Worker Buy-Out

Description

A worker buy-out occurs when an established firm (or a facility of an established firm) is sold to the employees for the specific purpose of maintaining the jobs of those employees. This strategy is appropriate to the cases in which the community threat is the closure or potential closure of a firm or business facility. However, such closure is sometimes associated with possible bankruptcy or greatly reduced profitability; thus considering a worker buy-out is appropriate only when there is reason to believe that adequate profitability is possible. For example, a firm may plan to close a facility primarily because the rate of profit, say, 8 percent, does not reach or is not projected to reach higher corporate targets of, say, 15 percent. Under worker-ownership however, that same rate of 8 percent would be adequate to maintain the facility where jobs rather than maximum profits are the major consideration. In that situation, the workers and the community are well advised to consider purchasing the facility and running it as an independent business.

There are two types of structures that can be used for a worker buy-out. One is that of the Employee Stock Ownership Plan by which workers may buy different amounts of the company shares; and the other is the general format of the worker co-operative in which each worker-owner buys an equal share. Each of these formats has its own financial attraction. In the ESOP approach in B.C., the worker can receive an annual tax credit, for 20 percent of the investment, of up to $10,000 a year to a maximum of $50,000. In the co-op approach, dividends to workers are not taxed at the corporate level.

Worker buy-outs may proceed under pressure from community and/or employee sources or simply be a routine offer from a retiring owner, or may even be motivated by a retiring owner’s appreciation for his community and workers. One such case was that of Hugh Hamilton Ltd. of North Vancouver, which sold forestry consultation and mapping services. Although the owner had received other offers, he worked with a negotiating committee of employees who would take over when he retired. Today the business is larger than ever before.

Benefits

In addition to the important result of job retention in the locality, worker buy-outs can have the advantage of increasing productivity by enlisting the commitment and energy of the employees when they feel they genuinely govern the venture. Often, even financial performance can be shown to improve in an established venture that becomes worker
owned. Also, as mentioned, there are provincial and federal tax benefits that are targeted to co-op and other worker-owned ventures.

Two case reports will illustrate powerfully the benefits of the worker buy-out. One of these is of a co-op format, the other of the corporate share format. The detail of these cases will also help make clearer the worker buy-out model itself.

Among the successful co-operatives that have evolved from worker buy-outs is an automobile service centre in Moncton, NB, that the six employees purchased when the owner (a co-op itself, ironically) determined, after some years of unprofitable operation, that it should be closed. All of the worker-buyers were very experienced, two of them in their 60s, including the manager who had previously owned his own business in the field. With technical assistance from the original co-op owner and a co-op TA consulting group, they developed a business plan as well as financing (from the local credit union and from their own capital) in two months time from when they were notified of the projected shut-down; and then began operations which were profitable in the first year. Now, the new co-op is ending its second profitable year, having expanded and bought new equipment in the meantime. Another full-time employee has been hired as a mechanic, with an option to buy in as an equal owner. A full-time woman clerk and occasional part-timers in the shop have also been hired.

Especially in the beginning, it meant long hours for the new owners. “If it wasn’t our own business, we would never have put in those hours,” the manager has commented. He added that two other keys to success were managing without being afraid to carry out agreed-upon policies, even if co-workers are friends; and having clear basic guidelines on what each job consisted of. Workers Coop Auto Centre, 7 Foundry Street, Moncton, NB (David Longaphee, Mgr.).

Among the successful share corporation buy-outs is Algoma Steel, the major industry in Sault Ste. Marie, Ontario. Here the corporate owner in 1991 planned a major downsizing for a facility where it had had a history of very poor labour relations, including strikes, lockouts, layoffs, and walkouts. The union proposed employee ownership and produced a business plan. While originally the corporate owner and the banks were unfavorable, federal and provincial financial aid and firm support from the community helped clinch a deal within less than a year and a half. Employees got 57 percent of the ownership and a system by which workers had wide participation in company governance, including representation of the board of directors. To maximize the jobs retained, the workers took a 14.5 percent pay cut together with reduced vacation and a bonus freeze. Worker training for the changeover led to a continuing training program at $7 million annually. The company became the most profitable of its kind in North America. All workers with recall rights were re-hired, and the
pay and benefit cuts were reversed, while job satisfaction and productivity steadily increased. Three years later, needs for capital led the employees to reduce their holding to 30 percent, but this was accompanied by strengthening worker participation in company decision-making.

**Major challenges**

The process for worker buy-outs is difficult and complex, and for that reason almost certainly the group of workers must have outside specialized technical assistance and other support to accomplish their goals. A local CEDO may offer some of that support, as would national and regional specialized technical groups, accustomed to aiding worker-ownership efforts.

Moreover, the worker-owned structure (whether as a corporation or as a co-operative) places a premium on the skill and capacity of the workers to collaborate in management decisions, including any delegation of management responsibilities to a sub-group or individual. Thus key to success, quite apart from the conventional issues that any business must confront, is the initial training of the organizing group of workers, so that they are oriented to the perspective and tasks of group ownership and management. Also, a program of on-going training must be maintained for both continuing and new workers.

An additional major challenge for most buy-outs is to reach an early recognition of the tasks involved in taking over the firm. Most frequently, the circumstances of a company (or facility) that is about to close do not allow much time for its workers, management, and extant owners to solve all the necessary problems of a transfer of ownership. Thus the swift entry of appropriate technical assistance responsive to the workers will be important.

And finally, it is unfortunately true that all too frequently the established firm that is closing a facility in the community but expects to continue operations elsewhere will be reluctant (for good or bad reasons) to enter into negotiations with the workers (or others) interested in a buy-out. The task of even getting consideration of a buy-out may require extended and strenuous negotiations, never mind the terms of the buy-out. It is in that task that broad community support is critical.

**Some practical steps**

1. Employees must organize themselves to consider and decide on whether to pursue a buy-out.
2. They will need to seek out technical assistance organizations that are experienced in the process of worker buy-outs; and they will usually need to enlist the friendly aid or sponsorship of community organizations, unions, and even political figures.
3. The current owners must be approached to ascertain the degree of willingness to negotiate; and, if possible, the owners should be gotten publicly committed to at least considering a potential buy-out.

4. A formal feasibility study must be carried out to determine if the business can be successful under worker ownership; and a business plan will have to be developed, based upon the feasibility analysis.

5. As part of the feasibility and planning effort, it will be necessary to explore the availability of financing, beyond what the workers themselves can provide.

6. All through this process, the workers will need to be teaching themselves, with the help of technical consultants, the ins and outs of the business and its management tasks.

Resource organizations & contacts

- Specific consultation on starting a buy-out as well as on later managerial problems can be obtained from Employee Ownership and Incentives Association (EOIA) in Vancouver (toll free: 877-387-3767). They also have such aids as legal templates and basic publications. EOIA is affiliated with a similar Ontario group and with the National Center for Employee Ownership, 1736 Franklin St, 8th Floor, Oakland, CA 94612-3445 (tel: 510-208-1300; fax: 510-272-9510, e-mail: nceo@nceo.org, website: www.nceo.org).

Other contacts for corporate structure cases include:

- For B.C. projects, the provincial Employee Share Ownership Program (George Kennedy at 604-660-1045); Employee Share Ownership and Investment Association (Julia Markus at 604-687-3767);
- The Niagara Enterprise Agency (Glenn Stansfield at 905-687-8327).
- General assistance is also available from the non-profit Worker Ownership Resource Centre (604-520-3341).

For co-operative structure cases:

- Canadian Co-operative Association (CCA), B.C. Region (John Restakis at 604-662-3906).
- Diane Fitzgerald, Atlantic Cooperative CED Institute, P.O. Box 1872, Truro, NS B2N 6C7 (tel.: 902-899-0070; fax: 902-893-0109).

Publications

- EOIA (above) has many useful publications, particularly the Employee Buyout Handbook.
- Employee Ownership: An Ontario Perspective (Niagara Enterprise Agency, see above).
- For potential worker co-ops, CCA/BC (address above) has an array of materials.