

Business Conversion to Co-operatives: Background Information and References

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1. Background

The Coming Business Succession Crunch

A major challenge for Canada's 1.2 million small- and medium-sized enterprises (SMEs) is the potential for large-scale closures due to the growing number of retiring owners that lack a formal succession plan. With 59% of Canada's entrepreneurs over 50 years of age as of late 2018, it was estimated that nearly three-quarters of small business owners plan to retire in the next decade.* While 81% of these retiring SME owners intend to transfer or sell their businesses, only 14% have a solid retirement plan.† In addition to the increasing number of troubled enterprises due to the socio-economic ills brought on by the COVID-19 pandemic, a potential crisis of SME closures across Canada looms.

Retiring owners of SMEs usually first seek to transfer the business to their family or children (43%). Owners also seek to transfer or sell to private-sector, third-party purchasers (24%). But another option is the strategy of **business conversions to co-operatives (BCCs)**. A tried-and-true solution for business rescue and succession in numerous jurisdictions around the world, approximately 205 known BCCs have existed in Canada as of Feb. 2020, and the Co-opConvert Project records 173 enterprises‡ that have emerged from conversions and that are currently still active (see Figure 1).

However, there could be many, many more BCCs in Canada; the BCC solution for business succession and for saving troubled enterprises is still not broadly known among SME owners, workers, unions, and policymakers in Canada. We believe this is a lost opportunity for saving jobs and keeping potentially thousands of businesses alive in light of the SME succession crunch and the business closure risk due to our current pandemic reality.§

What are BCCs?

BCCs take place when private, public, or non-profit companies transition for a variety of possible reasons into a co-operative. In Canada, most conversions occur as part of a succession plan whereby a retiring owner or owners sell their business to staff and they, in turn, continue to operate the enterprise as a co-operative. BCCs can also occur as a community buyout (where consumers and other community stakeholders purchase the enterprise), or a multistakeholder buyout (where employees and other community stakeholders purchase the enterprise). A unique model to Quebec, a partial conversion occurs when a worker-shareholder co-operative (WSC) is formed by employees and they then enter co-ownership agreements with traditional investors; sometimes WSCs are a stage in the eventual full conversion of the enterprise into a co-operative.**

* CFIB, 2018.

† Vieta et al., 2021.

‡ Excluding housing co-operatives. The Co-opConvert Project is still tracking conversions of private or public housing to co-operatives, which is estimated to number in the hundreds throughout Canada.

§ Vieta et al., 2021.

** Vieta et al. 2016.

Former owners can and sometimes do also become members of the newly formed co-operative. This occurs usually when an agreement is reached between the former owner(s) and the new co-op members and can be a part of a staged retirement succession plan, a way for owners to pass on their knowledge of the business to the new owner-members, or a combination of these. At other times, usually in more crisis-based conversions or when owners are keen on fully retiring, owners completely exit the enterprise upon conversion. Increasingly, as the Co-opConvert Project⁺⁺ has found that over 50% of Canada's SME owners do not desire to fully retire and a BCC could make sense as a way for the owner to continue to participate in the business and secure its legacy.⁺⁺

BCCs are Part of Canada's Co-operative Sector

BCCs have been solutions for business rescue and succession in numerous jurisdictions around the world for decades. The research on BCCs shows that they save jobs and preserve the productive capacities of communities.^{§§} They do so because co-operatives are guided by values and principles of inclusivity, mutuality, economic democracy, and concern for community.^{***}

Co-ops are sustainable and viable businesses co-owned by interested members rather than disconnected shareholders, rooting capital locally. Canada already has more than 8,000 co-ops in most of its economic sectors, making up 3.4% – \$61.2 billion – of its GDP, significantly more than the telecommunication sector's and the mining sector's 1.8% of GDP respectively, and the motor vehicle parts and manufacturing sector's 0.9% of GDP.⁺⁺⁺

Despite the enduring presence of co-operatives throughout the country, and the overall success of Canada's approximately 205 BCCs to date,⁺⁺⁺ the BCC model is mostly overlooked and not well understood in Canada as an option for sustaining SMEs in crisis (pandemic or economic) or with succession issues.

How Many and Where are Canada's BCCs

The following is an overview of the BCC landscape in Canada as of Feb. 2, 2021. All data has been collected and analysis conducted by the Co-opConvert Project team (www.coopconvert.ca).

⁺⁺ www.coopconvert.ca

^{##} Vieta et al., 2021.

^{§§} Sanchez Bajo & Roelants, 2011; Vieta, 2020b; Vieta et al., 2017; Zevi et al., 2011.

^{***} Novkovic & Webb, 2014; Vieta & Lionais, 2015.

⁺⁺⁺ Duguid & Karaphillis, 2019.

⁺⁺⁺ www.coopconvert.ca

Figure 1: Conversions to co-operatives in Canada by province and territory, currently active enterprises (map, n = 173) and all enterprises in the Co-opConvert BCC database (pie chart, n = 205) (as of Feb. 2021)

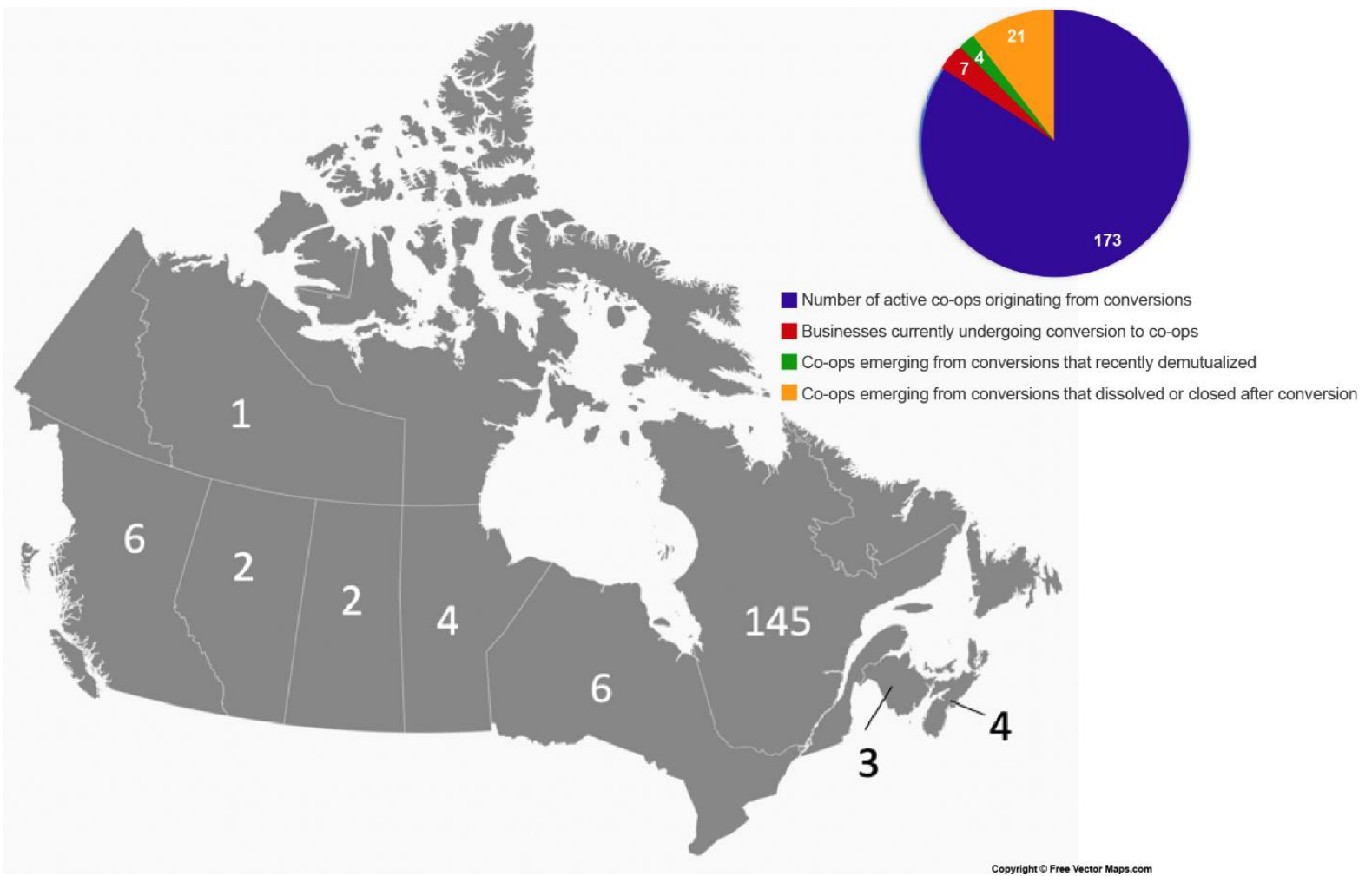


Figure 2: Conversions to co-operatives in Canada by co-operative type (n = 173, active as of Feb. 2021)

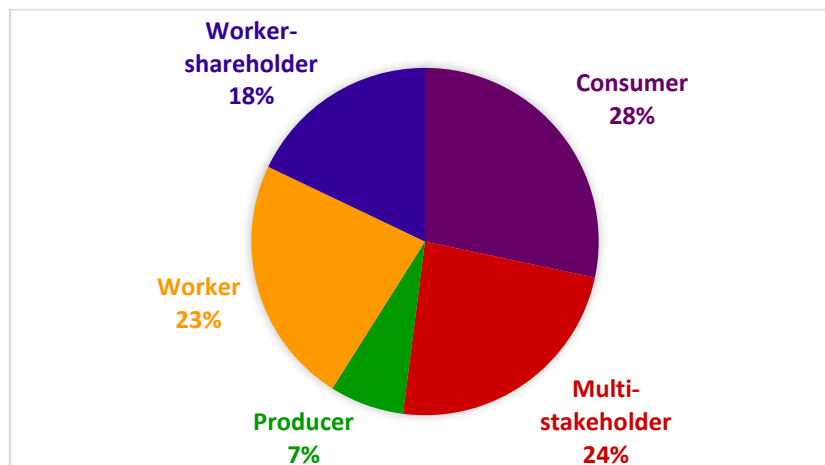


Figure 3: Conversions to co-operatives in Canada by industry/sector and NAIC code
(n = 173, active as of Feb. 2021)

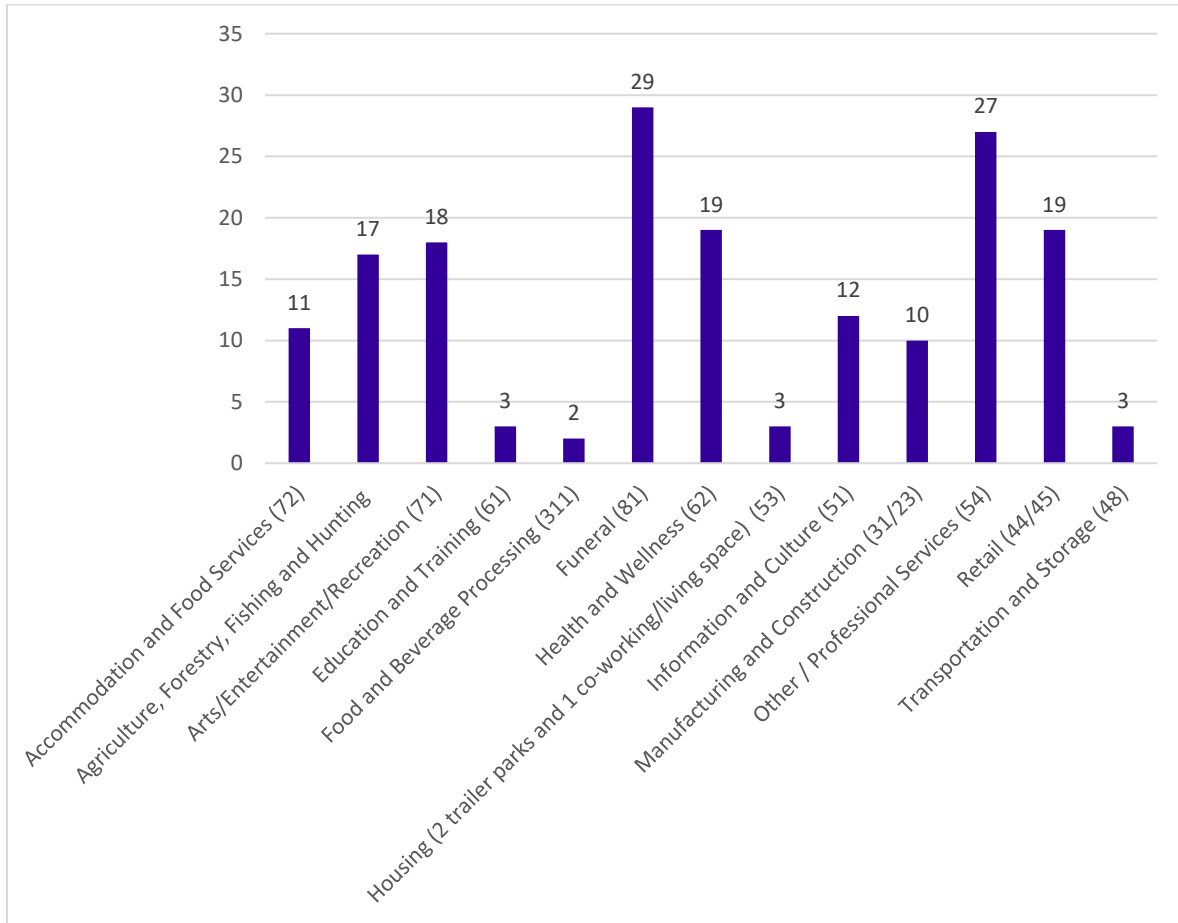
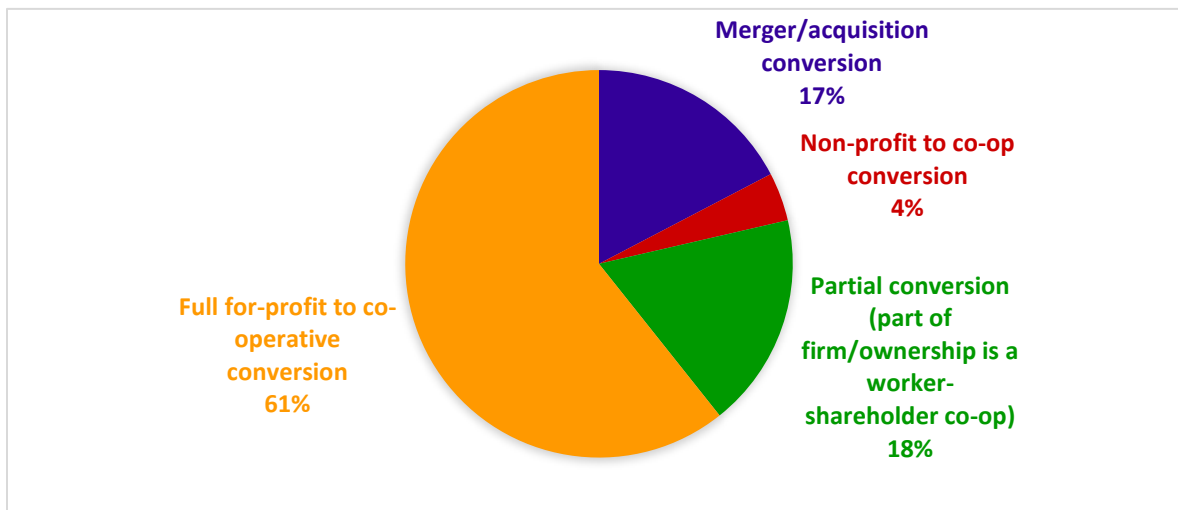


Figure 4: Typology of conversions to co-operatives in Canada
(n = 173, active as of Feb. 2021)



2. Key Issues

A major looming challenge for Canada's 1.2 million small- and medium-sized employer businesses (SMEs) is the potential for large-scale permanent closures due to the growing number of owners nearing retirement but without a formal business succession plan. With 59% of Canada's entrepreneurs over 50 years of age as of late 2018, it was estimated that nearly three-quarters (72%) of small business owners plan to retire in the next decade. While 81% of these retiring owners intended to transfer or sell their businesses, 41% had an informal succession plan, and 51% had no formal plan, according to the Canadian Federation of Independent Business (CFIB).^{§§§}

This lack of overall succession preparation is further complicated when we consider that almost half of these near-retirement owners (48%) plan to sell their business to third parties – almost always a challenging and time-consuming task – “while others prefer to pass their business on to one or more family members, whether through a sale (25%) or [inheritance] transfer (21%).”^{****}

At stake is over \$1.5 trillion in assets and the fate of 850,000 businesses,⁺⁺⁺⁺ affecting over a third Canada's private sector workforce.⁺⁺⁺⁺ This coming SME succession crunch, termed “the silver tsunami” by some, was already being discussed by the early 2010s in Canada.^{§§§§} Economic experts in the US and the EU have also been warning of a similar phenomenon on the horizon or over a decade now.^{*****} This was a significant concern before the added pressure and burden that COVID-19 has placed on this front. In short, jobs and the socio-economic wellbeing of Canada's communities are potentially at risk.

Canadian SME Owners' Succession Plans

Most of Canada's SME owners, as shown in Figure 4, have identified that they have had some form of discussion about selling the business (26%), transferring the business to family (20%), or transferring to employees (15%). These, however, are discussions; very few have identified that they have actually developed a formal succession plan.

While Canada's SME owners are optimistic about how successful their succession plans will be,⁺⁺⁺⁺ this is in stark contrast to how ill-prepared most retirement-aged SME owners are in practice for succession: Only 14%, for instance, have actually developed a formal succession plan, while a mere 11% have attempted to sell their business. Equally alarming, 38% of retirement-aged business owner respondents have not done none of the activities listed in Figure 5.

^{§§§} CFIB, 2018.

^{****} CFIB, 2018.

⁺⁺⁺⁺ CFIB, 2018.

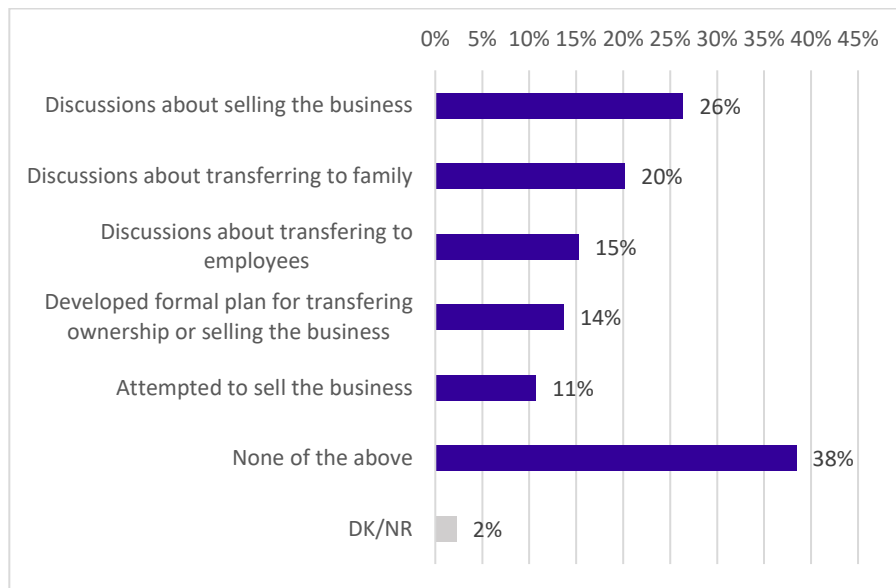
⁺⁺⁺⁺ Parkinson et al., 2015.

^{§§§§} Bruce & Wong, 2012; CBC, 2011; Israelson, 2017.

^{*****} CFIB, 2018; COSME, 2013; European Commission, 2011.

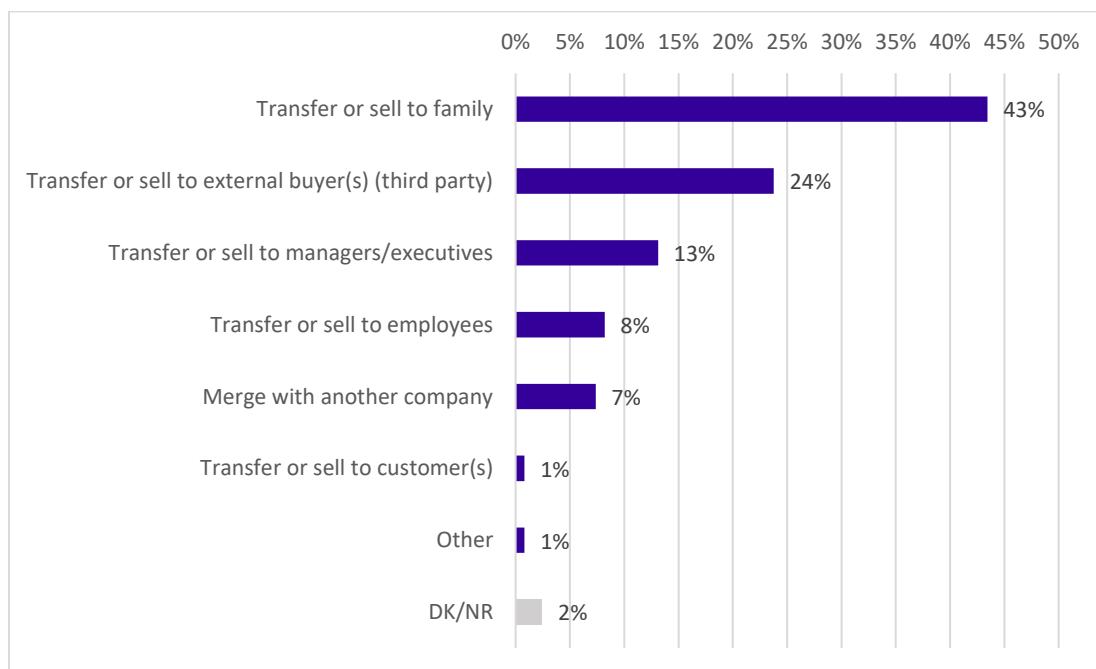
⁺⁺⁺⁺ See: CFIB, 2018; Vieta et al., 2021.

Figure 5: Succession activities in SMEs over the past 5 years (n=305)****



As shown in Figure 6, the intention of retirement-aged SME owners who have planned towards succession. By far most of these respondents are looking to transfer or sell the business to family (43%), however almost a quarter (24%) plan to transfer or sell to an external buyer. Further, some respondents have identified they will transfer or sell to managers or executives (13%) or to employees (8%). There is also some interest in merging with another company (7%), but very little interest in selling to customers (1%),

Figure 6: Current succession plans for those SMEs that have considered transferring ownership or selling the business (n=122)



**** Multiple answers allowed.

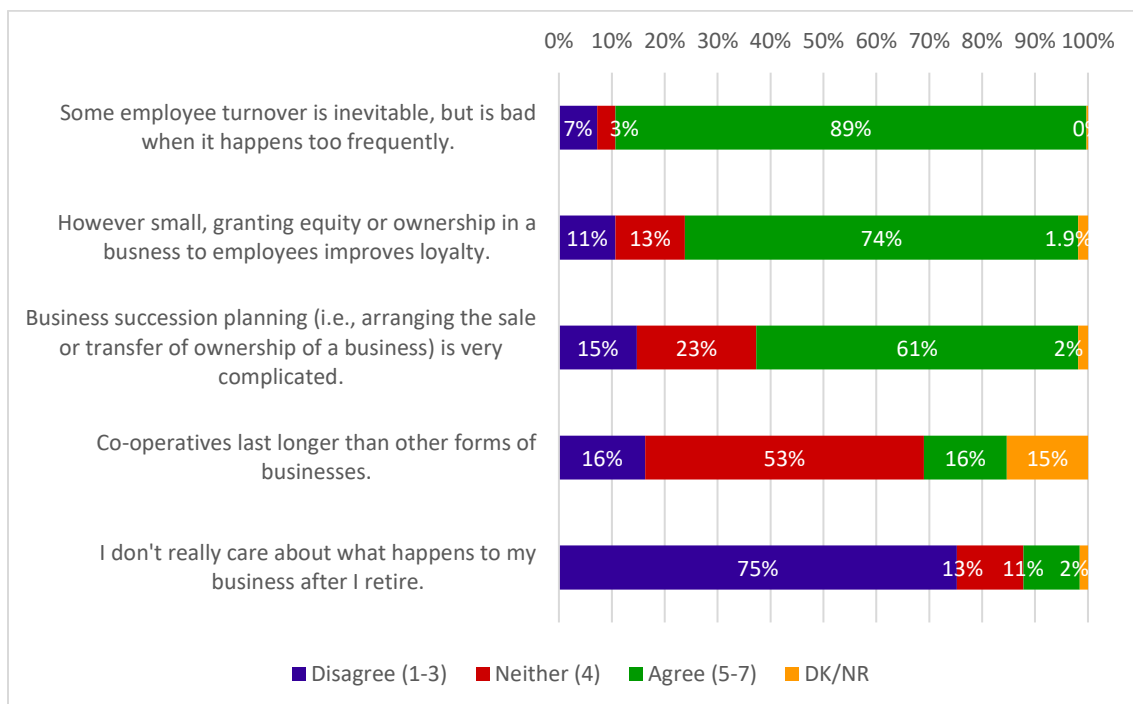
As shown in Figure 6, most SME owners are working under the assumption that they will either sell or transfer their business to family or to an external buyer. *At the same time, the opportunity to sell or transfer to internal figures (i.e., managers or employees) is not being widely taken up by Canada's SME owners, a lost succession opportunity.*

To provide additional context, business succession to family members has a very low success rate. Only 30% of family businesses survive into the second generation and a mere 12% are still viable by the third generation.^{§§§§§} On the other hand, succession plans that include selling the business to employees have a comparatively high success rate, and when they also convert to co-operatives, the survival rate of the subsequent enterprise is comparatively high.^{*****}

Lack of Knowledge of BCCs as an Option by SME Owners

Overwhelmingly, as Figure 7 depicts, 75% of SME owners care about what happens to their business after they retire. They agree that some employee turnover is inevitable but understand this to be bad when it happens too frequently (89%). They also agree that granting some equity or ownership in the business to employees improves loyalty (74%). Additionally, a majority (61%) agree that business succession planning is very complicated.

Figure 7: Attitudes towards broad themes related to succession (n=319)



§§§§§ Family Business Institute, 2016.

***** Ben-Ner, 1988; Vieta et al., 2017

These results show how the long-term viability of co-operatives – an empirically known strength of co-ops – is misunderstood by SME owners.

These results also suggest that there could exist more acceptance of the co-operative model by Canada's SME owners when thinking about succession if they were to know more about co-operatives and their benefits in addressing employee loyalty, ownership stakes, and business continuity.

This demonstrates that there is a clear opportunity for Canada's co-operative movement in partnership with governments, to further educate Canada's SME owners nearing retirement on the co-operative business model.

BCCs as Potential Solutions to Pandemic-Led Business Closures

Awareness of community- and worker-ownership is increasing in response to economic turmoil, including the COVID-19 crisis (Balsillie, 2020; Graham, 2020; Lingane, 2020). During the current COVID-19 crisis, Canada's co-operatives have readily responded to community needs, often sooner and with much more local impact compared with government and corporate responses (Vieta & Duguid, 2020). This crisis is demonstrating that local economies must be self-sustaining rather than reliant on volatile global value chains. Economist Michael Schuman (2020) refers to this as the "comparative resilience" of localities, which will be vital for Canada's rebuilding process post-pandemic.

Co-operatives are ideal ways to secure community resiliency. One sector where BCCs could be deployed during the pandemic is in the healthcare, care home, and home care sectors, for instance, which have been greatly affected by the COVID-19 crisis. Research indicates that non-profit care homes for the elderly (including co-operative care homes) are faring much better than private-sector care homes during the current COVID-19 pandemic, with far fewer resident deaths (CCPA, 2020; Ontario Health Coalition, 2020). Home care workers have also been effectively organized as co-operatives of care workers in Quebec and in the US. More of these non-profit care homes and home care co-operatives could be created through BCCs, ultimately establishing more stable and community-rooted management and ownership models for elderly care and for the care of other vulnerable communities (Armstrong, 2020).

BCCs, therefore, in health care and across Canada's economy, need to be seriously considered as viable responses to closing enterprises and lost jobs as a result of the pandemic.

3. Summary and Next Steps

Co-operatives and Mutuals Canada and the Canadian Worker Co-op Federation (CWCF), with the assistance of the Co-opConvert Project, would be delighted to provide more information if required, such as case studies. The CWCF also has [a proposal](#) to partner with the Government of Canada, *Building Community Resiliency*, and this priority that will be reflected in both upcoming pre-budget submissions.

It should also be noted one of the three priorities of the [People-Centered Economy Group](#) is the enabling of employee and community-based ownership succession and buyouts.

The idea of enabling conversions is already being explored through various government programs, notably:

- The [Conversions to Co-operatives Project](#) itself, as well as a secondary grant to work with the Ontario Co-operative Association that is specifically related to conversions and COVID, are funded by the Social Sciences and Humanities Research Council of Canada (SSHRC).
- The [Legacy Leadership Lab](#) (L3) is a project at the Waterloo Institute for Social Innovation and Resilience that is funded through Canada's Social Innovation and Social Finance Strategy's [Investment Readiness Program](#).
- Business Recovery, Stabilization, and Succession: Using Co-operatives and Social Enterprise to address COVID-19 and the challenge of rapidly retiring business owners in rural communities across Atlantic Canada is a project of the [Canadian Community Economic Development Network](#) that is funded by the [Atlantic Canada Opportunities Agency](#).

In conclusion, encouraging traditional business conversions to co-operatives would offer an option to retirement-aged owners who do not have a succession plan⁺⁺⁺⁺⁺ and help maintain local businesses threatened by financial hardship caused by the COVID-19 pandemic. Enabling conversions would safeguard businesses, jobs and keep communities resilient.

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⁺⁺⁺⁺⁺ Bruce & Wong, 2012; CBC, 2011; Israelson, 2017

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