3

Steps in the Buy-out Process

Worker Co-op Buy-out Guide

co-op ventures worker co-op

Prepared for:
Western Labour - Worker Cooperative Council
March 2009

Forward

In recent years a large number of working families have been threatened by workplace closures. Stress factors in the forestry, manufacturing, and food processing industries in particular have accelerated the rate of job loss in rural communities in Western Canada. The Western Labour-Worker Co-operative Council ("WLWCC" or the "Council") was formed in 2006 to support worker-driven interventions in situations of plant closure and threatened jobs.

Partners in the Council include the Canadian Labour Congress (Prairie Region), the Canadian Worker Co-operative Federation, Co-op Ventures Worker Co-operative, and the Ohio Employee Ownership Center. Lynn Williams, President Emeritus of the United Steelworkers, has played a key role in bringing these organizations together. The partners in the Council believe that the need to act is urgent.

This guide has been developed to build the capacity of workers to respond quickly. Whether unionized employees want to explore buying out a business as a worker co-operative or as another type of employee-owned enterprise, this guide can help.

It features basic information on how co-operatives work, how co-operatives work for workers through union supported worker buy-outs, and how to get started. We hope it gives you an idea how the co-operative model can meet your members' needs, how the buy-out process can happen, and what your first steps need to be.

Acknowledgements

Co-op Ventures Worker Co-op and the project partners on the Western Labour-Worker Co-operative Council would like to acknowledge the Ohio Employee Ownership Center, the United Steelworkers' Worker Ownership Institute, and the Canadian Worker Co-operative Federation.

This project was made possible by funding from the Innovations and Research component of the Co-operative Development Initiative (CDI), a federally-funded program managed by the Co-operatives Secretariat at Agriculture and Agri-food Canada. The partners gratefully acknowledge the support of the Co-operatives Secretariat.

This guide has been produced with the collaboration of:

CWCF FCCT

Ohio Employee Ownership Center OEOC

Canadian Labour Congress
Congrès du travail du Canada
Western Region

Alberta Federation of Labour

co-op ventures worker co-op

Secrétariat aux coopératives
Co-operatives Secretariat

Steps in the Buy-out Process

Why Buy-out the Boss?

This resource guide answers frequently asked questions about what workers can do to protect their jobs against plant closure and other threats, when a worker buy-out may be a viable option, and what steps need to be taken to carry out a union-led conversion to worker ownership. There are two kinds of situations where unionized workers may want to actively pursue the strategy of buying a business:

- Where jobs are threatened by plant closure.
- Where owners are retiring and wish to sell their business.

Plant Closure

When a plant closure is threatened, the available options are:

- Closure – the inevitable result if nothing else is done;
- Another buyer is found; or
- Employees take it over.

Two fronts for union action are possible:

1. Continue negotiating best closure agreement for the membership.
2. Explore the possibility of an employee buy-out.

Early Warning Signs of Plant Closures

The more lead time for planning you have, the higher the chances of success. There are always signs of a planned closure, such as organizational restructuring during periods of growth. Facilities at-risk during economic downturns may be viable enough to survive the downturn if critical market, production, or financial changes can be made in time. It is possible to devise an aversion strategy, but you need to know beforehand in order to plan and implement a strategy. A separate resource guide is available that includes a checklist of early warning signs.

Union membership can take some possible steps before a buy-out is imminent.

Use the collective bargaining process to assert workers' rights:

1. Negotiate a disclosure clause – the union needs to be informed if closure or sale is planned.
2. Negotiate right of first refusal if the plant is sold. This is the right to have the first opportunity to buy when a company or stock is put up for sale. Some employees are able to negotiate this right which strengthens the ability to buy the company if it is put up for sale.

Retiring Owners

In a situation where a local union is involved with an individual or group that wants to retire and sell a company, an opportunity exists for the local union to preserve their jobs. In these cases, the companies are generally in better financial shape and chances for success are higher.

The options available are:

- Another buyer is found;
- Employees take it over; or
- Closure – the result if neither of the first two works out.

Key Questions to Ask Before Attempting a Buy-out

Is the current owner willing to sell to the employees?

The owners may provide a "buyer's package" including essential information such as recent audited financial statements, key customer and supplier information, terms for existing financing and other essential information for assessing the opportunity. If the employer is not willing to provide this information, it is unlikely that a buy-out opportunity exists.

Do the employees and their union want to buy?

The answer only comes through asking. The employees need to decide whether they want to become owners of the company, whether they are willing to take personal and financial risks to be involved in structuring the purchase, and then how the company will be run. It is only worth pursuing this if the local union executive and a significant majority of members support it.

Will the new employee-owned company have competent management?

Can the competent members of the current management team be retained? Management and labour need to work together. You will need managers who have all the skills of conventional company managers plus the ability to inspire people to work together creating a spirit of service and responsibility.

What is the union role?

The keys to creating successful, democratic employee-owned businesses include:

- The structure of ownership of the firm;
- The structure of worker participation in decision-making; and
- The provision of training so employees can take an informed role as owners.

The WLWCC promotes worker-owned co-operatives as a model for employee ownership. Worker-owned companies are greatly enhanced by the presence of a strong, democratic union. Unions facilitate the creation of a culture of ownership in firms in which ordinary workers know they are owners, benefit from ownership, are informed as owners, have opportunities for input, and consequently exercise rights and responsibilities of ownership. Both management and the union expand their roles in employee-owned firms that are worker-owned co-operatives.

The local executive with the assistance of the regional and/or national union staff have to provide leadership, acquire the necessary technical support, represent the workers' interests in the process, and report back to the workers.

The Steps to Success

Whether it is a job threatened plant closure situation or a retiring owner, the steps to success are similar. First, a word of caution – The Ohio Employee Ownership Center has worked with 575 cases of potential worker buyouts, and of those 575 cases, 84 have become employee-owned firms. This process will not work in every case. Each case is unique.

Financing options vary in each case and will be very difficult in plant closure situations.

Owners in closure situations may have an agenda that includes moving production to a cheaper location and they may not want to leave the plant in Canada open to provide competition.

The following steps are meant as a general guideline. More detailed information is available from the WLWCC.

1 Create a Steering Committee

In this first step, the local union executive meets with union membership to determine interest in the buy-out option. If the commitment exists to pursue this option, create a steering committee to oversee and manage the work. Where there is sympathetic management, the steering committee can be made up of the key union representatives and key management representatives. Membership in the steering committee is usually open to all the potential future employee-owners. A leadership team is usually selected of labour or employee (includes local executive) and management representatives who will serve to represent the interests of all the employees. They will be in charge of overseeing the completion of the work required to complete the buy-out. There may be co-chairs. It may be necessary to incorporate the buy-out committee so that it can legally enter into contracts and administer various sources of funds to support the buy-out effort.

2 Complete a Pre-feasibility Analysis

The first thing the steering committee will want to do is assess whether or not to invest the time and effort required for a buy-out. A pre-feasibility analysis needs to be completed by a person or group with experience in the industry and who has the trust of the steering committee. The pre-feasibility assessment will identify whether or not the business will succeed as a buy-out and what conditions are necessary for success.

3 Commitment Letter

Sign a joint Commitment Letter with the business's owner(s), which outlines the commitments that both parties are willing and able to make to each other during the process. It contains such things as a timetable and an exclusivity clause. Its purpose is to protect both parties. The commitment letter may be signed before the pre-feasibility assessment.

A commitment letter is intended to protect the interests of both the members of the buy-out group and the owner. It may also include confidentiality provisions, conditions under which the research may be carried out, and opting out clauses for each of the parties.

The two parties mutually agree to key parameters for their negotiations:

- the actors involved, for example, a business valuation firm, a notary, the owner's financial consultant, the experts that the steering committee will need;
- the steps of the transfer process;
- the timetable for the process.

4 Develop a Conversion Plan

Analyze the business and define the mission and strategic directions of the future worker ownership. The pre-feasibility assessment can form the basis for a more detailed analysis.

To develop the takeover plan, the business must first be analyzed from every angle to gain a proper understanding of the issues and challenges of managing the business. In other words, a full diagnostic of the business must be completed. Elements of a conversion plan may include:

- Internal analysis (the business' strengths and weaknesses, its investment requirements, etc.);
- External analysis (its market positioning, business threats and opportunities in its markets, market trends, etc.).
- Financial Plan;
- Financing
- Cash Flow Management
- General Management Plan;
- Human Resources Plan;
- Equipment management Plan;
- Supply management Plan;
- Sales and Marketing Plan;
- Collective Agreement;
- Co-operative Framework.

5 Get Expert Training and Advice

Get expert training and information. It is important that all key participants receive adequate training on the logic and practice of managing and governing an employee-owned business.

The steering committee will need professional assistance that includes an experienced business analyst, a lawyer who can negotiate with the owner and an investment banker who may negotiate with the owner over terms of the sale and will pull together the financing. There would ideally be one coordinator for all professional assistance, who may be a co-operative developer or a succession coordinator.

6 Develop a Preliminary Financing Plan

The financial plan includes the terms and conditions for the employee purchase of the business. The buy-out group will need financial partners. Professional resource people will be needed to identify potential investors and/or other financial partners.

The preliminary financing plan includes three important pieces of information:

- an initial estimate of the value of the business provided by a professional business valuation;
- a precise estimate of what all members will be able to provide to finance the buy-out. This may include severance negotiated in the case of plant closure;
- a description of possible sources of outside financing and amounts that can be committed by them. One possible key source of outside financing is the current owner. Deferred payments to current owner or vendor financing is often essential to a successful buy-out.

7 Come to an agreement

Come to an agreement with the owner for determining the value of the business and on the payment arrangements. The preliminary financing plan represents the employees' offer on the price and payment arrangements, and is the basis for negotiating with the owner.

Once an agreement has been reached on the price and the various conditions, you will have to provide the owner with a letter of intent or an offer to purchase.

8 Develop a Business Plan

The business plan is the document that will guide the operation of the employee-owned business. It will incorporate elements of the conversion and financing plan and provide a blueprint for how the employee-owned business will move forward. The steering committee will participate in and monitor the development of the business plan. The greater the involvement of the employees and/or their representatives in the plan is, the higher the degree of success. A business plan is a management tool and a monitoring tool, which will enable the management of the buy-out to assume its key responsibility, that is, to ensure that the business succeeds and meets the interests of its members.

9 Develop a Training Plan

Develop an Education and Training Plan to address the transfer of intellectual property and other knowledge that is essential for running the business well. As was mentioned earlier, an education and training plan is an important factor in ensuring the ongoing success of the business.

Training in employee governance, labour-management relations and co-operative practice are generally required.

10 Develop a Succession Plan

A succession plan sets out the what, when, how and with whom of the process for management succession – the transfer of ownership and control from the former owner to the buy-out group. Although each case is individual, this information can be grouped into five major areas relating to the following:

- the supply relations (types of contracts, negotiation methods, managing accounts payable, etc.);
- the customer relations, in the case of a business that sells goods or services to other businesses, and the customer base in the case of a business that sells to the general public;
- the network of business partners (accountant, banker, lawyer, notary, as well as sectoral business association, chamber of commerce etc);
- the management structure and staff relations;
- the production process and delivery of goods and services, the seller's "tricks" of the trade.

11 Prepare the Documentation to Create the Co-operative

The co-operative will need to be incorporated. The process of forming a co-operative is clearly marked out by provincial legislation outlined in the Co-operatives Act and has established practices. A co-operative business advisor can provide advice and assistance in this process.

Remember that in addition to developing a business plan for the future co-operative, its governance structure must be determined as well. The governance structure is regulated by the co-operative's by-laws and policies.

The by-laws set out the mission of the co-operative, the process for becoming a member of the co-op, eligibility for the board of directors, executive committee and other committees.

Policies define the co-operative's relationship between the governance (co-operative membership and board) and management, such as a conflict of interest policy, a compensation policy for management, etc. Most policies are approved by the Board of Directors although sometimes policies are approved by the members.

12 Develop a Program for Learning the Business and Co-operative Management and Governance

Being a co-operator is a learned skill for most people. Very few people demonstrate a full range of entrepreneurial skills, but thankfully most can be acquired through training.

It is important to develop a training program not only for newly elected boards of directors, but for managers and members themselves.

The program can be developed based on the training needs of board members and the management team. The WLWCC can help you find training on a range of co-operative issues including director training, financial and strategic planning, etc.

Topics to cover during co-operative training:

For everyone:

- How they own the business and the type of co-operative created;
- What drives the business they own;
- Rights and responsibilities of decision-making authorities (understanding financial information);
- How a general meeting works;
- The skills to participate as a member in the co-op's democratic life.

For directors and management team:

- Logic of co-operative management;
- Reading and analyzing financial statements ;
- The strategic planning process in a co-operative;
- Roles and responsibilities of directors;
- How a board of directors works and is run.

13 Ensure the Proper Education is Provided According to the Plan

The co-operative's board of directors is responsible for ensuring that the plans regarding communications, training, and sharing of gains is followed, and that corrective action are taken, if need be. The board of directors and the executive of the local union have to work in unison. Success or failure depends on this.

If you need help

There are worker co-op development specialists and other professionals who are knowledgeable about worker co-operative development issues such as business planning, capitalization, by-law and policy development, member education, and training for the various roles within the co-operative. They can help you develop effective structures and strategies on both the business and governance sides. Assistance is available to employees to develop and implement the worker co-operative aspects of the employee ownership plan. The WLWCC can provide assistance in finding a qualified co-op development specialist and other professionals to meet your needs.

Sources:

Selling Your Business to Your Employees through an ESOP or a Co-op by John Logue and the Staff of the Ohio Employee Ownership Center, Unpublished.

Succession Planning Using the Worker Co-op Option by Peter Hough, Canadian Worker Co-operative Federation, 2005, p20-21.

David P. Ellerman (1988) The Legitimate Opposition at Work: The Union's Role in Large Democratic Firms Economic and Industrial Democracy 1988, p 437-453.

The Worker Co-operative Movement in Canada

Worker co-operatives in Canada are represented by the Canadian Worker Co-operative Federation (CWCF). It supports the development of worker co-operatives in Canada by providing technical assistance through its Worker Co-operative Developers' Network, term and patient capital through its small revolving loan fund (the Tenacity Works Fund), and general support to the sector through conferences, advocacy and services such as a Self-Directed Registered Retirement Saving Plan for worker co-operatives.

The Canadian Worker Co-operative Federation is prepared with its network of developers to provide resources and expertise in worker ownership. CWCF and the other partners in the WLWCC have resources and experience in organised worker buy-outs, and relationships with experienced professionals they can bring to bear to raise support for such a buy-out.

Call the Western Labour - Worker Co-operative Council for more information.

Hazel Corcoran, Executive Director,
Canadian Worker Co-operative Federation
(403) 276-8250;
hazel@canadianworker.coop