

# Ours to Share

## How Worker-Ownership Can Change the American Economy

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SURDNA FOUNDATION

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## FOREWORD:

# A Blueprint for Better Jobs

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One question we as funders committed to social justice ask ourselves as often as any other is “*how can we create more jobs?*” But not just any jobs—quality jobs with family-sustaining wages, benefits, and career ladders that are accessible to people who are most in need of them. We know that increasing the number of people working in quality jobs that confer a degree of pride strengthens the foundation of a local economy and increases economic mobility—all while giving people the ability to provide a better future for their families.

Given some of the economic rhetoric prevalent today, if we told you that there is a path to stable, equitable, well-paying jobs with dignity—you might be understandably skeptical. In the pages that follow, you’ll read about worker ownership, an economic development strategy with real potential for the U.S. economy, and one that can help workers reclaim some agency over their economic future. It’s a form of enterprise in which the wealth generated by workers’ ingenuity, efficiency, and productivity also accrues to them as owners.

*Ours to Share*, is a blueprint—a map to a little-known but important approach to economic development that is increasingly becoming a viable market solution that can help address some of today’s thorniest social and economic challenges.

Worker-ownership is not an abstraction, some sort of phenomenon found only in Europe, or something that’s far off in the future. In practically every major city in the

country, worker ownership is ensuring quality jobs and helping to sustain communities. These are healthy American businesses where workers have a voice in everything from operations to finances.

Let’s be clear: worker ownership is not a simple, one-size-fits-all cure. And, as with any business model, it is certainly not without risks. If worker ownership is to thrive—and the challenges are real—it needs more than capital from investors and philanthropic funders. We need more business owners to understand how this change can benefit them and their businesses, and we need more of these business owners to adopt it. If philanthropy gets behind worker ownership, we just might help it become a scalable part of an economic development strategy that recognizes, and is driven by the needs of people of color, women, and immigrants.

What’s most exciting to us is that worker ownership is one of those rare approaches to economic development that works anywhere in America, and *just makes sense*.

We invite you to learn more in this report, and to use the resources provided at the end to explore how you can support worker ownership.

Sincerely,

*Phillip Henderson*  
*President, the Surdna Foundation*

## INTRODUCTION

The global financial crisis that erupted in 2007 sparked widespread demand for reform, as many long-simmering social and economic problems came into focus.

At a macro level, this was the logical conclusion of a period since the early 1980s during which national and regional economic crises had flared up with historically unprecedented frequency, causing economic insecurity worldwide.<sup>1</sup>

At a micro level, the same period also saw rising income instability for people in the United States (U.S.) and around the world, especially those at the bottom of the economic ladder.<sup>2</sup> The macro crisis had punctuated the volatile conditions facing many individuals and families - after the financial crisis hit, the unemployment rate rose sharply from 4.5% to 10%,<sup>3</sup> and many more became underemployed. Employment has recovered since then, but the low quality of jobs continues to be a serious obstacle for many Americans.

The great recession was a wakeup call in many ways - a realization that economic stability may require different kinds of solutions.

For many, the crisis opened up the space for a desperately needed conversation about economic inequality. Most economically advanced countries have seen rising income inequality in recent decades, though the increase has been especially pronounced in the U.S.<sup>4</sup> Thomas Piketty's much-discussed book, *Capital in the 21<sup>st</sup> Century*, highlighted an important factor in this trend - as capital's share of income has risen relative to labor's share, and because capital income is distributed more unequally than labor income, income inequality has increased dramatically.<sup>5</sup> Wealth inequality, meanwhile, has risen at an even faster clip than income inequality, which is especially problematic in a context of

rising volatility.<sup>6</sup> Accumulated wealth, after all, serves as a buffer against uncertainty. Without the buffer of accumulated wealth, job losses, cutbacks in working hours, and other such shocks quickly place many low- and middle-income people in difficult circumstances.

These problems have been widely discussed even after the immediate crisis passed. But these discussions have tended to follow rather well-worn patterns, and organizational and institutional responses have been limited with few solutions on the table or new ideas to debate. This report is a departure - one in which we consider a system that may prove to be a viable path for economic security and recovery for the U.S. and potentially the global economy. *Ours to Share* looks at the role that broad-based worker-ownership is also playing in reorganizing firms, raising working standards, and reshaping the U.S. economy. And it asks how far worker co-ops could go in helping workers to reclaim some agency over their economic future.

Most who are involved in the worker cooperative movement agree that there has been a surge in co-op development since the global financial crisis, even if the overall footprint of co-ops remains relatively small. The U.S. also has an exceptionally large number of firms that extend ownership to a broad base of workers through employee share ownership programs (ESOPs) and other similar arrangements.<sup>7</sup> While there are vibrant discussions about the existing realities and future possibilities of worker-ownership in the U.S., they tend to stay within rather limited circles. This report aims to expand the conversation.

At the heart of the discussion is one key question: Are worker cooperatives and ESOPs a viable business model that could be scaled in the US economy?

## CHAPTER SUMMARY

### SECTION I: WHAT IS WORKER-OWNERSHIP?

- **Chapter one** is brief explanation of co-ops and ESOPs, the two most common forms of worker-owned companies.
- **Chapter two** looks at the key question of efficiency. For any gains that come from being a worker-owner to be durable, worker-owned firms need to succeed as businesses, and this chapter looks at their economic performance and ability to adapt to changing market conditions.
- **Chapter three** addresses issues of equity, both in wealth and asset-building and a broader sense of justice and fairness.
- **Chapter four** focuses on inclusion of groups that have historically faced economic marginalization. To what extent are immigrants, women, and people of color fully included in worker-owned firms? And, can worker-ownership help to break down broader barriers to full participation in American economic and social life?

### SECTION II: HOW CAN WE INCREASE WORKER-OWNERSHIP?

- **Chapter five** surveys the industry and geographic landscape of worker-ownership in the U.S., which serves as an important basis for understanding the challenges and opportunities facing those who wish to develop worker-owned firms.
- **Chapter six** delineates three pathways to expansion of worker-owned cooperatives, considering the factors that tend to lead down one road versus another, and the various tradeoffs that are involved. “Starting up,” “scaling up,” and “conversion” all have a role in the expansion of worker-ownership.
- **Chapter seven** examines the role of national and local ecosystems in the development of worker-ownership, considering the impact of government, incubating organizations, and community social ties.

#### KEY TAKEAWAYS FROM THIS REPORT:

The survival rate of ESOP firms is a higher through economic downturns compared to traditionally structured firms

- Productivity of ESOPs is as good if not better than traditionally structured businesses
- Turnover at ESOP firms is lower than at traditionally run firms
- Co-ops do not go out of business more often than traditional companies
- The small footprint of co-ops is due to lack of access to capital and other support infrastructure
- Enabling co-ops through legislation as well as supportive infrastructure makes a big difference in terms of where co-ops form and thrive
- Converting to an ESOP or co-op is an increasingly attractive succession plan as Baby Boomers retire
- There is a greater concentration of ESOPs in industries where technological skill and human ingenuity are critical to the business model
- While there is a relatively small number of co-ops, their formation rate has increased since 2007, particularly by disadvantaged communities, such as immigrants and women
- With the right supports and resources, ESOPs and co-ops can do create better jobs and wealth for workers

## **PART 1:**

What's a "Worker-Owned Firm?"

## CHAPTER ONE:

# Defining Worker-Ownership

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Employment today generally presents us with two options:

1. You can work for someone else, which means reporting to a boss and working for an organization in which you do not exert significant ownership and control rights.
2. You can also work yourself, as in the case of small business owners and growing numbers of independent contractors.<sup>8</sup>

What if there was another way?

Broad-based worker-ownership poses a different set of possibilities. **At their most basic level, worker co-ops and ESOPs make working people into part-owners of the enterprises where they are employed.** This can then serve as a foundation for transforming the terms of

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employment. Rather than working for someone else, or working for oneself on an individual basis, broad-based worker-ownership can allow people to work as part of a broader collective enterprise in which they share ownership and control rights with their peers.<sup>9</sup>

The simplest possible definition of “worker-ownership” means that people who are employed by the company also own part of the company, share the benefits of success (as well as

the risks of failure), and have some level of participation in decision-making. But of course, it can be somewhat more complicated than that. There is a wide variety of viewpoints on how firms should be governed, including worker-owned firms as well as companies that consciously practice employee engagement (see Appendix). ESOPs can range from simply providing additional benefits to workers or to resembling a highly democratic structure more akin to a co-op.

By addressing four key sets of factors, we can arrive at a basic understanding of what worker-ownership looks like within a particular firm.

1. **First, how widely is ownership extended?** Particularly in the United States, there are many firms in which shares or share options are granted to executives or workers in certain occupations, and, indeed, much discussion has been focused on how such compensation practices have served as a contributing factor in rising income inequality over the past several decades.<sup>10</sup> In this report, the focus is squarely on arrangements in which shares are extended to a broad base of workers.
2. **Second, what proportion of company shares do employees own?** In many cases where broad-based worker-ownership has been implemented, workers still own only a small fraction of overall shares. The majority of shares may remain concentrated in the hands of a select group of company insiders, among a set of outside investors, or some combination of the two. While many firms are marked by some degree of broad-based worker-ownership, it is reasonable to say that only those cases in which workers collectively have at least a majority of the shares truly warrant the label “worker-owned.”
3. **Third, how is ownership organized?** There are many different ways in which shares can be allocated. In many worker-owned firms, shares are allocated according to income. Assuming that people have varying incomes, they will also have differing property claims. However,

shares can also be allocated equally to each person in the organization, based on hours worked, or using indices that combine different factors. Even among firms that are 100% worker-owned, there can thus be big differences in how ownership is structured.

4. Fourth and finally, **does ownership mean control?** Many worker-owned firms do not differ significantly from firms with conventional ownership structures in this regard. However, there are a significant number that do carve out channels for workers to provide greater input over how their own tasks are organized and how their work teams go about performing their duties. Some ESOPs and most worker cooperatives also enable workers to exert voice in matters of firm-level governance. There is thus a broad spectrum of ways in which worker-ownership may or may not be linked to workplace democracy.

Reviewing two different kinds of worker-ownership helps us to see how these questions are answered in practice.

### EMPLOYEE SHARE OWNERSHIP PLANS (ESOPs)

Employee share ownership plans (ESOPs) were established with the passage of the landmark Employee Retirement Insurance and Security Act (ERISA) of 1973.<sup>11</sup> The ESOP was designed as a flexible form around which a variety of different kinds of organizational arrangements can be constructed. At its core, however, it is simply a benefit plan through which workers are granted shares in a company where they are employed.<sup>12</sup>

ESOPs are often grouped together with a range of other kinds of plans and schemes under labels including “financial participation” and “shared capitalism.”<sup>13</sup> Profit sharing and gainsharing are similar to ESOPs and other forms of employee ownership in that they link employee compensation to the performance of the firm, or, in the case of gainsharing, to a single unit within a firm. But these forms of sharing do not generally extend ownership claims to workers. Among the range of different kinds of employee ownership schemes, one key element that distinguishes ESOPs from many other kinds of share ownership programs is that they are broad-based—i.e., available to all employees meeting minimum service requirements. Another is that shares (and not just share options) are granted to employees rather than being paid for out of their savings. The ESOP is basically a

trust that invests in company stock and holds its assets in individual employee accounts.<sup>14</sup>

Most ESOP firms are not majority worker-owned, but a significant number are. Of the 7,000 or so ESOP firms that currently exist in the US, a recent estimate suggests that over 1,000 ESOPs are more than 50% worker-owned, including several hundred that are 100% worker-owned.<sup>15</sup> The largest majority worker-owned ESOP firms include companies such as Publix Supermarkets (160,000 employees), Daymon Worldwide (35,000 employees), and W.L. Gore and Associates, maker of Gore-Tex (10,000 employees).<sup>16</sup>

All ESOP plans are required to give some voting rights to participants. In publicly traded companies, participants receive the same voting rights as other shareholders. In privately held companies, the minimum requirement is for participants to vote on certain issues including mergers, acquisitions, and liquidation. A 2012 National Center for Employee Ownership survey on corporate governance found that 16% of ESOP firms provide voting rights that surpass the minimum requirement, including 11% that pass through full voting rights on all shareholder issues. Most ESOP firms allocated one vote per share, but 23% did so on a “one member, one vote” basis. Around the

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same percentage—22%—have “current employees who are not officers” on their boards of directors.<sup>17</sup>

Aside from participation in matters of firm-level governance, many ESOP firms provide other ways for workers to offer input and become involved in decision-making. The available evidence suggests that ESOP firms and other

firms with shared ownership or performance-based pay are more likely to have mechanisms for employee involvement such as self-directed work teams and quality circles.<sup>18</sup> Even in ESOPs without formal mechanisms for employee involvement, many create avenues for workers to participate on a more informal basis. According to Chris Mackin, founder of Cambridge, Massachusetts-based Ownership Associates, these more informal modes of participation are crucial to understanding the culture and operations of many ESOP firms, and yet they often remain beneath the radar of those who study worker-ownership.<sup>19</sup>

ESOPs can also be a means of creating positive incentives for employees, by linking their performance to that of the firm.<sup>20</sup> In cases where broad-based employee ownership has been implemented in large publicly traded companies, it has sometimes been a means of inoculation against hostile takeovers, with managers and large shareholders calculating that workers will be likelier to side with them over outside investors.<sup>21</sup>

There are other reasons for forming ESOPs that have little to do with economic self-interest. Many employers are motivated at least in part by a desire to build wealth for employees. For those engaged in succession planning, creating an ESOP can be a way of preserving their legacy, turning ownership over to people who have been with them over the course of the company's development. "Unfortunately, our entire philosophy today is to get all the money you can, in whatever way you can," Robert Moore, founder of Milwaukie, Oregon-based Bob's Red Mill, told ABC News in a 2010 interview, following a decision to transfer 100% ownership to employees of the company through an ESOP. "I've just truly, truly, truly tried to set some of that aside and do what I thought was the best thing for the group of people who made all of this possible." Moore's decision put hundreds of thousands of dollars into the coffers of each of the company's employees.<sup>22</sup>

The fact that ESOPs can challenge the distinction between capital and labor, extending ownership to a broad base of workers, is attractive from a democratic perspective. And, for some employers, the ESOP serves as a foundation for expanding workplace democracy, transferring ownership as well as control rights to a broad base of employees. However, this goes beyond what most employers have in mind. Even in ESOP firms that are 100% worker-owned, most apportion voting rights based on income. In those ESOP firms that do

operate on a one member, one vote basis, this voting power applies to a limited array of issues. And, regardless of voting rights, shares still tend to be allocated based on income.<sup>23</sup>

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It is important to underscore that the ESOP is ultimately a flexible form. Governance in ESOP firms has been configured in many different ways, some of which are significantly more democratic. Take MBC Ventures, which was founded in 1851 in Baltimore, Maryland as the Maryland Brush Company. In the late 1990s, the company's management and the United Steel Workers, the union representing the company's workers, joined together to initiate an ESOP. Now a 100% worker-owned firm,<sup>24</sup> MBC Ventures allocates stock based not on income but the number of hours an employee works in a given year.<sup>25</sup> MBC Ventures has thus put in place what is arguably a more democratic way to apportion ownership, accounting for people's varying time contributions to the firm's activities without assuming that higher-paid employees deserve more for their efforts.

## WORKER COOPERATIVES

Another kind of worker-ownership structure with a longer history than ESOPs is a worker cooperative or co-op.

Despite their much longer history, the overall footprint of worker cooperatives in the U.S. is far smaller than that of

ESOP firms. A recent estimate puts the number of worker cooperatives at 300 and the number of worker members at around 3,500, with \$450 million in total revenues.<sup>26</sup> Examples of ESOPs include W.L. Gore & Associates (makers of GoreTex); HDR, Inc. (one of the largest engineering firms in the country); and Publix Super Markets.

Unlike ESOPs – which are generally grafted onto conventionally structured firms, and may or may not end up transforming their organizational structures – most worker cooperatives are started from scratch and are worker-owned from the outset. These factors go at least some of the way in explaining why worker cooperatives are a much rarer sighting in the American economic landscape.<sup>27</sup>

Most close observers of the worker cooperative movement agree that there has been a surge in co-op development since 2007—part of a larger set of movements aimed at exploring economic alternatives in the wake of the Great Recession. Only time will tell whether this apparently generative moment leaves a lasting imprint on the bigger picture. But this wave of co-ops is decidedly more ambitious, and best represented by Evergreen Cooperatives in Cleveland (see case study inset), which is focused on maximizing profit to the benefit of its workers, according to John McMicken, Evergreen's Chief Executive Officer. While democratic decision-making and inclusion mechanisms are part of Evergreen's overall mission, business development is foregrounded based on the belief that the co-op has to succeed in order to make a difference in the lives of those who are most invested – the workers.

While Evergreen now has 110 employees, most worker cooperatives tend to be small (20 employees or less)

with a few notable exceptions. A 2013 report on worker cooperatives by Hilary Abell, founder of Project Equity and the Prospera group of worker cooperatives in Northern California, found 14 cooperatives with more than 50 workers. The biggest worker co-ops at the time that report was written were Bronx-based Cooperative Home Care Associates (2,300 employees and 1,100 members), San Francisco-based Rainbow Grocery (240 employees and 225 members), and Madison, Wisconsin-based Union Cab and Alexandria, Virginia-based Alexandria Union Cab (both with around 230 employees/members).<sup>28</sup>

As a matter of principle, worker cooperatives are clearly aligned with the democratic view of the firm. A core principle of the democratic view to which most cooperatives adhere is joint ownership and collective control on a one member, one vote basis. There is a range of different ways in which decision-making procedures are structured, however. Many worker cooperatives operate by majority vote, or some mix of majoritarian and consensus-based procedures.<sup>29</sup> Worker cooperatives also vary in their mix of direct and representative democracy. Many delegate a significant number of decisions to an elected board of directors.

As we will see in later chapters, there is an increasing interest in the formation of co-ops by workers as well as through institutional support. The most important question to be answered about both ESOPs and co-ops, however, is their viability in the current economic climate.

## CHAPTER TWO:

# Is Worker-Owenship Efficient?

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Before anyone should embark on the hard work of starting or converting a business to a worker-ownership structure, the looming question of whether worker-ownership is compatible with running an economically successful business must be asked and answered first: Is it “efficient”?

In the 1970s, the economist Arthur Okun famously suggested that there was a “great tradeoff” between equality and efficiency. More equality would generally mean less efficiency, and vice versa.<sup>30</sup> This contention has generated ongoing debate, with some suggesting that the organizational arrangements that promote greater equality tend to come at the expense of efficiency,<sup>31</sup> and others arguing that the two can in fact be reconciled.<sup>32</sup>

Okun’s tradeoff is relevant for thinking about broad-based worker-ownership. It would be great if worker-ownership advanced economic efficiency while promoting equality and the other social welfare-related outcomes. Some might even argue that compromising a bit on efficiency could be tolerable if the equality gains were significant.<sup>33</sup> Most, however, would be satisfied if it could be shown that broad-based worker-ownership was simply neutral from an efficiency standpoint.

In a general sense, we can think of efficiency as referring to the achievement of a given set of tasks with minimal expenditure of time and effort. So there is always the question of what these tasks or objectives are. They could include issues such as building wealth, enhancing job security, and providing economic opportunities to historically disadvantaged groups. Generally, however, conversations around economic efficiency assume that the aim is to maximize the production and delivery of goods and services with minimal inputs, placing distributional and other social-welfare related concerns into a separate bucket. For the sake of addressing the prevailing discourse on its own terms, the current discussion accepts these parameters.

Having defined efficiency in this way, there are still two dif-

ferent dimensions that need to be distinguished. One dimension is “static.” Were we to take a snapshot of two very similar firms, would broad-based worker-ownership tend to make a difference in their ability to generate economic outputs given the inputs at their disposal? A second dimension is “dynamic.” How well are firms able to make needed adjustments to how they produce and deliver goods and services over time? This includes the ability of worker-owned firms to successfully navigate the early stages of their development, overcoming the “liabilities of newness” to become established players. It also includes issues related to ongoing adaptability, including the capacity to innovate new products and processes that allow the enterprise the stay competitive.<sup>34</sup>

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### EFFICIENCY IN ESOPS

STATIC (Looking at how two different company structures perform at a moment in time): Comparing labor productivity in ESOP versus non-ESOP firms, the existing evidence suggests little difference. At the very least, employee ownership has a neutral effect on commitment, productivity, and other factors that would be expected to carry efficiency-enhancing implications. A meta-analysis of studies on productivity in firms with broad-based employee ownership shows that productivity in ESOP firms is probably a bit higher.<sup>35</sup>

One common argument for the potentially efficiency-enhancing aspects of worker-ownership is that it creates a link between individual performance and the performance of the firm. Individuals will be interested in boosting the performance of the firm to the extent that they end up seeing benefits in the form of higher share values. This will result in a tendency for worker-ownership to make workers more productive.<sup>36</sup>

However, some have suggested that the incentive to work harder will be neutralized by a tendency to pass the buck, assuming that someone else will pick up the slack. Moreover, it is argued, this tendency will only become more acute as firms grow in size due to a tendency known as the “1/N” problem: the calculation that individual expenditure of effort is unlikely to yield measurable dividends. But there is evidence suggesting that another feature of employee ownership counteracts this problem. Workers in settings with employee ownership tend to engage in heightened co-monitoring of their peers, which helps to neutralize the impulse to shirk.<sup>37</sup>

There is also evidence that turnover tends to be lower in firms with broad-based employee ownership. As discussed below, this stems in part from the fact that firms with broad-based employee ownership tend not to lay off as many workers, including when times are bad. But, aside from lower involuntary turnover, the evidence shows that voluntary turnover—the choice to leave a firm, perhaps taking a job elsewhere—is also lower in firms with broad-based employee ownership due to higher levels of employee investment and commitment.<sup>38</sup>

Another important finding is that the potential of employee ownership to boost efficiency seems to be unleashed in the presence of mechanisms that enhance employee participation. Employee involvement mechanisms such as work teams and quality circles are more likely to be present in firms with broad-based employee ownership. We also see that the positive effects of both ownership and participation are enhanced when the two are present together. *Employee ownership provides the incentive to participate, and concrete mechanisms of participation supply the means.*<sup>39</sup>

DYNAMIC (Looking at how two different company structures evolve over time): The evidence suggests that ESOPs do not go out of business at higher rates than conventional firms, including during economic downturns. If any-

thing, their survival rates may be higher.<sup>40</sup> A recent study on publicly traded companies shows that, after controlling for range of variables including industry, firms with broad-based employee ownership were significantly less likely to go out of business during the Great Recession.<sup>41</sup>

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Technology and technological change are more difficult to measure. Broad-based employee ownership is highly concentrated in a several technology-intensive industries, providing a basic indication of its compatibility with high levels of innovation. However, we do not currently have systematic evidence on the degree to which employee ownership affects the capacity of firms to innovate within a given industry or market segment. Moreover, as discussed below, it is important not to read too much into the existing industry distribution, as the reasons for these patterns are complex.

There are many examples of ESOP companies in which employee ownership has been used to support innovation. W.L. Gore and Associates, maker of Gore-Tex, is a 100% employee-owned ESOP company. The company’s founder, Bill Gore, broke away from DuPont in the late 1950s to establish the company. He was convinced that polytetrafluoroethylene (PTFE) could be commercialized and used for a range of different purpose. He also envisioned a company structured like a “lattice”—one in which all workers would be able to share and contribute their ideas. Gore-Tex’s innovation was not just on the product side, but the result of developing an organizational structure that supported the development new products that people would want to buy.<sup>42</sup>

Gore-Tex today has some 10,000 workers and recently reported more than \$3 billion in annual revenues.<sup>43</sup> In addition to being consistently named one of the best places to work, it is also rated as one of the most innovative companies. Employees of Gore-Tex are organized into work teams, but they are encouraged to collaborate and give 10% of their time to work on developing new ideas. The company's high-selling "Elixir" guitar strings were developed in this manner. Gore-Tex is a good example of a company that challenges notions of management that impose a separation between conception and execution. Instead, through greater autonomy and self-management, authority is more distributed throughout the organization, and employees play a greater role in the conception of new products and processes.<sup>44</sup>

### EFFICIENCY IN WORKER COOPERATIVES

As in the case of ESOP firms, the available evidence suggests that labor productivity is the same or better in worker cooperatives than in other firms. A 2012 study of some 7,000 French firms found that labor productivity is not any lower among the approximately 500 firms that are 100% worker-owned.<sup>45</sup> In the 1980s, a study of firms in the U.S. plywood industry found that labor productivity was slightly higher in the cooperative enterprises than in those with conventional ownership structures, although the sample size was much smaller (including 34 firms, seven of which were cooperatives). Finally, a meta-analysis shows that, on balance, the existing literature does not find productivity differences between co-ops and more conventional firms. Worker cooperatives, in fact, appear to do slightly better.<sup>46</sup>

Despite this evidence, the relative scarcity of worker cooperatives has been taken as an indication of their inefficiency. As the political scientist Jon Elster once asked, "If cooperative ownership is so desirable, why are there so few cooperatives?" Indeed, labor productivity provides just one metric for comparing co-ops against conventional firms, and there could be a range of other reasons why worker cooperatives are less apt to succeed from a business standpoint.

It is often assumed that the footprint of worker cooperatives is so small because they fail at higher rates than other firms. However, a recent paper by economist Erik Olsen that examines data and existing studies from a range of countries including the U.S. finds no evidence for lower survival

rates among worker co-ops. "Because the rarity of worker cooperatives cannot be attributed to performance," Olsen concludes, "it must result from a low formation rate."<sup>47</sup>

What, then, accounts for the fact that so few worker cooperatives are launched? One hurdle is the difficulty raising the necessary capital. If people who are interested in forming a cooperative enterprise do not have the startup funds necessary to do so, this can stop the process before it really starts. As in the case of other business ventures, those wishing to launch a cooperative enterprise can try to raise funds from external sources. Since most cooperatives are premised on the idea of equal voice being linked to equal ownership, there are important questions around the degree to which external funding might undermine these principles. Some cooperatives have addressed this concern by issuing non-voting shares.<sup>48</sup>

When trying to raise capital from banks and other lending institutions, the access and cost of capital may be an important barrier to tackle. Despite evidence showing that worker cooperatives are just as productive as conventional firms, and no more likely to fail, most mainstream lending institutions are not armed with this set of facts. So the perception that worker cooperatives are some kind of novelty, unlikely to succeed, is likely to color their perceptions and lending decisions.

Even to the extent that it is possible to raise the capital necessary to launch a worker-owned enterprise, there may be deeper sociocultural reasons explaining why worker cooperatives are started so infrequently. Simply put, when an individual or small group of people have a potentially lucrative idea, they will often prefer to capture the benefits for themselves.<sup>49</sup> There are instances where developing a cooperative makes sense even from the standpoint of an entrepreneur or group of entrepreneurs bent on maximizing economic benefits. In many cases, however, developing a worker cooperative enterprise entails a commitment to objectives in addition to maximizing personal economic gain.

To the extent that this is true, many would argue that barriers to forming cooperatives actually have less to do with culture than with human nature. Much of economic thinking is premised on the notion that individuals are rational agents driven to maximize their personal economic gain. On this assumption, cooperation driven by anything other than the pursuit of gain is out of step with how we are

hard-wired, which might help to explain why we see so few worker co-ops. But this assumption is debated by evolutionary psychologists.

It is also important to remember that profit maximization and the pursuit of gain can often coexist alongside more cooperative, collective impulses. North Central Italy has a higher density of worker cooperatives than anywhere else in the economically advanced world. The region scores high on measures of “social capital,” and members of worker cooperatives place value on relationships of trust and cooperation. But, like other enterprises, cooperatives are vehicles for the pursuit of economic gain, and they are an

important part of a regional economy that ranks among the highest in Europe in terms of GDP per capita.<sup>50</sup>

Given that ESOPs and worker co-ops are just as efficient and productive as traditional firms, we next turn to other questions about their relative advantage in terms of equity and inclusion. Do worker-owned companies actually create better, more equitable circumstances for workers, and are they able to participate in relatively equal numbers?

## CHAPTER THREE:

# Equity

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In the context of growing economic inequality and rising economic volatility, a core set of questions relating to the potential benefits of worker-ownership has to do with issues of equity. In a narrower, technical sense, “equity” actually refers both to share ownership and to wealth (i.e., assets minus liabilities).

Thinking about equity as a broader umbrella term that has to do with issues of justice and fairness brings up many important questions about the impact of worker-ownership. There are also important questions about the degree to which worker-ownership can help to advance economic fairness. Given increasing returns to capital relative to labor,<sup>51</sup> can worker-ownership, by expanding access to capital, promote greater income equality? Under certain conditions can it extend access to jobs with better pay benefits? Does it help to create jobs that are more stable and secure? Does it lead to greater job satisfaction and morale?

The following discussion uses the best available evidence to paint a picture of what we currently know about the equity-related implications of worker-ownership.

### EQUITY IN ESOP FIRMS

**Recent evidence suggests that ESOPs do help to promote greater equality in the U.S. wealth distribution.**

- **An analysis of a National Bureau of Economic Research (NBER) dataset on worker ownership shows that income-based disparities in share ownership are lower in ESOPs than in the U.S. economy as a whole**, such that expanding the relative proportion of ESOP share holdings will tend to reduce overall wealth disparities.<sup>52</sup> To the extent that shares are accompanied by annual dividend payments<sup>53</sup>, worker-ownership can also play a role in promoting greater income equality. Even though share distributions are less unequal in ESOPs in a relative sense, these distributions are still based on the premise that ownership stakes should

differ based on the size of one’s income. There are ways in which ESOPs can be structured to produce a more egalitarian distribution of accrued wealth and share-based income. MBC Ventures, where shares are allocated based on hours worked rather than income, is a good example.<sup>54</sup>

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Given increasing returns to capital relative to labor, can worker-ownership, by expanding access to capital, promote greater income equality? Under certain conditions can it extend access to jobs with better pay benefits? Does it help to create jobs that are more stable and secure? Does it lead to greater job satisfaction and morale?

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- **There is also evidence that ESOP firms have more stable employment than non-ESOP firms.**<sup>55</sup> There tend to be fewer layoffs, which is related in part to the fact that ESOP firms are less likely to go out of business.<sup>56</sup>
- Furthermore, recent work by economists Doug Kruse and Fidan Kurtulus suggests that publicly traded companies with employee ownership retain more stable levels of employment when facing both “macroeconomic negative shocks (increases in the unemployment rate,

decreases in the employment-to-population rate)” and “firm-level negative shocks (declines in firm sales, declines in firm stock price).” They hire less when times are good but also fire less when times are bad.<sup>57</sup>

Despite the potential benefits of employee ownership, there are also possible tradeoffs that warrant serious consideration. One major concern is undiversified risk, also known as the problem of putting all your eggs in one basket.<sup>58</sup> A recent paper on the subject suggests that it would be wise not to have more than 15% of one’s net wealth in company stock, but finds, based on analysis of the NBER dataset, that many ESOP participants do have holdings that rise above this threshold.<sup>59</sup>

Still, it is also important to gauge whether employee share ownership is substituting for other forms of wealth. Another analysis of the same data finds a substitution effect that is much less than “dollar-for-dollar,” with each additional dollar of ESOP holdings associated with a 20 percent drop in other wealth.<sup>60</sup> To the extent that the risk posed by employee ownership is mostly in relation to wealth that people would not have had without the ESOP in place, it poses less of a concern.

Overall, the patterns provide some reassurance. But it is important to acknowledge the numerous cases in which share ownership through ESOPs and types of arrangements has had negative and sometimes disastrous consequences for employees. There are high-profile cautionary tales—such as United Airlines—that remain salient in the public consciousness, and for good reason.

In the case of United Airlines, the company was facing heightened competition in the industry, and workers accepted wage concessions in return for what amounted to majority ownership. Following 9/11, as conditions in the industry worsened, United filed for bankruptcy. Not only did many workers lose their jobs. “[W]orkers lost all of the stock they bought with their wage and benefit and work rule concessions,” as Joseph Blasi, Doug Kruse, and Richard Freeman tell it in their recent book, *The Citizen’s Share*. “The failure was that United had set up its ownership system in ways that ran against what successful employee-owned firms have learned over decades of experience.”<sup>61</sup>

Cases such as United Airlines underscore certain cardinal rules, including not substituting shares for wages. Still, it

is important to recognize that there are some instances in which these generally sensible rules have been broken, and workers have ended up better off. For example, in a number of ESOPs that were jointly orchestrated by the United Steel Workers, workers faced with the possibility of plant shutdowns did agree to temporary wage concessions that helped to keep their companies in business.

## EQUITY IN WORKER COOPERATIVES

As in many other areas, the data on equity implications is spottier for worker cooperatives than for ESOPs, making it difficult to draw firm conclusions regarding equity. There are examples of worker cooperatives in which workers do accrue significant wealth as their shares appreciate in value and/or a portion of profits is distributed into their internal capital accounts. However, the available evidence does not allow us to assess the general differences between worker co-ops and non-co-op firms in the area of wealth accumulation.

Anecdotally, many who study worker cooperatives have suggested that they tend to be more equitable in how they compensate their employees.<sup>62</sup> This makes sense, as one might expect a flatter, more democratic authority structure to produce a flatter compensation structure. Still, additional work is needed to assess more definitively whether this is true in general, and, if so, to what degree. It would also be worth exploring whether compensation structures in worker cooperatives and conventional firms vary even after controlling firm size, industry, and other relevant factors.<sup>63</sup>

There is also some uncertainty concerning the question of whether worker cooperatives pay above-market wages. Again, we do see numerous examples of worker cooperatives that manage to do so. In many of the house-cleaning cooperatives that have emerged over the past two decades or so, members earn wages that exceed local industry averages and far outstrip what they were earning in previous jobs.

For these and other cooperatives in low-wage service industries, lower managerial and other overhead costs can help people to pay themselves more than employers in the same industry would tend to pay them.<sup>64</sup> Worker cooperatives can also appeal to customers who are willing to pay a premium for goods and services that are produced and delivered under better working conditions.

For co-ops, the strongest evidence that they provide ad-

ditional benefits has to do with their role in promoting job security. Studies comparing worker cooperatives and non-co-op firms in the US<sup>65</sup>, Italy<sup>66</sup>, and Uruguay<sup>67</sup> suggest that levels of employment tend to be more stable in worker cooperatives, including during economic downturns. However, these studies also suggest that worker co-ops tend to make bigger adjustments on wages in order to preserve more stable levels of employment. There are other potential equity-related benefits to being

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Worker cooperatives can also appeal to customers who are willing to pay a premium for goods and services that are produced and delivered under better working conditions.

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employed in a worker cooperative. Take, for example, issues related to work scheduling. Recently published research focusing on work scheduling issues among early career wage workers in the U.S. shows that most experience fluctuations in the number of hours they work. Significant numbers of people also report having little control over their work schedules, receiving inadequate notice of schedules and scheduling changes, and being on call without any guarantees of paid working hours. Those in low-wage occupations are more likely to encounter these problems.<sup>68</sup>

By contrast, at Cooperative Home Care Associates, members are able to sign up for a program whereby they are paid for a minimum of 30 hours of work per week, even if they can only secure work assignments that add up to less than 30 hours. Members can enroll in the program after three years of full-time employment at CHCA. They must also continue to meet certain conditions in order to participate, including calling into the office each weekday morning and being prepared to take an assignment if one is offered.<sup>69</sup>

In a recent paper, economist John Pencavel examines patterns of working hours in the plywood industry during the 1960s and 1970s, comparing worker co-ops and non-co-op firms.<sup>70</sup> As part of his study, he traces what happens in two non-cooperative firms that convert to non-cooperative ownership. Average working hours per employee go up, according to Pencavel, with the change reflecting a shift in orientation:

*To the capitalist management, the hourly wage is a cost whose effects on the owners' net revenues can be moderated by cutting hours of work; to the worker co-op, the hourly wage is a factor in a worker's income and the effects on his income can be enhanced by working longer hours. The wage plays a different role in the objectives of the two ownership forms.<sup>71</sup>*

Here, Pencavel touches on a broader difference between worker cooperatives and firms without broad-based ownership and control. Worker cooperatives are generally run primarily for the benefit of their members. Their ability to realize that mission will vary, and, as suggested in the foregoing, more work is needed to draw firm conclusions about the full range of equity-related implications. But, as a starting point from which to build, the basic premise of worker cooperatives distinguishes them from most other firms.

## CHAPTER FOUR:

# Inclusion

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The previous chapter focused on the extent to which worker-ownership helps to build wealth and extend justice and fairness at the workplace. An important part of understanding these equity-related issues has to do not only with how people are doing on average, or the overall distribution within the firm, but also the status of those facing various forms of labor market disadvantage. The current chapter focuses on the extent to which worker

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To the extent that members of historically disadvantaged groups find themselves in worker-owned firms, are they able to participate on equal terms?

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ownership promotes the inclusion of groups that have historically faced barriers to full participation in the economy and in society more generally: women, people of color, and immigrants.

**More bluntly: Can members of historically disadvantaged groups secure these jobs, or are they excluded?**

A second set of issues concerns dynamics of participation within worker-owned firms. To the extent that members of historically disadvantaged groups find themselves in worker-owned firms, are they able to participate on equal terms?

Finally, there is a set of issues related to whether worker-ownership can promote inclusion of historically disadvantaged groups in the larger economy and in society

more broadly. Do they help to break down broader barriers to economic opportunity and socioeconomic mobility?

### INCLUSION IN ESOP FIRMS

Data from the General Social Survey shows patterns of share ownership in the U.S. economy through ESOPs and other arrangements. While the data is not precise, it does provide a general picture of patterns of participation in broad-based share ownership.

The data shows that women, people of color, and immigrants are less likely to own shares than men, whites, and native-born people. However, these gaps are significantly reduced after controlling for other factors such as industry and educational background. In other words, the lack of participation of these groups in employee share ownership conforms to broader patterns in U.S. the economy rather than having to do with something about employee-owned firms specifically.

Recent work by sociologist Ed Carberry draws on the NBER study of 14 firms with broad-based employee ownership to examine the participation of women and people of color. In terms of share ownership, he finds that women are less likely to participate than men, and blacks and Hispanics are less likely to participate than whites. When they do participate, the value of their plans also tends to be lower. However, after controlling for differences in occupation, job tenure, and educational attainment, only the gender-based differences in plan value remain statistically significant.<sup>72</sup>

It could be the case that racial and gender bias factor into the occupational division of labor in these firms, in which case bias would have follow-on implications for share ownership. But there is no way to know this from the NBER data. Nor is there reason to believe—barring evidence to the contrary—that ESOP firms tend to perform any better or worse than other firms with respect to issues of bias and discrimination.

With respect to participation in decision-making within these firms, the evidence is mixed. There are measures that show women and people of color actually do better than men and whites. On balance, however, there are a greater number of areas in which women and people of color face statistically significant barriers to participation (e.g., involvement in work teams, department goal setting, and decisions about work organization).<sup>73</sup> To the extent that a sizable number of ESOP firms provide avenues for greater participation in decision-making, these findings point to the importance of ensuring that opportunities for participation are available to everyone. Otherwise, general efforts to promote greater inclusion can, in the same stroke, reinforce the exclusion of certain groups.

ESOP firms clearly have potential to address obstacles to wealth creation that confront members of historically disadvantaged groups, particularly immigrants and people of color. For example, McKay Nurseries, in Waterloo, Wisconsin, is an ESOP company that sells plants and provides landscape design, construction, and maintenance services to customers throughout the Midwest.<sup>74</sup> Latino migrant workers, most of whom are non-citizens and employed on a seasonal basis, make up nearly half of the company's workforce. Like most other migrant farm workers, their

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As seen in the union movement and the rise of worker centers, the greatest organizational growth is occurring among immigrants, women, and people of color.

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wages are low; McKay does not stand out in this regard. But, each year, the company contributes an additional amount—equal to around 20% of their total pay—into their ESOP accounts. Company managers cite this as a key factor in the relatively low turnover among its migrant employees, and those who continue coming back are able to build substantially greater savings than they would have

done performing similar work for most other employers.<sup>75</sup>

There are many other examples of ESOP firms that have increased the wealth of their employees. It stands to reason that more ESOP conversions would provide employees the potential for wealth creation. What's more, additional policy incentives for firms that mostly employ minorities could be a counterbalance to wealth inequality, which has increased greatly in recent decades, even more than income inequality.<sup>76</sup> A 2013 study by the Urban Institute showed that blacks and Latinos tend to have far less wealth than whites, and the disparities have only grown in recent years. In relative terms, blacks and Latinos lost more wealth than whites during the Great Recession.<sup>77</sup>

### INCLUSION IN WORKER COOPERATIVES

In recent years many of the new cooperatives are formed by immigrant women of color in segments of the domestic work industry: cleaning, childcare, eldercare, and care for those with disabilities. At Si Se Puede, a housecleaning cooperative based in the Brooklyn neighborhood of Sunset Park, members enjoy relatively high wages and consistent working hours. The work is physically demanding, according to Alicia Chavez, the current President of Si Se Puede. But the cooperative has given members greater control over their conditions of work, including the kinds of cleaning products they use. The co-op makes its own non-toxic, ecologically friendly cleaning solutions, ensuring lower levels of exposure to harmful chemicals that, over time, can exact a serious toll on the health of those working as housecleaners.<sup>78</sup>

Involvement in the cooperative has also endowed many members with skills and a sense of empowerment that carry over into their lives outside the cooperative. After years of tiring work as a housecleaner, Chavez says that she is laying the groundwork for her next act. She and several other colleagues have been developing plans for a new catering cooperative; the skills and experience they have built up while working for Si Se Puede have been enormously useful in drawing up a blueprint for the organization and developing a business plan.<sup>79</sup>

The recent emergence of cooperatives such as Si Se Puede and others like it mirror broader developments in the world of worker organizations. As seen in the union movement<sup>80</sup> and the rise of worker centers<sup>81</sup>, significant organizational growth is occurring among immigrants, women, and

people of color. There is increased interest in cross-fertilization among different kinds of organizations pushing for worker empowerment, and this is certainly true among organizations operating in the domestic labor industry and others where workers experience very acute forms of social exclusion and marginalization.

Domestic workers are overwhelmingly women, and this is an important reason why this work is devalued. Race has also played an important role in shaping conditions within the domestic work industry. In the 1930s, Southern Democrats fought successfully to exclude farm workers and domestic workers from coverage under the National Labor Relation Act (NLRA), which continues to regulate the formation of unions in the US. Large numbers of Southern black workers were employed in these sec-

tors, and unionization would have enabled them to build power.<sup>82</sup> In the shadow of this racialized history, worker cooperatives can be seen as an alternative way in which domestic workers have been able to mobilize collectively to improve their working conditions.

Cooperative organization is an important means through which people facing social exclusion have been able to assert some measure of individual agency and collective power. Together with other kinds of efforts and interventions, it holds potential for helping to transform the conditions of those who currently work and live at the margins of American society.

# The Cleveland Model:

## A bold experiment in worker ownership starts to pay off

**THE WORKER-OWNED** Evergreen Cooperative Initiative in Cleveland, Ohio was launched in 2008 by a group of community stakeholders to address a persistent problem that plagues many older industrial cities. Where major medical, educational and cultural institutions are thriving, the surrounding neighborhoods are failing and have been for decades. University Circle on the East Side of Cleveland is one such place. Within walking distance of University Circle – which has the fastest rate of job growth in Northeast Ohio, according to *Crain’s Cleveland Business* – there are abandoned homes, failing schools and high crime rates. This is true of similar areas around the country known as “Eds and Meds” districts, including Baltimore, St. Louis, Pittsburgh, Detroit and others. “Legacy” institutions continue to anchor Eds and Meds districts long after wealthier people moved to the suburbs while the surrounding urban neighborhoods steadily decay.

This is not a new story, but an innovative approach to worker ownership is poised to change the narrative. The co-ops that comprise Evergreen’s three businesses – a laundry service, a sustainable energy provider and a greenhouse – together have become known as the “Cleveland model.” Led by a group of Cleveland-based institutions (including the Cleveland Foundation, the Cleveland Clinic, University Hospitals, Case Western Reserve University, and the municipal government), the mission of Evergreen has been to connect the surrounding low-income neighborhoods – with a median household income below \$18,500 – to the thriving innovation economy of University Circle. Hundreds of millions of dollars are spent annually by these institutions on goods and services and yet very little of it stays in the community.

Many economic development programs have come and gone, but none of them have attempted to bridge the wealth gap through worker ownership. Most programs rely on a trickle-down strategy of tax breaks and subsidi-

dized loans for small businesses, which tend to benefit people who already know how to navigate the system. Job training programs focused on low-skill workers are the norm because they are relatively easy to fund but the results are spotty at best. The “Cleveland model” flips these approaches on their head. Rather than training people for jobs that may or may not exist, the Evergreen Cooperative Initiative is designed to create jobs within a worker-owner cooperative structure, and then recruit and train local residents to fill those jobs. The idea is to provide both employment *and* wealth building opportunities without putting the burden on every person to be their own entrepreneur.

Creating a local economy from the ground up, however, turns out to be a complex endeavor, **requiring a lot of hard work, patient investment money and continuous innovation**—all the while keeping an eye on the prize: profitability. Because first you have to create wealth in order to share it.

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**THE MEDIA LOVE** an innovation story, and Evergreen Cooperatives delivered an innovation story with a heart. A plethora of positive coverage – from the *Huffington Post* to *Time* magazine – had the unintended consequence of creating unrealistic expectations among co-op workers, its funders and the larger cooperative community that was watching Evergreen’s development carefully. Behind the scenes, however, Evergreen’s startup businesses were struggling mightily.

The first enterprise to be established, the laundry service, was opened on the basis of what everyone now understands was an unrealistic business plan. Of course, most startups would probably never get off the ground were it

not for a high degree of optimism. But that was just the beginning of a years-long struggle to stabilize what seemed like a slam-dunk: providing laundry services to the major hospitals in the area. But the hospitals were already committed to contracts and weren't inclined to dissolve them to send business to an untested laundry service. Indeed, in its first few years, no one on staff had laundry service experience, including consultants who cycled in and out.

Shortly after the laundry service was started, Evergreen launched the solar panel installation business. This enterprise has gone through several iterations and name changes, as the solar industry has been very volatile. To supplement the solar panel installation business, workers began rehabbing and weatherizing homes, an important and much-needed service but not necessarily a profitable one. What's more, it was seasonal and resulted in layoffs in the wintertime, which did not fit with Evergreen's core values.

Before the laundry and energy enterprises were stabilized, a third business was launched – Green City Growers – a large-scale greenhouse that required significant upfront investment. Opened in early 2013, the 3.25-acre hydro-



Candra Avery hadn't worked in four years when she got a job at Evergreen Cooperative Laundry. She recently got a raise and promotion. (Photo: Lisa Chamberlain)

ponic facility is close to capacity. But even at full capacity, profit margins are expected to be razor thin primarily due to enormous energy costs. Management has looked into employing its sister solar installation business to address the energy cost issue but that requires additional investment that will take time to pay off. Like any business, there are only so many issues that can be tackled at once.

"I always talk about how we did things out of order," says John McMicken, who started at Evergreen in 2011 as a consultant and later became CEO. "We started cooperatives without any attention paid to matters such as governance. The board wasn't formed until 2011 and didn't come together until 2012, years after the businesses were formed. There was a lack of financial oversight and accountability among those business units. If you really looked behind the curtain, it would be tough for anyone to honestly say these businesses were sustainable. I would not have opened the greenhouse when we did but it was already in motion when I came on board."

As the first CEO, McMicken recommended taking a big step back to straighten out a lot of the issues that had been neglected, such as setting up a proper 501(c)(3) non-profit corporation to oversee all three businesses, creating a board, and addressing management and accounting issues. "All of that work got done," says McMicken, "which was immensely important." The next step – arguably the most important one – was getting profitable, which the laundry service and the energy company have both achieved (more on that later). The greenhouse, the newest of the three businesses, is close to capacity and experimenting with higher margin micro-greens, but it is not yet breaking even and McMicken is careful not to overstate the greenhouse's potential for profitability.

**"For years people didn't realize we weren't profitable,"** says McMicken. "There were all these glowing articles and everyone was getting paid. Consultants were coming and going. It really was a disservice to the workers. They didn't understand why so many changes needed to be made and made quickly."

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**THE WORKERS WHO** have been around the longest have been deeply affected by the struggle and change—but are now seeing some modest payoffs. Tim Coleman has



An Evergreen Energy Solutions team installs LEDs in a Cleveland Clinic parking garage, saving money and reducing energy consumption. (Photo: Lisa Chamberlain)

worked at the laundry service since 2010. His primary job is as a trucker driver, picking up and delivering laundry. From the beginning, though, he has done almost every job in the laundry facility, including coordinating the other truck drivers and their schedules. He had been doing that job informally for some time, which was only recently made official with a promotion and a raise.

**“We volunteered a lot of time,” says Coleman. “Me and a few others. The Cleveland Foundation was very helpful. They kept the doors open.** We had to work on different machines. We had to spend so many hours just to keep things flowing. We would take no lunch break. They couldn’t pay us more than 80 hours every two weeks.”

The laundry business is the most stable of the three enterprises, says McMicken, due to a number of factors. A manager with laundry experience now runs the plant, and the skill level of the workers has improved dramatically over time, with people like Coleman getting promoted and helping to streamline a business they now understand

like the back of their hand. Most importantly, they finally landed a big contract with University Hospitals.

Coleman – who came to Evergreen through an employment agency that works with ex-felons, as have most of the employees – became a homeowner through a program sponsored by Evergreen that promotes neighborhood revitalization in the University Circle communities. He was able to buy a fixed-up house in the neighborhood where he grew up at below market rate and will be able to pay it off in five years. He lives there with his wife, who works at the greenhouse. Coleman is eager to share pictures on his phone of his house filled with kids and grandkids.

“That’s the American dream, to pay for your own home!” says Coleman. “The whole program overall, it’s a blessing. We have people in the neighborhood, they couldn’t pay rent here but now they go owning their own home. It’s like you’re a part of something. It’s your neighborhood, you’re a home owner, making money. Once you do a good job, you get more customers and bring more jobs in. It’s like a ripple effect.”

When asked about how things have changed, Coleman says he kind of misses the early days when it was smaller and felt more like a family. He is one of the workers who is on the co-op board, but it only meets once a quarter, as opposed to every week the way they used to run things. The new manager who brought his background in laundry service to the facility is improving operations but doesn't ask for much input.

Candra Avery, who also works at the laundry service, expresses a similar sentiment. She hadn't held a job in four years when she heard about Evergreen through a friend of her father's who worked at the plant. Candra was called in to help when a third shift was added, and she has been working there ever since. Like Coleman and other workers who were interviewed, she expresses enormous gratitude for being given a chance. She recently got a raise and a promotion and hopes to qualify for the homeownership program.

But like any job, she can't help but notice how things could be done differently. She says the volume they are expected to produce is sometimes more than the machinery can handle, which breaks down and they end up doing a lot of things by hand. "At first, it made you feel like you were a part owner," says Avery. "It doesn't feel like that now. They make decisions and just do it. When they make big changes, like with the machinery, they don't talk to us. We have ideas about what we need before we do something else."

While Avery is quick to add that she has benefitted enormously from her job, the bigger issue for her is that the workers are supposed to get bonuses. So far there have only been two profit-sharings—both of which were in 2014, six years after Evergreen's initial launch.

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**OF THE THREE** enterprises, McMicken is **most excited about the potential for the energy service business, Evergreen Energy Solutions, to reap the highest profits.** Despite a rollercoaster ride through several iterations – solar installation, home improvement, weatherization projects – he believes they have found the right fit for Evergreen: replacing outmoded lighting with LEDs. Major institutions across Northeast Ohio can save a lot of money by switching to energy efficient and long-lasting LED bulbs, particularly in parking garages.

Evergreen Energy Solutions has developed a green energy fund that allows institutions to pay for the service over time, rather than requiring an upfront investment. Evergreen swaps out the lighting fixtures and the institution or company pays for that work from money saved on lower energy bills, which takes an estimated six years to pay off. The fund replenishes itself as more jobs are completed and the initial investment comes back to Evergreen. What's more, there is an almost unlimited amount of business. With the laundry service and especially the greenhouse, there are four walls and roof that constrain production. Retrofitting LEDs, however, is only limited by the number of lights that need replacing. The jobs this creates range from low-skill bulb replacement to higher skilled carpentry and electrical work, as well as crew leadership positions. The latter is what DiCarlo Johnson does.

"I'm a worker owner and a crew leader," says Johnson, who also bought a house through Evergreen's homeownership program. "I have a lot of responsibility being in that position. They want me to keep track of hours, and assist so we don't go over budget. I run the crew, so I map our scope of work for the day—make sure we get done what we need to do."

As the LED business has taken off, Johnson spends the majority of his time in parking garages, but he started with Evergreen using his carpentry skills—first to install solar panels and then rehabbing houses. He's most proud of having rehabbed 30 abandoned houses on a single street. "Initially the street looked like a war zone," says Johnson. "People to this day drive up and down the street and come to us and thank us. We brought a lot of value back to the neighborhood. And my skills have definitely been sharpened up as far as construction goes, and electricity. My skills went from ten to a hundred."

When asked if there is anything he would like to see change, he says there's a lot of on-the-job training he has to do that slows things down. It would be better if there were a pre-training program people went through before they were placed with a crew. But Johnson is quick to add that overall, things are moving in the right direction.

"When I first started, we were still very new. We were sinking a lot. They kept us in the loop. We knew we were losing money. A lot of people are supporting the cooperative. They got our back. If it's a short month they help

out. They are protecting their investment. They might need to make changes, but they don't want it to fail."

Perhaps in the rarified world of the tech industry funded by venture capital, failing early and often is considered a good thing. But as Johnson points out, that is not really an option when institutions and foundations have made such an enormous investment as they have in the Evergreen Cooperative Initiative. That is why the upfront decisions and organizational structure are so important. Given all the mistakes that were made from the outset, the fact that two of the three Evergreen enterprises are experiencing modest profits and stability after six years is an indicator that the model is replicable on a shorter timeframe and with fewer losses.

"At our first profit-sharing event in 2014," says McMicken, "we distributed \$60,000 to 25 people. The average pay-rate for most of those employees is \$15 an hour. **Folks that had been around since day one got \$3,000 each, a ten percent bonus. Boy did that go a long way for morale,** especially the original employees who were skeptical about why we were making these changes. It was an amazing event."

The greenhouse employees, unfortunately, have not been able to reap any profits yet, and McMicken and the greenhouse manager are still trying to figure it out—be it working with the power company to lower their energy bills, switching to higher profit greens, and even looking at expansion. Built on ten acres of de-industrialized land in the middle of one of the poorest neighborhoods in Cleveland—about five miles from University Circle—the greenhouse is a highly visible symbol of revitalization. Seeing it fail would be demoralizing and a huge financial loss, to the tune of \$17 million in construction costs alone. But as one of three enterprises, it can't be allowed to sink the whole ship, either. At the end of the day it has to turn a profit or it simply doesn't fulfill Evergreen's mission.

"We look at this as what they are, small for-profit businesses," says McMicken, "We've met with a fair number of wins and several failures and major hurdles—not unlike other small for-profit startups. There's nothing really experimental about it. We're all working as hard as we can to accomplish the original mission to be profitable so that we can share that profit. It's a different end goal but to get there much of the pieces are the same."



Built on ten acres of de-industrialized land in the middle of one of the poorest neighborhoods in Cleveland, Green City Growers greenhouse is a highly visible symbol of revitalization

## **PART 2:**

# Expanding Worker-Ownership

## CHAPTER FIVE:

# The Current Landscape of ESOPs and Co-op

In order to understand how to expand ESOPs and co-ops, it's important to know where we are now. Where are they located? What are the legal, cultural and socioeconomic circumstances in which co-ops and ESOPs form more easily? In this chapter we will take a look at the current landscape before tackling the questions about how to create, convert or scale-up worker-owned firms.

The distributions of ESOP firms and worker cooperatives across the United States are weakly correlated, bearing little resemblance to one another. The differences in these patterns can be seen in Figures 9 and 10, which map out by the state-by-state variation in the density of ESOPs and worker cooperatives relative to the overall distribu-

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These patterns underscore the importance of local and regional ecosystems in the development of worker cooperatives.

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tion of firms across different states. This relative measure provides us with a sense of whether worker cooperatives and ESOP firms are “underrepresented” (values below 1) or “overrepresented” (values below 1) in a given state. Darker shades represent higher concentrations and lighter shades represent lower concentrations.

Looking at the distribution of ESOP firms, we see substantial variation. At the upper end of the distribution,

there are four states where the number of ESOPs is more than twice what we would expect given the total number of firms in the state: Iowa, Hawaii, Minnesota, and North Dakota. Overall, we see a number of Midwestern states with relatively high concentrations of ESOPs, though this is certainly not a uniform pattern. The states with the lowest relative concentrations of ESOP firms are Delaware, Florida, Rhode Island, and Nevada.

We see even greater differences across states in the relative concentrations of worker cooperatives. The “coefficient of variation,” which measures relative variation, is significantly higher for the co-op distribution than it is for the ESOP distribution.<sup>83</sup> In other words, co-ops tend to cluster in certain areas more than ESOPs. There are seven states in which the concentration of cooperatives is more than twice what we would expect given their share of firms overall. In Vermont, cooperatives are overrepresented by a factor of nearly thirteen, and, in Massachusetts, they are overrepresented by a factor of nearly five. Regionally, we see relatively high concentrations in the Northeast region and on the West coast.

There is a limitation to using the distribution across states as a measure of geographic variation, as it misses the local clustering that is a key feature of the worker co-op landscape. In California, 53 of the 62 worker cooperatives that responded to the USFWC survey are in San Francisco, with several more located in the Southern part of the Bay area. In New York state, 25 of the 33 cooperatives are in New York City. In other words, more than one-fifth of all U.S. cooperatives that responded to the survey are in San Francisco, and one-tenth are in one of the boroughs of New York City, with a particularly high concentration in Brooklyn. These patterns underscore the importance of local and regional ecosystems in the development of worker cooperatives.

## MAPPING THE INDUSTRY LANDSCAPE

Unlike the landscape of variation across states, we see somewhat greater industry variation among ESOPs as opposed worker cooperatives. Looking again at the distributions of ESOPS and co-ops relative to the distribution

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The picture that emerges generally seems to fit with the previous findings that ESOPs tend to be more prevalent in market environments that place a higher premium on human skill and ingenuity.

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of firms in general, we see a slightly higher “coefficient of variation” among ESOPs.<sup>84</sup> The categories displayed in Figures 11 and 12 are based on the North American Industry Classification System (NAICS). Calibrated at the “one-digit” level, these are broad industry groupings.

ESOPs are overrepresented among utilities by more than a factor of 10 and in managerial, manufacturing, and finance and insurance companies by more than a factor of 4. The picture that emerges generally seems to fit with previous findings that ESOPs tend to be more prevalent in market environments that place a higher premium on “human skill and ingenuity.”<sup>85</sup> In these kinds of settings, employers have an incentive to incentivize—more specif-

ically, to link employee compensation with firm performance, thereby spurring employees to boost their own productivity. Looking at the industry distribution of ESOPs, we see that, apart from wholesale trade, low-productivity services are clustered toward the bottom of the distributin.

As with the geographic distribution, is it important to note that proceeding at such a high level of aggregation can obscure important patterns from view, including the variation that exists within these industry groupings. For example, while ESOPs tend to be overrepresented in the manufacturing sector by nearly factor of five, there is wide variation across different kinds of manufacturing firms. “Other electrical equipment and component manufacturing” are overrepresented by a factor of nearly 34, while “electric lighting equipment manufacturing” firms are overrepresented by just a factor of 1.6.

The overall distributions of worker-owned firms should not be seen as completely settled, or simply the product of what is “efficient.” Institutional processes such as the copying of successful models can also play an important role in explaining the high density of worker-owned firms in certain parts of the economy. In recent years, for example, there has been a notable surge in the development of cleaning cooperatives that service homes, offices, and sometimes both. This new wave of cleaning co-ops has been inspired in important ways by the Prospera group of cooperatives in the Bay Area (formerly known as WAGES), and it is the biggest reason why co-ops are now overrepresented in the administrative and waste collection sector. Storylines such as this are not unusual. Indeed, the patterns identified above provide a snapshot of the current landscape of worker-owned firms, but this picture is continually being remade by many factors including the initiative of people who are interested in charting new paths of economic development.

## CHAPTER SIX:

# Three Ways to Grow The Co-op Movement

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Broad-based worker-ownership can bring a range of benefits. As shown in previous chapters, it can serve as a basis for building wealth and strengthening job security, expanding voice at the workplace, and promoting the inclusion of people who are socially and economically marginalized. Perhaps most importantly, worker co-ops and ESOPs create economic development opportunities for whole communities by retaining wealth at the local level.

How might these potential benefits be extended to more people? This chapter discusses ways to expand worker-ownership: start-ups, expansions and conversions (see Figure 13). Understanding the differences between these paths is important in particular instances where people interested in worker-ownership are considering the options at hand. The goal is to clearly delineate different paths to expansion, while outlining the factors that tend to lead down one road or the other, and clarifying the tradeoffs that may be involved. For funders of worker cooperatives and ESOPs, understanding these pathways is critical to evaluating potential grantees.

The University of Wisconsin Center for Cooperatives has posted “Guidelines for Cooperative Bylaws” on its website: [www.uwcc.wisc.edu/info/bylaw.html](http://www.uwcc.wisc.edu/info/bylaw.html)

### 1. STARTING UP

Most worker cooperatives are created from scratch. Typically the decision involves an interest in forging greater economic independence and security, which may be coupled with a desire to create a more democratic work environment. For many of those who have started their own worker cooperatives, developing an organization imprinted with the collective values and aspirations of the group is an experience that brings its own intrinsic rewards.

Deciding exactly how to build an organization that ex-

presses the value of the group is a critical first step. Should decisions be made by consensus or through majority rule? What should be the mix of direct and representative democracy, and of democracy and more traditional managerial procedures? How should new members be incorporated? Even though many worker cooperatives are launched by groups of people who already know each other quite well, establishing a set of cooperative by-laws that clarifies and formalizes basic rules, procedures, and matters of organization is important.<sup>86</sup> (See Appendix for more on the four approaches to worker-owner management.)

We see several factors as essential in starting new worker-owned cooperatives:

- **Understand the economics of developing a viable business.** Raising capital is one basic and essential requirement. However, according to David Hammer, President of the Boston-based ICA Group, a consultancy that supports the development of cooperatives and community-based enterprises, focusing on capital needs without developing a viable business plan is a common mistake.<sup>87</sup> ICA has worked with many groups of people interested in launching worker cooperatives, providing assistance in business planning and conducting market analysis and feasibility studies.<sup>88</sup>

In developing a worker cooperative, the choice must also be made about what kind of business entity is being formed in legal terms. There is a range of different ways in which cooperatives can incorporate. Generally, however, the choice is between forming as a cooperative corporation or a limited liability corporation (LLC). As described in a website focusing on co-op law developed by Bay Area-based Sustainable Economies Law Center and Green Collar Communities Clinic, “the cooperative corporation has the ideals of ‘one member, one vote’ embedded in its DNA.” Forming as an LLC provides greater flexibility,

including with respect to prevailing employment law. It allows for a situation in which co-owners to not pay themselves a minimum wage in the initial startup phase of the company.<sup>89</sup> But this flexibility also means that new members can more easily change the identity of the organization when they join.<sup>90</sup> For a fuller understanding of various organizational structures, see footnote.<sup>91</sup>

Section one of this report presented evidence suggesting that worker cooperatives do not fail at a higher rate than conventionally structured firms. But *any* new business faces significant risks. These risks never go away, of course, but they tend to be more acute at the outset before tapering off over time—a dynamic that has been referred to as the “liability of newness.”<sup>92</sup> In the context of a worker cooperative where members usually have their own “skin in the game,” and often do not have much to fall back on, this potential for failure warrants serious consideration.<sup>93</sup>

While the risks of starting a new business are real, those who wish to start worker cooperatives do not have to face them in isolation. New worker cooperatives often replicate or emulate other models, sometimes with direct advice or assistance from cooperatives that have achieved success in the same industry, and incubating organizations. Many of the cleaning cooperatives that have emerged around the country have drawn inspiration from the Prospera Group of co-ops in the California Bay Area (formerly known as Women’s Action to Gain Economic Security, or WAGES).<sup>94</sup> There are also several homecare cooperatives that have been modeled after Cooperative Home Care Associates, including some that the Paraprofessional Healthcare Institute (PHI), a research and development organization founded by CHCA, had a strong hand in developing.<sup>95</sup>

From a larger strategic standpoint, a critical set of questions that arises in the context of efforts to form a start-up co-op, a primary one is how small cooperative enterprises achieve scale.

- How can the benefits of working in a cooperative be extended to greater numbers of people?
- And, even in cases where many cooperatives are being launched in a given industry or geographic area, with total membership numbers that are significant, how can a collection of small enterprises exert the kind of power that helps to transform broader market dynamics?

One approach is the formation of federated structures that

bring together a group of cooperatives under a common umbrella while still enabling them to maintain their distinct identities and function as separate enterprises. Mon-

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While the risks of starting a new business are real, those who wish to start worker cooperatives do not have to face them in isolation.

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dragon in the Basque country of Spain, the world’s largest cooperative enterprise, is an oft-cited case in point.<sup>96</sup> One noteworthy feature of the Mondragon system is that members of co-ops that go out of business are often able to find jobs in other co-ops within the system.<sup>97</sup>

In the US, there are cooperative groups that, while operating on a much smaller scale than Mondragon, allow small cooperative organizations to be part of something bigger. Prospera is a good example of this, as is another Bay Area set of businesses, the Arizmendi group of bakeries.<sup>98</sup> In addition to providing technical assistance on various aspects of business development, these groupings have allowed co-op members to speak with a more powerful voice in the public domain.

## 2. SCALING UP

Distinguishing between starting up and scaling up becomes important when thinking about questions of strategy and resource allocation. If one is trying to extend worker-ownership to as many people as possible, does it make more sense to launch a set of new enterprises or try to expand on existing ones? In practice, of course, the lines are not so hard and fast. Generally, clusters of cooperatives are started in the hopes that at least some will be able to expand over time, perhaps absorbing workers from less successful enterprises. And, as suggested above, larger cooperatives or cooperative federations often play a role in launching new cooperatives, as in the case of CHCA.

Still, scaling up an existing business or set of businesses may come at the expense of launching a set of new ones. The Evergreen Cooperatives sheds light on some of these issues in the case study on page 21.

There are many potential benefits to scaling up. Presumably, this is done once a business has already navigated the more precarious early phase of its development. Often, increasing the size of the business makes it possible to take advantage of economies of scale, boosting efficiency and potentially increasing the returns that come back to worker-owners. Increases in size can also enable a worker-owned enterprise to spread its benefits to a larger num-

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Scaling up includes greater numbers of people in the economic benefits of a cooperative organization, even as it generally narrows, in relative terms, the circle of deep democratic engagement.

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ber of people, and, potentially, to wield greater influence in shaping broader market dynamic.

Creating federated structures and other kinds of cooperative groupings can be helpful in achieving impact at a larger scale. But scaling up within the context of a single, unified firm can bring added benefits. Some of CHCA's more innovative programs in scheduling and other areas are premised on having a sizable, integrated workforce. It has also leveraged its size to become a recognized thought leader not just in the cooperative movement but in the homecare industry and beyond, with a workforce development approach that has garnered widespread attention.<sup>99</sup>

Scaling up brings its own set of challenges. Established members have often sunk a great deal of time and money into the organization. The question then becomes, how to

make this initial investment fair and equitable when new members are brought on? Many cooperatives establish a buy-in period whereby new members pay for their share in the company over a period of time.<sup>100</sup> Even then, for mature cooperatives and those in capital-intensive industries, the costs of a share in the company can become prohibitive, effectively preventing all except those with significant economic means from becoming members.

Internal capital accounts help to address this problem. Developed as part of the Mondragon model, U.S. worker cooperatives began to adopt internal capital accounts in the 1980s. Under this system, the value of shares remains the same over time and dividends or profit distributions are allocated into individualized accounts. This makes it easier for new members to join while accounting for differing levels of time and investment in the enterprise.<sup>101</sup>

Scaling up can also raise concerns around issues of governance and organizational identity. Are new members compatible with the established ethos? And is the organization ready to adapt in order to fully include all its members? Apart from addressing possible new membership tensions, there are often questions about the degree to which increases in size will allow the organization to retain its democratic character. Organizations may be slow to change due to inertia. But, for democratic worker-owned firms that are considering the prospect of scaling up, there can be real intention behind the resistance to change, even in cases where it makes good sense economically. As organizations that do not just have a single bottom line, placing intrinsic value on democratic participation and, potentially, other objectives, the considerations are more complicated.

These competing aims often bring cooperative enterprises to a crossroads. The demands of effectively running a larger organization that turns greater profit and brings in more members may press in the direction of more representative rather than direct democracy, and shift from flatter decision-making structures to greater managerial hierarchy. Such changes might be understood as an evolution in the democratic character of the organization rather than a complete break with tradition. However, it might not feel that way to people who founded or joined an organization precisely because of its close-knit, participatory dynamic. Workers at the Cleveland Evergreen Cooperative articulated this dynamic in the case study on page 21.

Of course, even assuming that the members of a cooperative wish to scale up, there are still questions around how to do so successfully. So how did Cooperative Home Care Associates, by far the country's largest worker cooperative enterprise, successfully navigate this transition? Established in 1985 with twelve founding members, CHCA now has 2,400 workers, of whom around 1,700 are members. CHCA has quadrupled its workforce over the past 12 years and aims to double the size of its current workforce in years to come.

According to Michael Elsas, CHCA's current chief executive officer, the organization's structure has been designed for growth. Members elect a board of directors who officially have hiring and firing authority over the CEO. But, in day-to-day operations, significant power is vested in the hands of Elsas and other managers. This has allowed the managerial team to make quick decisions in response to changing market conditions, and to guide the organization through a process of growth.<sup>102</sup>

Another key factor, according to Elsas, is that CHCA figured out its business and expansion strategy and then went about creating an ecosystem that would help to achieve it. Together with PHI, the research and training organization that it founded in 1991, CHCA spun off a managed care company, Independence Care System (ICS), in 2000. CHCA had decided to focus its attention on managed care for people living with disabilities, a segment of the market regarded as undesirable by most other industry players. This type of care is funded by Medicaid, and federal regulations require oversight by a certified managed care agency. In creating ICS, CHCA and PHI sought to ensure the co-op's ability to secure contracts with an organization that was in tune with its values and objectives. Today, CHCA obtains 60% of its business through ICS.<sup>103</sup>

Those who work as CHCA caregivers enjoy a number of advantages over their counterparts working for most other employers in the industry, including strong training, relatively good health benefits, and the "guaranteed minimum hours" policy program. At the same time, most members are not deeply engaged in the democratic life of the organization. Around 1,700 of CHCA's 2,400 eligible employees are members, and, of these, only 200 to 300 participate in voting to elect the board of directors.

CHCA's experience, as well as Evergreen's, bring into focus some of the tradeoffs that are often involved: scaling up in-

cludes greater numbers of people in the economic benefits of a cooperative organization, even as it generally narrows, in relative terms, the circle of deep democratic engagement. =

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Often, increasing the size of the business makes it possible to take advantage of economies of scale, boosting efficiency and potentially increasing the returns that come back to worker-owners.

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### 3. CONVERSION

While most worker cooperatives are started up by groups of people who wish to own and control a shared enterprise, most ESOP firms are established by a set of existing owners who want to spread ownership to a broad base of employees. There are a variety of reasons that majority owners might decide to do this—some having to do with their own self-interest, and others having to do with a concern for the welfare of employees. Opportunities for conversions of firms to employee share ownership plans have grown with recent demographic trends—namely, the fact that many baby boomers have reached the point of succession planning.<sup>104</sup> There are significant tax advantages to a conversion, as opposed to an outright sale.<sup>105</sup>

One of the chief benefits of going through a conversion process is that, in most cases where such a move is contemplated, there is already a successful business in place. In many cases, the business has also managed to achieve significant scale. Conversions can also provide an opportunity to extend worker-ownership into industries where it might otherwise be difficult to gain a foothold.

The challenges that accompany conversion to worker-ownership depend a great deal on how deeply the organization is being transformed. In instances where an ESOP is established simply as a benefit plan, there may be little

that needs to be adjusted organizationally. In cases where there is a desire to create mechanisms of participation and to develop a culture of ownership, the adjustment will be more significant. Finally, changing the managerial and governance structure so that it involves broader-based participation in how the organization is run requires even deeper transformation of the organizational structure and a shift in the basic power relationships governing the firm.

Examples of conversions to a democratically structured ESOP include firms such as MBC Ventures and others in which the United Steel Workers have had a hand. There are also examples of full-fledged cooperative conversions, and there is a growing interest within the worker cooperative community in pursuing conversions as an approach. A recent tally by the U.S. Federation of Worker Cooperatives counts 38 worker cooperatives in the U.S. that were formed through conversions.

Isthmus Engineering in Madison, Wisconsin, is one such a company. Specializing in industrial automation, the firm began as a partnership of three people, and it has now grown to a worker cooperative with fifty workers. Isthmus built a worker cooperative out of its partnership structure during the early stages of scaling up. All members, who have a variety of educational and professional backgrounds, serve on the company's board of directors. Isthmus is also noteworthy for the degree to which a broad range of workers are involved in the design of engineering processes.<sup>106</sup>

There are also cases in which workers have mounted takeovers of businesses after existing owners have decided to shut down operations. In December of 2008, shortly after the onset of the global financial crisis, the management of Chicago-based Republic Window and Doors announced that it could no longer pay its loans and would be closing down its operations. The company's 250 workers were fired, told they would not be compensated for accrued leave, and advised that they would lose their health insurance coverage within two days.<sup>107</sup>

What happened next became national news. Republic workers, members of the United Electrical, Radio, and Machine Workers of America (UE), staged an occupation, demanding compensation and the opportunity to keep the factory open under the new ownership.<sup>108</sup> Within a week, the company's creditors had set up a fund to provide workers with severance, back pay, and two months

of health insurance. By February 2009, California-based Serious Metals announced that it would be taking over the company.

Three years later, however, in February 2012, Serious announced that it would be shutting down the factory. This time, a group of remaining workers decided to take matters into their own hands, negotiating to buy the factory's equipment themselves. By May 2012, they reopened as New Era, a worker cooperative with a flat compensation structure and equal decision-making rights for all its members.

At each step along the way, the group of people involved in this effort has received support from the UE as well as The Working World, an organization inspired by cooperative

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One of the chief benefits of going through a conversion process is that, in most cases where such a move is contemplated, there is already a successful business in place.

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movements in Latin America that now provides assistance to co-op development efforts throughout the Americas. The Working World played a key role in mobilizing the capital necessary for the workers to purchase the factory equipment.

Today, the 15 workers at New Era are immersed in the hard work of running a business. There are never any guarantees, but significant energy is being poured into securing additional clients. In the process, they have raised larger questions about what might be possible when groups of working people push back against business as usual. “Everyone can participate in building the economy we all want,” the co-op states on its website, “and no one should be treated as temporary or just raw material for someone else's business.”<sup>109</sup>

## CHAPTER SEVEN:

# The Supporting Infrastructure for ESOPs and Co-ops

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The surrounding environment plays a crucial role in shaping decisions about how exactly broad-based ownership is pursued, and whether it is contemplated in the first place. As we saw in chapter five, the landscape of worker-ownership varies in significant ways geographically and by industry.

We can start with the dictum, “institutions matter.” Institutions include the formal and informal rules that govern economic activity.<sup>110</sup> The formal rules tend to be enforced by governments. In a broader sociological sense, institutions also include conventional understandings of how business is conducted, and normative views on how it ought to be pursued.<sup>111</sup>

We then need to overlay on this institutional structure an understanding of the organizational landscape—not just worker-owned firms, but the larger set of organizations that can play a role in supporting their development.<sup>112</sup> Finally, we can add networks of interpersonal interaction—again, not just the interactions that occur within worker-owned enterprises, but the broader sets of social relationships in which they are embedded.

The relations among institutions, organizations, and social networks are complex. Organizations and people are constrained by institutions. Over time, however, they can also mobilize in ways big and small to act creatively within existing institutions, and, in some cases, to press for meaningful institutional change. We can think about local and regional ecosystems as structured but evolving social-institutional frameworks.

### GOVERNMENT

Government is clearly a key player in setting the terms under which economic activity takes place, including what does or does not happen in the area of broad-based work-

er-ownership. For the present purposes, we can focus on two basic dimensions of the role that government plays. First, it establishes and enforces the basic legal-institutional frameworks in which economic activity occurs.<sup>113</sup> Second, it can marshal resources in ways that support certain kinds of economic activities and ways of doing business over others.<sup>114</sup>

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But many who are engaged in the world of worker cooperatives suggest that providing resources, more so than enabling legislation, would be more effective in terms of growing the cooperative movement.

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Thinking about the role of government in establishing formal rules, much of the action does not occur at the local or regional but rather the federal level. Rules governing the formation of ESOPs are a good example. ERISA provided a legal architecture for the establishment of ESOPs that was and remains largely uniform nationally, despite some relevant state-level differences in tax treatment. There are no doubt important reasons why the density of ESOP firms varies geographically, but legal variation across states and localities do not seem to be a significant cause.

State governments have played a role in mobilizing resources for ESOP development, and there are examples

of states where such support appears to have made a difference. In Ohio, the state government has helped to fund the Ohio Employee Ownership Center (OEOC) at Kent State University, which supported the development of numerous ESOPs throughout the state, including many that have come with significant governance rights for employees.<sup>115</sup> Partnering with the Democracy Collaborative in Maryland, the OEOC was also a key partner in the development of the Evergreen Cooperatives.

Additionally there are some cases where cities have played a strong and additive role.

- In August 2015, Jerry Brown, Governor of California, signed a bill into law to facilitate the creation of worker-owned cooperative businesses in California. The new law, Assembly Bill 816, will remove unnecessary barriers to the creation of new worker cooperatives in California and improve operations for some existing worker cooperatives.
- On June 23, 2015, the New York City Council approved a second year of funding for the Worker Cooperative Business Development Initiative, expanding its commitment to support cooperative businesses that are owned and controlled by residents of New York City. The current funding for \$2.1 million is a 75% increase over last year's grant of \$1.2 million, and follows supportive legislation passed in March requiring the city's economic development arm to track municipal support of worker cooperatives.
- Beginning this year, the city of Madison, Wisconsin will invest \$1 million per year for five years in establishing new worker-owned businesses, commonly known as worker cooperatives.

The legal architecture is much more variable across states for worker cooperatives versus ESOPs. The first state in the U.S. to implement a statute devoted explicitly to the formation of worker cooperatives was Massachusetts. It was drafted by David Ellerman and Peter Pitegoff, who, at the time, were both based at the Boston-based Industrial Cooperative Association, which later became the ICA Group. ICA has been a critical to the formation of new cooperatives.

Many other states have since adopted similar laws that explicitly provide for the development of cooperative corporations, including several New England states, New York, and California.<sup>116</sup> States including Wisconsin, Minnesota, Iowa, and Tennessee have established more flexible

cooperative status that draw on aspects of limited liability company law.<sup>117</sup>

What is the impact of legal provisions that explicitly allow for the development of worker cooperatives? Such provisions can make cooperative development easier, in part by providing greater clarity for people who wish to form cooperative enterprises as well as law firms, banks, and other organizations that may be involved in the process. They can also serve a legitimating function that may lead more people to consider forming and supporting the formation of worker-owned enterprises.

Legal reform can have a role to play in changing the rules, and in shifting, however gradually, norms and conventions. But many who are engaged in the world of worker cooperatives suggest that providing resources, more so than enabling legislation, would be more effective in terms of growing the cooperative movement.<sup>118</sup> Even in states without measures that explicitly provide for the development of worker cooperatives, the law is flexible enough to allow co-ops to be fomed.

In New York City, the City Council passed a \$1.2 million initiative in early 2014 that is aimed at supporting the development of worker-owned firms. Spearheaded by the Federation of Protestant Worker Agencies (FPWA) and the New York City Network of Worker Cooperatives (NYC-NOWC), the initiative was designed to strengthen the organizational infrastructure that supports co-op development in New York City. Funds from the initiative have been divided among eleven incubator organizations, allowing many of them to increase capacity by hiring new staff.<sup>119</sup> The \$1.2 million is small relative to New York City's massive budget. But the total sum is the largest ever provided by a U.S. city government to promote worker co-op development. As elsewhere, the worker co-op movement in New York City is still relatively small, and so a little support has the potential to go a long way.

## INCUBATING ORGANIZATIONS

There are a range of different kinds of organizations that help to incubate worker-owned firms, including law firms, university-based clinics, consultancies, government agencies, social service organization, and member associations. In many cases, a range of different organizations work

together to support the development of a given cooperative or group of cooperatives, bringing complementary skills and expertise to support work that itself becomes a collective endeavor.

On the ESOP side, most company owners and managers who are contemplating the establishment of an ESOP will seek legal and accounting advice. Beyond that, the need for outside help depends largely on the degree to which the mission of the ESOP is linked to broader changes in the organizational structure. There are numerous consultancies, law firms, and other organizations that offer strategic advice establishing an ownership culture and mechanisms for greater employee involvement, and, in certain cases, using the ESOP as a foundation for building democratic governance. An example includes the law practice of attorney Deborah Groban Olson in Gross Pointe, Michigan.<sup>120</sup>

Since most cooperatives are started from scratch as democratically owned and controlled organizations, their members have to think about issues including raising capital, business planning, management and governance, and the legal identity of the organization. The availability of strategic advice and technical assistance would presumably increase the likelihood that people with the germ of a cooperative idea will make it to the planning phase, and that fledging co-ops would rely on these services to get beyond the challenging early stages. The New York City co-op development initiative is premised on this assumption.

The Center for Family Life (CFL) in the Brooklyn neighborhood of Sunset Park is one of the organizations that has received funding as part of the New York City initiative, which it has used to hire additional co-op developers. When the organization's executive director attended a worker co-op conference a few years ago, something clicked, and CFL's co-op development program was launched shortly thereafter.<sup>121</sup> To date, CFL has supported the development of 9 worker cooperatives with some 145 members. It often enlists the help of other consultants and organizations as well.

Apart from helping to incubate worker cooperatives, CFL has taken on a role as an "incubator of incubators" in the New York Area, providing training to other organizations that are interested in supporting co-op development. The organization's own efforts are largely centered in Sunset Park, where its co-op developers have cultivated relation-

ships with local community members, many of whom are immigrants from Latin America and China, over a period of many years. Its broader training activities have allowed it to extend the reach of its model into other communities.<sup>122</sup>

National membership organizations can play an important role both in providing services to existing cooperatives and strategizing about the future expansion of worker-ownership. On the ESOP side, the major membership organizations are the ESOP Association and the National Center for Employee Ownership (NCEO). The Foundation for Enterprise Development (FED) has also taken a prominent role in supporting ESOP development nationally. On the worker cooperative side, the U.S. Federation of Worker Cooperatives is the major member association. USFWC

“ It is often noted that geographic areas with relatively high concentrations of worker cooperatives tend to have a high degree of social cohesion. ”

recently underwent a split that reflects the dual identity of these national organizations. The Democracy at Work Institute (DAWI) was spun off to focus on expanding the movement, while USFWC will focus on serving existing member organizations.<sup>123</sup>

This split represents a natural division of labor. Those employed at worker-owned firms tend to be focused on the day-to-day realities of what is happening within their enterprises, while staff members of supporting organizations are often charged with addressing broader strategic questions about the direction of local, regional, and national expansion strategies. Still, there are important questions about the lines of communication that exist between firms and developers, and the degree to which those taking up leadership positions reflect the rich diversity of these movements. These concerns are not unique to movements

for worker-ownership. The union movement has faced similar questions throughout its history.<sup>124</sup>

### COMMUNITY RELATIONSHIPS

Firms that fail to come to terms with the cold, hard facts of market competition are not bound to last very long. Successful businesses need to make products people want to buy, at prices they are willing to pay. In modern economies, customers tend to have more choices with respect to most goods and services, and the broad tendency has been for economic transactions to become increasingly impersonal.

Too often, however, these tendencies are overstated. Interpersonal ties are clearly important in the formation of many worker cooperatives. They play a role in developing a shared “ownership culture” even in worker-owned firms that are not democratically governed. Forming jointly governed enterprises from scratch usually presupposes personal relations of trust and cooperation—within the organization, and often with outside supporters of the kind discussed in the previous section. It is often noted that geographic areas with relatively high concentrations of worker cooperatives tend to have a high degree of social cohesion.<sup>125</sup>

It is also important, though, to place these kinds of relationships based on trust and cooperation in context. Cultures high in “social capital” are often long in the making.<sup>126</sup> But we also need to understand the broader conditions that help to account for high or low amounts of trust and cooperation.<sup>127</sup> For example, trends of growing economic insecurity and declining public investment that are felt more acutely in certain communities can be an important reason for general mistrust and social distance, even as they may lead certain community members to bond more tightly. It is thus important to situate discussions about “cultures of cooperation” within a broader understanding of the social conditions that bring people together, and drive them apart.

When a group of mostly Brazilian women in the Boston area were thinking about starting a cleaning cooperative, the market analysis they conducted with the support of the ICA Group addressed the different layers of building a customer base. The analysis started by identifying the segment of the population that could afford housecleaning services. It then assumed that a smaller slice within this group would be attracted by the fact that the co-op planned to make and

use its own non-toxic, eco-friendly cleaning products, and that an even more specific set of people would care enough about the cooperative structure of the enterprise for it to potentially affect their purchasing decisions.

In the end, the co-op targeted areas that would have higher concentrations of people who checked all three boxes, and these people now comprise a disproportionate share of the co-op’s customer base. Co-op members make wages that are significantly above the industry average. Customer loyalty is solidified by the interpersonal ties that develop between clients and cleaners, coupled with the awareness among clients that this demanding work is being performed under more favorable conditions than those that generally prevail in the industry.

Customer relationships can also be established with organizations. Procurement policies by large organizations such as schools and hospitals can help to give worker-owned organizations a large and steady consumer base. In Cleveland, the development of Evergreen Cooperatives was supported by the Cleveland Foundation and “anchor institutions” such as the Cleveland Clinic, which can be counted among the incubating organizations that have been crucial to this initiative.

Even beyond the world of worker-owned firms, local relationships of trust and cooperation play an important role in ways that often go unnoticed. Political scientist AnnaLee Saxenian has argued that the success of the Silicon Valley high-tech corridor can be attributed in part to the way in which interpersonal networks have developed within and across firms. These networks of interaction encourage horizontal learning among different divisions within given enterprises, and between firms and their suppliers.<sup>128</sup> Examples such as these are not in short supply. The makings of an economy that blends cooperation with competition are more widespread than is commonly realized.

**ANNE CLAIRE BROUGHTON** has been working in employee engagement and sustainability for more than twenty years. Currently she is the Principal and Founder of Broughton Consulting in Durham, NC, which is actively involved in educating retiring business owners and their advisors about the possibility of employee ownership as an exit strategy. Speaking broadly about worker ownership, employee engagement as well as ESOPs (employee stock ownership plans), Ms. Broughton clarifies these terms and shares some of the success stories of companies she has worked with and written about. The following Q&A was edited and condensed from three conversations.

**Q. Wealth building, particularly among low-skill workers, has been a focus of yours for many years. There's been a lot of discussion about "income inequality" but not as much about "wealth inequality."**

Wealth inequality is the concentration of resources in fewer hands, and that is getting worse. The middle class is shrinking. There's a lot of data on that. There's also evidence that the meritocracy that we believe in doesn't exist in the United States as much as we would like. Your socioeconomic status at birth is likely where you will eventually end up. In terms of income inequality, real wages have not kept pace with inflation over 30 years. That contributes to the wealth gap but is not the only cause.

Employee owned companies find smart ways to deal with both of those issues. Incomes are enhanced through profit-sharing and gain-sharing. And when employees own a piece of the company, that builds wealth over the long term.

**Q. What is gain-sharing and how is that different from profit-sharing?**

With gain-sharing, you set a goal for how much a company, or a division within a company, is going to make. Or you might set a productivity goal. If you exceed your goals, a bonus is distributed to employees. Gain-sharing is characterized by more frequent payouts. It could be biweekly, monthly or quarterly. Profit-sharing is distributing some portion of year-end profits to employees. It's not as closely aligned with specific goals other than overall

company success. Gain-sharing can be used to reinforce behaviors that drive improved performance.

**Q. Let's talk about what an ESOP is and how it can help workers build wealth.**

An ESOP is an employee benefit plan which can set aside or borrow funds to buy shares of company stock. These shares are put in a trust and allocated to individual employee accounts that vest over time. When employees retire or leave the company, they cash in their shares. I've seen many examples of workers of modest means who are able to retire in a manner that they never would have been able to do were they not part of a worker-owned firm. For example, employees of one New England-based ESOP I wrote about were able to achieve their dreams and retire to Arizona and North Carolina. The benefits can be very powerful.

**Q. Some research that you shared shows that ESOPs provide retirement benefits that are both larger and more equitably distributed than most other retirement plans. Can you talk about the reasons why?**

Many hourly workers have no retirement plans at all. An ESOP not only provides ownership equity but usually there's a secondary plan as well, such as a 401(K). But it's more than just about retirement plans. The reason a well-run ESOP benefits everyone is because it's a good business strategy. To quote some more of the research from NCEO [National Center for Employee Ownership], "ESOP companies are 25 percent more likely to stay in business, increase sales and productivity 2-5 percent per

year after the ESOP is adopted, and have 25 percent higher job growth over a 10-year period.”

**Q. What are the benefits to an owner of converting to an ESOP as an exit strategy?**

One company that I wrote a case study about is King Arthur Flour. The business was owned by a single family for five generations. They had been practicing employee engagement strategies for years. The owners wanted to exit the business and began phasing-in employee ownership over time. It started with 30 percent of the company, and a few years later went to 70 percent and eventually became 100 percent employee owned.

Converting to an ESOP provides enormous tax advantages to a departing owner because it defers capital gains taxes indefinitely. It also preserves a company’s legacy. If you sell to an equity firm or some other entity, you have no idea what’s going to happen to the company that you’ve devoted your life to. And since the employees of King Arthur Flour were already practicing open book management and were deeply invested in the company’s success, it was a good succession plan for them.

**Q. What is open book management?**

Open book management is more than just sharing the financials with employees; it’s an employee engagement tool that ensures that everyone understands how the business makes money, and how they can contribute to and participate in company success. Companies that I’ve studied and written about that actively practice open book management train employees in financial literacy and involve them in planning and budgeting.

Employees actually live with the financials. It’s not about sharing a dead set of financials from last month that can’t be changed. Instead, you work together as a team to forecast how this month is going to end. You put employees in charge of different line items on the profit and loss statement and meet weekly to stay on top of how the month is progressing. This enables employees to deal with contingencies in real time. So the financials become

a living guide to decision making. This is very different from how most businesses operate.

**Q. Can you give an example of how this helps a company?**

For example, there’s a catering company in Chicago where an hourly employee was put in charge of fuel costs. He figured out that gas was cheapest from Monday through Wednesday. So they only fueled up on those days, and he also made sure nobody idled their trucks longer than 10 minutes. The company started saving thousands of dollars in fuel costs. You can see how much more effective that is than a boss saying, “Spend less on fuel.”

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Converting to an ESOP provides enormous tax advantages to the owner because it defers capital gains taxes indefinitely. It also preserves a company’s legacy.  
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**Q. Can you give an example of an ESOP company you’ve worked with that practices open book management?**

SRC Electrical, they are part of SRC Holdings, the group of companies that developed open book management. The founder, Jack Stack, wrote my favorite business book, *The Great Game of Business*. SRC Electrical taught me that you can’t rest on your laurels – you have to keep training new employees and refreshing those who have been there a long time. One thing they do to keep it fresh is

to incorporate 10 minutes of financial literacy into their weekly meetings through game playing. Teams create their own Monopoly board, renaming everything to fit their division, and create a balance sheet of the transactions just completed. If you make a purchase, how does that impact your cash? It is a smart and fun way to train people in financial literacy and make sure people understand the balance sheet.

**Q. But a company doesn’t have to be an ESOP or a co-op to implement open book management or other employee engagement strategies, and vice versa.**

There may be companies that will never be ESOPs but are increasing their employees’ incomes through gain-sharing or bonus pools. On the other hand, if you do form an ESOP or co-op and give people ownership, then it makes a lot of sense to implement open book management and

other employee engagement strategies. That's how workers can make informed decisions, and they will think and act like owners.

You can convert a traditional hierarchical command-and-control business to an ESOP that is implementing a limited employee benefits plan but that is not the same thing as a worker-run business. What I've been engaged in for many years is helping companies become *more successful because they are worker run and worker owned.*

**Q. What's an example?**

I wrote a case study about the Dansko shoe company. It's a part of their ethic to be a responsible company and they want to preserve that legacy. They had been a highly transparent, employee-focused company for a while and now they are a 100 percent worker-owned ESOP [as of 2012].

My work with them was specifically around their new distribution facility. They outgrew their old facility and were not able to serve new customers, and it was getting very frustrating. So over several years, they were able to buy land, sell the old facility and move. But because of permitting and other issues, they closed the old facility on a Friday and moved into the new facility on Monday. There was no time to work out any of the issues that come up when you create a whole new operation. But because of the high level of employee engagement, everyone was super involved in how to do their jobs the most efficient way. The first year everyone was working hard to figure it all out, making suggestions and trying new things. It was all hands on deck to make it work.

**Q. You hear all the time about companies that expanded and then things went wrong, and the company imploded as a result. Could you make the argument that having such a strong culture at an employee-owned company prevented a disaster?**

When you have strong employee engagement in a worker-owned company, every employee is thinking about the business. They are excited to come to work and they are

able to solve problems as they come up. In these businesses, employees are respected. Their ideas are solicited and implemented. Employees are not just cogs. So I would say yes, you definitely could make that argument.

**Q. We currently have three generations in the workforce: Boomers, Generation X, and Millennials. What can we say about how these three demographics are driving the current trends we are seeing?**

The world is becoming more collaborative and less top-down. A lot of this is driven by Millennials, who are a growing part of the work force. By 2020 they will be almost half of the work force. And they certainly want to be engaged by their work. They are educated, great with technology, they really want to collaborate in teams. So employee ownership is very well suited to them. Baby Boomers, who still are quite present in the workforce, are

more used to a hierarchical workplace. You pay your dues, and work more individually. Generation X is the bridge. They can work either way. They're used to top down but they also love this emerging, collaborative, flat model.

**Q. As you said, Boomers are still very much a part of the workforce. How are they dealing with this changing culture?**

One company I wrote about is Tasty Catering. Three brothers who founded the company had run it in a traditional command-and-control fashion

for 16 years. As they were approaching their 60s, two of their millennial employees—their sons—went into the CEO's office one day and said, things have to change or we're leaving. We need an employee-centric culture. We need to have a say in how things are run, and to solve problems in constructive ways. The owners faced a choice: change how the company is run or lose their next generation of leaders.

So together they read the business book *Good to Great*. They defined their core values and gave each core value a number. This created a common language, which gave them the tools they needed to resolve conflicts in constructive ways, and problem solve as a team. The CEO

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Open Book Management helps workers make informed decisions, enabling them to think and act like owners.  
————— ”

now calls himself the Chief Culture Officer and spends his time helping people do their jobs better rather than micromanaging. They talk a lot about freedom within a culture of discipline. People are empowered to make their own best decisions.

Whenever I speak at conferences people always ask, can a company really change its culture or do you have to start from scratch? I answer that question with this story. Tasty Catering really did change its culture.

**Q. What I find intriguing about worker ownership is that it creates wealth without having to make every single person their own entrepreneur – be their own boss, worker, bookkeeper, health insurance provider, etc. It allows you to build wealth without having to be that kind of risk-taker.**

That is true, but entrepreneurship and worker ownership can go hand-in-hand, too. Entrepreneurs are great problem solvers. They can innovate by looking at things in a new way. I think that's what we're seeing with employee ownership. A number of CEOs say it creates a whole company of entrepreneurs. You're training all your employees to think in an entrepreneurial way. If everyone knows the big picture and everyone has the data, then everyone can be very empowered to come up with creative ways to do things differently from wherever they are sitting.

For example, Zingerman's Roadhouse restaurant in Ann Arbor benefited from their practice of open book management when they were looking for ways to reduce their high food costs. A dishwasher said, "I throw away a lot of French fries. Why don't we give smaller portions but offer free refills?" If you've got every employee thinking like that, it adds up.

**Q. Given that you've been working in this field for more than 15 years, what do you think is the key to significantly expanding worker ownership across the US?**

We will see more ESOP and co-op conversions over the next ten years as Baby-boomers retire in large numbers. Statistics I've seen indicate that 66% of businesses in the US are owned by Baby-boomers. And they had fewer children, compared to the previous generation, to pass on their businesses to. So people are taking notice. At stake are many companies worth a lot of assets and many

jobs. Private equity funds are angling to get this business as transactions to new ownership. But if we can do a lot of education of Boomers and their advisors – bankers, lawyers, and accountants – we can facilitate many more ESOP conversions. It's great from a tax perspective and it's a great way to continue your legacy.

There are business owners that do it purely for the tax benefit, but then they're surprised when the business doesn't do well because they haven't created the culture of ownership. So one of the things I do is help new ESOPs by forming a participatory system. That's how you unlock the magic of an ESOP. If it's done right, ESOPs perform better than traditionally run companies, and that builds wealth for workers over time.

**Q. Generally speaking, an ESOP conversion is better for larger companies, and a co-op conversion is better for a smaller company. Is that right?**

To form an ESOP, you need at least 20 employees, and it needs to be profitable, and you need to be big enough to pay for the ESOP transaction. A rough estimate is that it takes about \$40,000 for the conversion. So you have to be able to take on that debt. A co-op conversion is a better option for smaller businesses, and can be done with fewer resources.

The best thing that organizations like NCEO [National Center for Employee Ownership] and other groups are doing is educating business owners of the possibility of selling to their employees via an ESOP or a co-op. NCEO is national but they are supporting the development of state centers now. The pilot center is in Pennsylvania and I'm talking to them about starting a center here in North Carolina. Several states, including Ohio and Vermont, already have successful employee ownership centers. But much more needs to be done locally.

And then there's what I do, which is telling the stories of companies that are more financially successful because they engage employees at all levels and share ownership broadly. Those stories can be very powerful.

## CONCLUSION:

# Our Role as Foundations

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The potential for co-ops and ESOPs to expand in the United States is unquestionable. They currently make up a tiny fraction of the overall economy, and yet they are having a big impact on the people who are lucky enough to participate. Not every co-op and ESOP is successful, to be sure, but many of them are not only surviving but also thriving to the direct benefit of their employee-owners.

We see this moment in history as an ideal time to push for greater investment in the formation and expansion of worker-owned businesses as one method for closing the income and wealth gaps and increasing economic activity. Perhaps just as importantly, we believe that worker-ownership can add up to a whole that is greater than the sum of its parts. Beyond wealth and income is the shared ideal, even among conservatives, that an ownership society creates benefits everyone. When we invest in a cooperative culture, civility thrives. Our increasingly sorted and mediated culture is splintering the most important principles upon which our democracy was established. While these are clearly much bigger problems than the formation of a co-op or the conversion of an ESOP could ever fully address, making a difference in the lives of everyday people is the pebble that causes a ripple that creates a wave. We are advocating for people to think systemically about how to increase worker co-ops and ESOPs: How to fortify the financial system to support worker ownership, how to include worker ownership in policy discussion and as a tool of community and economic development.

What we know from this report is that there is no efficiency disadvantage to worker-ownership, whether it is a

co-op or an ESOP that provides additional benefits. Given the efficiency of these structures, then, shouldn't we be on the side of equity, inclusion and democracy? Clearly we believe the answer is yes.

The small footprint of co-ops is not for a lack of interest but a lack of resources. The ones that have succeeded have had to overcome long odds. Providing resources and support to viable co-op ideas—and giving them the chance to work through the inevitable rough patches—is critical. Promoting the benefits of converting to an ESOP or worker co-op to the many baby boomers who are on the verge of retiring from their companies is another critical avenue. Committing additional resources to the incubators, educators and consultants will have a multiplier effect. Further research into where ESOPs and co-ops have clustered and thrived will also help refine what we already know and fill in gaps about many things we still do not know about how co-ops and ESOPs succeed.

In short, we want to drive investment that helps prove the concept of worker co-ops and ESOPs, and grow from there. We encourage our fellow funders to contact us about working together—to form a co-op of sorts—that would create an alliance among foundations that are keenly interested in addressing income and wealth inequality head-on through the great potential that is worker-ownership.

## APPENDIX 1:

# Four Views on Firm Governance

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In examining the specific forms that worker ownership has taken in the US, it is useful to set a broader conceptual backdrop. What do existing views on firm governance have to say about the allocation of ownership and control among different sets of actors: owners, managers, and workers?<sup>129</sup>

- 1 We can start with the “managerial” view. As shown in Figure 1, this perspective allows that the owners of capital should retain their basic property rights. But it suggests that, especially as firms grow in size and complexity, professional managers are in the best position to make decisions about how to deploy the firm’s resources most efficiently. All else being equal, vesting greater authority in the hands of professional managers will thus tend to enhance the performance of the firm.
- 2 A second approach is the shareholder view. As firms grow in size and complexity, owners face a dilemma. They need managers to oversee the activities of the firm. But there is the risk that managers will seek to advance their interests in ways that do not align with those of the firm’s owners. Even if immediate control rests in the hands of managers, the shareholder perspective is concerned about ensuring that ultimate control resides with owners (see Figure 2). Formulated in part as a way of dealing with increasingly dispersed ownership in the context of large, publicly traded firms, this view has often used the language of “shareholder democracy” to advance its claims.<sup>130</sup>
- 3 A third perspective takes the discussion beyond the relationship between owners and managers, arguing that a wider range of interested parties should play a role in firm governance. Berle and Means provided a bridge to this “stakeholder” view of the firm. They were concerned about the assertion of managerial authority at the expense of shareholders. But they also argued that shareholders in widely held companies tend to be far removed from any active role in exercising stewardship over their assets. As such, the claims of shareholders need to be balanced against those of others who have a stake in the firm’s activities, including workers and the surrounding community (see Figure 3).
- 4 Finally, a fourth perspective poses a more fundamental challenge to the basic hierarchical assumptions that underlie all of the other approaches.<sup>131</sup> Even the stakeholder view tends to allow that labor will ultimately remain a “junior partner” to capital, leaving intact the basic property rights of a separate class of owners. Under a “democratic” view, the firm is owned and controlled by all of its members. In the work of thinkers such as Robert Dahl<sup>132</sup> and David Ellerman<sup>133</sup>, this democratic view has been built around the notion that the right to self-government should extend into the sphere of work, with ultimate authority over the firm’s activities being allocated on a one-member, equal share/one vote basis.

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### Chapter 5: The Current Landscape of ESOPs and Co-ops

83. Looking at relative concentrations across all states, we see that the coefficient of variation is .42 for ESOP firms and 1.93 for worker cooperatives. If we leave out states in which there are zero worker cooperatives, the coefficient of variation is .39 for ESOP firms and 1.47 for worker cooperatives.
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### Chapter 6: Three Ways to Grow The Co-op Movement

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89. The danger in being able to avoid the strictures of prevailing employment law is that the "cooperative" can become a platform for exploitation. Legally, however, the exemptions from employment law should apply only to partners/co-owners who are effectively functioning as their own bosses.
90. Here, the issue is that new members may not place as much as value on preserving the democratic nature of the organization. However, if decisions on organizational changes are being made by a broad base of members, old and new, then this could itself be considered a democratic process. Such potential conflicts between old and new members are an important tension when thinking about the democratic identity of worker cooperatives.
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### Chapter 7: The Supporting Infrastructure for ESOPs and Co-ops

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#### Appendix 1: Four Views on Firm Governance

129. There are important differences within each of these categories. The owners of capital may be company founders with a controlling stake or minority owners holding a few shares. The managerial category ranges from top executives to middle- and low-level managers, with the latter often wielding minimal

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