long as the benefits need not be widely distributed, growth will still be sought.

These characteristics account for the fact that detailed studies of financial returns of corporations as a function of asset size show a steadily decreasing efficiency of asset use, as one would generally expect from the principle of diminishing returns. That is, the ratio of net benefits to assets employed falls as size increases. The critical issues once again are control and power, not efficiency.

The institution of small business, on the contrary, intrinsically distributes power and control more broadly; it helps increase distributional equity in the society. This applies both within firms and to firms as market units.

Internally, small firms offer individuals a sense of the whole and a chance to see the value of their own efforts. They enable personal relationships with executives, owners, and decision makers. In larger firms these things are generally not true--a situation which we know

leads to feelings of apathy, alienation, and lowered mental health. Smaller firms also provide both more visible and more genuinely accessible opportunities to individuals, and role models that are more realistic. For example, there is a greater proportion of women managers in small than large firms. Problems related to productivity and the quality of work life are increasingly apparent, particularly in large firms. These problems can be ameliorated by appropriately combining a broader distribution of influence within the firm, with direct rewards. However, these arrangements in principle are more consistent with smaller firms and easier to apply to them.

Externally, of course, a system of independent and modest-size firms regenerates a healthy market, consistent with American political ideals that depend critically on the absence of large centers of private power. There would also then exist a greater array of perceived opportunities for individuals or groups to launch a business of their own, an established American way of increasing one's status and mobility. A system composed of relatively small organizations is demonstrably more accessible and can readily be seen as within the grasp of any person or group with sufficient interest and capacity, unlike the very large entities which presently populate our industrial universe.

A system of manageable and independent firms also helps provide the needed integration between economy and society, enhancing people's sense of coherence in their personal lives. This is doubly true where businesses participate in communities as interdependent systems, each adding strength and stability to the other. Such businesses are also more likely to multiply economic resources within the community. The relationship between

firm and community becomes influential in decisions regarding environmental impact, hiring, purchases from local suppliers, and use of local labor. Similarly, the distribution of benefits and opportunities between the firm and the community is likely to be more balanced, and a greater sense of local pride is derived from the presence of truly local firms, as against branches of externally-controlled enterprises. In the former case the firm necessarily considers its community. In the latter, the community is held hostage, since its interests are peripheral to powerful and externally-controlled firms. There needs to be deliberate exploration of a variety of other control alternatives and support for those showing promise. For example, community development corporations, as I have argued elsewhere, combine better-than-typical performance with important community, social, and human resource benefits.

In light of these conclusions, I propose for the Committee's consideration some possible changes in both legal structures and administrative practice. The aim is not sudden change; that would be neither appropriate nor most effective. Rather, it is to shift the course of future developments to increase the proportion, over time, of more independent, community-sustaining, opportunity-enhancing, and effective smaller businesses.

1. Explicitly recognize size as a continuous variable; firms are not merely small or large. Tax abatements, preferential contracts, set-asides, and subsidies should be redesigned along graduated lines up to fitting levels.

2. Such benefits should also take into account issues of control and distribution of equity as, for instance, in Iran. Single-plant firms should have preferential access to certain favored treatments. Firms whose ownership is locally or community-based should receive similar preference.

3. Both these arrangements should be tailored to the specific industry, and perhaps location, involved. In principle, differentiate firms as much as is practical along these several dimensions to relate rewards closely to desired actions and outcomes.

4. All government support for multi-plant firms should require justification in each case; there should be no such general or categorical subsidy.

5. In antitrust proceedings resulting in divestiture orders, the units to be divested should be functionally complete, and able to operate as firms in the market. Preference for purchase should be given to independent groups; those proposing to distribute control broadly within communities, or among workers or relatively disfavored persons, should have access to financial assistance.

6. All forms of existing government aid to business, notably from the SBA, should be readily available to community development corporations, cooperatives, and the like. At present, this is not the case.

7. A detailed study should be made of the limits that existing laws set on the use of potentially valuable structural and work alternatives, especially in smaller businesses. The Fair Labor Standards Act of 1938,

for example, prevents full application of innovations involving more flexible use of time.

In conclusion, arrangements in which large firms control many small plants that could be effectively independent permits certain beneficiaries of the large firms to derive extra benefits at the expense of a much larger but less powerful fraction of the population. As I have shown elsewhere, facilities are routinely shut down, or moved from one community to another, not because they are ineffective but because different arrangements generate preferential benefits. In this regard, New York City and Cornell, Wisconsin have had similar problems. Our present economic structure does not achieve essential and widely sought social goals. We must provide other means. Support for independent, smaller-sized, single-plant, community-enhancing businesses is an important aspect of the necessary new policies.

Thank you.

the community context of economic conversion

BARRY STEIN

CENTER FOR COMMUNITY ECONOMIC DEVELOPMENT / NOVEMBER 1971
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INTRODUCTION

By the end of April 1971, at least 100,000 highly skilled professionals--engineers, scientists, and other specialists--were without work for the first time in most of their lives.[1/] Many had been engaged in key industries and laboratories producing steady advances in many areas of science and technology using skills said to be crucial to the nation. Almost without exception, their education and their experiences had led them to believe that these skills were, and would always be, needed; that their options and rewards would grow; and that the investment needed to achieve these skills would be repaid many times over. Now these skills appear to have become nearly worthless. Moreover, while public and government attention has focused on the plight of these professionals, many other workers, less visible, have been placed in the same position. Accordingly, the national unemployment rate went from 3.2 percent at the end of 1969 to 6.0 percent in April of 1971.[2/]

Since the bulk of the jobless professionals had been engaged in programs and services for the Department of Defense, either directly or through civilian contracts, most of the resulting outcry has been directed toward the need for economic conversion: the shift of that considerable fraction of American industrial effort involved in

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defense-related activities to the production of peacetime goods and services. This issue is not new; it grew steadily through the 1960's, its momentum fueled by a continuing flow of books and articles on conversion and such related issues as the military-industrial complex, the war economy, and the need for new priorities in national spending. As the National Journal commented, "Most of the conversion debate of the past 10 years centered on proposals to shift priorities and spending away from military programs to social programs."[3/]

The inevitable consequence has been a tendency to view the only possible solution, or ameliorating programs, as necessarily involving action at the national level. Some have asserted the need for a sort of civilian NASA--a large centralized agency--whose role it would be to channel federal funds into more appropriate (peaceful) channels.[4/] President Nixon, acting administratively, launched a pilot program to convert those professionals affected by layoffs into urban and social problem specialists, on the assumption that the professional skills lying fallow can be profitably redirected towards such areas as municipal services, transportation, and housing. In Congress, more than twenty major bills have been filed as a direct result of the conversion debate, in addition to much local and state government activity. These generally propose retraining, relocation, various forms of interim support, and establishment of new federal agencies to coordinate and plan.[5/]

It is most unlikely that any but a small fraction of these pilot programs or proposals will be generally implemented.[6/] Even if they were, however, their utility would be limited, since they place primary emphasis on the individuals affected. The individuals laid off, and the groups to which they are attached, however, are not distributed uniformly or randomly, in terms of either geographic or socioeconomic criteria. Even when the economy is relatively prosperous (e.g., unemployment less than 4 percent = ca. 3,000,000 people), some areas are much worse off than the average, with economically vulnerable communities and poorer citizens hardest hit. The situation is reminiscent of the story of the man who drowned crossing a stream that had, as he had been told, an average depth of three feet; that is, zero at the banks and six feet in the center.

In such communities, strategies of conversion aimed at relocating individuals are too narrowly conceived. The economic shock wave from, say, the closing of a local plant, spreads rapidly through the community and its surroundings. People not directly involved are enmeshed in the problem through a web of economic exchanges which spreads the initial impact like ripples in a pond. Even if new jobs can be found promptly for all those laid off, those less directly affected are not necessarily helped. Moreover, the longer the time lag, the more severe the total impact, because people and businesses alike become forced to make irrevocable decisions. The target group may regain its former income but the community economy will have been strained, sometimes terminally.

There are some who suggest that these local dislocations are the inevitable price of general prosperity. This paper proposes an alternative: an increase in community economic autonomy based on social processes different from those now deemed conventional and rooted in organizations whose prime focus is the community itself. Economic conversion, therefore, is regarded in this paper as a problem needing community-oriented action. How widespread is that problem in this country, what features identify such communities and what communities should aim to convert to are questions that need examining.

THE SCOPE OF THE PROBLEM

Although federal unemployment figures are useful for purposes of national planning, they mask the wide variations that exist among regions and, still more, in smaller areas. Of the 100,000 skilled professionals mentioned earlier in this paper, more than 10,000 were located in eastern Massachusetts, primarily in the northwest quadrant of Boston's suburbs, more than 20,000 around Los Angeles, and a further 14,000 in the Palo Alto/Stanford area.[7/] Conversely, some other parts of the country were essentially untouched.

As to general unemployment, similar concentrations existed. Thus, the April 1971 national figure was 6.0 percent, but for Massachusetts it was 7.0 percent. California unemployment reached 7.1 percent, Maine 8.4 percent, and the state of Washington 11.0 percent.[8/] In

addition, unemployment in some smaller areas within these states was greater yet. For example, unemployment in the Lowell, Mass. SMSA (Standard Metropolitan Statistical Area) stood at 11.6 percent and in the employment area of Newburyport at 15.3 percent.[9/] Such concentration is not, however, necessarily limited to small towns; Seattle, Washington (the home of Boeing) has 13.1 percent of its work force unemployed.[10/] In general, however, metropolitan areas show rather less variation than smaller ones, and their absolute level of unemployment is lower although wide variations may exist within any given SMSA.

Given these figures, it is clear that thousands of communities are (1) dependent for their economic health on too narrow an economic base, (2) that this narrow base is subject to loss suddenly by virtue of decisions made outside the boundaries of the community, and with only secondary concern for its health, and (3) that these situations arise in the main first from federal (especially DOD) contracting practice, secondly from absentee ownership of local facilities, and third from economic trends that change the competitive relationship among different areas, regions, and countries. Moreover, John E. Lynch has written in a study of military base closures that what characterizes the local communities "is the small number which have actually recognized their overdependence on nearby military facilities."[11/] The same point can be made more generally: communities are slow to note their often precarious economic condition. It is useful at this point to look at

some detailed illustrations of these problems.

Defense Contracts

Seattle, Washington stands as the most extreme example (because of its size) of how devastating such dependence can be when fortune changes.

> Within Seattle's city limits alone live some 600,000 people; the SMSA of Seattle-Everett included a population, at last count, of 1,340,000. It is a port of trade with the Orient, a link with Canada and Alaska, and a center for the lumber and fishery industries.
>
> It is also home for the Boeing Company, which employed, at its peak in 1968, 106,000. In May 1971 Boeing's work force had dropped to 40,000; by the end of 1971, it may drop to 29,000. More than 100,000 people are without work; the unemployment rate officially stands at 13.1 percent; and welfare workers estimate the true rate at twice that level (i.e., taking account of unreported unemployment). According to one survey of the city's central slums, the unemployment rate is 48 percent. As A.E. Fitzgerald aptly noted, Seattle is the world's largest mill town.
>
> Boeing is, nevertheless, regarded as one of the most efficient aerospace firms in the country. 707's, 727's, and now 747's dominate the commercial market. The demise of the SST and the shift in DOD requirements, compounded by a "softening" of the commercial aircraft market, are responsible for Boeing's problem. To quote The Economist, "The root of [Seattle's] problem lies in the economic dominance of the area by one giant corporation, the Boeing Co." and "As jobs at Boeing declined, a domino effect throughout the economy pared away service and trade jobs." 12/

Even though the top 100 or so contractors account for about two-thirds of all procurement dollars, there are all told 22,000 prime

contractors serving the defense industry and another 100,000 subcontractors operating plants in 5,200 communities in every state, or, said another way, in 363 out of the 435 congressional districts.[13] Because of local concentration, even the smaller facilities in this network can represent, to a small community, a dangerous dependence on the defense industry.

Defense-related (including AEC and NASA) contracts reached their peak of $63.3 billion in the second quarter of fiscal year 1968. By the third quarter of fiscal year 1970, it had dropped by 18 percent ($11.4 billion). In the process, some 1,300,000 people lost jobs with defense contractors.[14] In addition, many more who were suppliers of general (i.e., not specifically associated with a defense program) goods and services to the contractors and their employees, and therefore also largely dependent on such production, lost incomes. Estimates of the fraction of all U.S. employment more or less closely related to the defense industry go as high as 20 percent.[15]

One might assume that the current situation is temporary, and to some extent it is, but it is also unrealistic to assume the defense industry will recover to its high 1968 level. For while the federal budget in fiscal year 1972 includes $77.1 billion for defense-related expenditures--which is an increase of $1.5 billion over fiscal year 1971--inflation, salary increases, incentive pay to volunteers in the armed services (an added $9.5 billion between 1968 and 1972), and

changes in procurement priorities, will prevent most affected individuals or firms from regaining their lost position.[16/]

Compounding this problem for communities is the fact that the government owns a large amount of equipment, land, facilities--some in the form of government (primarily military) installations, and some used and/or operated by private contractors--and it would rather maintain control of these facilities than make them available for productive use by the local community.[17/] The director of the DOD's Office of Economic Adjustment recently explained that it would be "unfair" to let others use facilities that the government might be forced to recapture on short notice. This is no small affair: the DOD owns 29,000,000 acres of land and the aggregate value of its total real property holdings in the U.S. (including facilities and equipment) was $202 billion as of June 1969.[18/]

Even assuming real interest on the part of a community, recovery of surplus land from the government is no easy matter. The town of Maynard, some 25 miles from Boston, sold 890 acres to the DOD in 1941 for $501. When the land was declared surplus in 1970, the town expressed strong

interest in re-obtaining the use of it for conservation, recreation, water resources, and industrial expansion. No matter; it was put up for auction, and a significant part was acquired by the Massachusetts National Guard for training purposes. Negotiations are continuing, but even if the National Guard relinquishes its interest, it reverts to DOD, thence to the Central Services Administration (for any other federal agency) and then to the state.[19/] Frequently, therefore, facilities and properties either lie unused and unavailable for productive employment, or alternatively, they remain used in defense production if only to keep the jobs in the community!

Absentee Ownership

A second situation that has increasingly been responsible for the economic problems of communities is absentee ownership, as manifested by the recent turn of events in Mechanicville, New York.

> Mechanicville, New York, 21 miles north of Albany on the Hudson River, is a small (population about 7,500) industrial city of modest, somewhat run-down homes scattered along the river bank, and centered around a cluster of low red-brick stores and small office buildings. But for the modern cars, the seven mile drive from Interstate Highway 87 into Mechanicville is a 50 year drop in time.
>
> The largest employers in town are, and for many years have been, manufacturers of pulp and paper. Skilled paperworkers have passed their trade on to sons, again and again, for several generations. One plant has been in nearly continuous operation since 1876. Since 1904, this plant has operated

as a wholly-owned subsidiary of Westvaco Corporation (formerly West Virginia Pulp and Paper Company). In the production of pulp and specialty papers, it employed some 750 people--about one-third of the town's labor force.

Early in 1969, Westvaco shut down the pulp mill and severed 400 employees, most of whom, but not all, have found other work. Toward the end of 1970, Westvaco announced it was closing the remainder of the plant, transferring production to facilities elsewhere, and terminating most of the remaining 350 employees. In 1970, Westvaco (#255 in the Fortune 500) had total sales of $420,344,000 and 15,660 employees. 20/

Westvaco's pattern of operation is not an isolated case. In fact, most large corporations in the U.S. have widely spread facilities both at home and abroad. General Motors operates 118 plants in 68 cities/towns in the U.S. The conglomerates which, until recently, were far and away the most glamorous companies on the stock exchange, are especially prone to this tendency because of their pattern of growth by acquisition into highly diversified industries. IT&T, for one, has 96 plants in the U.S., many of modest size. Even #500 on the Fortune list of the 500 largest American industrial companies (Arvin Industries) employs 7,850 in 20 plants, and owns $109,000,000 of assets. 21/ The overall importance of these examples lies in the fact that the Fortune 500 produce, in the aggregate, 65 percent ($463.9 billion) of all American manufactured goods. 22/

Thus, to a great and increasing extent, U.S. manufacturing plants are owned or controlled by multi-facilitied corporations absent from

the communities in which they operate. In 1963, the last year for which comprehensive figures are available, 18,600,000 people were employed in 402,000 separate units. However, multi-facilitied corporations, although constituting only 4 percent of the number of firms, accounted for about 35 percent of the units and 70 percent of the employees. The trend over time is also clear. Between 1954 and 1967, multi-facilitied firms increased their share both of the number of separate manufacturing establishments controlled, and total employment. In the former case, the percentage increased from 11.1 percent to 16.9 percent. As for the latter, whereas only 61.0 percent of all manufacturing employment was in units of multi-facilitied corporations in 1954, it had reached 71.9 percent by 1967.[23/] Moreover, specific data in support of this proposition can be found in a recent study of the State of Vermont.

> "In a study of the ownership of the 31 largest manufacturing plants in Vermont, it was found that 2 of the 2 plants employing more than 2000..., 4 of the 5 plants employing more than 1000, 13 of the 15 plants employing more than 500 and 23 of the 31 plants employing more than 250... are owned by out-of-state corporations. [24/]

The test being applied in that study is stringent indeed, since it involves ownership outside the state, not merely the community.

That this pattern of external ownership is widespread is attested to by the fact that as of 1968, the fraction of statewide manufacturing employment in units employing over 250 persons (which tend to be

multi-facilitied firms) was over 40 percent for all except the eight least industrialized states: Alaska, Montana, Nevada, New Mexico, North Dakota, South Dakota, Wyoming, and Hawaii.[25/] In other words, the trend in the process of industrialization has traditionally involved a shift to larger manufacturing units (to meet the imperatives of mass production) which, as has been noted, are more likely to be owned outside the community in which they reside. Governor Milton Shapp of Pennsylvania commented recently that while there were some 60 independent firms of reasonable size in the eastern part of the state a few years ago, there were now only four or five, the rest having either been acquired by outside interests or closed.[26/]

Industrial Trends

The problem of absentee ownership is in many ways simply a reflection of another problem--that of changing industrial trends to which companies respond with deadly certainty; profits first, community second. The case illustrated here is a poignant, but not untypical, example.

> Roanoke is a small city of 5,000 located in the central part of Alabama, near the Georgia border. The town has been dependent, for more than 50 years, on two textile mills which, until recently, employed some 62 percent of Roanoke's labor force.

> Last November (1970), Handley Mills, the larger of the two, closed its doors; 844 workers were idled. The other factory, the Rolare Manufacturing Company, filed for bankruptcy at the end of March. A further 440 workers lost their jobs. An executive of Handley Mills predicted at the time: "And a hundred more plants will close next year if something isn't done." Since then, the economic shock wave has hit nearly every local institution and other businesses have closed.
>
> Handley's general manager, according to the N.Y. Times, "said he felt Handley had 'turned the corner' and was on its way back to prosperity when the closing came. 'But I guess everybody just sort of lost faith.' In a footnote, he added: 'We were just getting ready to move the corporate headquarters down from New York. It would have been the first time in 50 years that control of the mill would have been in the hands of the people living in Roanoke.'" 27/

The Roanoke example is typical of the continuing series of economic crises that afflict small communities as whole industries shift their focus. The textile industry, for example, concentrated itself in New England for 100 years before World War II. Literally hundreds of towns were built, or grew, around the mill, which often constituted the basis of such communities' economic health. 28/ By the onset of the war, however, the cheaper labor in the rural South encouraged firms to move.

The war itself and the widespread affluence following it deferred the inevitable, but one by one, firms went out of business or moved their plants into more modern and/or less expensive southern facilities. Moreover, important supporting industry--textile machinery, for example--

either moved or was itself superseded by new technology, in this case, synthetic fabrics and new production processes.

Some local enclaves maintained their vitality--a few still do--but competitive pressures, obsolete equipment, decaying facilities, and little or no sophisticated personnel have taken an inevitable toll. A casual tour of northern New England, in particular, makes obvious the extent of local dependence on those enterprises. They now stand as picturesque ivy-covered ruins, empty shells, or at best, home for one or more much smaller enterprises. Most of these towns have never regained their former vigor; some are virtual ghost towns. Harrisville, New Hampshire, for example, the home of Cheshire Mills, is for sale--nearly lock, stock and barrel.[29/]

But, as the earlier vignette suggests, there is no permanent solace even in the South. Some 27,000 textile workers in that area lost their jobs in 1970 alone. It took more than a century for New England to lose its mills; the process is being repeated in parts of the South within a couple of decades. And the textile industry is but one example among many. The rate of change is increasing, and whole areas--particularly economically dependent communities--must consider new alternatives to assure their continued health, and perhaps survival, in light of these effects.[30/]

Examples of communities disrupted are not scarce; one can hardly look at the newspapers without being assaulted by others. Consider:

- Unemployment in Bristol, Connecticut, stands at 21 percent (5,200 workers), largely due to layoffs in heavy manufacturing industries.[31/]
- Tyrone, Pennsylvania is "for hire" according to a full page ad placed in the Wall Street Journal. The town has 7,500 people, of whom 550 lost their jobs when Westvaco Corporation moved its pulp operations to Kentucky.[32/]
- Lackawanna, New York, dominated by the Bethlehem Steel Company, has seen over 4,000 workers laid off within the last year. Exact figures are hard to get; the company evades the question.[33/]
- In Cornell, Wisconsin (population 1,590), St. Regis Paper Company is planning to close its paperboard mill early in 1972, thus putting some 300 people out of work. The mill has been operating for over 50 years.[34/]
- The central Maine region of Oxford, South Paris, and Norway has seen its last two remaining shoe manufacturing companies shut down. Nearly 700 shoe workers in the area are without work; unemployment stands near 20 percent.[35/]

It is possible, of course, that there is no meaningful solution short of massive programs such as relocation. Certainly, some communities and some areas will suffer no matter what new politics and programs develop. But the visible part of the problem is only the tip of the iceberg: we confront a crisis in community economic health. If, as has been said, a healthy nation is composed of healthy communities, then unlikely or difficult strategies that are potentially helpful deserve consideration. In particular, reducing the vulnerability of communities to economic disaster would be highly beneficial.

JOBS AND THE COMMUNITY

When individuals lose their jobs, they can be found others in all good conscience. When communities lose their economic base, however, finding jobs for the individuals most directly and immediately affected is not adequate. To understand the reason for this distinction requires examining what might be called the quantization of production, and the chain of events that follows when production in a plant on which a community is dependent grinds to a halt.

The Economic Elements of Production Decisions

In looking at the factors needed for production (labor, capital, materials, facilities), it is evident that some can be subdivided more finely than others. Capital is obviously such

a factor in principle. An expensive machine is not; half of a lathe is not much use. Moreover, even for those factors which are completely or even relatively divisible (e.g., steel ingots), the unit cost increases as the quantity required decreases. That is, the ingots that can be purchased for say, $100/ton in quantities over 10 tons may cost $200/ton if only 1/2 ton is needed. The same is true of labor, particularly specialized. Economies of scale in production arise largely from this source. Facilities designed to operate at a certain level of output accordingly find their unit production costs rising as output is reduced beyond some point.

Now, if that were the only issue at hand--the increased unit cost at lower production--some tradeoffs might be possible; less profit or margin in exchange for continued operation of the unit. At a certain point, however, a quite different element enters the calculation. Usually alternative methods of production, or sources of supply, or means to the ultimate end, are available in any given situation. Since the present situation of interest involves industries and firms that are either explicitly operated as part of a larger economic organization (e.g., branch plants, or independent plants producing intermediate goods) or are compelled, willy-nilly, to compete very broadly with others (e.g., local textile or shoe firms in New England), other alternatives are indeed available.

If then, the government decides to reduce its investment, in, say, certain defense systems, or if a large company shifts its product line, the chain of events that follows involves a re-evaluation of the entire process by which the end targets are to be met. As a consequence, frequently a local plant producing a specific subcomponent may lose a (perhaps critical) market, the decision having been made to use a different method of construction, not requiring that item. Or the item may now be purchased from a different source that was previously unable to meet the order. The net result: a plant is forced to close, or one of its product lines is dropped, along with the employees involved in its production. In other words, relatively small changes in final demand may cause a larger change--a quantum of change--elsewhere. The same holds true for decisions made by corporations operating branch facilities elsewhere. Their interests may be better served by similar quantum changes.

But this is not the end of the chain of events. It is not merely that a plant closes, or that production of a piece of defense hardware is shifted elsewhere. That by itself is bad enough. The crisis and its more complex problems arise because modern industrial economies are built like an upside-down pyramid. At the base, typically, rests productive manufacturing, converting raw or semi-finished materials to more valuable products. In support of such efforts, other firms spring up to take advantage, on the one hand,

of the supplies and services required by the plant, and on the other hand, to retail goods and services to those employed. In this way, more of a community's economy is related to the obvious direct benefits conferred by an enterprise than is apparent at first glance (referred to as a "multiplier" effect).[36/]

Some part of this multiplier is due to a generally applicable effect: employees earn money which they spend on consumer items and help support, in the process, retail stores and some producers of goods and services. However, a portion of these ancillary activities are specific to the firm. Some of its needs are particular and directly related to the goods it produces. If it is a manufacturer of electronic subassemblies, it will very likely buy components, instruments, and hardware from other local firms that depend on that business. Under the circumstances, if that manufacturer either goes out of business or goes into a different business, these secondary firms will suffer, and possibly fail. And of course, even the general multiplier effect can be the source of further problems, as local businesses leave, change, or collapse.

As the aggregate income of community citizens drops, due to layoffs, cut-backs, or reduction in pay, the local economy decays faster than would be suggested by only the immediate or pivotal event. Moreover, additional factors exacerbate even this effect. When fewer people are employed in the community, local resources are drained--

savings accounts leave local banks, which are thus less available for local loans; municipal funds must be expended in welfare and relief measures, and cannot be invested in the community; sm merchants, businessmen, and professionals lose income and are deferred payment on debts owed them, which reduces their ability to purchase goods and services from others--and so it goes.

The Impact on Communities of a Plant Closing

This process of economic decline has been observed in detail in smaller communities. Herman R. Lantz, in his study of Coal Town, commented as follows on the events succeeding the slow decay of the town's major industry, the coal mines.

> "With time the signs of economic decline became more pronounced and patterned. Out of this appeared a kind of 'natural history of community decline' which possesses some predictability and regularity."

He further identified the pattern as consisting of: initial rumor (expressing fear of trouble), changes in working patterns, (general) business decline, mobility (people who can leave tend to do so), changes in consumer habits (careful budget planning, fewer luxury items sold), homes deteriorate and property values fall, gossip (about misfortune), and finally a variety of psychological effects (pessimism, cynicism, and hopelessness). Although Lantz is speaking explicitly of a "one-company" town, the same effects show up, if in somewhat modified form, whenever a significant loss occurs in a community's economic base. 37/

Any such firm is, in short, more than a place where certain individuals work, or where exists a set of specific jobs. It is an institution that transforms energy, labor, and materials in ways unique to that unit and that community. To quote William F. Whyte:

> "The factory is, in one respect, a status system, and this system is closely related to the status system of the community. The two systems are mutually interdependent so that changes in one inevitably have an impact upon the other." 38/

Such an organization plays an extremely complex role in its community. Individuals tend to derive specific roles, and to shape their self-image, in ways which are conditioned by their position in the enterprise. Firms also exert a strong influence on interpersonal relationships to the extent that people are already related in some fashion through their independent relations to the firm. Let the firm disappear, or even change its productive focus (and therefore, the roles played by its employees), and the social structure of the community changes accordingly.

For both economic and social reasons, therefore, a major change in the organization's tasks and purposes, or in its internal processes (as, for example, when the local mill is bought by outside interests), is traumatic to the community. Some suppliers of goods and services will simply disappear, their previous functions no longer useful. Others will be able to readjust, but only in time and at a cost.

At the same time, the processes by which the community operates will themselves change to accommodate the new circumstances; venerable traditions will suddenly appear inappropriate or meaningless. Under these conditions, even the immediate replacement of individual jobs by other individual jobs does not prevent serious strain within the community.[39/]

In actuality, the community's problem will be worse for several reasons. First, many people only secondarily involved will lose their jobs (with no prospect of immediate replacement), second, supplier firms or those using the plant output as a material to be processed further will necessarily cut back or go out of business, and third, even those directly involved will require time to regain their former income. Some never will, though all will have to expend considerable energy in redefining their identity and their role within the community.

It should also be noted that certain elements of the population suffer more than others, and are, in consequence, more susceptible to personal problems. The chain of events described above, which distribute the results of a discrete act (e.g., a local plant closing), comes to an end when the individuals and organizations involved cannot redistribute their difficulties, or further share them. That is, anyone whose income is suddenly reduced will limit his spending, reduce his expenses, and defer payments due as much as the situation permits. He

will, in short, try to conserve his resources and stretch them as far as possible. So also with businesses.[40/]

Those people and firms reasonably well embedded in the economic structure--those who have some resources, who have a degree of credit and standing in the community, who experience a dependable and regular flow of income--have some useful flexibility in time of crisis. The poorer members of the community are in no such position. Since they tend to occupy the most marginal jobs--if any--they can most easily be let go or their services not used. Moreover, since their general level of income is, by definition, either at or below the lowest requirement for tolerable living, they have little or no opportunity to save or accumulate resources.

Of necessity, they immediately require greater support and relief, both in the form of direct payments and indirect subsidies. This calls for increased community spending at the very moment when community income is reduced. Whenever the community experiences an economic crisis, the poor, in particular, are forced to suffer most immediately and totally. Even if, during relatively good times, they are attempting to improve their skills, or otherwise accumulate for the future, these "routine" economic changes tend to wipe out such investments.

Finally, let no one suppose that such events occur only once in a great while in a given community. The economic system exists routinely in a state of flux, with general conditions now better, now

worse. 41/ Roland Warren has written of

> "the broad sweeps of economic activity which bear communities--differentially but inexorably--now up on one wave of high economic activity, now down into the generally shared trough of recession."

Moreover,

> "...specific events or decisions...,though minimal in the total economic picture, may be crucial on the local scene. [They]...all have a local community impact which may cause the level of economic activity in the community to depart drastically from the national trend." 42/

If communities are going to insulate themselves in whatever modest measure against these forces, what they need is an opportunity to exercise a degree of control and to increase their economic autonomy. Further, it is crucial that any new instruments and devices conceive of the problem in terms of the community at large and not in terms of individuals and individual jobs.