

# Employee Owned Business Structures

A comparison of worker co-ops and ESOPs



## Worker Co-op

A type of business that is majority owned and controlled by its employee members. Eligible employees are entitled to own up to one share of common stock (one equal voting-share) of the business.

## Employee Stock Ownership Plan

In an ESOP structure, a trust acquires some portion — sometimes all — of a company's stock, and holds it for the benefit of employees. The company board generally appoints the trustee who administers the plan. Fundamentally the ESOP is a retirement or separation benefit, but a variety of employee ownership-rights can be included.

Topic	Worker Cooperatives	Employee Stock Ownership Plan (ESOP)
Membership	Membership is open and voluntary for eligible employees. The co-op determines eligibility requirements.	Everyone over 21 who works more than 50% time, with one year of service becomes a participant.
Voting Rights	Each member gets one vote. This typically applies to electing the board of directors and other select decisions identified in the articles and bylaws.	Employee shares have limited voting rights that vary depending on the company. The ESOP trustee (who acts as the legal shareholder) votes on corporate issues. Some ESOPs own 100 percent of their company's stock and can incorporate democratic voting structures.
Governance	Board of Directors (BOD) is elected by members. Typically composed of mostly member owners (outside BOD members are allowed)	BOD determined by ownership of shares. An ESOP is overseen by a trustee. Any shares still held outside of the ESOP still have the same rights as before the ESOP sale
Management	The BOD typically hires and oversees a general manager, or management team, that is responsible for general operations.	The BOD typically hires and oversees a CEO and officers that are responsible for general operations.
Typical company size	Can be any size over 3 employees. The largest in the USA is over 2000 employees, and globally they can reach over 75,000.	Often reserved for large enterprises, typically 100+ employees. The largest in the US has over 200,000 employees.
Allocation of Profits	Based on member hours worked, wages, or some other equitable formula.	Based on shares held. ERISA requirements ensure that allocation policy will be clear.
Legal Structure	Minnesota has specific co-op statues available (308A and 308B), but other types of incorporation can work	Can incorporate as C-Corp or S-Corp, or LLC
Potential For Seller To Retain Partial Ownership After Sale To employees	Yes, seller can participate as a member or own shares outright. The nature of the ownership will determine 1042 rollover eligibility.	Yes, but seller's holding must be outside the ESOP
Employee-owner Sale of Stock Outside of Company	Not permitted. When members leave, they must sell back to the company or to an incoming member.	Usually not permitted. When a member leaves the company, must offer them an opportunity to sell stock back to the company.
Valuation of Individuals common stock	Does not change unless determined by BOD (changes in an employee's "stake" is determined by individual capital accounts).	Fair market value based on independent valuation performed annually.
Cost To Set Up	Typically in the range of \$20K - \$50K, but can be more or less	Variable, but typically in the range of \$100K - \$200K or more
Annual Maintenance Cost	None, unless the co-op choses to require a valuation.	Mandatory audits often bring annual costs above \$20K
Potential Tax Benefit To Seller, when selling to employees	Can defer capital gains tax on the capital gains tax on the proceeds of the sale if they are invested in 'approved securities.' At least 30% of the business needs to be sold to the co-op.	Can defer capital gains tax on the capital gains tax on the proceeds of the sale if they are invested in 'approved securities.' At least 30% of the stock needs to be sold to employees.
Outside Equity Investors	Permitted with various restrictions.	Permitted. The stock held by the ESOP trust must be voting common stock with the greatest dividend and voting rights of any class of common stock, or preferred stock that is convertible.