CO-OPERATIVES UK

FRESH IDEAS 3

# Saving business through worker co-operatives

## A strategy for employee buyouts in the context of insolvency

*Dr. Anthony Jensen, University of Sydney*

"Workers often see potential in a business not seen by investors and anchoring jobs and capital locally through a worker take-over has a significant positive impact."

“As businesses globalise, market places are more complex and operations continue to diversify, co-operation is a critical organisational capability in gaining competitive edge. Only when co-operation is present can the best ideas be exchanged, innovation be harnessed and new ideas be executed with speed and sophistication.”

Professor Linda Gratton,
London Business School

# Context

## Administration is often a wasteful and costly process, both to employees and to the economy at large. Company insolvencies in the UK are currently running over 7% higher than a year ago, at around 17,000 businesses per annum.

Within this number there are many companies that on economic grounds could be saved. A large number, forty four percent, are wound up because of poor management prior to insolvency. This represents a potential in theory to save up to 7,500 enterprises.

Workers taking over an insolvent company to preserve their jobs and entitlements is now recognized internationally as an area for policy leadership.

Employee ownership through worker co-operatives solves what the International Association of Restructuring, Insolvency and Bankruptcy Professionals describes as an intractable problem in insolvencies, which is marginalizing of employees that are 'often the lifeblood of the enterprise', the loss of their employment and their entitlements.

Workers often see potential in a business not seen by investors and anchoring jobs and capital locally through a worker take-over has a significant positive impact on the social cohesion of the local economy.

There is empirical evidence of positive productivity gains from a worker take-over. There is also evidence that the businesses that result can be more resilient to economic downturns.

# Work to date

## We have been exploring how a pilot or programme could be developed in the UK to test the potential for worker co-operatives in the context of insolvency.

Previous research supported by Co-operative Action has reviewed the innovation of worker buyouts, to create 'sociedades laborales' (worker societies) in Spain. This programme resulted in 120,000 jobs being saved or created through the formation of 12,000 employee-owned enterprises.

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The report Insolvency, Employee Rights and Employee Buyouts was launched in 2006. Although the insolvency rate was lower at this time given a more benign economic climate, the key finding was that a significant opportunity existed for a similar model in the UK.

Companies are increasingly burdened by employee liabilities due to employee rights and the elevation of employees as stakeholders in insolvency through the Transfer of Undertakings (Protection of Employment) Regulations 2006 (TUPE); and the Pensions Act 2004. The most appropriate purchaser, with the right finance and support, of an insolvent business burdened with employee liabilities' is therefore the employees. The trades unions, however, opposed this move, which led the shelving of potential work on this.

More recently, the idea of a 'right to bid' has been raised by a number of commentators, including Graeme Nuttall and Centre Forum. The potential to achieve this through insolvency has been downplayed, however, on the assumption that business success rates would be low and worker co-operatives would not be competitive.

The international evidence suggests that, with careful design, the opposite can be true. Indeed, while recognizing the complexity of insolvency law, insolvency might be the ideal place in which to introduce such a right, something that would be particularly timely given the urgency of restarting the UK enterprise economy.

In terms of a 'right to bid' framed in legislation, insolvency in theory is a good place to start. It is now recognized that worker's entitlements are an investment in the company and these deserve governance considerations and a say in the outcome of the insolvency process. This is supported by the view that workers are not creditors but investors and residual claimants, leading to the argument that employees should be given the opportunity, within the administration process, to consider the purchase of the business to preserve their jobs and entitlements if this is their wish.

This could introduce what insolvency lawyer Vanessa Finch of the London School of Economics describes as a 'democratic ideal into corporate life'.

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There are, however, different ways of designing in to the insolvency process an opportunity or even a 'nudge' in favour of worker buyouts. It could be a formal 'right to bid' with a legislative process introduced to enable this. Or this could be a voluntary model, including signals of support to the insolvency profession with enabling guidance and support from the Insolvency Service.

# Learning from overseas

## In France, over 700 businesses on the verge of closing down have been transformed into co-operative businesses between 1989 and 2010, representing over thirty enterprises a year, saving thousands of jobs.

Appropriate enabling legislation also exists in Spain, Sociadades Laborales (SAL), and Italy, the Marcora Law.

In a period of economic crisis in the 1980s, both countries enacted legislation in 1985 to support workers take over thousands of failing enterprises. Both countries based the legislation on encouraging workers to become entrepreneurs in saving their jobs by taking their entitlements, and three years projected social security payments, in a lump sum payment, and investing these in the new company. This was supported by government loans and advice.

The Marcora Law set up the Campagnia Finanzaria Industriale (CFI), a financial institution to support workers establish a workers co-operative, to take over the failed company. CFI also provided advice, finance and has the right of a seat on the board of the co-operative.

Both these programmes were suspended by the European Union (EU) in the 1990s. The reason given was they contravened European competition law. However discussions with Italian and Spanish officials involved in the programs at the time indicated that it was also due to the over generous financial state support for one form of business model - worker self-management.

The SAL programme then refocused on worker start ups by displaced workers. The Marcora Law reemerged post 2000 reconstructed offering financial support to workers on a 1:1 basis rather than 3:1 (CFI to worker contribution) for worker co-operative buyouts. Professor Alberto Zevi of CFI reported in 2011 that the Marcora Law was working well, with eleven buyouts assisted in recent months.

# Evaluation

## Worker co-operative buyouts of insolvent businesses have been successfully carried out in many countries as measured by their longevity, job saving and job creation and performance impact.

There are successful case studies in the UK: UBH International, Tower Colliery and a number of smaller buyouts in Wales. There have also been failures when best practice has been ignored namely a viable market, strong leadership, a homogeneous culture and ongoing advice.

Research into the Marcora Law and an evaluation of companies assisted by CFI demonstrated that this law provided the effective infrastructure to overcome the barriers to worker ownership in the form of finance, advice and ongoing mentoring to ensure worker co-operative buyouts were an effective strategy.

# Next Steps

## Exploring action to save business through worker co-operatives

Not every business can be saved. But the success of programmes overseas points to the potential to save some through employee buyouts.

The provision of support to workers in insolvency and the subsequent buyout and reconstruction requires a different process, learning and methodology to a buyout in a normal business succession.

BIS is committed to working with Co-operatives UK and the Insolvency Service to scope a pilot scheme to test worker co-operatives and employee buyouts as a solution in relevant business rescue situations. This would run from 2013.

The menu of options may include voluntary pilots, a wider programme or the potential for legislative change to introduce a 'right to bid' in the insolvency process.

This opportunity chimes well with current Liberal Democrat and Government priorities in economic and social policy, including in the context of the declaration by the United Nations of 2012 as the International Year of Co-operatives, "highlighting the contribution of co-operatives to socio-economic development".

ABOUT THE AUTHOR

Dr Anthony Jensen is an economist and industrial relations specialist, currently based at the University of Sydney Business School. He has written widely on employee ownership and share schemes, and works as a researcher, advisor and policy consultant.

# Co-operatives UK

Co-operatives UK works to promote, develop and unite co-operative enterprises. It has a unique role as a trade association for co-operatives and its campaigns for co-operation, such as Co-operatives Fortnight, bring together all those with a passion and interest in co-operative action.

Any organisation supportive of co-operation and mutuality can join and there are many opportunities online for individuals to connect to the latest co-operative news, innovations and campaigns. All members benefit from specialist services and the chance to network with other co-operatives.

**www.uk.coop**

Printed during the United Nations International Year of Co-operatives 2012: a unique opportunity to open the lid on one of the world's best kept secrets. Co-operatives are more than successful businesses - they are a global movement that is building a better world by giving everyday people an equal say and their share of the profits. The International Year of Co-operatives is a chance to find out more.

2012 International Year of Co-operatives

Co-operatives UK's International Year campaign is generously supported The Co-operative Group, The Midcounties Co-operative, Midlands Co-operative Society, Scotmid Co-operative, The Southern Co-operative, Anglia Regional Co-operative Society, East of England Co-operative Society, Benenden Healthcare, Lincolnshire Co-operative, Chelmsford Star Co-operative Society, Heart of England Co-operative, Channel Islands Co-operative Society, HF Holidays and CDS Co-operatives.

**www.uk.coop/2012**

Administration is often a wasteful and costly process, both to employees and to the economy at large. *Saving business through worker co-operatives* argues that up to 7,500 enterprises could be eligible to be saved through action to allow workers to take over the businesses.

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