

# COOPERATIVE OWNERSHIP TRANSITIONS

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## Moving Cooperative Conversions Forward With Owner-Led Transitions

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### Why Owner-Led Cooperative Ownership Transitions?

The worker cooperative community has long recognized the potential of converting existing businesses as a way to rapidly scale worker ownership while also providing a valuable tool for anchoring jobs and businesses in communities. However, the rate of cooperative conversions has remained relatively stable despite growing interest in employee ownership from the localist, sustainable, and good business communities.

While there are undoubtedly a number of reasons for the low rate of business transitions, one large factor may be the mismatch between the traditional cooperative conversion process and the realities of owning and running an operating business. A traditional cooperative transition requires several things to happen all at once: the owner rapidly (within a year) devolves control to their employees, while the employees must grow their capacity to govern and manage the business in the same period, all while conducting the purchasing process, operating the business, and enjoying their daily lives. This timeline is daunting to say the least.

Many case studies of cooperative conversions show that the transition process truly takes around five years to firmly shift the culture of the cooperative. An owner-led process recognizes that timeline by leaving most decisions in the hands of the owner, their leadership team, and cooperative developers at the start of the process, while building the capacity of the employees to own, govern, and manage the business over time.

### What Does an Owner-Led Transition Look Like?

In an owner-driven process, the owner, leadership team, and cooperative developers:

- Draft the starting bylaws for the cooperative, including initial membership criteria
- Work with an outside valuation firm and financiers to set a fair price for the business
- Define a plan for the cooperative members to assume increasing levels of governance control from the former owner, as shares are transferred from the owner to the cooperative.
- Define a 2-3 year management plan for the cooperative
- Commit the cooperative to a training and capacity building plan for new worker-owners, board members, and managers
- Create an offering document for the final sale, and communicate it to the potential worker-owners in plain language. Employees have the opportunity to buy in to the company at this offering, or to remain employees without ownership.

After the sale takes place, the company can best be described as a proto-cooperative, with a board composed of worker-owners and the former owner's appointees, including possibly the former owner. The company then undertakes a process of participatory culture creation and democratic ownership trainings at a pace appropriate to their business cycle. As these trainings conclude and the owner's shares and board appointees drop below having any form of control in the business, the business can be truly called a worker cooperative.

## What are the Challenges of an Owner-Led Transition?

The three chief obstacles to the long term success of an owner-led transition are similar to those in any traditional conversion: appropriate valuation of the business, lack of access to growth capital, and the successful transfer of leadership from the original owner(s) to the new cooperatively run business and its Board of Directors.

In recognizing these challenges and facing them head-on, an owner-led conversion is perhaps better suited to address them than the conventional all-at-once conversion method.

- **Valuation:** It is critical that the owner come to the table to negotiate a price with a knowledgeable bargainer. This neutral party could either be a second cooperative or business developer equipped with an independent valuation, or the primary financiers of the deal, who have a strong interest in not overburdening the company with more debt that it can handle. It is often necessary for the owner to self-finance a portion of the deal; if that note is the most vulnerable financing in the transition, this may help ensure the owner does everything possible to support the company's success after their departure.
- **Capital Access:** An owner-led transition may be a stronger loan candidate than a less structured cooperative conversion, since a structure with a clearly defined transition period for both ownership and management is more likely to inspire the confidence of loan officers and other financing sources to invest their capital.
- **Leadership:** Clearly, the transition of governance, and the implementation of a functional participatory culture is key to any successful cooperative ownership transition. For that purpose, any business of significant size should negotiate a training contract and scope of work with the appropriate sources for cooperative and business technical assistance before the sale is made to the new worker-owners. Excellent and comprehensive technical assistance will mitigate risk for all parties. An investment in training will help create a culture of investment in worker-owners, and in the business, that is necessary for fostering a true feeling of cooperative, and in turn good governance, engagement in management, and a constantly improving business.

## Are Owner-Driven Transitions the Way Forward for Cooperative Conversions?

Adhering strongly to cooperative principles while thinking creatively about how to transition to a full cooperative model could be just the new approach needed to meet the growing interest in cooperative ownership transitions. There is enormous potential locked up in the millions of businesses with retiring owners and no succession plan. Owner-driven conversions – and the tools to support them – may just be the key that unlock possibility and support business transitions moving forward at a speed and scale that makes a real difference.