STATEMENT OF
THE OHIO EMPLOYEE OWNERSHIP CENTER
KENT STATE UNIVERSITY

TO THE
FINANCIAL INSTITUTIONS AND CONSUMER CREDIT SUBCOMMITTEE
COMMITTEE ON FINANCIAL SERVICES
U.S. HOUSE OF REPRESENTATIVES

ON
THE U.S. EMPLOYEE OWNERSHIP BANK ACT

JUNE 10, 2003

Mr. Chairman and Members of the Subcommittee:

The Ohio Employee Ownership Center of Kent State University appreciates this opportunity to present its views to this Committee and your willingness to consider them.

Employee Ownership in Ohio

Ohio is one of twenty-eight states that have passed legislation encouraging the creation of employee-owned businesses; it is one of just eight, however, which have created a state-supported program to achieve this end---The Ohio Employee Ownership Assistance Program, first passed by the Ohio Legislature in 1988 and renewed in 1994 and again in 2000; in each instance, the vote was unanimous in both Houses of the Ohio Legislature.

By way of introduction, the Ohio Employee Ownership Center (OEOC) is a non-profit, university-based program established in 1987 to provide outreach, information and preliminary technical assistance to Ohio employees and business owners interested in exploring employee ownership. The OEOC also provides ownership training on a single and multi-company basis to existing employee-owned firms and is partially funded by grants from the Ohio Labor-Management Cooperation Program of the Ohio Department of Development, private foundations, dues from firms belonging to Ohio's Employee-Owned Network, income from training contracts and donations. The OEOC also administers the prefeasibility study grant program for the Ohio Department of Job and Family Services' Rapid Response Unit. In addition, the Center coordinates the U.S. Department of Labor's National Steel/Aluminum Retention Initiative (NSARI), a national program to assist durable manufacturing in dealing with the continuing threat to the steel and other durable goods industries. The OEOC partners with the Industrial

Cooperative Association in Boston, the Center for Labor and Community Research in Chicago, the Steel Valley Authority in Pittsburgh and the Washington State Office of Trade & Economic Development on this effort.

Since 1996, the OEOC has coordinated the Business Owner Succession Planning Program in the Cleveland area in partnership with the Greater Cleveland Growth Association and CAMP, Inc. to help business owners explore a wide range of succession planning options, including selling to their employees. The program works to preserve jobs that might otherwise be lost from an owner's failure to plan for succession. Succession planning can benefit the owner, his family and the employees of the company. Too often, failure to plan for succession leaves liquidation as the only remaining option. That means that the owner likely won't realize full value of the business and the employees will lose their jobs. Through the Spring 2003, 438 business owners and managers from 355 companies employing 31,000 people participated in the program.

The Ohio Employee Ownership Center works closely with the 59 small and medium-sized firms that are members of Ohio's Employee-Owned Network. The Employee-Owned Network provides a forum for employee-owned companies to meet on a regular basis, and learn from each other's experiences. Member firms receive training on topics such as improving supervisory practices, financial education, open book management, employee participation structures, and other aspects of building high performance workplaces. During 2002, for example, the Network provided training for 335 individual employee owners, ranging from union leaders and shop floor workers to CEOs.

The Ohio Employee Ownership Center also hosts an annual Ohio Employee Ownership Conference that provides a forum for discussions on various issues relating to employee ownership. The one-day event typically draws in excess of 300 employee owners and other interested parties from Ohio and surrounding states.

The mission of the OEOC is to broaden ownership among working Ohioans and to deepen that ownership through employee participation, communication and training in the employee-owned sector. Our overall aim is to anchor capital and jobs locally through participatory employee ownership. That builds productive assets for working families and increases community prosperity. Economic development is quite clearly at the heart of the OEOC's mission.

The Results of OEOC's Programs

Since the inception of Ohio's program in 1987, the Ohio Employee Ownership Center has worked with 436 company owners and buyout groups investigating whether employee ownership makes sense in their particular case; these company and employee groups represent 83,133 employees. Of these, 63 firms, employing 12, 825 have implemented partial or complete employee ownership. Many of these employees would otherwise have lost their jobs to plant shutdowns or corporate downsizing. As a consequence, thousands of jobs have been saved in communities throughout the State because the program existed.

Employee ownership provides a unique opportunity for building strong labor-management partnerships and for anchoring capital and securing jobs in Ohio communities. Co-ownership of businesses by employees and managers expands opportunities for cooperative work practices by establishing common goals, achieving a common understanding between labor and management, and developing mechanisms for employee participation from the shop floor to the boardroom.

Employee ownership helps to create stronger common goals among all those who work at the firm. A common set of goals and shared values are key components of developing a high performance workplace to remain competitive in the future. Twenty-eight years of experience with employee ownership clearly has demonstrated that employee ownership, by itself, doesn't necessarily mean improved company performance. What does seem to improve performance is the combination of employee ownership along with employee participation, open communications about the business and employees having the skill to use the participation system and having the knowledge to understand the business information that may be shared. Employee-owned companies that do all of these things are much more likely to improve their performance relative to their competitors than employee-owned companies that don't do them. These basic conclusions have been reached and confirmed by a number of studies done over roughly the last twenty years. Empirical evidence from national studies done by the National Center for Employee Ownership, by the General Accounting Office, by the U.S. Department of Labor, by the Washington State Department of Community, Trade and Economic Development, and yes, by the Ohio Employee Ownership Center since the mid-1980's suggests persuasively that employee-owned firms in which employees have avenues for participation achieve significant improvements in productivity and in other measures of economic performance.

Employee ownership is a proven tool for job retention and job creation and for economic development in Ohio communities. The Ohio ESOP study cited in *The Real World of Employee Ownership* (Cornell University Press, 2001) found that 49% of employee-owned companies outperformed their industries in job creation and retention, 50% matched their industries, and only 1% under-performed their industries. Employee-owned businesses clearly contribute to healthy local economies.

Employee ownership benefits individual Ohio firms and their communities in many ways. For individual firms, it can create a market for a departing owner's stock, provide significant federal tax breaks, reduce debt service burdens, complement a commitment to participative management, and improve corporate performance. For the local community, employee ownership can be an economic development strategy used to retain businesses that might otherwise be liquidated at the retirement of an owner without a successor, anchor the ownership of businesses in the community, secure jobs that might otherwise be moved out of state, provide additional capital for reinvestment and expansion and increase the competitiveness of Ohio businesses.

The Cost

Cost per job retained, created or stabilized through the Ohio Employee Ownership Assistance Program in calendar 2002 in the firms that implemented ESOPs was $423 per job in Ohio Department of Development funds, a small number compared to the costs, financial, physical and psychological, associated with unemployment. The program is highly cost effective because it helps people help themselves.

As an economic development strategy, employee ownership yields long-term benefits in four additional areas:

1) Employee-owned firms reinvest in capital improvements in existing facilities at a higher rate than other firms. While this is motivated primarily by the employee-owners' interest in job security, it helps to increase the competitiveness of Ohio firms and to anchor capital and jobs in our communities;

2) Employee-owned firms also reinvest in their human capital at a higher level than is common in our region. The consequence is a movement up the scale toward high performance work systems with higher productivity and profitability.

3) There is growing evidence that employee-owned firms have a higher economic multiplier effect in their communities, in part because of a preference for local suppliers and in part because anchoring the ownership of productive wealth in a community among employees generally supports higher levels of home ownership, purchases of consumer durables and higher retirement benefits;

4) Employee-owned firms create significant assets for Ohio families. To date, the Ohio Employee Ownership Center has helped more than 12,000 Ohio employees become owners. We have estimated that these employee owners are building roughly $40 million annually in additional assets through their employee ownership plans. That amounts to about $3300 per employee owner and comes from the creation of new employee-owned companies, employees in existing employee-owned companies increasing their number of shares as well as by increases in the valuation of the company. That wealth creation effect also anchors capital locally and helps solidify our communities' economic base.

In short, employee ownership has proven to be an effective means to retain and increase jobs in Ohio. Today, some 425 partially or wholly employee-owned companies headquartered in Ohio employ more than 325,000 people.

Obstacles

Nevertheless, for many years, the Ohio Employee Ownership Center has had to struggle with issues of how to obtain adequate loans and equity for employee-owned companies. In theory, capital looks so easy to obtain; in practice, however, employee-owned companies and small and medium-sized companies in general, have trouble getting financing. The median size of the companies we work with is about 100 employees doing about $10 million in sales. Of the 59 companies that are part of Ohio's Employee-Owned Network, only 3 have more than 500 employees. In short, we work largely with classic small and mid-market companies. And they are often strapped to get capital for growth.

Every year, in our technical assistance at the OEOC, we have lost at least one otherwise viable employee buyout because of the lack of timely, friendly capital. To put it bluntly, almost every year for the last fifteen, we have seen at least one viable employee buyout effort fail with the loss of 100-200 jobs because no one could round up financing in a timely fashion.

Following are four relatively recent potentially viable buyouts in Ohio that could have benefited from a friendly lender:

CSC Steel, Warren, 1,350 employees The closing of CSC was announced in the third quarter of fiscal 2001. The ODJFS Rapid Response program funded a two-stage prefeasibility study. Stage one determined that the facility was viable and that the shutdown occasioned by lack of debtor in possession working capital had dramatically diminished the value of the plant while making a re-start extremely difficult for employees because of the working capital needs. This stage one study found employee ownership could work with an outside equity partner. Stage two determined whether a partner for the employees could be located and apparently found one in Renaissance Partners, a Pittsburgh-based investment fund. Throughout the first quarter of FY02 Renaissance Partners continued their due diligence for a purchase and the employee buyout group was optimistic about a successful sale and re-opening of the facilities. Immediately following the end of the quarter, however, Renaissance Partners announced that it had ended its interest in pursuing the purchase of CSC; there were, Renaissance Partners told the press, better opportunities available for turnarounds in the aftermath of September 11th.

HPM, Mt. Gilead, 500 employees In FY01 a two-phase study was commissioned. Phase one reached positive conclusions about the viability of a restructured HPM provided a partner could be found for the employees. The second phase of the study then offered three potentially viable options for restructuring the company. During the first quarter of FY02, however, HPM failed to keep control of the company. The consequence was that the lender, Fleet/First Boston, seized HPM's assets, threw the company into bankruptcy and closed down the plant. Fleet proceeded to sell the assets of the company to a buyer of dubious ability to perform in terms of keeping the plant open, or, perhaps, even completing the deal. This was in preference to selling to the partner whom the employees had found who pledged to run the company and to sell to the employees as an exit strategy.

Massillon Stainless Inc. Massillon, 92 employees----Massillon Stainless, Inc. was a stainless cold rolling operation. Major markets for stainless steel strips include household appliances, food processing and restaurant equipment, elevators, architectural trims, pipes and tubing and transportation equipment. At the request of the Steelworkers Local Union and members of salaried management, a prefeasibility study was commissioned. The buyout group selected Locker Associates to perform the study. While the study was being conducted, the company announced plans to close the facility.

The study was completed October 24, 2002 and concluded that the facility could restart and operate profitably if it could find an outside equity investment partner and assure itself of a supply of raw materials. The study also noted that a minority ESOP would make sense given the employees' strong commitment to the company and its excellent labor-management relations. A supply of raw materials was found, however at this writing, the search for an outside equity partner is continuing and the plant remains closed, with the possibility that the machinery could be sold to interests in China.

Cold Metal Products, Youngstown, 116 employees----Cold Metal Products was a manufacturer of strip steel products for precision parts manufacturers. The company announced closure of the plant on August 15, 2002 and then filed for bankruptcy the next day. Subsequently, the Cold Metal Employee Buyout Group filed an application for a prefeasibility study grant that the OEOC approved.

The Buyout Group selected Kokkinis & Associates to do the study. The study got underway late in September and was completed in early December 2002. The study found potential for a successful restart of the facility, however, because of the capital requirements of such a restart, it recommended the employees work to get an outside equity investor involved that would entertain a minority employee ownership position for the workers.

The plant remains closed, however, the employee buyout group is working to salvage a portion of the business with a fraction of the number of employees that used to work at the facility and continues to search for financing.

The Proposed Legislation

The impetus behind this draft legislation is the fact that the United States has lost a couple million good-paying manufacturing jobs over just the last few years. The loss of manufacturing jobs has been going on for some period of time, although the pace of job loss has picked up in the more recent past as we have battled with economic recession, the crisis in the steel industry and the adverse effects of massive international trade deficits.

The U.S. Employee Ownership Bank Act is, in essence, aimed at job retention and job creation and proposes to retain more manufacturing in America by helping American workers buy their plants, educating them in employee participation strategies so they can be more competitive while anchoring capital locally in the process.

The Act proposes to establish a “Bank” within the U.S. Treasury Department that will provide grants to the States to provide technical assistance, participation training, education and outreach along with loan guarantees and/or subordinated loans to help employees purchase the business provided a prefeasibility study shows that employee ownership is a viable alternative. The existence of such a “Bank” would, in our opinion, have made a positive difference in the outcome of the four buyout efforts cited above.

The Act also includes a provision that would require an employer closing a plant to provide 90 days advance notice before such plant closing and to offer the employees the opportunity to purchase the business. This provision would have been of particular utility in the case of Brainard Rivet in Girard, OH. Brainard Rivet is now employee owned and part of Fastener Industries, a 100 percent employee owned company in Ohio. However, it was a major struggle to get to that point. Brainard was part of Textron when the parent shut down this profitable specialty fastener operation so that it could move the production to a non-union plant in Virginia. The move didn’t work out because the employees in the Virginia plant did not have the skill level needed to be competitive. The turning point in Brainard’s road to employee ownership came when it was discovered that Textron was sending much of the Brainard business to competitors rather than running it at its Virginia plant. This revelation resulted in political pressure from the Ohio Congressional delegation as well as from state and municipal representatives. Since Textron was the recipient of a number of government contracts, it became more cooperative in the employee’s efforts to buy the facility.

Conclusion

The Ohio Employee Ownership Center at Kent State University supports the proposed U.S. Employee Ownership Bank Act. Its passage would allow our Center and others like us to more fully and effectively focus on our core mission of broadening employee ownership while also providing a needed financing source to help employees buy the facilities where they work rather than see them close and the production move elsewhere.

The OEOC, like other organizations, faces a continual battle to raise the funds needed to carry out its mission. In recent years, Ohio, like many other states has had budget problems which has meant that funding for programs such as ours has been cut. We have, in some cases, had to go away from our core mission in order to get grants to help pay the bills. We could obviously do more with additional funding. The U.S. Employee Ownership Bank, by providing additional funding would allow us, and other centers like us, to more fully concentrate on broadening ownership in the United States.

We believe the track record the OEOC has established over the years makes a good case for the benefits to the American economy that could come from the establishment of a U.S. Employee Ownership Bank.