

# Employee and worker ownership in COVID-19 recovery strategies

June 2020

## Summary

### What?

City regions should include measures to support the creation of employee and worker owned businesses, via both start-up and conversions, in their COVID-19 (C19) recovery strategies.

### Why?

Employee and worker ownership could be instrumental in helping city regions to 'build back better' by:

- creating decent new livelihoods
- replacing / rebuilding livelihoods lost through C19
- keeping viable jobs in communities

Employee and worker owned businesses: create decent jobs; increase economic fairness; enhance wellbeing; reduce inequalities; build resilience into firms, local economies, supply chains and communities; all while maintaining high commercial performance.

### How?

Support start-ups by: awareness raising and outreach; specialised business development; start-up grants and improved access to specialised finance.

Support conversions by: engaging SME owners early on succession/exit plans; engaging workers and their representatives early; feasibility studies; providing expert advice and support; providing access to specialised finance.

In response to businesses in crisis, supporting workers to start new co-ops will often deliver better outcomes than supporting the conversion of an existing business that is in trouble.

A public holding company that acquires ownership stakes in struggling but potentially viable businesses, could be instrumental in supporting conversion to employee and worker ownership in some circumstances.

Supporting the ongoing development of employee and worker owned businesses is essential.

## 1 Introduction and background

1.1 City regions should include measures to support the creation of employee and worker owned businesses, via both start-up and conversions, in their COVID-19 (C19) recovery strategies. Employee and worker ownership could be instrumental in helping city regions to 'build back better' by:

- creating decent new livelihoods
- replacing / rebuilding livelihoods lost through C19
- keeping viable jobs in their communities

1.2 By employee and worker ownership we mean: firms in which workers have a controlling

ownership stake and a meaningful degree of democratic influence in corporate governance. The key models in the UK are worker co-ops and employee ownership trusts (EOTs).

- 1.3 The two main ways these businesses are created in the UK are start-up or conversion of existing businesses as part of planned ownership succession.
- 1.4 The paper summarises the benefits of employee and worker ownership (**part 2**), what works for supporting start-ups (**part 3**) and conversions (**part 4**), and reviews evidence on how to support employee and worker ownership as a response to business crises (**part 5**).

## **2 Benefits: livelihoods, fairness, resilience, performance**

- 2.1 Data from the UK and other countries shows that worker co-ops are, on average, better at creating jobs, compared to businesses generally.<sup>1 2</sup> And crucially, employee and worker owned businesses create and sustain *decent* livelihoods. Worker co-ops are found to have significantly lower pay ratios than other businesses and to share profits equitably among every worker.<sup>3 4</sup> There is also evidence to suggest that more engaging, empowering and democratic workplaces are good for worker wellbeing.<sup>5 6</sup>
- 2.2 Importantly, these gains in economic fairness do not come at the expense of commercial success. There is good evidence that mutual purpose and democratic governance in worker co-ops boosts performance and enriches culture.<sup>7 8</sup> These benefits are also reported in EOTs.<sup>9 10</sup>
- 2.3 Furthermore, co-op start-ups in the UK and around the world are shown to be significantly more resilient than start-ups generally.<sup>11 12</sup> And worker co-ops are shown to be more resilient and better at preserving decent livelihoods in downturns.<sup>13 14</sup>
- 2.4 Lastly, a healthy base of employee and worker owned businesses should be part of any strategy for more resilient local economies and supply chains. Employee and worker ownership roots operations, jobs, investment and decision-making in places. This can be critical in an era of mobile and itinerate capital and talent. Alongside start-ups, the conversion of established businesses to employee and worker ownership is critically important here, as this limits the number of successions that fail, or fail to deliver for local economies and communities.
- 2.5 There is strong evidence from countries with lots of employee and worker ownership conversions (France, Italy, Spain) that converted businesses are on average more resilient over the long term, compared with other businesses.<sup>15 16</sup>

## **3 What works: start-ups**

- 3.1 In the UK almost all new start employee and worker owned businesses use the worker co-op model. This model establishes worker ownership and control within a single corporate entity, through its rules or articles.<sup>17</sup> It is a simple, flexible and low cost arrangement. Worker co-ops usually incorporate as a co-operative society or a company limited by shares/guarantee.
- 3.2 Currently, there are no local or national government programmes to support the formation of new worker co-ops anywhere in the UK. So our evidence for what works must draw on historical examples in the UK and contemporary examples abroad, particularly successes in municipalities in the United States. We can also draw on contemporary successes in supporting community business start-ups in England.
- 3.3 From the mid-1970s through to the late 1980s many city councils in the UK ran programmes to support worker co-op formation. This period coincided with a dramatic increase in the number of worker co-ops in the UK that has not been repeated since.<sup>18</sup>

3.4 If the objective is to see a step change in the formation of commercially viable worker co-ops, with significant benefits for disadvantaged groups (low skilled, BAME, contexts of high deprivation), then we suggest:

- Putting time and resource into **awareness raising and outreach** in target communities of interest and/or place, partnering with **community-based organisations**,<sup>19</sup> trade unions, professional associations, small business networks, co-working spaces and higher/further education institutions
- Providing a package of **specialised developmental support**, which includes pre-start capacity building and team facilitation, start-up advice and support,<sup>20</sup> peer mentoring, all **combined with a start-up grant** <sup>21</sup>
- Providing access to **ongoing specialised business support** for a minimum of one year after the start of trading <sup>22</sup>
- If possible, providing the option of **'co-op-friendly' investment** (equity and/or debt) <sup>23 24</sup>
- Ideally, combine a city-regional worker co-op development programme with **community-led economic development** programmes in more deprived neighbourhoods <sup>25 26</sup>
- Perhaps combine with a city-regional community wealth building agenda <sup>27</sup>

#### Worker-community hybrids

3.5 There is great potential in 'worker–community hybrids', which combine worker ownership and control with a separate membership for community stakeholders and investors.<sup>28</sup> Such co-ops have purposes to provide decent livelihoods and also to benefit the community. This would draw on the entrepreneurial opportunities and drive in communities. It would also provide access to significant sources of 'co-op friendly' equity investment in the form of 'Community Shares'.<sup>29</sup>

#### In an economic crisis

3.6 There will be significant economic and social value in supporting the formation of new worker co-ops in the C19 crisis. With the right support, many who lose their jobs through redundancy and business closures, could rebuild better livelihoods through worker co-ops. We expect support for entrepreneurship to be part of any jobs strategy in this crisis. This should include support for co-operative entrepreneurship, as outlined above.

3.7 For more on the potential role for new start worker co-ops in responding to business failures, see **part 5**.

## **4 What works: conversions**

4.1 The EOT model is well-suited to most conversions, because it allows for a phased, full or partial, transfer of ownership and control. EOTs also lock in collective employee ownership and stewardship of the business for the long term. However, EOTs require two or three corporate entities and layers of governance to be created,<sup>30</sup> so are more costly to set up and administer than worker co-op models. This can act as a barrier to the conversion of micro-small enterprises. Encouragingly, learning from the United States suggests that the simpler, lower cost worker co-op model can plug this gap for micro-small business conversions.<sup>31</sup>

#### Lessons from Scotland

4.2 In recent years the UK has seen a surge in the number of established businesses converting to employee ownership as part of planned ownership succession, using the EOT

model.<sup>32</sup> In proportion to size of business population, Scotland has a significant lead over the rest of the UK in the rate of conversions.<sup>33</sup> Experts in the field believe this is because Scottish Government has developed a very effective programme over the past decade; one that increases awareness of employee ownership as a succession option and then provides access to specialist advice and support to help conversions happen.<sup>34</sup> An independent evaluation for the programme (which is called 'Co-operative Development Scotland') cited a sixfold return on investment for every pound invested in on-the-ground support.<sup>35</sup>

4.3 Scottish Government's successful approach leads us to make the following suggestions:

- Focus primarily on conversions as part of **planned ownership succession**, not rescue (though this does not exclude cases where reduced profitably motivates a more hurriedly planned sale/exit, with risks of job losses)
- **Engage SME / family business owners** on the subject of their exit/ divestment / retirement plans
- Position conversion as **one option among others** for succession / exit / divestment, and ensure the option is introduced as a matter of course
- Understand and respond to **the motivations of business owners** who could be interested in a conversion
- Provide access to **specialist advice and support** to help business owners, managers and workers explore the option in detail, conduct **feasibility studies** and, where the conditions are right, to support the conversion transaction (e.g. specialist legal services)

4.4 However, there are also aspects of Scottish Government's approach that we recommend modifying:

- A singular focus on the EOT model and a policy/programme emphasis on business scale, has left the 'market' for micro-small enterprise conversions in Scotland very under-developed
- A policy/programme emphasis on the number of 'deals' - the legal transfer of company shares to an EOT - has resulted in too many EOTs that lack an effective degree of employee control in corporate governance<sup>36</sup>

4.5 Including the worker co-op model as an option alongside the EOT, especially for micro-small conversions, will help spread the benefits of any programme among a broader range of businesses, sectors, workers and communities. A stronger policy/programme emphasis on giving worker owners an effective degree of influence and control in corporate governance, will strengthen the evidenced benefits of employee and worker owners, in terms of commercial success as well as economic fairness and wellbeing.

#### Community wealth building

4.6 While Scottish Government's programme has been national, this support is now being plugged into a community wealth building programme in North Ayrshire.<sup>37</sup> It is hoped that this will create local momentum for conversions. Shifting more procurement spend into the local economy and developing local supply chains should create more commercial opportunities for converted businesses.

#### Financing conversions

4.7 The established financing mechanism for conversions in the UK, via an EOT, usually involves the EOT's purchase of shares being financed by debt. This debt often includes 'vendor financing' where the seller agrees to be paid the full sale price over a period of time *after* the transfer of ownership. Some debt financing can also come from banks and specialist institutions. Sometimes part of the EOT's share purchase is financed from the

target company's cash reserves. Workers may sometimes contribute to the EOT purchase, though this has not been a significant part of financial mix during the recent surge in conversions.<sup>38</sup>

- 4.8 There is a potential for deficits in worker agency in these arrangements. These deficits in agency could be reduced by the provision of more specialised financial support, to fund both the acquisition and investment afterwards. In France, Italy and Spain this specialised finance comes from institutions within the co-op sector and institutional investors, and in some cases the state.<sup>39</sup> In both Spain and Italy workers at risk of unemployment can receive would-be future unemployment benefits in lump sums. These grants can be used to help fund the acquisition of a going concern, or to start-up a new entrepreneurial endeavour, including worker co-ops.<sup>40 41</sup> Unfortunately the co-op sector in the UK does not currently have the resources and institutions to aid conversions found in France, Italy and Spain. Policymakers in city-regions should consider what they can do to provide a degree of comparable financial support.

## 5 What works: supporting employee and worker ownership in response business crises

- 5.1 It is sometimes possible to strengthen, or even save, struggling businesses via conversion to employee and worker ownership. However we must stress that employee and worker ownership is not in itself a solution to business failure.
- 5.2 Of the OECD countries with the strongest records on conversions, Italy and Spain stand out in terms of conversions *in crises*. Indeed Italy's leading state-mandated provider of development finance to worker co-ops (*Cooperazione Finanza Impresa*) has reported that 90 percent of the conversions it has financed were triggered by 'company crises' (linked to broader economic downturns, mismanagement, falls in demand in specific markets or moves by business owners to divest and/or offshore).<sup>42</sup>
- 5.3 Encouragingly, academic research has "*found quite outstanding rates of survivability*" for Italian worker co-ops created out of "*once troubled firms*".<sup>43</sup>
- 5.4 But it is critical to note that in both Italy and Spain these successful outcomes often arise from the formation of new worker co-ops that acquire productive assets from insolvent businesses, as well from as the successful turnaround of the existing business following transfer to worker ownership. Policymakers in the UK considering how to support employee and worker ownership in the context of business crises should make a distinction between:
- **worker 'buyouts'**, wherein the workers acquire a controlling stake in a going concern
  - **worker 'restarts'**, wherein workers in a distressed company form a 'newco' co-op with the specific intention of negotiating acquisition of some or all of the firm's productive assets, as part of the insolvency process

### Financial support

- 5.5 Research into conversions in Italy finds that the availability of specialised financial support is a particularly critical success factor when it comes to buyouts and restarts in a crisis:
- "Where no other financial supports specifically geared at WREs [worker reclaimed enterprises] or WBOs [worker owned businesses] exist, conversions of healthy companies into worker cooperatives - either via a retiring owner's selling or bequeathing the firm to employees - tend to have better prospects"*<sup>44</sup>
- 5.6 In Italy, most such funding comes from specialised institutions within the co-operative sector,<sup>45</sup> which are themselves be capitalised by other co-ops, institutional investors, and in some cases with seed capital from the state.<sup>46</sup>

- 5.7 In both Spain and Italy there are also mechanisms that provide workers at risk of unemployment with would-be future unemployment benefits in lump sums. These are used to help fund the acquisition of a going concern, or to invest in a new entrepreneurial endeavour, including 'restart' worker co-ops.<sup>47 48</sup>

#### Business circumstances

- 5.8 Evidence suggests that successful crisis buyouts are more likely in businesses with profitability projections that are too low for current owners and potential external investors / buyers, but still sufficient to give workers the prospect of a decent livelihood in the longer-term.<sup>49</sup> This could still fall within the bounds of lessons from Scotland set out in 4.3.
- 5.9 Another key successful factor for crisis buyouts is an early, expert and impartial assessment of the feasibility of continuing the business under employee and worker ownership. This includes forensic analysis of the financial situation, business plan and management. And it includes detailed consultation with workers and business owners to understand their motivations, interests and aspirations. In France, Italy and Spain this is generally provided by specialised institutions within the co-op sector.<sup>50</sup>
- 5.10 Note that the same assessment can also help workers to identify when a restart is a better option than a buyout.

#### Workforce engagement

- 5.11 Another critical success factor for both crisis buyouts and restarts is the early involvement of workers, their representatives and experts in discussions about the future of the business. These discussions need to be transparent and informed.<sup>51</sup> In Italy, workers are given a clear right to participate in such discussions and a 'right to bid' under the Marcora Law.<sup>52</sup>

#### Ongoing developmental support

- 5.12 Last and by no means least, evidence from Italy, France and Spain all shows that the long-term success of buyouts and restarts, from a crisis or otherwise, is heavily dependent on ongoing support for co-op development. This includes developing skills, behaviours and culture to help workers to become effective, responsible co-owners of a business.<sup>53</sup> It also includes ongoing support around organisational design and governance, as well as business development and investment.<sup>54</sup>

#### Lessons for city regions in the UK

- 5.13 Clearly the awareness and support programme for conversions in Scotland would not be sufficient to support conversions in crisis circumstances. A whole ecosystem of support is required, initiated by a number of significant policy interventions.
- **Target support carefully** – Is there a viable buyout or restart in there that will sustain decent livelihoods? The focus should be on quality long term outcomes for workers and communities, not outputs in terms of number or size of 'deals'.
  - **Prioritise engagement** – Even though in a crisis things need to move fast, the evidence shows that these things must be done thoroughly. Empower workers and involve trade unions, community organisations and business networks.
  - **Provide specialised financial support** - Public money would be needed to help finance acquisitions (of going concerns or productive assets) and to provide investment afterwards. This would most likely need to include a combination of grants, soft loans and 'co-op-friendly' equity. A specialised financial intermediary could be useful, as this could lever in private investment (including social impact and community investment).
  - **Include worker-community hybrids** – Workers and local communities will often

come together to try and save a business and/or livelihoods.<sup>55</sup> The worker-community hybrid model (see 3.5) should be explored as an option for both buyouts and restarts. This model can mobilise vital social and financial capital in the community. It could have particular potential for micro-small businesses with local significance.

- **Community wealth building** - Shifting more procurement spend into the local economy and developing local supply chains should create more commercial opportunities for buyouts/restarts to be viable.

5.14 The idea of a public holding company that acquires ownership stakes in struggling but potentially viable local businesses, with a view to possible divestment to worker ownership, is worthy of exploration. The outcome could be divestment of a going concern to workers (in part or whole) or divestment of productive assets to a new worker co-op, or co-ops. The holding company could focus on local businesses that would likely have been viable but for C19. Most importantly acquisition by the holding company could provide *time* to:

- stabilise financial position
- assess feasibility of various divestment options including to worker ownership
- engage workforce and other stakeholders
- provide advice and support
- arrange finance to aid a buyout or restart

## 6 Concluding remarks

- 6.1 Co-operatives UK and the Employee Ownership Association have secured more than a million pounds in funding to pilot *some* of the approaches set out in **parts 3, 4 and 5**. We will be working in one or two places in England. This work will help inform best practice for all city regions seeking to support employee and worker ownership.
- 6.2 City regional and national government could do much to extend this work and magnify its impacts. Furthermore, the C19 economic crisis is urgent and all city regions should include support for employee and worker ownership in their C19 recovery strategies.
- 6.3 Co-operatives UK is ready to support all governments that can make firm commitments in terms of policy and resources. We will help make the case for policy change and resource allocation where needed.

## Contact

James Wright, Policy Officer

e: james.wright@uk.coop

t: 0161 214 1775

## About Co-operatives UK

Co-operatives UK is the national association of co-operative businesses. We have over 800 co-operatives in direct membership, including leading consumer co-operatives, worker owned businesses, community businesses and farmers' co-operatives.

---

<sup>1</sup> Worker co-ops in the UK create 35 percent more ‘job’ with every £1 of turnover than UK employers as whole, based on all worker co-ops we have the data for compared with government business statistics all UK employers

<sup>2</sup> Virginie Pérotin (2015) [‘What do we really know about worker co-operatives?’](#)

<sup>3</sup> Ibid

<sup>4</sup> Co-operatives UK (2018) [‘Gender Pay Gap Report’](#)

<sup>5</sup> Coad & Binder (2014) [‘Causal linkages between work and life satisfaction and their determinants in a structural VAR approach’](#)

<sup>6</sup> Employee Ownership Association (2017) [‘The Ownership Dividend’](#)

<sup>7</sup> Virginie Pérotin (2012) [‘The performance of worker co-operatives’](#)

<sup>8</sup> Fathi Fakhfakh, Virginie Pérotin, Monica Gago (2011) [‘Productivity, Capital and Labor in Labor-Managed and Conventional Firms’](#)

<sup>9</sup> Employee Ownership Association (2017) [‘The Ownership Dividend’](#)

<sup>10</sup> See the evidence presented in the 2012 [Nuttall Review of Employee Ownership](#)

<sup>11</sup> Co-operatives UK (2020) [‘The Co-op Economy’](#)

<sup>12</sup> Co-operatives UK (2019) [‘Co-operative Business Survival’](#)

<sup>13</sup> Virginie Pérotin (2012) [‘The performance of worker co-operatives’](#)

<sup>14</sup> EURICSE (2015) [‘Cooperation in Italy during the crisis years’](#)

<sup>15</sup> CECOP (2013) [‘Business Transfers to Employees under the Form of a Cooperative in Europe’](#)

<sup>16</sup> Vieta, Depedri & Carrano (2015) [‘The Italian Road to Recuperating Enterprises and the Legge Marcora Framework Italy’s Worker Buyouts in Times of Crisis’](#)

<sup>17</sup> See [model rules for worker co-operatives](#)

<sup>18</sup> <https://labour.org.uk/wp-content/uploads/2017/10/Alternative-Models-of-Ownership.pdf>

<sup>19</sup> New Work City Council funds and oversees a programme that supports the formation of worker owned co-operatives. The programme works mostly in New York’s poorer neighbourhoods, with significant numbers of minorities and migrants among those founding co-operatives. Key to the success of the programme in supporting co-operative formation in challenging circumstances, is the significant role played by community-based ‘non-profits’ in awareness raising, pre-start facilitation and capacity building within neighbourhoods and communities. Activity to increase awareness of, interest in and adoption of the worker co-operative model, is plugged into wider community-led economic development activities. [See here](#).

<sup>20</sup> Successful programmes such as that in New Work City have taken this approach. A \$2.9m commitment in 2018 has supported almost 50 new worker co-operatives.

<sup>21</sup> The combination of start-up advice and grant for new community co-ops via the [Bright Ideas Fund](#) has proven especially effective

<sup>22</sup> Ongoing support for new worker co-ops is a critical component of the ecosystem in Italy that has proven so effective at growing worker co-ops, often out of crises – [see here](#)

<sup>23</sup> The size and strength of the worker co-op economies in Italy, Spain and France rests in part of the availability of specialised patient investment (equity and debt) for new starts and conversions

<sup>24</sup> The existence of a specialized equity model and market for community co-ops (Community Shares) is also a critical success factor in the growth of community co-ops in the UK in the past decade

<sup>25</sup> New York City’s approach exemplifies this

<sup>26</sup> For primary research showing the importance of this approach in developing community businesses in contexts of high deprivation, see: CLES and Power to Change (2019) [‘Building an inclusive economy through community business: The role of social capital and agency in community business formation in deprived communities’](#)

- 
- <sup>27</sup> For a summary of community wealth building, [see here](#). Shifting more procurement spend into the local economy and developing local supply chains should create more commercial opportunities for new worker co-ops to become viable.
- <sup>28</sup> Great recent examples include new starts [Equal Care Co-op](#) in Calderdale, which raised £300,000 in Community Shares and [Kitty's Launderette](#) Liverpool
- <sup>29</sup> See the [Community Shares Unit](#)
- <sup>30</sup> Government's own model documentation and guidance provides a useful overview of the options for employee influence and control in EOTs, [see here](#)
- <sup>31</sup> New York City Council (2018) '[Working Together: A Report on the Fourth Year of the Worker Cooperative Business Development Initiative](#)'
- <sup>32</sup> Robinson & Pendleton (2019) [Employee Ownership In Britain: Size and Character](#)
- <sup>33</sup> Scotland now accounts for 16 percent of all EOT-owned businesses ([see here](#)) in the UK but only has 6 percent of all UK businesses ([see here](#))
- <sup>34</sup> See Graeme Nutall [here](#)
- <sup>35</sup> See [this independent evaluation](#) of Scottish Enterprise's programme to support conversions to employee and worker ownership
- <sup>36</sup> Significant employee influence and control is not the default in EOTs. In many EOTs employee influence is restricted to minority representation on the 'trust board' and/or a consultative council. Co-operatives UK recognises as co-operatives those EOTs that have significant, democratic, employee influence and control. We have only be able to confirm this in a minority of cases, though this is at least in part down to limited clear publically available information on EOT governance arrangements.
- <sup>37</sup> <https://www.north-ayrshire.gov.uk/council/community-wealth-building.aspx>
- <sup>38</sup> Capital for Colleagues provides a useful overview of this [here](#)
- <sup>39</sup> CECOP (2013) '[Business Transfers to Employees under the Form of a Cooperative in Europe](#)'
- <sup>40</sup> In Spain, a mechanism called the [Pago Unico](#) ('single unemployment benefit payment')
- <sup>41</sup> In Italy this is provided for under the [Macora Law](#)
- <sup>42</sup> Vieta, Depedri & Carrano (2015) '[The Italian Road to Recuperating Enterprises and the Legge Marcora Framework Italy's Worker Buyouts in Times of Crisis](#)'
- <sup>43</sup> Ibid
- <sup>44</sup> Ibid
- <sup>45</sup> Ibid
- <sup>46</sup> For example, in Italy public money provided seed capital for a specialised institution financial institution (*Cooperazione Finanza Impresa*)
- <sup>47</sup> In Spain, a mechanism called the [Pago Unico](#) ('single unemployment benefit payment')
- <sup>48</sup> In Italy this is provided for under the [Macora Law](#)
- <sup>49</sup> CECOP (2013) '[Business Transfers to Employees under the Form of a Cooperative in Europe](#)'
- <sup>50</sup> Ibid
- <sup>51</sup> Ibid
- <sup>52</sup> Vieta, Depedri & Carrano (2015) '[The Italian Road to Recuperating Enterprises and the Legge Marcora Framework Italy's Worker Buyouts in Times of Crisis](#)'
- <sup>53</sup> Summers and Chillias (2019) '[Working in employee-owned companies: the role of economic democracy skills](#)'
- <sup>54</sup> Vieta, Depedri & Carrano (2015) '[The Italian Road to Recuperating Enterprises and the Legge Marcora Framework Italy's Worker Buyouts in Times of Crisis](#)'
- <sup>55</sup> Ibid