Employee Ownership & the State Small Business Credit Initiative

As states grapple with how to address both long-entrenched and newly-emerging forms of economic insecurity in the wake of the COVID-19 pandemic, there is no better time to look to **effective but lesser-known solutions, such as broad-based employee ownership** (EO). EO encompasses several business forms, including worker cooperatives, employee stock ownership plans (ESOPs), and employee ownership or perpetual purpose trusts. EO can help advance the goals of state governments and development finance agencies to build economic resilience and high-quality jobs, including in historically marginalized communities.

Employee-owners of California Solar Electric Company on the job. Cal Solar transitioned to a worker cooperative in 2019 and has doubled in size to 40 employees in the past 5 years.

THE CASE FOR EMPLOYEE OWNERSHIP

The benefits of employee ownership are clear, with many studies across decades documenting positive outcomes for businesses, employees, entrepreneurs and retiring business owners, and society at large.

Employee ownership has transformative impacts on businesses and their employees that stand the test of time, and positive ripple effects for their families and communities. In addition to enjoying higher quality jobs, research shows that employee-owners are significantly less likely to be laid off, reducing claims on unemployment insurance and other public benefits. Some examples:

- Wages and Assets: Research on younger employee-owners found that they had 33% higher wages, 53% longer job tenure, and 92% higher household net worth than their peers (NCEO 2017).
- Resilience: A study by the Employee Ownership Foundation and Rutgers University documented the **high performance of employee-owned companies during the COVID-19 pandemic**: they were "3.2 times more likely to retain staff—even when other businesses received funding through the Paycheck Protection Program and the employee owned firms did not" (EOF/Rutgers 2020).

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THE CASE FOR EMPLOYEE OWNERSHIP, CON'D

- Public Benefit: A study by the National Center for Employee Ownership found that lower job losses among employee-owned firms **saved the federal government approximately $17 billion in 2014, and $37 billion in 2010**, a recession year (NCEO 2015).

Worker-owners at The Local Butcher Shop in Berkeley

Here are two examples of employee-owned companies that demonstrate this resilience and public benefit. The 100% ESOP-owned **Recology**, for example, **committed early in the pandemic** to paying full salaries even if it did not have work for everyone. And **California Solar Electric**, a successful company that transitioned to a worker cooperative in 2019, not only weathered the economic shutdowns but innovated and thrived, raising wages by 20% during the pandemic. **There are approximately 7,000 employee-owned businesses across the United States.** *Some of their stories can be found here.*

A Project Equity report called **The Case for Employee Ownership** (2020) summarizes the evidence that both Employee Stock Ownership Plans (ESOPs) and worker cooperatives strongly benefit businesses, workers and communities, and describes ways that state and local governments are promoting employee ownership.

HOW STATES CAN ADVANCE EMPLOYEE OWNERSHIP THROUGH SSBCI

While interest in employee ownership is growing every day, there are two significant barriers to unlocking the potential benefits of employee ownership: insufficient pipeline of companies considering EO, and lack of understanding among capital providers of how employee buyouts can be financed and underwritten. The State Small Business Credit Initiative will infuse states with large amounts of capital to support small businesses, and state agencies can use SSBCI funds to address these barriers to employee ownership.

Nearly 3 million businesses employing more than 32 million people have owners who are nearing retirement age, and most lack succession plans. Many of these owners can find a win-win solution by selling their companies to their employees. However, in order for them to explore

Delta Pipeline Inc. transitioned to 100% employee ownership in 2017 through an Employee Stock Ownership Plan (ESOP). Learn more here

employee ownership as an option, they need to know that it is an option and be able to access support from qualified technical assistance providers.

» This new round of the State Small Business Credit Initiative (SSBCI) explicitly allows funds to be used for employee ownership buyouts (see regulatory language below). **State agencies in charge of implementing SSBCI should publicly affirm that employee ownership transitions are an eligible use of SSBCI funds** and embrace EO as a potential vehicle for job and business retention and sustainable and inclusive economic development.

» Applications to the U.S. Department of Treasury for technical assistance funding are due October 14, 2022. **State agencies should consider including EO-specific education and technical assistance in their technical assistance funding application.** This would address the demand among businesses for a wider range of strategies for business resiliency and succession.

The State Small Business Credit Initiative Capital Program Policy Guidelines, released November 10, 2021, affirmatively name employee ownership transitions as an eligible use of SSBCI loan proceeds:

Prohibited Loan Purposes – 12 U.S.C. § 5704(e)(7)(A)(i)(II)

Each financial institution lender must obtain an assurance from the borrower affirming that the loan proceeds will not be used to: … Purchase any portion of the ownership interest of any owner of the business, except for the purchase of an interest in an employee stock ownership plan qualifying under section 401 of Internal Revenue Code, worker cooperative, or related vehicle, provided that the transaction results in the employee stock ownership plan or other employee-owned entity holding a majority interest (on a fully diluted basis) in the business.

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