



Program Summary

THE GREAT GAME OF BUSINESS: UNLOCKING THE POWER AND PROFITABILITY OF OPEN-BOOK MANAGEMENT

Based on a Presentation by Management Forum Series Speaker

Jack Stack

November 10-11, 1998

Background of workplace culture

Jack Stack's presentation told the story of how he came to be plant manager of the Springfield, Mo., plant owned by International Harvester (IH). IH as a corporation was first created in 1870, and during the Industrial Revolution grew to become a major manufacturer of farm implements and heavy construction equipment, as well as a major producer of truck utility vehicles. By 1979, when Stack was designated plant manager of the Springfield plant, IH was a highly industrialized, highly bureaucratic company listed by *Fortune* magazine as one of the 500 largest companies in America.

He offered a sketch of how workplace policies and rules came to be so pervasive throughout organizations in America, whether in business, education or government. He asserted that during the early years of the Industrial Revolution businesses (primarily the East Coast mills) led the movement to lay down rules of conduct in the workplace. Educational systems were begun in order to prepare a labor force for the mills. Of course, the educational systems followed closely behind business in the movement to erect rules and policies systems that governed work behaviors.

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Jack Stack is president and C.E.O. of the Springfield Remanufacturing Corp. (SRC), a remanufacturer of engines and their components. Stack's tenure at SRC began in 1979, when International Harvester owned the Springfield, Mo., plant and he was appointed plant manager by IH. In 1983, Stack led the plant employees in a buy-out of the facility from IH, and turned it into what *INC.* magazine called "one of America's most competitive small companies." He is the author of the book, *The Great Game of Business*. It related the Open-Book Management style that involved all levels of the SRC organization, and is credited by Stack as the secret of success for SRC. Stack's style and SRC's extensive educational and participation programs have attracted people from all over the world to study this way of operating. Employees of SRC have been recognized by network television news programs, and won the National Business Ethics Award and the Business Enterprise Trust Award. SRC was selected as one of the Top 100 Companies to work for in America.

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Background of workplace culture

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The biggest problem businesses faced at the height of the Industrial Revolution was labor turnover. Labor turnover problems companies are experiencing today pale in comparison to those during the Industrial Revolution; then labor turnover for manufacturing companies was 10% a day. That was at a time with no rules, no regulations, and no 650-page labor union contracts. Workers left companies in droves for a nickel-per-day raise.

A Ford factory in the early 1900s hired 30,000 people to fill 10,000 jobs in one year. The solution to the problem of turnover was to make jobs simple, by figuring out how to break down each job function in such a way that workers could be brought up to speed as quickly as possible. That way, in the event workers left, new workers could perform the necessary tasks within a day.

During the Industrial Revolution, the intent of implementing the rules was to take thinking out of the workplace, to transfer the ideas of management to hands of employees to do their jobs – nothing more, nothing less. Such rulemaking allowed for mass production of automobiles, tractors, and all sorts of other products utilizing interchangeable workers who unsurprisingly lost all motivation to produce.

That’s how the first rules of business were set up. Everybody hated it – the employees hated it, the supervisors hated it, the managers hated it. America worked for 100 years with this model, and no one ever questioned it. Countless studies were conducted to try to figure out how to motivate people, and through it all no one ever questioned the underlying system.

Through all the years, rules were piled upon rules. During wartime, security regulations were added. No rules were ever rescinded and, when the wars were over,

the security regulations remained in effect. By 1968 only two people had access to the entire IH plant – the plant manager and the mail person.

Stack’s management background was forged in such an atmosphere, where people spent their entire lives, 25 or 30 years, never seeing that they were doing anything of significance, never feeling that they were part of an organization, and never understanding how their jobs made a difference to the company’s success one way or the other.

American business had designed a system that took the intellectual capacity outside of the business, with no way for employees or managers to be able to change the way things were done. By the late 1970s, every single industry in America had to have three support people for every one person who was actually doing the job.

The industrial society lasted so long, in spite of shoddy products, because the competition’s products came out the same way. “In fact, by the late 1970s, almost every single product that came out of our businesses were duplications of other American businesses’ products. For example, construction equipment produced by IH, Caterpillar, John Deere, and J. L. Case all was painted yellow. Nothing differentiated one product for another. In fact, many of the parts from the various manufacturers were interchangeable. We were sitting ducks for global competition.”

The single most important flaw in this system, the one thing we could not do was ask the people in the work force one simple question: “Who knows how to do the job better than the person now doing the job?” That was profound. Competitive companies in Asia were actually going out on the shop floor and asking the workers how to build a better product.

SRC emerges from Harvester collapse

IH as a company was collapsing in the early 1980s. Across the country factories were closing. Employees at the Springfield plant were asking Stack about their futures, and he had no answers. One of three possibilities could happen, he told them in at a plant meeting: 1) they could close the Springfield plant because it was a non-core business, 2) that because IH owed \$6 billion as a company, by the time any capital improvements would be made to the Springfield plant, no one presently employed would ever see it, or 3) IH would sell the plant. Stack suggested to the employees that if IH were to sell the Springfield plant, why shouldn't the employees themselves buy it.

Through the years, companies had taken words like "cash" and "profit" out of the vocabulary, and replaced them with insidious words like "prime for piece worker," "days of supply," "process time," and "lead time." The language of business had nothing to do with the economics of the business. No one, including Stack himself really knew the nuts and bolts of business economics. In the ensuing months, he learned and eventually taught the employees.

For 14 months Stack searched for financing, visiting 54 lending institutions to save the jobs of the people at the Springfield factory. Finally, he located an institution known for making risky loans – Bank of America. On February 1, 1983, the Bank of America loaned SRC \$9 million with only \$100,000 of employee equity. The company had an 89 to 1 debt to equity ratio, at an interest of 18%. Within 17 days, the company owed \$96,000 in interest on the loan with a \$3 million payroll.

"Our Human Relations manager brought everyone in the company together, opened up the balance sheet and

said, 'If you can get a job somewhere else, we would highly recommend it, because our chances of survival are nil.'"

Stack told the group that if the owner-employees of the factory (now called Springfield Remanufacturing Corp.) could go from \$89 worth of debt to \$89 worth of equity, they would succeed. Business should be all about building values; it should be all about building the economics inside the company. At that moment, Stack promised the workers that "we will open up everything, and we will share everything, and we will work through everything."

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What Stack hoped to do was establish a new methodology a new mechanism that will run companies in ways that employees will see the difference their work makes to the company and to each other's lives. He called his system Open-Book Management.

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Elements of the Great Game of Business

The three key elements of the Great Game of Business are: 1) Know and Teach the Rules, 2) Follow the Actions and Keep Score, and 3) Provide a Stake in the Outcome. Where these three elements overlap emerge the values of the organization.

To begin understanding the tools of the Great Game of Business, one should look at the origin of those tools. Basic book-keeping and accounting in the forms of income statements, balance sheets and cash-flow statements are those tools, and were invented by two Venetian monks in 1454. These tools have not changed in more than 500 years, and it is extraordinary how few people really understand them.

While Stack wanted the employees at SRC to quickly understand the value of those instruments to the individual workers, he found enormous resistance to learning about them. The workers had difficulty even understanding the role personal and corporate taxes played in the infrastructure of society, let alone grasping the fundamentals of corporate accounting.

Stack had to “demonstrate that the accounting numbers were really stories about people.” He made very little headway getting the workers to understand the specific numbers about building engines, until one day Candy, a woman in the work force, approached him and said, “I don’t like engines. I make nozzles. I make 6,000 nozzles a month, and I want to know about the nozzles.”

So Stack supplied Candy with the specifics about nozzles: cost of labor, overhead, materials, competitive

data – information about every single dollar associated with the production of nozzles. Within two weeks he found an amazing cultural and behavioral change. The

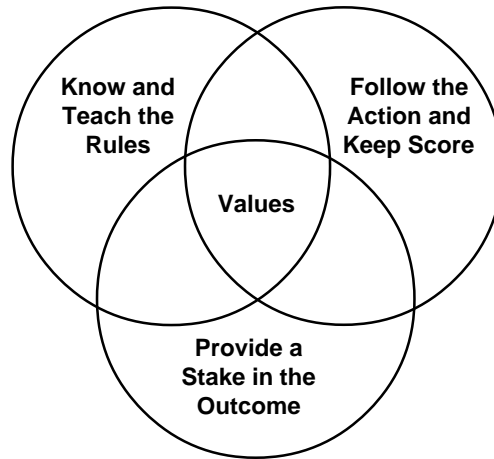
work area was immaculately clean – no six-cent washers strewn about, no \$17.20 nozzle tips haphazardly tossed in bins, no spacers scattered. Everything was in order and there was no loose inventory. Candy realized that she was using 10,000 washers a month. Productivity was up an incredible amount. A sign was posted above the area that read: “When in fear/ Do not shutter/ For we are/ Your bread and butter.” She also had posted graphs that displayed the group’s financial figures to six decimal points.

Candy told Stack, “We happen to have the highest gross margin of anyone in the company.” It didn’t matter that she was the only person who knew that. She had supplied her workers with T-shirts inscribed with “Nozzlettes.”

In that encounter, Stack realized his open-book management experiment would work. He saw pride, self-esteem, winning – everything he wanted changed in the work culture.

Candy previously had been a person who thought washers cost two cents a box (not six cents apiece). She began to see that as she picked up each little part she no longer scrapped it out. Her material utilization went down, and when that happened, her profits went up. Candy realized that the value of the Great Game of Business.

The one common denominator for all the workers that transcended religion, race or any other factor was the answer to one question: “Do you like to lose?” The unanimous answer was, “No.” No one likes to lose, and he used that common denominator to “trick” his employees into learning the measurement tools of business – income statements, balance sheets, and cash-flow statements, and a few others.



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Know and teach the rules

The secret to Open-Book Management is for the employees to learn to read and understand the company's financial reports, and having those employees understand how those reports affect each person's job and long-range future. Those reports are, in fact, the real rules of the workplace.

The eight tools that make up the real rules of business are:

- income statement
- balance sheet
- cash-flow analysis
- sales and marketing plan
- capital plan
- inventory plan
- organization charts
- compensation plan

To achieve such understanding, management itself must know the rules and be aggressive in teaching those rules to the employees.

The biggest barrier to success is ignorance. Ignorance takes three forms

- The ignorance of top management in assuming that people down the ladder are incapable of its problems and responsibilities.
- The ignorance of the people on the shop floor about why managers do what they do and thereby attribute every mistake in the company to a combination of greed and stupidity.
- The ignorance of middle managers about the goals of top management being different from the workers – there should not be a difference.

High Involvement Planning

Employees have to be involved in the planning at all stages. "If we have done our job in terms of giving everyone the information to create the entity (or department), then it is also our job to step back and give them the opportunity to set the standards."

Once the employees have done that, management must accept the standards set by the employees.

The four aspects of high involvement planning are: 1) Develop a sales and marketing plan, 2) Establish a financial game plan, 3) Identify the critical number, and 4) Approve and implement a bonus plan.

Sales and Marketing Plan – The sales and marketing plan needs to analyze the market, show competitive data and industry comparisons, establish realistic growth goals (i.e., sales by dollars, sales by units, etc.), and present contingency options (i.e., What-if scenarios).

Financial Game Plan – In establishing a financial game plan, all associates are given the sales plan, and all are asked their input on the costs and expenses necessary to support that sales plan.

If there is one thing that needs to be realized it is that there is a person responsible for every single line in the general ledger, for every single line in the income statement and balance sheet.

It is absolutely necessary to assign line-item accountability to individuals. Such a move will give those individuals ownership and eliminate the attitude of entitlement. It will also show people where they can make a difference and foster teamwork.

Comparing industry standards lets people know where their company stands in the marketplace.

The financial game plan gives everyone the same vision of the future.

Identify the Critical Number – This aspect of the high involvement planning allows the people to compare their company's ratios to the industry averages, or isolate one ratio that has the biggest impact on their company's long-term success. It can also foster consensus building throughout the organization, and develop a reward system for improvement.

Approve and Implement a Bonus Plan – This is an absolute must. A bonus plan is your insurance policy. It can provide instant gratification. It will be its own educa-

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Business Training

Business training involves employee orientation, formal classroom training, tuition refund, and interactive/informal training.

Employee orientation teaches business and financial literacy. It emphasizes how business works by using financial decision games.

Formal classroom training is comprised of several aspects. Each employee is required to attend a minimum of 20 hours of classroom training each year. Internal coaches conduct most of those classes. Appropriate outside speakers are engaged. In addition to bringing in outside training companies, the company ought to develop its own two-day seminars.

Tuition refunds (reimbursement) should pay 100% of tuition costs for passing grades for any employee taking college- or university-level course work up to and including Ph.D. When the need is demonstrated, those costs should be prepaid. No commitment from the employee should be required.

Interactive/informal training achieves several goals. It provides an ongoing measurement and appraisal system. It keeps learning channels open, and it really creates desired changes.

They are now finding that people in the workplace learn 30% from classroom training and 70% from informal learning processes that are inside the organization.

Follow the action and keep score

Following the action and keeping score encompasses three things: 1) opening the books, 2) huddling, and 3) creating wins.

Opening the Books involves translating the numbers in the financial reports into individual stories, activities and performances. This move creates trust in the organization. The financial reports actually show the playbook, the translation is the execution of the plays.

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Huddling is the basis for organizational communication. People have to see the effects of what they do, or they won’t care. It doesn’t matter if the effects are good or bad. Huddling tells the people we care. The frequency of the huddles should be determined by what fits the group’s needs. One value of the value of the huddle is that everyone leaves with the same set of numbers.

Creating Wins establishes that winning is a process. Little wins add up to big wins. Wins foster pride, teamwork and improved self-esteem, which are things that do not happen by accident.

Hidden Talent

One day I was walking down the hall past the janitor pushing a broom. He said, “You know you have been telling us for eight months that our job security is dependent upon getting our debt down. I looked at your balance sheet the other day. Do you know that 76% of our receivables are in the truck market, and do you know that the truck market has a recession every six years? Do you know that even if we get this debt down and there is a recession that you will have to lay off one-third of the people working here?”

And he was right. I went to the employment office to find out about this janitor. It turned out he was a former Merrill-Lynch stockbroker who burned out in the early 1980s and took a job with no stress.

I learned a lesson about life: you never know the talent that is in the people who are in your organization.

Provide a stake in the outcome

We look at providing a stake in the outcome three different ways. First, we want instant gratification. We want the small win; we want our people to feel like winners. At the same time we have the bonus program that tells them that any time our people beat the marketplace they are going to get a reward. Our bonus program pays out on a quarterly basis.

When we find a weakness inside of the company, and drive that weakness out, we reward the people for killing the weakness.

Second, we want to create ownership. We created an Employee Stock Ownership Trust in order to motivate our people and take advantage of financial leveraging. The American system is great. We found that for every dollar in profit our company could put on our bottom line, someone will spend \$50 for that \$1 in profit. This is the earnings multiple used in the stock market. We decided to maximize the multiple. (SRC is selling currently for a 14-to-1 earning multiple.) Every employee had stock in the company. They began to realize that their personal worth was greatly enhanced as the value of the stock rose from 10 cents a share to \$7 per share.

While that was good, one employee pointed out that whenever the company generated cash, that cash was used to buy equipment. When people retired they didn't want equipment they wanted their money. Where was that money going to come from?

We had to create an enduring company. We looked at diversifying the company. We began producing auto parts because in a recession our core business (building engines) declines because people keep their old vehicles longer, but those vehicles need lots of repairs to keep running.

Also, we began starting other companies, then when people wanted to leave the company all we had to do was sell one of the other companies to pay off the employees.

Third, we want to create career opportunities for all our people. Anyone with an idea for a new product was encouraged to pursue it.

One employee developed a method to remanufacture oil coolers at a cost of about \$12. Brand new oil coolers cost \$55. We asked what he needed to get started. He said about \$60,000. We gave him \$1,000 in equity, and a loan

of \$59,000. If he could make the new company work he would own 26% of the company, with the rest of the employees owning 74%. His first year he did \$280,000 in sales, this year he expects to do \$10 million. That \$1,000 equity is now worth \$3.3 million.

Other entrepreneurial efforts included a part-time, virtual company that supplied auto parts using spouses of current employees (low overhead because there was no health-care costs – they were already covered as dependents). Today, that subsidiary is doing \$18 million in sales annually, using 35 part-time employees.

SRC started a publishing company, a bank and several other companies. The value of SRC today is somewhere in the \$50 million to \$60 million range.

The first 300 people who came into the company in the early years have a stock portfolio in the company worth about \$120,000.

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Creating Open-Book Management is a difficult process if you don't have vision, not only from people inside the organization, but from top management as well.

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Application Points

Open-Book Management can be an effective approach to operating any organization, but a close examination of the conditions that exist should be made. You might begin by answering questions posed by Jack Stack's presentation.

What rules of business currently dominate your organization? What is it about those rules that define the organization culture in ways that change is effectively stymied? What rules of business can be altered in your organization in ways that foster Open-Book Management?

What is the language of business in your organization that needs to be altered that will emphasize the economics of the business?

Since basic accounting and bookkeeping reports define the “real” rules of business, what kinds of reports can you make available to your employees to begin managing with an open book?

What do you need to do that will keep your employees involved and empowered? (Look at ways to involve your employees in the planning, then accepting their ideas. Also, look for ways to reward productivity through bonus plans.)

Since interactive/informal training can account for as much as 75% of workplace learning, what steps can you take to foster greater opportunities for such interaction?

How can you demonstrate that the tasks you are asking your employees to undertake are not impossible?

What alternatives to regular staff meetings can you initiate that will accomplish organizational communication that Stack achieved through huddling?

What kinds of winning processes can you establish for people in your organization that can foster pride, teamwork and improved self-esteem?

What ways can you devise that will provide your employees with a stake in the outcome of the work? (Remember, Stack approached this three ways: 1) instant gratification, 2) create ownership, and 3) provide career opportunities.)