Employee Ownership as a Mechanism for Reducing the Racial Wealth Gap in Mecklenburg County

THE CURRENT STATE OF EMPLOYEE OWNERSHIP AND OPPORTUNITIES FOR EXPANSION 2022

UNC CHARLOTTE
Urban Institute

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INTRODUCTION

Wealth disparities between the races in Charlotte - Mecklenburg region cut deep and wide.

In 2014, Charlotte was ranked last in upward mobility among the 50 largest U.S. cities, meaning there is only 4.4% likelihood that children from the families at the bottom of the income distribution will achieve a higher standard of living than the household in which they were reared. For Black families, the probability is even lower at 2.6%. Today, nearly one in three Black or Latinx households in Charlotte have a zero or negative net worth. Lack of wealth decreases the odds of buying a home, accessing business opportunities, saving for retirement, and passing down wealth to their children.

Despite the growing body of research on the benefits of employee ownership as an asset building strategy, too little is known about the ways it can help to close the growing racial wealth divide. It can be largely attributed to the fact that only 10% of the national workforce has ownership in the organizations where they work, and Black and Latinx workers having even less employee ownership. This research aims to fill the gap in the understanding of the wide-ranging advantages of employee ownership to equalize wealth-building opportunities.

Wealth is critical to economic stability. For people of color, business ownership plays a significant role in building wealth. However, they represent only 18 % of the nation's 5.6 million business owners with employees. According to the U.S. Census Bureau, there are 36.742 minority-owned businesses in Charlotte-Mecklenburg[1]. The Covid-19 pandemic crisis has disproportionately impacted those businesses across all sectors and industries, forcing many to close or sell to larger corporate competitors. For communities of color, the loss of local ownership can be devastating, and it can irreversibly affect the community's vitality and character. Moreover, the crisis revealed that 80% of the U.S. small business owners do not have a written succession plan, and many have never discussed exit plans[2]. As a result, such business owners jeopardize their families' ability to transmit wealth down to future generations and guarantee that jobs are kept in the areas where they operate.

The accelerated retirement of the Baby Boomers induced by Covid crisis will speed up a "silver tsunami" of business sales or closures, meaning a potential transfer of billions of dollars in business assets to new owners. Currently, the Baby Boomers cohort owns 46% of all businesses with employees in Mecklenburg county[3]. The absence of succession plans poses a substantial problem for those business owners, but also represents an opportunity for increased employee ownership.

This twin business crisis has spawned a renewed interest in employee ownership as a resilient tool for driving equitable economic recovery and growth. Employee ownership, often called "the best-kept secret of our economy" can concurrently address a number of the factors contributing to racial wealth gap. It has been found to reduce wealth disparities by providing equity to working-class people and distributing

> *"Wealth gives you choice. Wealth gives you freedom. Wealth gives you opportunity. But it takes wealth to beget more wealth."*
>
> *Darrick Hamilton, the Duke University*

INTRODUCTION

wealth more evenly across all demographic groups. In addition to the positive impact on wealth distribution, some forms of employee ownership give small business owners access to liquidity at fair market value and an opportunity for workers to diversify their assets efficiently. It can significantly improve business closure to sales ratio helping business owners of closely held companies to retire with significant wealth and sustain local jobs.

The results of our study suggest that employee ownership has been an underutilized tool among Charlotte businesses. Almost 80% of respondents didn't express an interest or were unsure about pursuing an employee-owned model for their companies. However, our analysis shows that Charlotte has an existing market for conversion of smaller minority-owned firms. Converting those companies into employee-owned to preserve their business legacy and provide wealth-building opportunities to their workers is a pressing opportunity.

Because recognizing the scope of a problem is pivotal to solving it, UNC Charlotte researchers and the North Carolina Employee Ownership Center (NCEOC) undertook this study to identify the underlying issues that prevent local business owners from entering the employee ownership model. In addition, the study highlights ways to help more people embrace it in the Charlotte - Mecklenburg area.

Understanding the local context will allow the development of a better business support ecosystem and reduce the growing racial wealth inequality triggered by the twin business crisis.[4] Education and outreach can be a cost-effective and robust approach. Therefore, one of the purposes of our study is to educate the Charlotte business community and local decision-makers about the benefits of employee ownership as a strategy that contributes to the resilience of the local businesses and helps improve the communities they operate in.

We found that Charlotte can gain a lot from supporting employee ownership as an innovative strategy to bridge the growing racial wealth gap. The family wealth-generation process starts in the community, and building a stronger community for the benefit of existing residents and employers will have a long-term impact on attraction of asset-building opportunities.

Therefore, employee ownership should be embraced as an innovative tool within a larger strategic framework and anchored within the local context and community to capitalize on the opportunity. If widely adopted, it could substantially leverage economic mobility and wealth-building opportunities for people of color while strengthening the local economy.

This study paves the way for future programs that assist businesses in transitioning to employee ownership by increasing understanding of the current state of employee owned businesses in Charlotte-Mecklenburg, identifying employee ownership candidates and raising awareness of employee ownership among local business owners. The white paper also outlines the long- and short-term recommendations to address the racial wealth gap in Mecklenburg County through employee ownership strategies and sets a stage for further discussions.

DEFINITIONS

Wealth or net worth, the total of household financial and non-financial assets less any debt or liability

Employee Ownership, any arrangement in which a company's employees own shares in their company or the right to the value of shares in their company[1]

Employee Ownership Culture is one where employees feel a sense of ownership over decisions, results and performance

Minority, a group of the population that ethnically or racially differs from the majority group – white, non-Hispanic.

Small business, independent business having fewer than 500 employees[2]

Minority-owned business, a company owned, operated or controlled by an individual who is an ethnic or racial minority[3].

Certified Minority Business Enterprise includes businesses that receive certification, formally recognizing them as a minority-owned business or enterprise.

Legacy Business, typically, small local company with under 20 employees which has been in operation for 20 consecutive years.

Support organizations include organizations that provide resources, services or products to minority-owned small businesses.

Ecosystems include businesses and the organizations that support them. These organizations range from non-profit to private agencies.

Infrastructure, the physical, technical or organizational structures and/or facilities needed for the operation of an enterprise.

Financial capital, the money used to produce goods, provide services and fund future growth.

Demutualization, conversion referred to changes in the ownership structure of user-owned and controlled organizations from a cooperative (or mutual) to a for-profit, proprietary organization[4].

Microbusiness, small business with 1-9 employees and those that are "nonemployer businesses" and have no paid employees

Upward mobility, the movement of individuals, families, or any other categories of people from one social level or stratum to a higher one

[1] NCEO, What is Employee Ownership
[2] U.S. *Small Business*Association (SBA)
[3] National Minority Supplier Development Council (NMSDC)
[4] Chaddad, 2003

Understanding the context

VICIOUS CIRCLE OF RACIAL WEALTH INEQUALITY

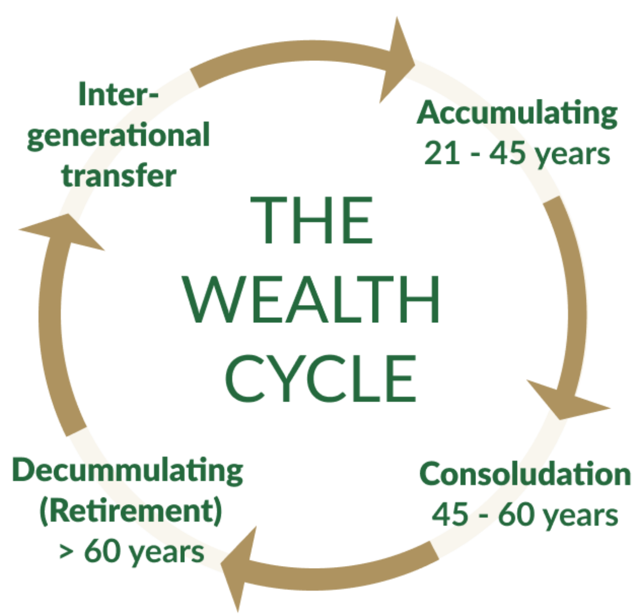
Employee-owned businesses create wealth for their employees. They cultivate great cultures, outperform the competition, and help to strengthen local economies.

However, less than 10% of the American population has ownership in the organizations where they work. According to the National Center for Employee Ownership (NCEO), around 7,200 private enterprises utilize various forms of employee ownership in the U.S. [5] Examining the impact of the economic shift to broad-based employee ownership on wealth concentration in the U.S, Dudley & Rouen (2021) argued that if all private firms became 30% employee-owned, those currently in the bottom of the wealth distribution would see substantial gains, with many of these gains going to traditionally marginalized communities. [6]

There is a stark and widening racial wealth gap in the United States created through decades of discrimination, economic and political injustice, and a shortage of social capital in those communities. As a result, particularly Black and Latinx families continue to face cumulative and systemic hurdles in creating wealth within a single generation, let alone across generations.

However, wealth is critical to economic stability. Household wealth, or net worth, is understood as the value of all family assets minus debt. Wealth reflects a family's ability to deal with unexpected financial challenges such as job loss or economic crisis and provides security to achieve and maintain financial stability. Moreover, family assets can be leveraged or invested, contributing to the more stable future of the current and next generations of a family. Other forms of wealth accumulation include business and homeownership, education and job skills, access to savings plans, inheritance, gifts, and individuals' savings. Unfortunately, Black and Latinx minorities have uneven access to each of these components. Today, the typical white household has eight times the wealth of the typical Black household and five times the wealth of the typical Latinx household[7]. Lack of wealth prevents them from moving to better and safer neighborhoods, accessing business opportunities, saving for retirement, and investing in their children's education.

Racial wealth gap grows with age. Whites in their 30s have three times as much average wealth as Blacks, and in their 60s, they have seven times as much. Those wealth disparities also correlate with substantial inheritance disparities, resulting in lower levels of “starter” wealth for future generations. In 2019, only 8% of Black and 5% of Latinx families received an inheritance, compared to 26% of white families, and their inheritance value was 65% lower than that of white families. [8]

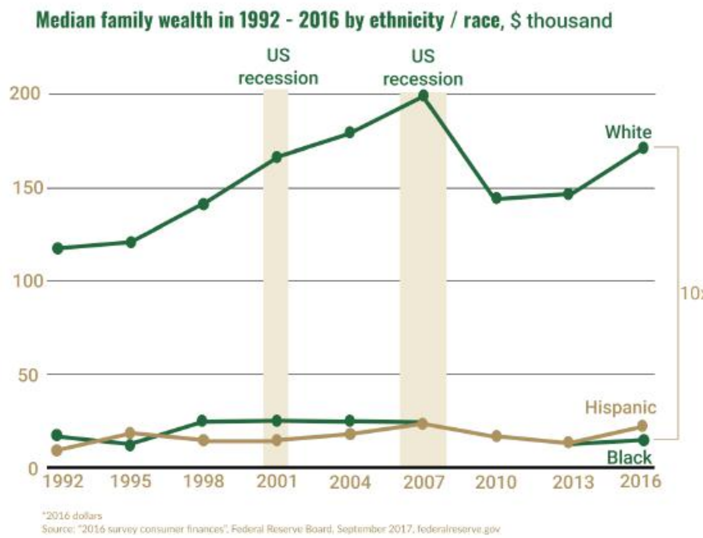


Understanding the context

VICIOUS CIRCLE OF RACIAL WEALTH INEQUALITY

Lack of inheritance and family financial support negatively impacts the family's prospects of becoming homeowners or moving into more economically advantaged areas.

Examining the racial wealth gap in Charlotte-Mecklenburg, we found patterns consistent with national trends. Nearly one in three Black or Latinx households in Charlotte have a zero or negative net worth. In the event of income loss, nearly 50% of Latinx families and 45% of Black families would be unable to afford necessities for a three-month period. Additionally, home ownership rates are 27% lower among Black households and 31% lower among Latinx households, compared to white households[9]. Over 60% of Black and Latinx households do not have retirement savings through traditional retirement accounts.



Growing up in poorer neighborhoods, characterized by lower economic activity and access to opportunities, Black and Latinx become trapped in a vicious circle of wealth inequality from the early years. Obstacles that reduce their future earning potential and the likelihood of achieving higher standards of living in the future come in the form of poor school quality, differential treatment in the criminal justice system, racial discrimination in the workplace, reduced access to high-paying jobs, and a lack of mentors and role models who can guide professionals' career advancement. In 2015, in Mecklenburg county, only 17% of Latinx and 19% of Black households with income in the bottom of the income distribution had a bachelor's degree or higher compared to whites and incurred on average $11.778 in student loans. A lower level of education attainment and growing student debts further complicate the financial challenges of Black and Latinx young adults and constrain their future economic mobility. Moreover, they negatively affect the skills people of color bring to businesses they create and restrict their access to business credit and growth opportunities. Those disparities are then passed on to the next generation, beginning the cycle again.

TALE OF TWO CITIES:

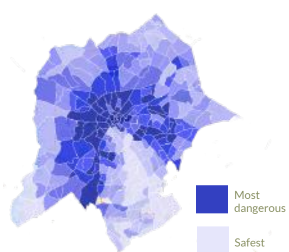
The City of Poverty, the City of Prosperity

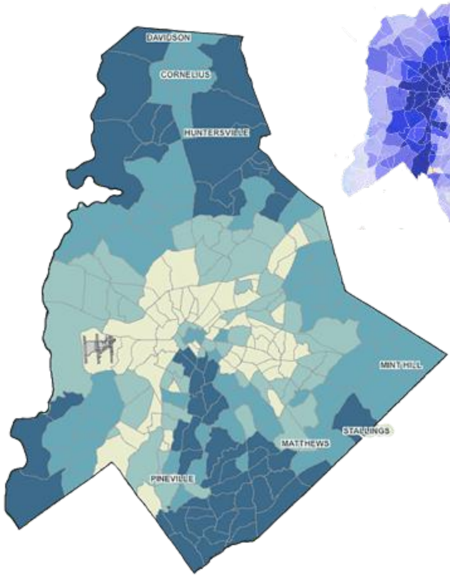
More than any other culprits of racial wealth inequality, intergenerational mobility in Charlotte comes with a narrative. Despite the growing number of new jobs and booming economy, the Land of Opportunity Study (2014) ranked Charlotte last in upward mobility among the 50 largest U.S. cities[10] Children from the families in the bottom quantile of the income distribution, with an annual household income of $27,000, had only a 4.4% probability of reaching the top quantile as adults or earning over $107,900 in household income. The probability for Black families in Charlotte was even lower and accounted for 2.6%[11]. Racial and residential segregation, lack of family stability, and opportunities in the neighborhoods with a higher concentration of minority population were among the primary reasons for the low positioning.

Charlotte is deeply divided geographically by income and wealth, which can explain profound disparities in economic mobility across racial groups and separate neighborhoods within the community. The top 20% of households earning more than half of the city's wealth are located in the South of Charlotte, which makes up less than 25% of the geographic area of the city. Only 7% of white residents live in poverty, compared to 18% of Black and 25% of Hispanic Charlotteans. Structural differences in mobility limit the potential for overall economic growth and exacerbate inequalities in other areas such as education, housing, and access to opportunities. Lower upward mobility in American communities is largely driven by dramatic economic disadvantage among Black men.

Upward Mobility in Charlotte Mecklenburg

Charlotte Crime Rates[4]





1 in 3

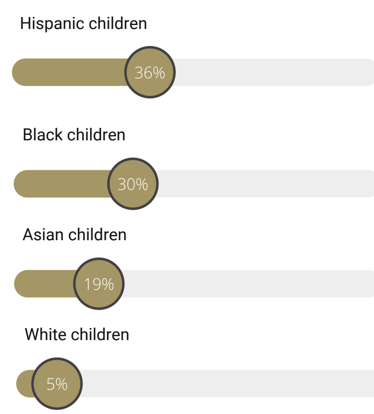
Single Moms

in Mecklenburg County live in POVERTY

2.6% OF BLACK **12%** OF WHITE

FROM THE BOTTOM QUANTILE WILL MAKE TO THE TOP AS ADULTS[3]

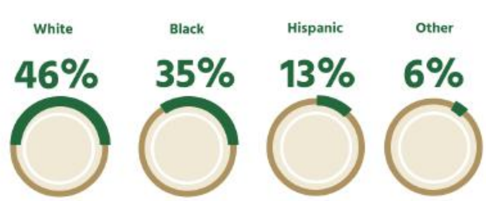
Child Poverty in Mecklenburg County



Median Household Income for Charlotte Mecklenburg

$76,947 - $200,000 | $53,505 - $76,946 | $36,505 - $53,504 | $0 - 36,504[1]

Racial Breakdown in Charlotte



Segregation in CMS schools[2]

1 in 2 schools are segregated by race
1 in 3 schools are segregated by poverty[2]

1. U.S. Census Bureau, 2013 American Community Survey
2. North Carolina Department of Instruction, 2012-13)
3. Chetty et al., 2014
4. FBI Database, 2021

TALE OF TWO CITIES:

The City of Poverty, the City of Prosperity

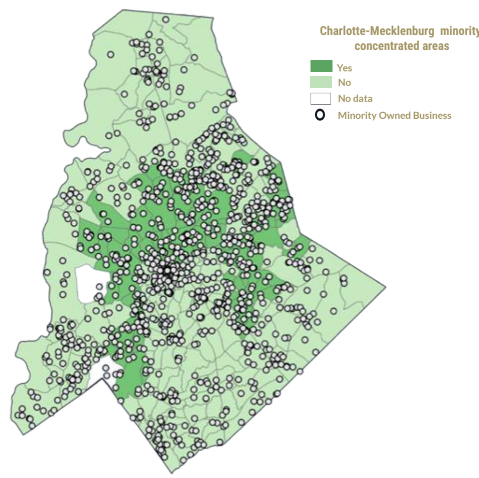
In Charlotte, Black men who grew up in low-income families have an average household income of $19,000 in their mid-thirties, compared to $32,000 for white men growing up in a similar neighborhood.

Business ownership plays a significant role in building wealth for people of color and can boost their economic mobility. However, almost 40% of Charlotte-Mecklenburg minority-owned businesses are located in economically disadvantaged, minority-concentrated neighborhoods[12]. The lack of businesses and jobs in those neighborhoods fuels not only a crushing cycle of poverty but also crippling social problems, such as drug abuse and crime [13].

It is common for small subscale businesses to be excluded from the wider economic activity in an area. Insufficient access to capital, networks and markets beyond their neighborhoods limits their potential to grow wealth for their families and attract the community's own spending power. Employee ownership can address many culprits of economic problems facing those neighborhoods by significantly improving access to wealth-building opportunities.

Today many U.S. cities, such as New York, Philadelphia, Washington, or Cincinnati, choose employee ownership as a part of their long-term workforce development strategies.

Intergenerational mobility, often aligned with zip codes, is a local problem, "one that could potentially be tackled using place-based policies"[14]. However, the effectiveness and efficiency of those policies largely depend on the political will of local governments and require enormous amounts of financial and human resources.



Source: UNC Urban Institute. Minority-Owned Small Businesses, Charlotte-Mecklenburg, 2021

Benefits of Business Ownership

White-owned businesses	**Asian**-owned businesses	**Hispanic**-owned businesses	**Black**-owned businesses
create 55.9 million jobs*	**create 3.8 million jobs**	**create 2.5 million jobs**	**create 1 million jobs**
which is enough to	which is enough to	which is enough to	which is enough to
employ 44% of the working-age White population	**employ 33% of the working-age Asian population**	**employ 8% of the working-age Hispanic population**	**employ 4% of the working-age Black population**
and with annual revenues of	and with annual revenues of	and with annual revenues of	and with annual revenues of
$12.9 trillion	**$793.5 billion**	**$473.6 billion**	**$187.6 billion**
they could give EVERY working-age White American a check for	they could give EVERY working-age Asian American a check for	they could give EVERY working-age Hispanic American a check for	they could give EVERY working-age Black American a check for
$102,000	$67,000	$14,000	$7,000
every year	**every year**	**every year**	**every year**

* jobs = hired employees. This does not include owners of businessses who only employ themselves.
Source: U.S. Census Bureau, 2012 Survey of Business Owners, 2012 Census Bureau Annual Estimates of the Resident Population by Sex, Single Year of Age, Race, and Hispanic Origin for the United States: Population Division
Black-owned business: Blacks or African Americans own 51 percent or more of the equity, interest, or stock of the business.
Working-age adults: adults age 18-64. All figures are rounded.
Table adapted from BlackDemographics.com

TWIN BUSINESS CRISIS

The Covid-19 pandemic has disproportionately impacted the small businesses across all sectors and industries, forcing many to close or sell to larger corporate competitors. As a result, the number of Black business owners dropped by a staggering 41%, and the number of Latinx business owners fell by 32%[15]. According to the National Urban League survey, almost 80% of the surveyed business owners of color do not have a written succession plan, and many of them have never discussed their exit plans. Such business owners jeopardize their families' ability to transmit wealth down to future generations and to guarantee that jobs are kept in the areas where they operate.

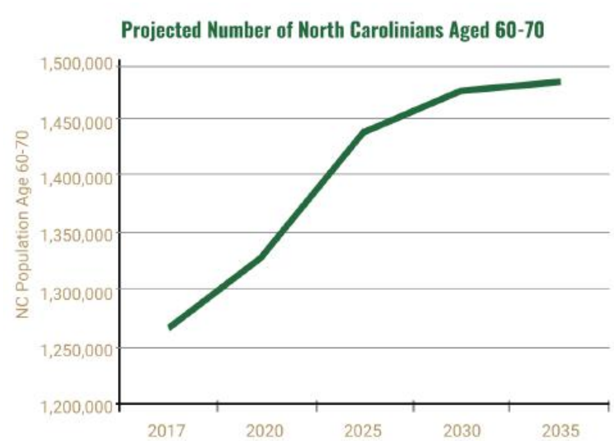
Furthermore, the American population is graying at an unprecedented rate, with 10 000 Baby Boomers turning 65 every day. The rapid demographic aging trend indicates that these numbers will only grow. By the year 2050, every fifth American will be 65-year-old or older. Currently, the Baby Boomers cohort owns 46% of all Mecklenburg businesses[16] with employees, and their retirement underpinned by the Covid crisis will speed up a "silver tsunami" of business sales or closures, meaning a potential transfer of billions of dollars in business assets to new owners.

In North Carolina, business closures outnumber business sales five to one, and many of the businesses that close provide jobs and services that are vital to local communities. Additionally, failure to plan for business succession poses a substantial problem for retiring business owners, many of whom are people of color.

The Twin Business Crisis sprawled a renewed interest in employee ownership as a resilient and innovative tool for driving equitable economic recovery and growth. A recent study by Aspen Institute showed that during the Covid pandemic, employee-owned companies were 3.2 times more likely to retain staff than non-employee-owned businesses. Amidst the pandemic, employee-owned businesses were significantly better at protecting the health and safety of their employees and were more likely to send employees home to work which resulted in maintaining working hours[17]. With unions power eroding and the new economic crisis looming, employee ownership could significantly contribute to business resilience and job retention in our communities and play an essential part in supporting their economic progress.

5 to 1

Ratio of business closures to business sales among North Carolina businesses operating more than 25 years



Source: Office of State Management and Budget. State/County population projections. Down Home Capital report

WHAT IS EMPLOYEE OWNERSHIP?

Employee ownership is a broader concept that encompasses various forms. It refers to any scenario where employees own shares or the right to share in the companies they work for. These arrangements may take several different forms that can be tailored to meet the specific needs of individual companies. For small business owners, business succession can be the most common trigger for transition. For example, retiring owners can defer or entirely avoid capital gains taxes by selling stock using an Employee Stock Ownership Plan (ESOP). Other points relevant to adopting employee ownership during the business lifecycle include expansion and growth, business rescue, or start-up. According to Kruse & Blasi (1995), employee ownership is defined across the following dimensions:

- the percentage of employees who participate in the ownership
- the percentage of ownership held within the company by employees
- distributions of ownership stakes among employee-owners
- the rights and privileges that ownership confers upon employees

Forms of Employee Ownership: Find the Right Fit for Your Company

The two most common types of employee-owned business plans are Employee Stock Ownership Plans (ESOPs) and worker cooperatives, both of which provide employees with wealth building opportunities.

ESOPs

Under ESOPs, company assets are held in a trust, and profits are reinvested in employee 401k plans. When employees retire, they receive their shares or the cash value of those shares. Typically, companies use credit to fund the purchase of company shares by ESOPs. As the loan is paid off, the company distributes the shares to all employees with ESOP accounts. In a "leveraged" ESOP, the ESOP borrows money and buys the owner's stock. The ESOP stock is allocated to employee trust accounts. The company usually guarantees the loan and contributes enough money each year to enable the ESOP to repay the loan. In a "non-leveraged" ESOP, the ESOP uses company contributions to purchase stock each year rather than to repay a loan. The company deducts the contributions from its taxable income.[18]

Worker Cooperatives

In worker cooperatives, employees directly own a portion of the business, are entitled to one voting share, and receive regular payments through profit sharing. Worker cooperative model is more common among small businesses who have close ties with their community and put worker and community benefit at the core of its purpose[19].

In North Carolina, five or more people may organize a cooperative association for any lawful purpose[20]. After each profitable year, a coop invests some of its surplus in retained earnings[21] and allocates the rest to individual worker-owners on the basis of “patronage,” which is typically measured by work performed or hours worked. Some of the patronage then stays in the members’ internal capital accounts, which are itemized on the company’s balance sheet, and the rest is paid out in cash to the members.[22] The wealth that the business generates is thereby directed to those who create it through their labor.

In cooperatives, worker-owners largely benefit from workplace democracy. Surveying worker cooperatives in various industries, the Institute Co-op study found that the non-financial benefits of workplace democracy may be more important than wages to workers in cooperatives relative to those in traditional firms[23]. The majority of workers in worker cooperatives across the United States are women and people of color. According to the 2019 Worker Cooperative Economic Census, women make up 62% of all worker cooperative employees. Black and Latinx make up 13% and 38%, respectively [24].

WHAT IS EMPLOYEE OWNERSHIP?

Employee Ownership Trusts

Employee Ownership Trusts (EOT) are a relatively new form of employee ownership "imported" from the U.K. and gaining popularity among U.S. businesses. Under EOT, employee-owners do not accumulate shares in individual accounts but receive a percentage of ongoing profits throughout the duration of their employment. Shares are transferred to the EOT and held perpetually on behalf of all present and future employees. This legal structure is significantly less expensive and time-consuming to establish and govern than ESOP and requires neither annual valuation nor regulation with the Department of Labor. The trustee manages the business on behalf of the staff. Unlike in ESOPs, EOT owners do not receive any significant tax benefits. However, EOT can be a neat succession solution for business owners willing to trade off tax advantages and value maximization for other, usually socially beneficial, gains. Those may include preserving business character, employee well-being, giving back to the community, or social and environmental values. One of the differentiating features of EOT is that, unlike in ESOPs and worker cooperatives, trust can be designed to sustain employee ownership of the company in perpetuity without the risk of unwanted sale. A trustee of ESOP, for instance, is obliged to sell the company out of employee ownership when a sufficiently high offer is made, which can effectively discontinue employee ownership. For worker cooperatives, demutualization can significantly impede employee ownership perpetuity.

> *"The precise model a business will use to adopt employee ownership will differ according to the objectives of the business and its circumstances. This diversity of the precise model used is a strength and reflects the dynamism of the sector."*
>
> *Graeme Nuttall, 2012*

Forms of Employee Ownership

for Closely Held (Private) Companies

ESOP

- Good for established company with over 15-20 employees and annual revenue over $ 2 million
- Primary use: to be a new owner of the business, often when the current owner wants to retire
- Can own any percentage of company
- Seller and company motivated by tax deduction
- Regulated by Internal Revenue Service (IRS) and US Department of Labor (DOL)
- Requires annual independent valuation
- High set-up and ongoing costs offset by tax benefits

Worker Co-op

- Works best in small companies
- Primary use: preserve the culture, protect the work force, or maintain a values-based decision-making process; business transitions in closely held companies[1]
- Less expensive and less regulated than ESOPs
- Harder to raise capital due to co-op member control rules
- Workers are the owners & not subject to oversight by a trustee
- Dividends based on hours worked and are tax-deductible to the company
- One vote per person
- 100% of company owned

EOT

- Primary use: business perpetuity and employees' well-being
- Significantly less expensive and less time-consuming than ESOPs
- Doesn't require annual valuations
- Not regulated by the Department of Labor
- Profit sharing paid to employees is a deductible expense
- Can own any percentage of company
- Can choose their own formulas for profit sharing
- Shares are owned by an EOT, not the individual employees

[1] NCEO, Employee Ownership Guide

BREAKING THE LOOP

How can employee ownership bridge the racial wealth gap?

There are several reasons why employee ownership can be a more sustainable, inclusive, and resilient solution for closing the racial wealth gap.

It was found to reduce wealth disparities by providing equity to working-class people and distributing wealth more evenly across all income demographic groups. Using data from the Survey of Consumer Finances, Dudley and Rouen (2021) provided robust evidence that only a 30% shift in broad-band employee ownership would have a dramatic positive effect on the total wealth gains of those at the bottom of the wealth distribution, while only having an impact on the top 1%. For example, the net wealth of the average Black family could grow more than 400%, from $24,100 to $106,271, and the effect would be similar on those with no high school diploma. [25]

Although employee ownership wealth does not substitute for lower wages or other forms of wealth, it was linked to diversified wealth-building opportunities for worker-owners. There is empirical evidence that ESOP companies are more likely to also set up 401(k) accounts, and that these accounts tend to be diversified, often because companies provide investment advice to achieve that outcome.[26]

According to the 2020 Annual Business Survey, Latinx employee-owners have twelve times the median wealth of Latinx households nationwide, while Black employee-owners have three times the median wealth of Black households. Employee owners of color have a 30% higher wage income than non-employee owners of color. Women employee owners earn 17% more than their non-employee-owner counterparts.[27]

In addition to the positive impact on wealth distribution, some forms of employee ownership give small business owners access to liquidity at fair market value. Employee ownership was also found to positively affect post-adoption business performance and job outcomes for workers. Workers at employee-owned companies are more likely to benefit from better job security and improved well-being. They are seven times less likely to be laid off and have an average of $147, 522 in retirement savings from their ownership stake[28]. Study of National Longitudinal Survey of Youth (2020) found that formerly incarcerated ESOP employees earn 25% more in annual income compared to formerly incarcerated workers who are employed but not working for an ESOP firm. They are also significantly less likely to be arrested, convicted, and incarcerated.

The studies on compensation under employee ownership showed that ESOPs have higher survival rate in the time of unfavorable economic situations. That can be largely attributed to the fact that complementary asset-building policies adopted along with ESOPs give employees more economic flexibility, which in turn creates a more committed workforce.

> *"As more small business owners age and look to transition their businesses, employee ownership is a great option to keep jobs and profits local."*
>
> *M.A. State Rep. Paul Mark*

BREAKING THE LOOP

How can employee ownership bridge the racial wealth gap?

Employee ownership dividend pays off at three levels: for business owners, for employees, and for communities and the wider economy which makes it a potentially strong tool to address the widening racial wealth gap.

Employee ownership benefits

BENEFITS FOR BUSINESS OWNERS

- Tax incentives
- Immediate access to capital at fair market rates
- Opportunity of assets diversification
- Greater levels of business productivity and efficiency
- Higher workforce retention
- Strong and resilient business strategy in the long run
- Committed and engaged workforce
- Happy customers
- Succession plan in place

BENEFITS FOR EMPLOYEE OWNERS

- Higher salaries
- Increased retirement security
- Improved health and well-being through better quality of working environment and work-family balance
- Building resources for intergenerational transfer of wealth
- New and advanced working skills through job trainings
- Work in collaborative environment
- Sense of ownership over decisions, results and performance = nurturing ownership culture

BENEFITS FOR COMMUNITIES

- Keep wealth and jobs in the community
- Preserve and scale up community-anchored businesses
- Bring new business and financial opportunities
- Improve livability and economic growth
- Social equity
- Mentors and role models
- improvement of the community vitality and character

OWNERSHIP CULTURE

One of the primary purposes of employee ownership is to create a highly engaging culture in the organization.

When "financial ownership is bundled with an ownership culture"[29] the actual effect of employee ownership as a wealth-creating mechanism can be much broader. Ownership culture positively affects productivity and performance of the business and improves employees' well-being. According to NCEO, companies with ownership cultures generate an incremental 6% to 11% growth per year beyond what would be expected based on their previous performance.

Ownership culture also gives workers an additional path to building wealth by developing soft skills such as problem-solving, idea-generating and leadership skills. Exploring the managerial approach to employee ownership, Weitzman & Kruse (1990) argued that ownership culture is key for better performance. It “emphasizes company spirit, promotes group cooperation, and encourages social enforcement”.[30] Moreover, several studies showed that companies nurturing ownership culture tend to be more competitive, more resilient during economic downturns, and less likely to move out of their communities. The latter is crucial for "legacy businesses," which contribute to the community's vitality and identity and are more often owned by people of color.

RESEARCH

Objectives and methodology

When identifying the potential of employee ownership in closing the racial wealth gap in Mecklenburg County, it was essential for us to get a baseline understanding of the current state of business ownership and determine the feasibility of employee ownership expansion in the region. First, we surveyed local minority business owners to assess their business demographic information and familiarity with employee ownership models. Questions ascertaining business demographic characteristics included the age of the business, the demographic makeup of employees, and the company's financial stability, all of which influence the feasibility of transitioning to employee-owned businesses. We also assessed participants' general understanding of the different forms of employee ownership and their utility, perceptions and attitudes to employee ownership transition, and the model's suitability for their businesses.

Participants were recruited via email to complete surveys using the Mecklenburg County Minority, Women, and Small Business Enterprises (MWSBE) database (N=1403) as the sampling frame. Before sending the survey, the study team created a one-page fact sheet highlighting information about employee-owned businesses to disburse via email to a list of selected MWSBE business owners. The fact sheet introduced MWSBE firms to employee ownership. It also served to increase response rates by framing participation in a survey as a chance to learn about a potential business strategy for the company. Respondents were entered in a random drawing for a chance to win one of three $100 DoorDash giftcards. Survey questions consisted of 20 multiple choice and open-ended questions and 24 Likert scale questions. Descriptive statistics and analysis of the survey responses were performed. Weights were applied to gender, race, business type, and industry to reflect the population of Charlotte MWSBE businesses more closely.

One hundred eighteen participants completed the survey and met the eligibility requirements of being in a C-suite or decision-making position in their respective companies. Based on the survey results, the expertise of the NCEOC, and the research on racial wealth disparities specific to Charlotte, we aimed to identify a set of criteria for the candidates with good conversion potential.

Second, we conducted in-depth interviews with organizational leaders at existing employee-owned (ESOP) firms in Mecklenburg County to assess their perceptions - satisfaction levels, progress, concerns, and recommendations - surrounding employee ownership. In addition, we sought to identify the mechanisms and best practices for structuring ESOPs as a wealth-building strategy for business owners and employees. Participants (N=6) were recruited using an NCEOC dataset containing information on regional employee-owned businesses. The face-to-face and Zoom interviews were conducted by the NCEOC executive and consisted of open-ended and Likert scale questions. The open-ended questions were transcribed and analyzed for content and consistent themes. The interviews provided us with significant insights about specific challenges faced by local business owners during and after the employee ownership transition.

Finally, we looked at several national best practice examples of how broadening employee ownership across various sectors can make a socially equitable impact. Today many U.S. cities, such as Washington, New York, Philadelphia, Pittsburgh, or Cincinnati, choose employee ownership as a part of their long-term strategy to address racial wealth inequality. Their experience can be a valuable inspiration for Charlotte policymakers and the business community. The city could benefit a lot by learning from innovations that have the potential to scale employee ownership conversion.

Limitations of the study

Limitations of the study include using the MWSBE database versus a comprehensive database of all small businesses in the Mecklenburg area, as it is possible that MWSBE businesses are not representative of typical small businesses. However, given the pronounced racial and gender wealth gap and the researchers' interest in programs to reduce this gap, the MWSBE represents an appropriate database to draw participants from. In addition, surveys of employee-owned business leaders in Mecklenburg County include qualitative data, which is subjective. Therefore, to address the researchers' and participants' bias and support the findings, we triangulated data sources, meaning that the survey and interviews were cross-referenced.

triangulated data sources, meaning that the survey and interviews were cross-referenced. Because of self-reported data, some survey participants might have misinterpreted the survey questions, actual condition on questions about business revenue, the possible employee-owned business status, or other issues. Additionally, nonresponse bias presented an issue with the low response rates (8.4%) to the surveys of MWSBE businesses and structured interviews of leadership staff of employee-owned businesses. However, we aimed to increase response rates by framing participation as a chance to learn about a potential business strategy for their company.

SURVEY OF CHARLOTTE MWSBE BUSINESS OWNERS

Executive summary of survey results

Participant profile

Survey respondents represented a variety of different industries, with the heaviest concentration in the professional services (legal services, accounting, insurance) and construction industry. Women-owned businesses made up 100% of all health and personal care businesses, 60% in other services and almost 50% in wholesale and retail as well as entertainment and food categories. The share of Black-owned businesses was larger across all industries compared to white and Latinx companies. However, Latinx-owned businesses were significantly underrepresented in all categories (Fig.1).

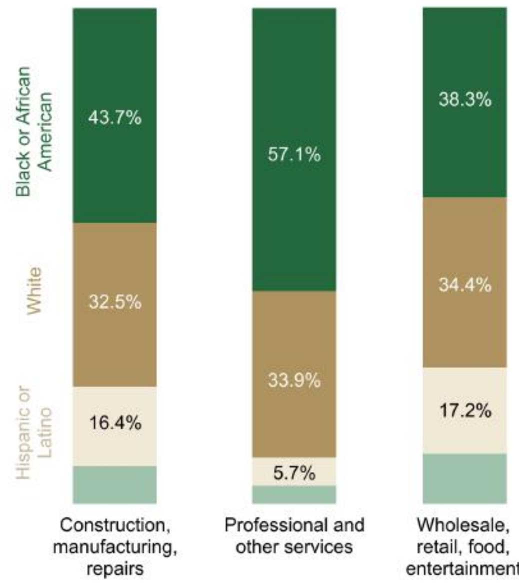


Figure 1: Race distribution for each industry category

Almost 70% of the surveyed businesses were not employee-owned and 43% were family-owned. Some but not all businesses offered profit sharing and 401(k) plans as asset-building opportunities for their employees. In terms of legal structure, the majority of survey businesses were relatively evenly split between LLC and Corporation election. Thirteen percent of businesses represented sole proprietorships, the rest were split between S-corps, partnerships and other business structures.

A sound financial position can be necessary to comply with regulatory requirements when transitioning to a certain form of employee ownership. As a “rule of thumb”, NCEO recommends a $2M revenue threshold for ESOP candidates, and only 8% of the surveyed businesses could meet this threshold[31]. Of businesses generating $2M+ in annual revenue, 19,6% were white-owned compared to 5,5% of Black-owned businesses and none of the Latinx businesses. Furthermore, 50% of Black- and 22% of Latinx-owned companies had less than $200K in annual revenue, implying that those businesses would face significant barriers in obtaining capital the traditional way among other challenges. Thirty-two percent of white-owned firms have their revenue $1M or higher and 47% of Latinx businesses have revenues close to $1M threshold, suggesting that those companies are more capable of funding their businesses with retained earnings. Figure 3 indicates the revenue range of the target population surveyed.

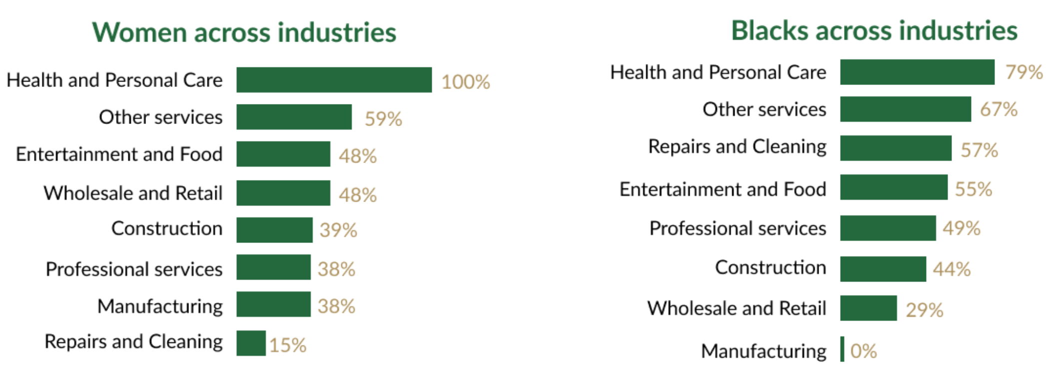


Figure 2: Percent of Black and female respondents within each industry

SURVEY OF CHARLOTTE MWSBE BUSINESS OWNERS

Executive summary of survey results

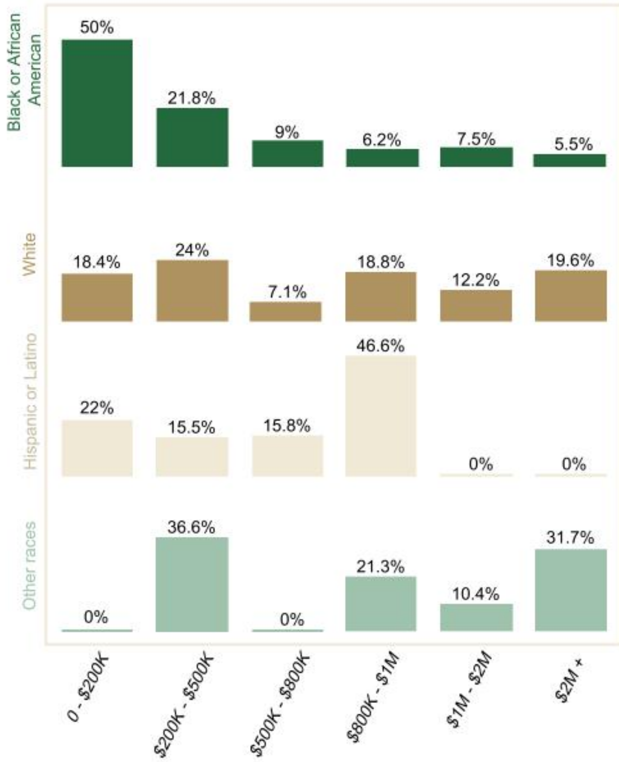


Figure 3: Estimated annual revenue distribution across races

The number of years the company has been operating on the market can be important for the transition to employee ownership. The relevant longevity of the company likely means having a more durable business model, a good customer and supplier base, more knowledge and skilled workers, and likely a more stable financial situation. In our sample, 33% of the companies were operating for five years or less. Thirty-four percent of the surveyed businesses were established before the economic crisis of 2008, demonstrating the longevity of the corporate structure. Twenty-seven percent of businesses remained under current ownership for more than 15 years, suggesting a good track record of sustaining business success for those owners. Thirty-four percent of businesses were 20 or more years in operation.

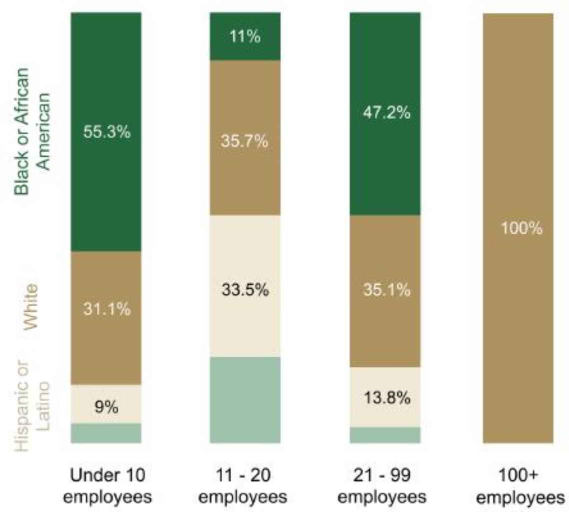
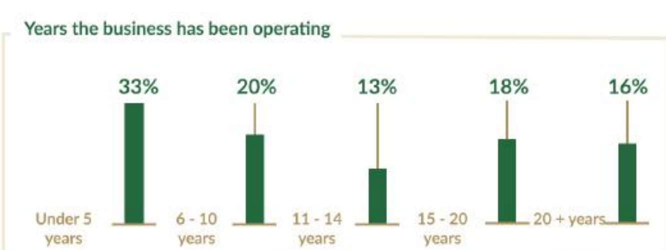
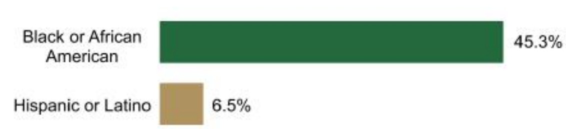


Figure 4: Race distribution for each business size category

Twelve percent of the surveyed businesses had no employees. The majority of respondents had employee bases of less than ten employees, 55% of which are Black owned businesses. Over 30% of companies having between 11 and 20 employees were Latinx owned and 11% were Black owned (Figure 4). Forty-eight percent of business owners were 50 and older, and 60% had 15 years or less until retirement. Of the percentage of business owners retiring in the next 15 years, 45% were Black business owners, and 6.5% were Latinx.



Percentage of Black and Latinx business owners retiring in the next 15 years



SURVEY OF CHARLOTTE MWSBE BUSINESS OWNERS
Executive summary of survey results

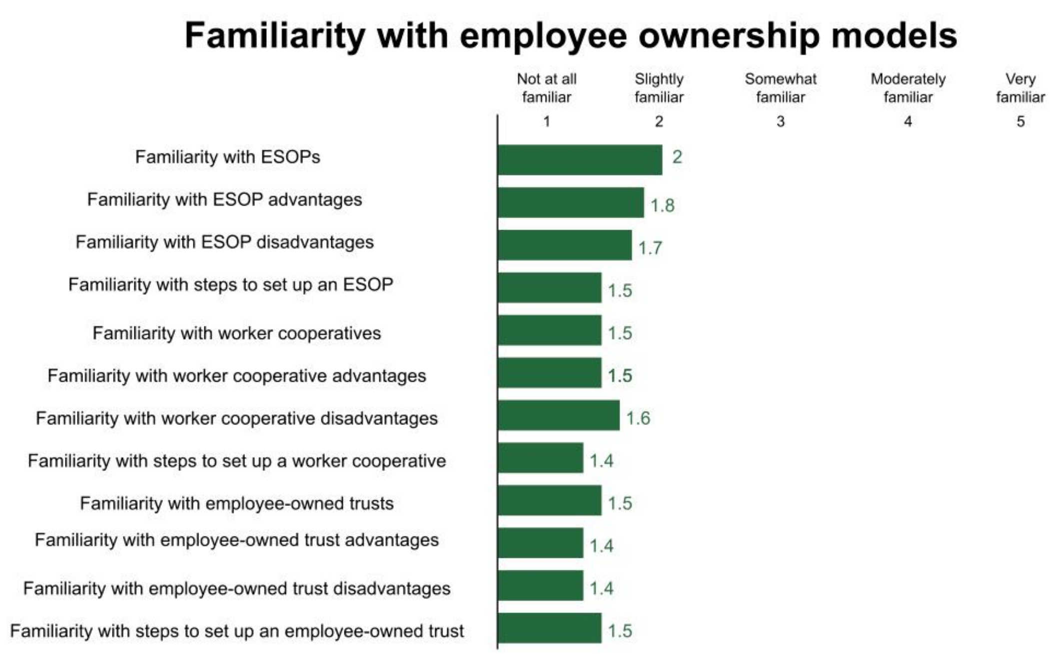
Familiarity with employee ownership

First, the survey participants were asked a series of questions designed to gauge their knowledge and familiarity with the three types of employee-owned business models: ESOPs, worker cooperatives, and EOTs. Survey participants were asked to rate their familiarity in a series of statements on a scale of "Not at all familiar" (1) to "Extremely familiar" (5). We used the mean response to each question to determine how well participants are familiar with each form of employee ownership, its benefits and disadvantages, and the processes related to transition/running the business. The survey findings suggest that employee ownership remains largely unknown among the Charlotte MWSBE businesses. Many business owners who may be interested do not yet know about the possibility of conversion to worker-ownership, or the benefits to themselves, their employees, and their communities. Although a larger share of the respondents was "slightly familiar" with the primary forms of employee-owned businesses - ESOPs, worker cooperatives, or EOTs, a considerably smaller share had a deeper understanding of their utility and the processes involved in setting up and running employee-owned businesses.

- **Awareness** was growing with company size, with a significant jump at 20 employees: from 6 to 28% for ESOPs, from 5% to 15% for worker cooperatives, and from 1% to 17% for EOTs.

- **Familiarity** differed by business age. Out of all business age groups, businesses operating within 5-10 years had a better understanding of ESOPs, while those operating 11-14 years were better familiar with employee trusts. The younger businesses (<5 years) had the best familiarity with worker cooperatives out of all groups.

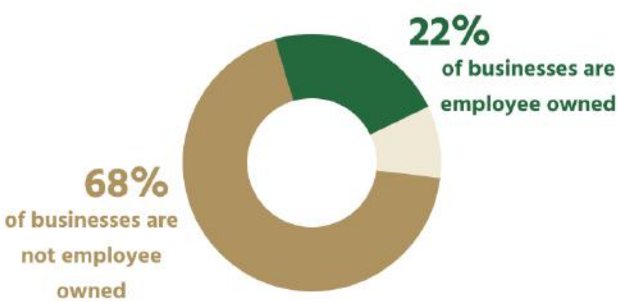
- The crosstab results also showed that among business owners retiring in the next 15 years, 52% were "familiar" or "very familiar" with ESOPs, and 30% were "familiar" or "very familiar" with worker cooperatives, suggesting that this pool of respondents has been likely engaging more in exploring the possibility to conversion compared to other groups.

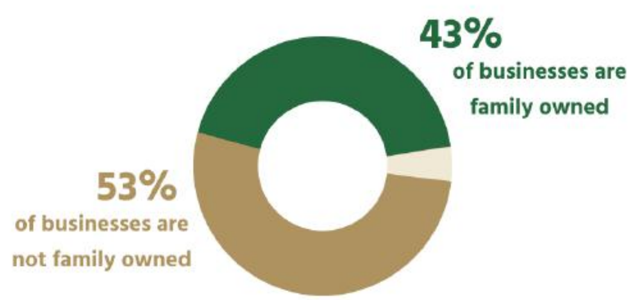


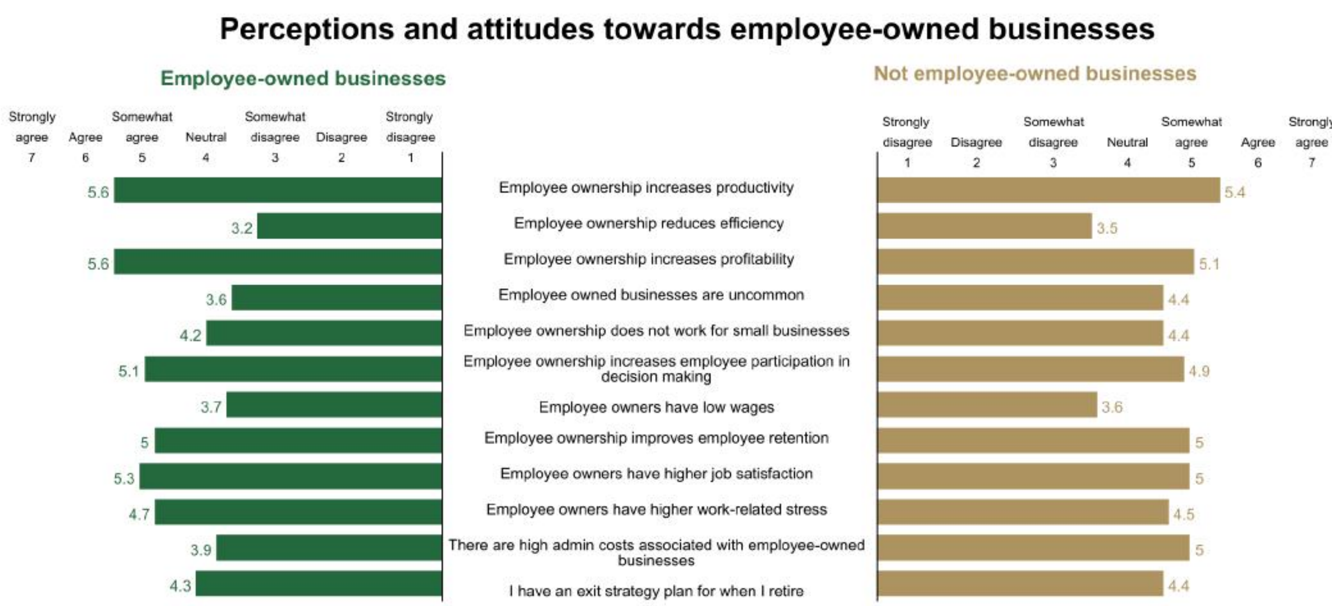
SURVEY OF CHARLOTTE MWSBE BUSINESS OWNERS
Executive summary of survey results

Attitudes and Perceptions

We disaggregated survey respondents based on their employee ownership status to measure attitudes and perceptions towards employee ownership. Survey participants were asked to rate their attitudes, perceptions, and beliefs towards employee-owned businesses in a series of statements on a scale of "Strongly Disagree" (1) to "Strongly Agree" (7). We used the mean response to each question to determine the prevailing sentiment among employee-owners and not employee-owners. Both leaders of employee-owned and not-employee-owned businesses believe that employee ownership can increase productivity and business profitability, improve job satisfaction, and retain jobs, with employee-owners agreeing more strongly with the statements. For owners of non-employee-owned businesses, the perceived startup costs were higher, and they also tend to believe more that employee ownership is uncommon for small businesses. The crosstab results showed that family-owned businesses likely placed less importance on business legacy issues than not family-owned companies. Only 32% of family-owned businesses chose " I already have an exit strategy plan for when I retire," compared to 42% of non-family-owned firms.



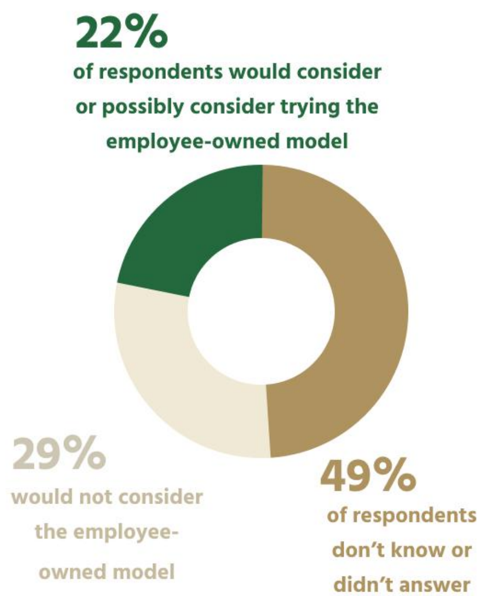


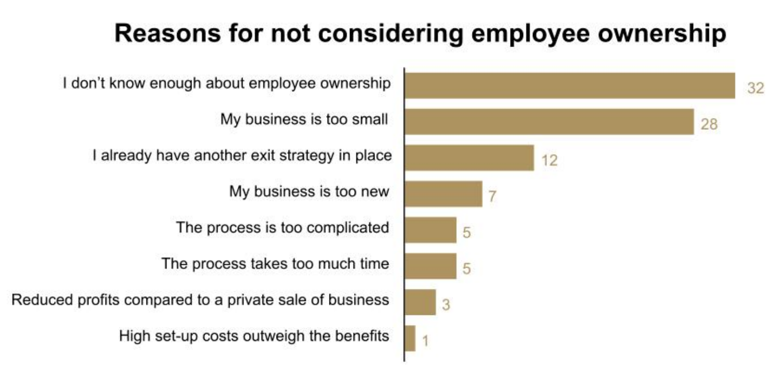


Reasons for considering employee ownership

As one of the concluding questions, participants were asked whether they would consider transitioning their business to an employee ownership model. The participants who answered "yes" or "no" to this question were asked to select one or more reasons for why they would (respectively would not) consider trying employee ownership.

A significant share of respondents was unsure about transitioning their businesses to the employee-owned model. Only 22% of respondents expressed their interest in potential transitioning. "I do not know enough about employee ownership" and "my business is too small" were the two primary reasons for not considering employee ownership as an option. Of the percentage of the participants considering trying the employee ownership model, "rewarding a loyal workforce" and "attraction and retention of good employees" were the most important reasons to consider conversion. For 17 respondents, employee ownership as "a good exit strategy" represented a valuable reason for transition. However, "tax benefits" or "raising capital" appeared to be the least important reasons to consider the conversion.





INTERVIEWS WITH LEADERS OF EXISTING ESOPs

Summary of results

The research team completed in-depth interviews with executives at employee-owned (ESOP) companies in Mecklenburg County to get insights about their experience with ESOP and specific challenges faced by local business owners during and after the employee ownership transition. Interviews were conducted from May to June 2022. All companies were 100% ESOPs, ranging in size from 52 to 5800 employees and representing manufacturing and professional services sectors. All the businesses offered variations of asset-building opportunities beyond the ESOP, including 401(k) plans and other pension plans. Some of the owners took part in the transitioning process, some joined an already employee-owned business.

It is essential to note that our sample was not designed to represent all of Charlotte's employee-owned businesses. Rather, we sought to assess perceptions about employee ownership - satisfaction levels, progress, concerns and recommendations - from the company management perspective. We also aimed to find businesses across a range of sizes and years under ESOP to compare wealth-building paths of company employees.

Storytelling has a powerful inspirational effect and can create awareness in a number of ways. Hence, our findings focus on lessons learned that may be useful to others interested in employee ownership as a wealth-building strategy.

Drawing on the qualitative interviews, we have identified several areas of impact where ESOP adoption can create the asset-building opportunities:

- Personal wealth, ESOPs foster economic stability and security, providing workers with an opportunity to accumulate wealth through their shares.
- Retention and job stability, ownership appears to shape how employees behave and perceive participation, inclusion, ownership value, trust and equity.
- Development of workforce capabilities and opportunity through new skills, knowledge and leadership development.
- Fostering innovation in the company through employee culture

100%

OF PARTICIPATING BUSINESSES ARE 100% EMPLOYEE OWNED

50% of participating businesses are in the professional services industry. Others include manufacturing and construction

BUSINESS SIZE RANGING FROM **52** TO **5800** EMPLOYEES

100% PARTICIPANTS WERE MALE
WITH 67% IN THE 51-64 AGE RANGE
AND 33% BETWEEN 31 AND 50
5 PARTICIPANTS WERE WHITE
AND 1 WAS HISPANIC

Participant Profile

50%

OF PARTICIPATING BUSINESSES HAVE BEEN EMPLOYEE OWNED FOR OVER 25 YEARS

ALL BUSINESSES ARE BASED IN MECKLENBURG COUNTY

67% BACHELOR'S DEGREE

33% MASTER'S DEGREE

EDUCATION LEVEL

BUSINESS AGE RANGING FROM **25** TO **158** YEARS IN OPERATION

INTERVIEWS WITH LEADERS OF EXISTING ESOPs

Summary of results

Reasons to choose ESOP

Apart from the obvious taxation-related benefits, company growth, employee engagement and a neat exit strategy for retiring owners who aim to preserve their business legacy were among the most cited reasons for choosing ESOP. Many respondents discovered the ESOP model looking for "some type of a vehicle to perpetuate their business".

"Around four years ago we started looking to acquire some companies and to grow our business, as well as trying to figure out succession for myself and my partner"

Bill Champion, President of MCI

"You know, for me, it's like a hidden gem. It's something that I think more companies, especially privately held medium sized companies that may not have a perpetuation plan in place but may have some really good qualified key leaders that are growing within their organization, it's a great way to set up a structure to make this an organic transition year over year"

Keith Mann, CEO and CFO of Scott Insurance Company

Benefits of an ESOP

Employee retention was mentioned by 100% of respondents as one of the most important ESOP benefits. Employee culture and economic benefits from owning a stake in a company worked in tandem to significantly boost employee retention, job stability, and retirement security for employees. Moreover, keeping employees with the company for as long as possible is a cost-effective decision that reduces hiring expenses and protects a company from unplanned pre-retirement payouts.

First, employee retention had a strong positive association with a "very real" monetary retirement value of ownership stake, particularly for companies that operated under ESOP for more than 25 years.

"I think there's been a retention benefit to retain long term employee owners over a long period of time, that insulated Scott from many challenges that may have arisen over the many years we've been an ESOP, including during the most recent pandemic. Some of the pressures with the great resignation and people looking for personalization and just changing jobs in general, over the last three years. I think we were somewhat more insulated through the same time period because of the ESOP"

Keith Mann, CEO and CFO of Scott Insurance Company

INTERVIEWS WITH LEADERS OF EXISTING ESOPs

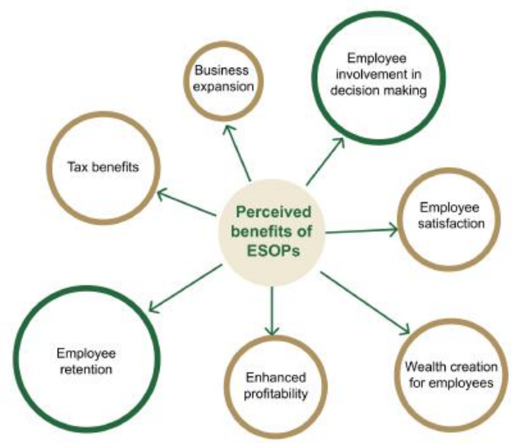
Summary of results

Second, the gains from having an engaging employee culture were positively associated with better retention and company performance. A sense of ownership over decisions, results, and performance creates a collaborative culture in the businesses where everyone understands and shares the same vision and business values.

> *"I do believe that individuals are taking pride in what they're doing, because they do know that they're an owner of the company, they have a direct impact on how the company performs and that affects them directly"*
>
> *Scott Hinesley, President of REI Engineers*

Having an engaging employee culture is a win-win situation for both the employees and the management of the business. Employee culture nurtured by the owners creates a lot of intangible non-monetary benefits for the employees, such as better working relationships, greater job flexibility, or higher levels of job satisfaction. Happy employees are more likely to stay longer with the company and be more loyal, which brings a lot of benefits for the business, particularly when combined with the monetary value of being an employee owner.

> *"I think one of the benefits is that the employees tend to try to perform to the best of their ability. That's always difficult in general in any company, but I think they understand that extra costs or extra expenses do change the value. I think that's been one of the main advantages of the ESOP, and then the second is, of course, trying to do better every ensuing years, so the share values do go up."*
>
> *Dom Medina, President of Flynn Burner Corporation*



Leadership role

Leadership defines the success of any business, and for ESOPs, that goes double. All respondents stressed the importance of leadership and a long-term vision for the ESOP success. Managing employee perceptions takes time and requires wisdom and patience from the management. There's a large share of transparency and trust involved, and not every business owner is ready to give up the power. However, the ability of company owners "to give ownership to folks from various backgrounds, skill levels, levels of education, every position within the organization, their ability to participate" says Keith Mann from Scott Insurance) creates synergies and empowers both sides.

> *"Part of making a successful ESOP is having good leadership, not necessarily at the top, but the second tier and who's going to take [business] over time. And getting that understanding from the senior leadership and making sure they've understood - and some of them are stockholders too - what ESOPs look like, it takes some time"*
>
> *Keith Pehl, President of Optima Engineering*

> *"This is the same for any business owner that's looking at a transition. If the business owner is looking to transition into an ESOP because they're looking for an exit strategy, they're gonna want to make sure that they find the right leadership to stay behind"*
>
> *Scott Hinesley, President of REI Engineers*

INTERVIEWS WITH LEADERS OF EXISTING ESOPs
Summary of results

Challenges

For businesses established more than 20 years ago, conversion to ESOP was a steep learning curve. The respondents mentioned specific transition-related challenges like a lack of adequate information from reliable sources, limited availability of well-informed officials and supporting organizations providing guidance with the transition process, and higher costs associated with ESOP set-up and running. Managing the ESOP can take significantly more time, effort, and initial investment than managing traditional pension plans. In addition, there are specific regulations to follow and external annual valuations to be held. One commonly heard challenge was finding attorneys, evaluation advisors, bankers, and accountants familiar with ESOP formation, and "they can be very expensive."

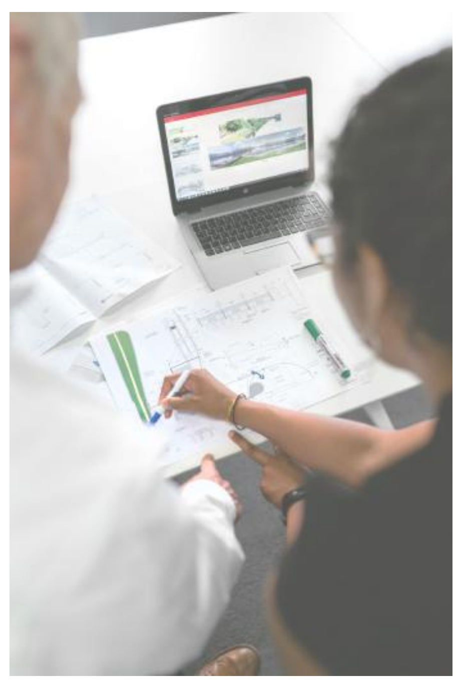
Many were inspired by the examples of the existing ESOPs, others had to gather information piece by piece on conferences, workshops or on the internet.

> *"When we first started doing our education and research on how an ESOP works and operates. We interviewed two ESOP Trustees and they both pointed us to one of the largest HVAC ESOPs in the industry, TD Industries based in Texas. While in Texas a few months later, we were attending a Pre-Fabrication convention, and we were able to visit their headquarters. While showing us the facility. The Vice President was a huge cheerleader for ESOPs, stating it was a game changer in building an employee ownership culture, and even pointing out at some point to an employee that walked by, stating "See that guy? He's a Mechanic and has worked here his entire career. And he is Millionaire". That resounded in me even today."*
>
> *Bill Champion, President of MCI*

With the rising interest in employee ownership, the situation changed dramatically. Companies which have converted to the ESOP in the recent couple of years noted a much smoother transition process which took around 6-8 months and was not as costly and complicated as anticipated.

A lot of "one-stop shop" support and guidance was available from the local ESOP association and the NCEOC.
Despite the 100% satisfaction with having the ESOP, one thing the participants unanimously agreed upon is that ESOP is not a perfect model for every company.

> *"For an ESOP to be a viable option as a succession plan, your company needs to have not only a good and profitable business model, but you usually need over 70 people to make the numbers work and multiple years of experience to prove evidence of repeatable profit as a rule of thumb. As for the ownership, you must have a different mindset and goal. What are your short and long-term goals for exiting or transitioning your business? Unlike most M&A transactions, you won't get a large check on day one. It takes years for the buyout to happen. But for an owner who still has a long remaining runway for continuing to work and is truly concerned about keeping the culture and spirit of why they built their business, an ESOP is a wonderful succession tool in that every single person that works at that business will benefit in the long term"*
>
> *Bill Champion, President of MCI*



INTERVIEWS WITH LEADERS OF EXISTING ESOPs

Summary of results

Speaking about the most challenging part of converting to employee ownership, Bill Champion said: "The due diligence piece! They are going to forensically look at all of your accounting numbers".

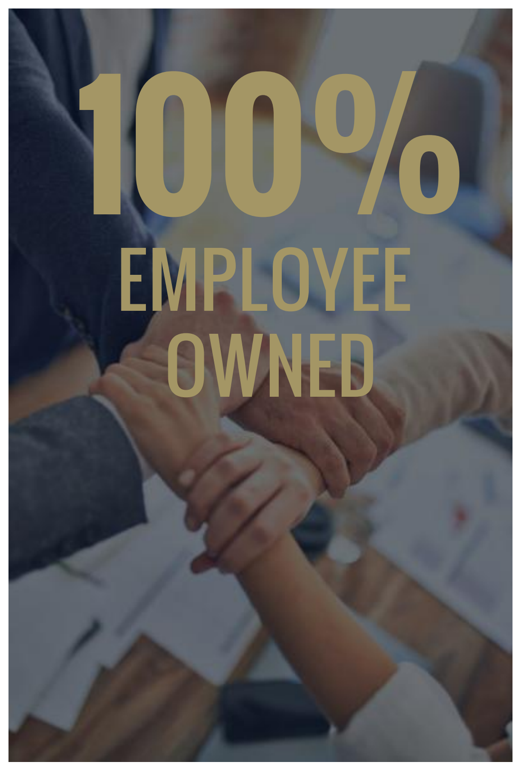
> *"There's a lot of legalities involved in that, which, I think, is the biggest hurdle to get through. It is complicated, there are a lot of rules, there are a lot of expenses along the way between the valuations and other things. So I would just look into all those things before you decide that you want to go that route. And if you are a S-corp, definitely be sure that you're not going to have any issues that are going to force you into a C-corp because of the percentage of ownership situation"*
>
> *Dom Medina, President of Flynn Burner Corporation*

Getting the employees to understand what the ESOP is, how it works and how it can benefit them was another significant challenge mentioned by the majority of respondents.

> *"They [employees] are not used to thinking like an owner. Many are still kept thinking they got to put money into this, and it's too good to be true, so there's a long education process to go through. I think it took us two or three years after the implementation to get it to really sink in".*
>
> *Keith Pehl, President of Optima Engineering*

Getting the employees to understand what the ESOP is, how it works and how it can benefit them was another significant challenge mentioned by the majority of respondents.

> *"I think there's some skepticism that may be in the workforce, where folks come in and look at something like this and feel like it's too good to be true. There're some people that don't get it, especially early in their career, but then, once they get that report after three, four or five years it's vested and they're growing, then there's a big shift."*
>
> *Keith Mann, CEO and CFO of Scott Insurance Company*

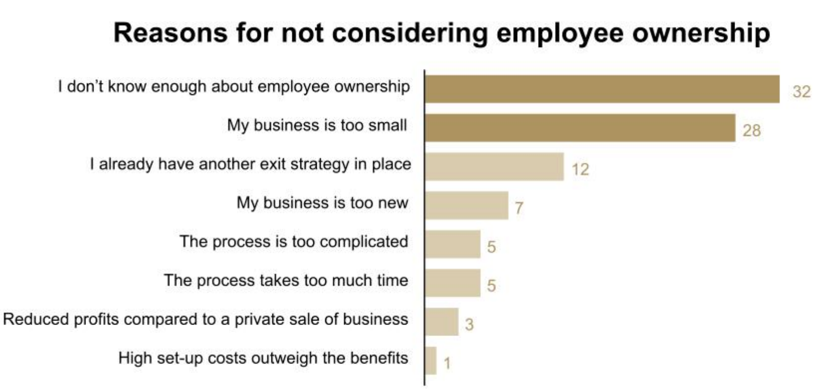


BARRIERS

The benefits of employee ownership are well documented in numerous studies. However, Black and Latinx business owners lag behind White business owners in transitioning their business to the employee ownership model. A recent Aspen Institute study (2020) named systemic racism as a major structural barrier for business owners of color to access employee ownership as a wealth-building strategy. Surveying small minority businesses in Charlotte in 2021, UNC Charlotte researchers documented inequitable access to capital, opportunities, and social networks between minorities and non-minorities, which compromises success in business ownership for people of color.

> *"The racial wealth disparities and occupational segregation make access to conversion capital and working capital more challenging for business owners of color."*
>
> *Aspen Institute, 2020*

Our analysis showed that lack of knowledge and information could be a significant obstacle to the broader adoption of employee ownership in Charlotte. Subsequently, choosing the suitable form of employee ownership can be a complicated task for the surveyed small business owners. When asked about challenges to employee ownership conversion, survey and interview respondents described an array of transition-related challenges. Many not employee-owned business owners have not considered the transition due to the complexity of the process and a lack of familiarity with the benefits and disadvantages of each model. The smaller size of the business was another perceived barrier to conversion. The interviewed ESOP executives mentioned difficulties in obtaining information and guidance on ESOP formation and running, higher perceived costs associated with ESOP set-up and running, and limited availability of attorneys, evaluation advisors, bankers, and accountants familiar with ESOPs. ESOP owners also framed the problem in terms of managing employees' "skepticism" about ownership value. Management of ESOP was associated with a higher perceived level of ESOP-specific knowledge, leadership qualities, and a necessity of a long-term vision for business development.



EMPLOYEE OWNERSHIP. CITY SUCCESS STORIES

CITY SUCCESS STORIES

Experience of the U.S. cities and communities successfully leveraging the potential of employee ownership to drive the equality of wealth shows that local governments play a key role in supporting employee ownership transition.

By creating an enabling environment and connecting local engagement and local resources, municipalities can efficiently address the specific challenges faced by minority-owned businesses and create paths to build wealth for them, their employees, and their communities. Today, more and more cities across the country recognize the potential of employee ownership as a long-term strategy to preserve local jobs and anchor small businesses in the communities they serve. Cities can successfully address pressing economic issues by changing from redistributing to creating wealth through various employee ownership strategies and initiatives. Those value-creating and highly-impactful initiatives can be integrated with municipal economic development strategies and enabled through the existing business support ecosystems.

Improving access to knowledge and opportunities. Employee Ownership New York

Lack of knowledge and information can be a significant obstacle to the broader adoption of employee ownership. To address the challenge, the New York City council, in coordination with the New York Department of Small Business Services, launched the Owner to Owners business transition hotline as a part of its NYC Employee Ownership municipal initiative. Owner to Owners functions as a call center and a website and offers expert support for businesses planning or implementing the transition to employee ownership. As a significant portion of New-York small businesses is immigrant- and minority-owned, the hotline is available in 10 languages to amplify the exposure. Services are provided at no cost to company owners, including business readiness and eligibility assessment, estimation of business value, and succession planning. In addition, eligible businesses can receive further assistance with access to loan funds, guidance through a sale process, and training for managers and employees to support a successful transition.

Although initially intended for business owners already set on transitioning to employee ownership, it inspired other businesses to consider employee ownership as a strategy. This outcome would be impossible without promoting the initiative through municipal channels, partnering with community-based organizations, and the Owner to Owners ambassadors network. Expert support for businesses is provided through collaboration with Democracy at Work Institute, The Working World, the ICA Group, and the Business Outreach Center Network. The program is expected to reach at least 20,000 businesses.

Cities need to know who they are reaching out to. The webpage or hotline assisting with employee ownership transition can be a good source of business demographic and socio-economic data otherwise difficult to obtain. The scarcity of workforce demographic data can represent a significant barrier to a targeted employee ownership promotion. When using employee ownership to reduce the wealth gap in a specific neighborhood or city area, targeting businesses solely located in those areas is often mistakenly considered a sufficient strategy.

CITY SUCCESS STORIES

According to Zen Trenholm, Director of Employee Ownership Cities and Policy at **The Democracy at Work Institute,** targeting only businesses in communities with the greatest poverty leaves out all the companies located elsewhere but employing the residents of the target neighborhood. In order to get the most impact out of a targeted employee ownership promotion, cities must adopt a more holistic approach to outreach activities by focusing on workforce flows and addressing larger issues of business owners, service providers, and communities.

The soul of the city. Legacy businesses preservation

Employee ownership can be integrated into legacy businesses preservation programs and strategies. Legacy businesses are typically small local companies with under 20 employees which have been in operation for 20 straight years. They are often clustered in inner cities or pedestrian-friendly areas serving as neighborhood gathering spots and preserving community character. Thriving legacy businesses are essential for the local economy. First, they contribute to job stability by providing residents with employment. Second, legacy businesses contribute to a city's unique identity and strengthen a city brand by maintaining the city's cultural and historical heritage.

Like many other small businesses, the Covid-19 pandemic put many of them at risk due to soaring rents, increased development pressures, and a lack of succession plans. Studies reveal that longstanding businesses are far more likely to close than to be sold, with 83% of them being closed due to an owner's retirement. If not reversed, this trend indicated that job losses from retiree-related closings would continue to grow. [32]

Cities like Los Angeles, Seattle, Durham and San Francisco recognize the importance of preserving and celebrating legacy businesses due to their dual role in contributing to the city economy and look at various ways to support them. Legacy business preservation programs primarily focus on building awareness about legacy businesses and their importance to the community. Initiatives range from promoting their stories through events and social media to business networking and point-of-sales labels raising perceptions of their quality and importance.

Long-standing culturally and historically significant businesses can apply to the Legacy Businesses Registry to be eligible for Rent Stabilization and Business Assistance grants, technical and other support services from the city. Resources and training for succession planning are provided in partnerships with local Small Business Development Centers and the Democracy at Work Institute. For example, in the fiscal year 2018-2019, the Legacy Business Program of the City and County of San Francisco approved 104 Business Assistance Grants totaling $589,527 and paid 10 first-year Rent Stabilization Grants and 14 second-year Rent Stabilization Grants to landlords of Legacy Businesses totaling $356,916

Communities need to have an inventory of available assets to promote. The Registry can also serve as a database of small businesses and succession planning services, including employee buyouts [33], making it a valuable source of workforce demographic. Eighty-four percent of San Francisco legacy businesses mentioned "Recognition" as the reason they applied to the Legacy Registry, indicating the significance of the initiative for local businesses.

Branding cities through history and culture

In a broader sense, city branding is a set of strategic activities aiming to create a sustainable competitive advantage of a place which will define its success and boost its economic growth. History and culture play a key role in facilitating an authentic experience of a place. Many cities successfully use their cultural and historical assets to motivate people to visit them. Culture has a capacity to influence and underpin all city brand components, from a city's physical and economic aspects to its presence on international markets. By adding an emotional value to a city's brand, history and culture have the potential to leverage residents' and visitors' behavior and perceptions. The cultural distinction of a place can evoke emotions and create memories that, combined with personal experience and expectations, can be a strong driving force in terms of consumer behavior.[34]

CITY SUCCESS STORIES

Leveraging employee ownership transitions for equitable wealth consolidation in critical industries. Lessons from Worker Co-ops in Philadelphia, Buffalo, and Brooklyn.

For industries providing essential services for the community but employing a low-wage workforce, conversion to worker cooperatives can be a valuable strategy to secure higher income and job security for the most vulnerable workers. In addition, by assessing the needs of a community, cities can bring to light the areas to be addressed and focus on targeting those industries with investment and support.

The Covid-19 crisis demonstrated that healthcare and childcare were among the industries most vulnerable to downsizing and disruption. Childcare has the third-largest share of minority business owners of all industries, with much of its 756K businesses built by women of color. The lack of federal investment support for childcare workers is rooted in historical perceptions of childcare as a low-skilled, undervalued, and low-compensated sector. The median pay for childcare workers is $24,230 a year (U.S.Bureau Labor Statistics, 2021). According to the 2019 Motherly report, America's childcare workers make less than Amazon delivery drivers.

The recent pandemic revealed a massive childcare shortage in the U.S., meaning that millions of women were kept off the workforce and further entrenched in poverty. According to the National Association for the Education of Young Children survey, only 12% of minority-owned childcare businesses have not had to lay off or furlough staff during the pandemic, compared to 27% of the industry overall.

Employee ownership can offer a sustainable solution for critical but disrupted industries such as childcare or healthcare by offering better job security and wealth-building opportunities for workers critical to the economy. Industry can only benefit from creating new co-ops or transitioning the existing businesses to worker ownership. It can attract much-needed financial and technical support from private and public investors and collaborative partners. The democratic employee culture can give the childcare workforce the dignity and opportunities for knowledge and personal development.

Childspace in Philadelphia was established in 1988 as a worker co-op in partnership with the School District of Philadelphia and Help Philadelphia non-profit. Since its founding, Childspace has advocated and promoted the dignity and quality of childcare jobs—from increasing subsidy reimbursement rates to establishing the TEACH program that allows workers to advance in educational attainment while working—as the building blocks of employee retention and satisfaction.

The Rose Garden Early Childhood Center in Buffalo transitioned to employee ownership in 2017 after the retirement of its owner. Today, five female employee-owners serve on the board, set organizational policy, and participate in community events to help grow the business. They promote trust and quality childcare as the most significant values of their organization.

Beyond Care Childcare Cooperative was launched in Brooklyn, NY, in 2008 with the support and guidance of the Center for Family Life. Founded by 17 immigrant women and founding members, it currently grew to 38 members. Beyond Care promotes living wage jobs in a safe and healthy environment and provides social support and educational opportunities for its members as a part of its social mission.

CITY SUCCESS STORIES

Secondary Worker Cooperatives

Secondary worker cooperatives can be a valuable model for communities with small subscaled minority-owned businesses, particularly microbusinesses and sole proprietorships, which otherwise struggle with an array of challenges on their own.

The nonprofit **Prospera** in California's San Francisco Bay Area has incubated a network of worker cooperatives, where most worker-owners are Latina women. Prospera's vision is to foster community-rooted sustainable businesses led by Latina entrepreneurs. Built on the principles of social justice and equality, Prospera provides educational, financial and technical support and offers access to opportunities for 825 Latina women in the community, coming from low-income households. Since the first cooperative was founded in 1997, Prospera has helped to create jobs across seven cooperatives operating in professional eco-cleaning, consultancy, food and event industries; 325 Latina women graduated from their core cooperative development programs. In 2021, these cooperatives had a combined total of $1.2 million in revenue. The network has also 35 businesses in the incubation phase. Once mature, those businesses will join the network. Shared control of the cooperative enables workers to influence their own wages and vote in key decisions. Workers benefit from a better and safer working environment and equitable share of profits. By joining the Prospera, the median income of worker-owners increased from $24,000 to $40,989.

"Inclusive food systems are critical to the health of communities, and to their economic prospects. Food businesses provide opportunities for improved health and wealth building for many people in the District. Now is the time to expand those opportunities to earn a good wage, work with dignity, and pass down wealth to the next generation, and the Nourish D.C. Fund is an excellent catalyst for that vision for all D.C. residents, particularly those in disinvested neighborhoods in the city"

Ellis Carr, president and CEO of Capital Impact Partners and CEO of CDC Small Business Finance

"For municipalities that are focused on strengthening their existing small businesses, secondary cooperatives enable local governments to engage with a single entity that represents multiple enterprises, amplifying small business negotiating power in the policymaking process"

The Principles Committee and the Alliance

Washington DC. Creating an ecosystem of impact

Reducing racial wealth gap with workforce development strategies requires a cohesive approach when different stakeholders collaborate to provide expertise, financing and legal support to businesses that need them the most. Washington DC is a vibrant food and restaurant cluster, however many minority-owned food businesses find it difficult to compete due to limited access to capital and opportunities. Nourish DC Collective, partnership between the city and the Capital Impact Partners fund, was established with the aim to foster the development of a strong and equitable ecosystem of locally owned food companies to reduce access inequities and promote higher quality jobs and worker ownership in the District of Columbia. It primarily focuses on helping minority-owned businesses located in historically disadvantaged neighborhoods underserved by grocery stores and food facilities. Through partnering with the Washington Area Community Investment Fund (Wacif) and the Capital Impact Partners Fund, Nourish D.C. provides necessary technical assistance, catalytic grants, and lending products which will allow those businesses to develop and thrive. It supports the entire food value chain in order to create an inclusive food system which gives access to nutritious, affordable, and culturally appropriate food and promotes health equity.

"Women often lack the support we need to launch our wildest entrepreneurial dreams. At Prospera, we take tools from traditional business incubator programs, infuse them with culture and love, and make them accessible for Latina immigrants. We begin to see the possibilities, open doors for each other, and dream bigger!"

Prospera

CONCLUSIONS AND RECOMMENDATIONS

CONCLUSIONS AND RECOMMENDATIONS

Roadmap to closing racial wealth gap with employee ownership

Employee ownership has a proof record of being an innovative and time-tested solution in creating wealth-building opportunities for people of color. If widely adopted in Charlotte, employee ownership could substantially increase economic mobility and strengthen the local economy. To capitalize on the opportunity, employee ownership should be embraced within a larger strategic framework and anchored within the local context and community. This requires a collaborative approach with active engagement of all local stakeholders: government, public and private organizations, academia, and civil society. Experience of the U.S. cities successfully leveraging the potential of employee ownership to bridge the racial wealth gap shows that the government plays a leading role in enabling collaborative processes. In the cohesive city context, policy makers have the actual power and instruments to create the partnerships between the market, society, and the government and to connect local engagement with local resources. When referring to resources, then, not only funding is essential but also consensus development, capacities, and broader impact. Such a strategy takes time to develop and nurture, and our study aims to initiate this process.

Educate, inspire, connect

Our research identified that low awareness of employee ownership and its forms, insufficient support and guidance through transition, and financial barriers are the common obstacles to broader employee ownership adoption in Charlotte. Our recommendations address these barriers to help build more opportunities for the Charlotte community. Building upon the research findings, we recommend that the following efforts should be pursued:

- **Identifying and targeting candidates with good conversion potential**. Targeted outreach can be a time- and cost-effective strategy. To multiply the outreach impact, cities need to know who they are reaching out to. Cities are typically talking to small businesses more often, data can be also obtained through local Small Business Development organizations. However, obtaining information from mid-size businesses with 50 or more employees can be challenging. Opt-in business registries, hotlines, and websites related to employee ownership can be a good source of business demographic data. The city can also partner with local universities or consulting businesses for workforce data collection and mapping. Partnering with local business and trade associations, chambers of commerce, and organizations who serve the low-income minority-concentrated communities can help identify leads in selecting companies for conversion.

- **Raising awareness in a structural way**. Most surveyed minority businesses mentioned a lack of knowledge about employee ownership and its utility as a primary reason for not pursuing the transition. Education and information dissemination about broad-based employee ownership benefits among business owners, government agencies, and business services providers can reduce those barriers. Local business development organizations play an essential role in ensuring business owners know the option exists. They also have capabilities to initiate a dialogue and encourage city departments, commissions, committees, and task forces to consider employee ownership a powerful tool for building an equitable and sustainable economy.

- **Providing feasibility analysis and technical assistance to companies interested in conversion to an employee-owned model**. Companies need skills, tools, knowledge, and resources to run their businesses efficiently. In addition, there are multiple requirements to consider including but not limited to feasibility assessment, set-up costs, legal arrangements, and a fit with the company's goals for employee ownership. Building the city capacity to provide resources and high-quality assistance for transition is imperative for the success of the strategic employee ownership development. Partnering with local and national technical assistance providers can increase the impact. For example, Colorado, one of the most employee ownership-friendly states in the country, has created a national model for how states can build a sustainable economy through employee ownership.

CONCLUSIONS AND RECOMMENDATIONS

- **Improving access to capital.** Access to capital represents a significant challenge for the growth of small minority businesses, and government organizations can play an essential role in connecting them with public and private money. Furthermore, small minority-owned firms have closer ties with their communities, and the social benefit of having an employee-owned company is likely to be extended to the whole community. This fact can incentivize more interest from the private impact investment funds. Currently, employee ownership is largely missing from impact investing.[35] However, impact capital could play a key role in ensuring that a significant portion of these "silver tsunami" firms transition to employee ownership, creating the momentum needed for broader adoption of the model.[36]

- **Creating Legacy Businesses Preservation program**. Cities like Los Angeles, Seattle, Durham, and San Francisco recognize the importance of preserving and celebrating legacy businesses due to their dual role in contributing to the city economy and look at various ways to support them. Legacy business preservation programs primarily focus on building awareness about legacy businesses and their importance to the community. Initiatives can range from promoting their stories through events and social media to business networking and point-of-sales labels raising perceptions of their quality and importance. Long-standing culturally and historically significant businesses can apply to the Legacy Businesses Registry to be eligible for Rent Stabilization and Business Assistance grants, and technical and other support from the city. Resources and training for succession planning can be provided in partnerships with local Small Business Development Centers and the Democracy at Work Institute. Small Business Development center can also measure and analyze the effects of the grants, establish marketing and branding activities for the legacy businesses, and research new opportunities for assisting Legacy Businesses, for example, with the purchase of commercial spaces.

- **Prioritizing employee ownership strategies that have proven economic impact in communities of color and among disadvantaged workers: worker cooperatives, EOTs and secondary worker cooperatives**. Both EOTs and worker-owned cooperatives can be a less regulated and simpler model for conversion that many small businesses can capitalize on. Moreover, one of the "spillover" effects of scaling on worker cooperatives is their potential to build a more inclusive economy which can justify their future local support. By prioritizing scalable worker cooperatives and EOTs development strategies in the industries with job improvement potential, Charlotte can prevent business closures and make a measurable economic impact on communities of color.

CONCLUSIONS AND RECOMMENDATIONS

- **Supporting mentorship and leadership programs.** Our interviewees named leadership a pivotal quality for the managers of employee-owned companies. Good leaders inspire their employees and ensure everyone is aligned with a company's vision and mission. They augment business success by creating a productive employee culture. A lack of mentors and role models who can guide professionals' career advancement has a negative impact on the leadership potential and the soft skills people of color bring to the businesses they create. By expanding business leadership education through coaching, workshops, mentoring, and networking with local employee-owned company executives, Charlotte can grow a new generation of business leaders of color.

- **Learning from innovations and best practice examples.** Further explore opportunities for employee ownership conversions to benefit low- and moderate-income workers, people of color and disadvantaged communities. Establish goals and implement metrics to measure outcomes, seek input from communities and report progress to key stakeholders.

Possible criteria for identifying candidates with good conversion potential

To identify businesses with good conversion potential it is essential to have a data-driven approach. It is critical to identify workforce demographics and follow their development in dynamics.

Based on the existing research and our interview and survey results, we have identified a list of possible data-driven criteria for
identifying candidates for transition:

- Number of employees
- Estimated annual revenue
- Number of years in operation
- Age of the owner(s)
- Appropriate industries, where employee ownership has potential to positively transform jobs and create wealth

In addition to data-driven criteria, interviews with existing ESOP leaders helped us identify characteristics and attributes of owners likely to be receptive to employee ownership:

- Owners looking for an exit strategy
- Owner interested in business continuity after they exit the company
- Owners interested in employee retention and well-being
- Business with a stable track record in their industry

Examples from the MWSBE survey

Respondents who would consider trying employee ownership

Business profile

54% are Black-owned
8% Latinx-owned
70% are in professional and other services
27% in construction/manufacturing/repairs
55% are LLC
34% are C corporations
56% have 1-5 employees
41% have been in operation for 15+ years

Respondents who are retiring within 15 years

Business profile

45% are Black-owned
7% Latinx-owned
52% are in professional and other services
43% in construction/manufacturing/repairs
38% are LLC
34% are C corporations
50% have 1-5 employees
35% have been in operation for 15+ years

Legacy businesses

In operation for 20+ years

18% are Black-owned
0% Latinx-owned
56% are in professional and other services
24% in construction/manufacturing/repairs
28% are LLC
56% are C corporations
89% have under 20 employees

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