



August 4, 2017

**To: House Standing Committee on Finance**

**Re: Pre-budget consultations, 2018 budget**

**How Worker Co-operatives Can Contribute to Improving Canada's Productivity, Competitiveness and Resilience**

**Executive Summary**

Employee-owned co-operatives are effective, competitive enterprises. Employee ownership has inherent benefits including improved productivity as people have an ownership stake, and ability to create jobs in economically challenged regions. The USA and Europe have far more employee-owned enterprises than does Canada, per capita. Canada has not yet realized its potential for increasing productivity through developing this form of enterprise.

Our recommendations are as follows.

- 1) **Create a Co-op Business Succession program** and support worker co-op development.
- 2) **Restore pre-2011 Co-op RRSP rules.**
- 3) **Provide distinctive tax treatment for indivisible reserves.**
- 4) Invest in the Canadian Co-operative Investment Fund.
- 5) Implement CWCF's Climate Change Statement.

**What are Worker Co-operatives?**

Worker co-operatives are business enterprises that are owned and democratically controlled by their worker-owners. Their purpose is to provide a work environment that supports professional and human development, and pays competitive wages and benefits.

Worldwide, they operate using the seven [Co-operative Principles](#) recognized by the International Co-operative Alliance.

**Worker Co-ops Are More Productive than Conventional Businesses**

Employee-owned co-operatives enhance productivity. Because the enterprise belongs to the employees, they participate directly in business decisions and they share in the resulting profits. This provides a built-in motivation for member-owners to operate the business effectively and

efficiently, and in larger firms, eliminates the need for one - two levels of supervisory management.

A recent study<sup>1</sup>, by Professor Virginie Pérotin of [Leeds University Business School](#), reviewed two decades' of international data on worker-owned co-operatives, and compared their results to conventional businesses:

"What the data on different models of business shows is that worker-owned businesses often out-perform conventional firms - and the reason is that the people who work in them control the business and want it to continue to provide good and meaningful employment."

"The boost to productivity, for example, stems from the workers having a say in decisions and owning the business, so they work harder and make better informed decisions. Employee-owned businesses provide good quality, stable employment, which is likely to have beneficial effects on local communities."

Various Canadian studies have also shown that co-operatives have a survival rate multiple times better than conventional businesses.<sup>3</sup>

Worker co-operatives are in a unique position to contribute to the daunting challenges of retiring baby boomer business owners and of young adults struggling to leave the "precariat". Employees of small and medium sized enterprises ("SME's") with soon-to-retire owners will be highly motivated to save the business that employs them, and the worker co-operative model gives them a proven alternative. Regarding young adults and their precarious employment, worker co-operatives provide a successful model for collective entrepreneurship.

## **What is CWCF?**

**The Canadian Worker Co-operative Federation (CWCF)**, incorporated in 1992, is a national, bilingual membership organization of and for worker co-operatives, related types of co-operatives, and organizations that support the development of worker co-operatives. CWCF represents over 150 worker co-operatives including through its three large federation members in Quebec.

## **CWCF Proposals, 2018 Federal Budget:**

1. CWCF encourages the Government to partner with CWCF to:
  - a. Facilitate worker buy-outs through Employee-Owned Co-op Business Succession (along with our partner organization, [Co-operatives and Mutuals Canada](#), "CMC").
  - b. Facilitate start-up of employee-owned co-operatives through a support program.
2. CWCF asks that the Government restore the Co-op RRSP rules to those from prior to 2011 federal Budget (Finance Canada)

3. CWCF seeks distinctive tax treatment for indivisible reserves in those worker co-operatives which have them, since purpose is to collective benefit as in a non-profit organization, not private benefit.
4. CWCF requests that the Government demonstrate its support towards co-operative development by making an investment of in the [Canadian Co-operative Investment Fund \(CCIF\)](#) to supplement the \$25 million already raised by the co-op sector – supporting CMC’s request.
5. CWCF asks that the Government implement a [Climate Change Statement](#) similar to the one declared by CWCF in the lead-up to the Paris Conference - a focus on an integrated and cross-departmental regulatory approach to reducing greenhouse gas emissions in Canada.

Only proposals number 1 (a), 2, and 3, above, will be detailed below. Others are either supporting that of another organization (#4), are not primarily a Budget matter (#5), or are not fully developed yet (#1b).

### **1 a) Co-operative Business Succession Program, with CMC**

Canada’s aging population is creating a growing hole our country’s economic fabric, and is particularly impactful with the growing number of retiring business owners.

- While over 500,000 baby boomer owners of SME’s are planning to retire in coming years<sup>ii</sup>, some experts report that less than 1/4 of small business owners<sup>iii</sup> have a formal succession plan, while others suggest that the number could be as low as nine per cent.<sup>iv</sup>
- For many SME owners, the volatile emotional situations behind transitioning their business leads to a delay in seriously undertaking succession planning. The default plan is to search for a buyer for their business in the few years before retirement, however the majority will have great difficulty finding a suitable buyer.<sup>v</sup>
- If these businesses can’t find buyers, a large number of jobs and businesses will be threatened. It is estimated that up to thirty-five percent of the private sector workforce will be impacted by this business succession crisis.<sup>vi</sup> This is especially critical in rural communities where the loss of a local business can mean a loss of essential local services vital to the community’s ongoing sustainability.

As the boomer generation retires, it is critical to develop clearer pathways to successful business succession to maintain these businesses and the employment they create.

### **The Co-operative Solution**

Co-operatives – including worker co-operatives, community ownership, multi-stakeholder co-operatives - have proven to have more than twice the survival rate compared to other forms of ownership.<sup>vii</sup> In addition, businesses owned by co-operatives and employees have much lower employee turnover, build jobs faster and are more resilient during downturns.<sup>viii</sup> Converting an existing business to a co-operative owned by employees and/or community members who use the business, offers current business owners an improved likelihood of selling the business and increasing their financial security in retirement. Co-operative conversions can enable business

ownership for the millennial generation and new immigrants and provide them an opportunity to participate directly in collaborative entrepreneurship and meaningful job creation.

Over a decade ago, the co-operative sector in Canada recognized the opportunity and potential crisis being precipitated by the very large retiring baby boom cohort of SME business owners. Since then, the sector has established expertise to support the conversion of SMEs with retiring owners to co-operatives. The sector has done research, created guides and adapted best practices from organizations in other countries dedicated to this business succession solution.

### **The Offer**

CWCF and CMC have designed a Co-operative Business Succession Program that will address several major areas of public policy impacted by this situation:

1. The security of retirement for older Canadians.
2. The employment of Canadian youth and immigrants.
3. Maintaining of key services, especially in rural communities.

The Co-operative Business Succession Program would be estimated at approximately \$23 million over a 5-year period with project participants contributing half of this amount. The proportion of government support would decrease as the program becomes sustainable.

This investment will achieve three tangible outcomes:

- (1) an estimated 200 successful business successions resulting in the retention of over 1,600 jobs, and secure retirements for former owners - at a cost of approximately \$7,500 per job to government.
- (2) improved awareness and uptake of the co-operative model for business succession, resulting in retiring owners converting to co-operatives where other options aren't available or as suitable.
- (3) enhanced cross-Canada expertise to enable a continuation of co-operative business transfers into the future.

## **2) Co-op RRSP Issue**

In the 2011 Budget, the government changed the criteria for 'prohibited investment' in RRSPs and RRIFs which brought them into conformity with the TFSA regulations. These changes negated the eligibility of many co-operative shares; in particular worker co-operative shares in start-ups and small worker co-operatives whose opportunities for capitalization had been previously strengthened by ensuring their shares were eligible for such placements. The earlier positive provisions providing for this eligibility had been introduced by Paul Martin, Minister of Finance in 1992 and used by many co-operatives in the following years.

The key change which the Liberal Government made at that time was to remove the restriction requiring that the annuitant of the RRSP hold less than 10% of the shares of his/her co-operative for the shares to be an eligible investment. Instead the criteria for eligible investments became – either to own less than 10% of the share of the co-operative or *if owning higher than 10% of the co-operative's shares, that the shares eligible for inclusion in the holder's RRSP be restricted to a maximum of value of \$25,000*. It is the later provision, eliminated by the Conservatives, that we would like to see reinstated. Given inflation since 1992, we would

suggest that the \$25,000 cap be increased, to approximately \$37,500 or another appropriate amount, with indexing every three to four years.

This program was used by many co-operatives across Canada and was particularly beneficial for the early capitalization of co-operatives. Since the 2011 Budget negated this eligibility provision, new and smaller co-operatives have been handicapped in their capacity to finance their own co-operatives using RRSP funds.

It is respectfully requested that this eligibility provision be reinstated in the 2018 Budget. For consistency and equity reasons, we also believe that this fiscal measure should also apply to both RRSP's and TFSAs to broaden the capacity for co-operatives to use these programs.

### **3) Distinctive tax treatment for indivisible reserves in worker co-operatives**

An indivisible reserve in a worker co-op is property owned by the co-operative which cannot be divided among members. It is permanent co-operative capital, and is notionally seen as the value of the common effort of the members. As long as the co-op is operating as a co-op, it can use the indivisible reserve like other retained earnings. This reserve can be controlled by the members, but not accessed by them for distribution to themselves individually. "Indivisible" means that if the co-op ceases to exist as a co-operative (e.g., because it is wound up, or sold), the reserve will go to a co-op development fund or another co-operative organization and not be available to the individual members.

Because indivisible reserves cannot be cashed out by individual members, they provide long-term investment capital that supports longevity of the co-op, across generations. The indivisible reserve is a means by which worker co-op members can demonstrate strong commitment to the worker co-operative movement and its values.

The indivisible reserve can be created either because it is required by legislation (a mandatory indivisible reserve, as in Quebec or Newfoundland – for all co-op types), or because the co-op decides to adopt it (possible in other provinces and under federal legislation).

As a result of a multi-year research project and member consultations, CWCF has decided that it will work on behalf of our membership for distinctive tax treatment for indivisible reserves in worker co-operatives.

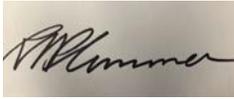
### **Conclusion**

The worker co-operative form of enterprise has unique, proven advantages. In a global study on Co-operatives and Employment completed in 2014, our international counterpart, CICOPA<sup>ix</sup>, concluded that:

No other type of enterprise can claim to provide employment to so many people and, at the same time, show such resilience to crises and economic downturns and provide such high employment stability (in many producers' families, for generations), and be characterised by such a balanced distribution between urban and rural areas.

In Canada, outside of Quebec, worker co-operatives have not had supportive public policy, and therefore, have not been able to meet their full potential. The Government has a historical opportunity to lever the worker co-operative model to build a comparable and resilient system throughout Canada.

Yours sincerely,



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<sup>i</sup> Virginie Pérotin, “What do we really know about worker co-operatives?”, Co-operatives UK, 2016.

<https://www.uk.coop/newsroom/research-reveals-benefits-worker-co-operatives>

<sup>ii</sup> Innovation, Science and Economic Development Canada, Key Small Business Statistics - June 2016

<sup>iii</sup> <http://www.cbc.ca/news/business/10-surprising-stats-about-small-business-in-canada-1.1083238>

<sup>iv</sup> Canadian Federation of Independent Business *Passing on the Business to the Next Generation*, 2012

<sup>v</sup> Canadian Federation of Independent Business *Passing on the Business to the Next Generation*, 2012

<sup>vi</sup> The Globe and Mail *The Boomer Shift: Boom Bust and Economic Echo* Jan 5, 2017

<sup>vii</sup> Quebec, Department of Economic Development, Innovation and Export Trade, *Taux de survie des coopératives au Québec*, 2008

Richard Stringham and Celia Lee, *Co-op Survival Rates in Alberta*, BC-Alberta Social Economy Research Alliance, 2011.

Carol Murray, British Columbia Co-operative Association, *Co-op Survival Rates in British Columbia*, 2011

<sup>viii</sup> *Sharing Success : The Nuttal Review of Employee Ownership*, 2012

<sup>ix</sup> *Co-operatives and Employment: A Global Report*, by Bruno Roelants, Eum Hyungsik and Elisa Terrasi, 2014:

<http://www.cicopa.coop/Cooperatives-and-Employment-a.html>