STAFF PAPER

Worker Cooperatives: Case Studies, Key Criteria & Best Practices

By

Greg Lawless & Anne Reynolds

UWCC Staff Paper No.3 July 2004

University of Wisconsin Center for Cooperatives
230 Taylor Hall, 427 Lorch St.
Madison, WI 53706
Ph: (608) 262-3981
www.wisc.edu/uwcc

Worker Cooperatives: Case Studies, Key Criteria & Best Practices

By Greg Lawless
&
Anne Reynolds

Greg Lawless is an Outreach Specialist at the Center for Cooperatives, at UW-Madison.

Anne Reynolds is the interim director of the Center for Cooperatives, at UW-Madison.

A version of this publication was originally submitted on June 3, 2004 as a final report for the World Council of Credit Unions.

For additional copies, please contact us at

University of Wisconsin Center for Cooperatives
230 Taylor Hall, 427 Lorch St.
Madison, WI 53706
Ph: (608) 262-3981
www.wisc.edu/uwcc

Worker Cooperatives: Case Studies, Key Criteria & Best Practices

Worker cooperatives are enterprises that are owned and controlled by their employees. Each member purchases a share in the cooperative, and assets are collectively owned by the membership. Worker co-ops operate on the one person/one vote principle, regardless of the member's investment. The primary purpose of a worker co-op is to provide employment for its members.

The International Organization of Industrial, Artisanal and Service Producers´ Co-operatives (CICOPA) has a membership of over 70 organizations in 57 countries. They estimate that the number of member/workers in employee-owned organizations has risen from six million in 1975 to 50 million currently. Much of this new impetus was due to the privatization of a number of economies (eg China).

Employee ownership has become increasingly popular in the United States. Companies that provide their workers with a share of ownership can garner tax advantages while providing a cost-effective employee benefit. In conjunction with a participatory management style, they may also enjoy productivity gains.

About 12,000 U.S. companies offer employee stock ownership plans (ESOPs), a common method for granting employee ownership. Of these, 95% are closely held (non-public) firms, in which the median employee ownership percentage is 30-40%. About 3,000 ESOPs are now majority employee owned.

A less common but increasingly credible alternative for employee ownership is the worker-owned cooperative model. There are approximately 400 worker co-ops in the U.S. In general, they are 100% worker-owned and ascribe to the cooperative principle of "one member, one vote". They vary widely in their management and pay structures, from remarkably "flat" to more conventionally hierarchical. The country's largest worker owned co-op is Cooperative Home Care, a home health care agency in the Bronx borough of New York City. With 780 employees, it ranks 93rd on a national list of majority employee-owned companies.

Most worker co-ops are much smaller, ranging from 20-200 employee-owners. They are found in a wide variety of industries. In this publication, we will look at four diverse worker cooperatives in the U.S. Following these case studies, we will consider key criteria and best practices for starting and maintaining successful worker-owned co-ops.

Four Case Studies

Burley Design Cooperative

This co-op in Eugene, Oregon began as a small family-owned business in Fargo, ND that sold hand-sewn bicycle bags to small bike stores and at outdoor public markets. After moving to Cottage Grove, Oregon, the owners decided they were not comfortable being "bosses", and they had a vision of democratic workplace, with shared responsibilities and decision-making. So in 1978 they offered their employees a stake in the business, and Burley Design Cooperative was incorporated. About the same time, this founding couple wanted a way to cart their merchandise to market and take their new daughter along on bike trips. Using wooden blocks and parts from a swing set, they designed their first bicycle trailer, which has since become the mainstay of the business. However, in the early 1980s, the couple left the company, and economic difficulties reduced the co-op to only four members. Working for little pay and pledging personal belongings as collateral to secure outside financing, they expanded their marketing effort nationally. To attract more workers, they moved to Eugene. They also narrowed their product line, refined their product pricing, improved their accounting procedures, and reorganized production. With additional loans they purchased a building as their first significant asset. From 1983 on, trailer sales increased dramatically. Membership rose from 15 in 1986 to 40 in 1989, at which point, after much debate, they voted to transfer governance from the full membership to an eight-member board of directors. Meanwhile, they invested in research and development as well as international marketing. By 2003 they had grown to nearly 100 members, with $10 million annual sales. To this day, all member owners receive the same hourly wage.

Union Cab

Union Cab Cooperative of Madison, Wisconsin arose from the ashes of bitter labor conflicts in the mid-1970s. Substandard equipment, minimal benefits or rights, and low morale drove workers to stage a series of strikes that ultimately bankrupted two of city's top cab companies. In January 1979, five former employees resolved that there was enough expertise among drivers and clerks to run their own cab business. They incorporated and applied to the city for 20 taxi permits. Within just eight months, they raised $150,000 from a private bank, two local organizations and sales of preferred stock and then purchased and equipped eleven cabs and began operations. Even with drivers earning only 80 cents per hour, they lost $35,000 the first three months. But when the city permitted cab companies to raise rates, and the city bus drivers went on a two-month strike that summer, the taxi business picked up. As the business grew in the early 1980s, new challenges arose. Born as an outcome of intense labor activism, the co-op was pressured to take various political stances. But needing to cater to the entire spectrum of potential clients, after much internal debate the board of directors established a policy forbidding company statements or disbursement of co-op funds to support extraneous political causes. Meanwhile, increasing demand led to decreased service and lower morale. Outside advisors helped reorganize the management structure and improve internal communications. In 1985 a loan from National Cooperative Bank put computers in every cab. For the first time, full-timers earned a week's paid vacation, and morale improved. By 1987 the entrance of a new competitor cut into sales and there was a major turnover in top management. The new management team cut expenses and attacked the business account market, and once again the red ink flowed black. Continuing to adapt in this volatile industry, Union Cab has grown to 150 active or probationary members, with 58 cabs and gross annual revenues hitting $3.75 million in the early 2000s.

Rainbow Grocery Cooperative

Started in the Mission neighborhood of San Francisco in the early 1970s by a spiritual community, Rainbow Grocery quickly became a secular project. It was one of twelve small community grocery stores that grew out of the People's Common Operating Warehouse, which strove to build a "People's Food System" as an alternative to what they saw as mainstream industrial agribusiness. Of the original twelve groceries, Rainbow is only one of two that continue today. They credit their comparative success to three long-standing attributes: (1) a service-orientation that grew out of their spiritual foundation, (2) the business skills and backgrounds of their early leaders, and (3) superior product selection, which was a by-product of the their concern for service and good business practices. Organized for simplicity's sake under the legal ownership of two married founders, Rainbow initially operated with entirely volunteer labor. In 1976 the business transferred ownership to a nonprofit organization, adapting the corporate documents and guiding principles of the Peoples Warehouse in order to appease activists who felt they weren't political enough. The nonprofit status proved problematic when they went to private banks for lending support. After only a few months of operating, the business generated enough income in their 2000 square foot store to hire two active volunteers at minimum wage. Located central to many counterculture youth, the business continued to grow. In order to avoid taxable profits, they increased compensation to workers and diversified into a second store that included high mark-up vitamins and supplements. Sales peaked again when they took steps to curtail shoplifting, improved pricing, attended trade shows and took better inventory. In 1983, unable to secure bank financing, they raised $250,000 in customer loans, combined their two stores and moved into a 9,000 square foot building. While for years they were one of the Bay areas largest health food stores, by the late 1980s private competition moved in, bringing higher customer expectations of service, selection and shopping experience. Looking to expand again, they finally converted to a cooperative corporate structure in 1993 and, with backing from the city, were able to obtain a million dollar bank loan. Moving into their present location in 1996, sales grew 55% in one year and in a couple years the worker-members doubled to 200. Today, the store generates over $30 million in revenue annually, while operating without either a general manager or department managers. Fourteen departments do their own hiring, scheduling, and training, operating almost like fourteen independent collectives that combine to form one larger cooperative.

Cooperative Care

In the 1990s, Waushara County in rural Wisconsin faced growing demand for in-home care providers to enable its elderly and disabled citizens to remain in their homes. But low wages and lack of benefits resulted in a serious concern by the home care workers and certified nursing assistants (CNAs) that they could no longer personally afford to continue working in this field. Using limited public resources, for twenty years the county acted as a third party fiscal intermediary between patients and caregivers, but that arrangement was severely jeopardized by a recent IRS ruling that required the county to assume more liability and costs. The county human services director heard about a worker-owned, in-home care co-op in New York City. With technical assistance from a cooperative specialist from a U.S. Department of Agriculture office in Wisconsin, the county approached its existing home care providers with the idea. After fifteen months of meetings, co-op education training, market analyses, and a myriad of related business start-up tasks, Cooperative Care was incorporated in February 2001. A contract with the county for $800,000 allowed the co-op to secure a loan with a local bank for $125,000, and members contributed a modest $4,000 in equity. They rented office space, hired an executive director, and enlisted a retired electric co-op executive to help develop financial systems. As a private company, the co-op was able to go beyond its contracted work with the county and serve other counties and private clients. Since beginning operations in June 2001, the co-op has surpassed all expectations. Membership has grown from 61 to 81 members. By combining public and private revenue sources, the care providers have enjoyed increased pay, workers compensation, increased holiday pay, ten days paid vacation, travel reimbursement, and 50-75% health insurance coverage. Moreover, the co-op was profitable in each of its first three years, distributing $40,000 as patronage refunds in 2002. Nevertheless, there have been challenges, including three executive directors in as many years and membership turmoil resulting from those position transitions. Thanks to a major state budget crisis and resulting county level shortfalls, reimbursement rates to the co-op had to be twice renegotiated downward. Rising health insurance costs have been difficult to absorb, but despite these challenges the county and the co-op members are optimistic. Recently, the project was named Wisconsin's the Top Rural Development Initiative for 2003, and it is currently one of 15 finalists in the Harvard School of Government's prestigious Innovations in American Government Awards.

Key Criteria for Starting Worker Co-ops

The keys to success for worker-owned co-ops are in many ways no different from any other private company. But as the four cases above illustrate, starting worker co-ops involves some fairly unique attributes.

Visionary cooperative leadership

The four cases reveal that leadership in new worker co-ops can arise in various ways. An individual entrepreneur can resolve that sharing ownership with employees can relieve the management burden, or boost productivity. Or, a group of workers, unemployed by a strike or a company gone bankrupt, can pull together and combine their expertise to run a company as well or better than their former bosses. A collective of like-minded individuals can band together and establish a co-op as a means to spiritual or political ends. Finally, public service professionals, acting as outside agents, can guide a group of independent, disadvantaged service providers through the process of establishing a worker-owned company.

Even when the leadership arises from a single, visionary individual, clearly the challenge is to transfer and expand the business to a group of people, who undoubtedly vary in skills, motivation, and resources. Leadership then becomes a shared endeavor, demanding excellent communication, conflict negotiations, long hours of meetings, and collective decision-making. In essence, a cooperative culture is required.

Appropriate organizational structure

The four examples of worker cooperatives also reveal a variety of legal and organizational structures. This is partly a result of incorporation statutes that vary from state to state. The grocery example illustrates that a co-op can essentially operate for years in what is essentially an inappropriate business structure. But eventually, in order to obtain bank financing, they transitioned from a non-profit to a cooperative model, which more clearly identified ownership.

Perhaps more important than the legal framework, it is critical to develop an organizational structure that reflects and promotes a culture best suited to the particular business. As we have seen, worker co-ops can involve more conventional hierarchies with general manager and an elected board of directors, or no managers and all members serving on the board. Regardless, it takes time to establish company policies, decision-making procedures, communication systems, incentive systems and work assignments that guide the operation of the business.

Creative financing

Most worker co-ops are small businesses, and like any modest enterprise, raising necessary capital is a major challenge. Sometimes, it can be harder because many banks do not understand or appreciate the cooperative model. At the same time, more people can draw capital from more sources. A typical small business owner generates "sweat equity" with long hours of unpaid work. In a co-op, that burden can be spread over more people, voluntarily accepting lower wages as a means of financing the business. The grocery co-op revealed its ingenuity by tapping its appreciative customers for quarter million dollar loan, while the home care co-op leveraged its contract with the county to secure a private lender's support. Where available, cooperatives should take advantage of regional and national financial institutions that specialize in loans to cooperatives.

Strong business orientation

Perhaps it is the participatory nature of the worker co-op model that makes it an attractive model for people who aspire to social and political ideals. While those motivations can inspire employees, and even carve out a niche in the marketplace, it's also imperative that the co-op maintains a strong business orientation. The grocery co-op outlived most of its contemporaries because it focused on customer service and product selection. The cab co-op likewise didn't allow extraneous political causes to thwart its business goals. The bicycle manufacturing co-op distinguished itself in a highly competitive marketplace by developing very innovative products. The home care co-op modified its pay scale requirements, benefits, and patronage refunds to build a larger reserve. In all four of these cases, the workers made the wise business decision to forego short-term satisfaction by investing much of their profits back into the business.

Best operating practices

Successful worker cooperatives take advantage of their strengths and avoid potential pitfalls by innovating from within and adopting the best operating practices of other well-functioning co-ops.

Members understand both their industry and their cooperative.

Continuous education for members is vital for a successful cooperative. Members must be able to understand the financial situation of the co-op, the decision-making process, the cooperative's mission, values and policies. Since the members are responsible for the strategic direction of the business, they must be knowledgeable of the key trends in their industry or sector. These trends include the economic, political, competitive and regulatory environment, as well as the workplace culture (wages, benefits, job expectations) of similar businesses.

Co-op members are encouraged through subsidies and in-house classes to continue their education. Successful cooperatives are continuous learning organizations, where members are leaders in their sector, open to new models for decision-making, and able to envision the future.

Governance structures are supported by the membership.

Worker cooperatives can be managed as collectives or with a board/management hierarchical structure. In either case, members must understand their role and participate actively. In order to do this, they must have access to information and be given the tools to contribute effectively – either by running for the board, serving on committees/councils or participating in the meetings of the collective or their work team. These governance institutions must be vital and effective. Over time, they may become formalized or stagnant. Successful cooperatives encourage debate on the structures that guide their democratic practice, and create new institutions that encourage informal and dynamic decision-making.

Transparency is also an important component of governance, and should be the default policy, recognizing that some issues must be confidential. Democracy must permeate the organization, so that meeting facilitation is fair and voting/consensus is consistently applied to group decision-making situations.

The cooperative has a clearly defined mission and focus.

Like all organizations, worker cooperatives must fully understand their business environment and make decisions based on their strategic goals. These goals should be based on the co-op's mission and values, which may include a commitment to the community and the co-op's customers, as well as a fairly-paid workforce. A good strategic planning process, involving co-op members and other stakeholders, can be an excellent vehicle for encouraging renewed commitment, resolving contentious issues, and making decisions on growth.

Managing growth is challenging for any business. Every growing business establishes new structures that allow people to work together effectively. A collective that operated well as a single decision-making body for 25 members may need to divide into sub-units when the membership grows to 40. The co-op board may need to establish more committees to involve more members in decision-making. Successfully managing growth requires both flexibility and a strong commitment to the co-op's basic values.

Personnel practices reflect the cooperative's culture.

Members of worker cooperatives are often faced with creating personnel practices that work for them. It may be challenging for new employees to move into an ownership role in their workplace. Peer review, team meetings, and social events are often a very intentional part of a co-op's personnel practices. Co-op members are often very involved in establishing work rules and procedures. Whether the cooperative is managed as a collective or employs a manager, committees and councils are often important vehicles for decision-making. Selection committees may have final authority on hiring decisions. A grievance committee may have the authority to over-rule a manager's decision. Committees may have the authority to make recommendations on critical issues, which are rarely over-ruled by the board.

Many worker cooperatives have members and non-members working side by side. There may be a lengthy probation period before membership is offered to an employee. The process of being accepted as a member is often rigorous, since the new member is essentially a business partner.

The cooperative maintains adequate financing.

Cooperatives are financed through a combination of member investment and debt. Members invest both their labor and their capital, through purchase of a membership share. As owners, they also reinvest a portion of their profits annually in the business. Most cooperatives rely on some degree of debt financing, so they need to develop relationships with financial institutions. They may also self-finance through member loans, which are repaid at a designated interest rate.

In order to make good decisions, members must be familiar with the co-op's financial position. They must understand the balance between present and future rewards. Members will consider tangible and intangible benefits when participating in the co-op's financial decisions. Wages, future profits, job security, benefits, and professional growth are all part of the mix, much of it highly personal. Maintaining a balance between members' personal goals and the co-op's business success is always a challenge. Successful cooperatives take advantage of the investment worker members have in the business, and then create commitment through a combination of trust, transparency and a shared vision.

SOURCES

Bau, Margaret and Dianne Harrington, "House Calls," *Rural Cooperatives*. Rural Business-Cooperative Service, U.S. Department of Agriculture, May/June 2003.

Burley Design Cooperative website: http://www.burley.com/Images/PDF/burley%20history.pdf. June 1, 2004.

Cheney, George et al, "Democracy, Participation, and Communication at Work: A Multi-disciplinary Review", *Communication Yearbook 21*, pp 35-91.

Center for Cooperatives, University of California-Davis, "Made in the USA: American Worker Cooperatives," a 34-minute video, 2003.

National Center for Employee Ownership webpage: http://www.nceo.org. June 2, 2004.

Rainbow Grocery Cooperative website: http://www.rainbowgrocery.org/AboutUs/2.3.pf.html. June 2, 2004.

Union Cab website: http://www.unioncab.com/coop/history.html. June 1, 2004.