Social economy and green transformation in the European Union

Edited by: **Sebastjan Pikl**

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David P. Ellerman and Tej Gonza

Classical Liberalism, Social Responsibility, and Employee Ownership

1 Abstract

Classical liberalism has always emphasised the agency and empowerment of individuals to help themselves as opposed to government organisations 'doing good things for people.' The usual imagery is an individual acting as a 'sovereign' in the marketplace. But there is a tradition of democratic classical liberals, represented by Alexis de Tocqueville, John Stuart Mill, John Dewey, and James Buchanan, who have also emphasised the agency and empowerment of individuals in organisations such as the workplace. In an insider-owned organisation like a family firm or farm, there is a natural self-regarding incentive for social responsibility since people are inclined not to 'foul their own nest.' But much of modern industry is characterised by absentee ownership where the decision-makers do not face the adverse consequences of their decisions. Within the tradition of democratic classical liberalism, there is, however, the recurrent theme of employee ownership which restores the natural incentives for social responsibility. After outlining these arguments in the first part of the paper, we turn to the rather recent social invention in America of the Employee Stock Ownership Plan or ESOP that has proven an effective way to increase employee ownership (e.g. 10% of the private US workforce work in ESOPs). There is now a generic model of the ESOP that can be implemented in Europe or other private property market economies, which presents a complementary tool for succession or ownership change.

2 Theory: The philosophy of democratic classical liberalism

Doing good

Political philosophy deals with many difficult questions, and one of the most relevant is about how governments might *"do good"* for the citizens in a given society. In general, we may recognise two different political philosophies for *"doing good."*

1. (progressivist) the purpose of obtaining political power is to do good things for people (particularly those in most need) which usually takes the form of social programmes that are universal and available as a matter of rights (e.g. social security, health care, education including higher education, basic income, and so forth); and

2. (classical liberal) the purpose of obtaining political power is changing the conditions of empowerment so that people can do good things for themselves (which does not preclude short-term targeted government social safety-net programmes).[1]

Classical liberalism expresses a scepticism about universal governmental programmes and organisations being able to *"do good"* for people. The reasons for the general ineffectiveness of the government to directly do good for people are not unique to government; the reasons apply as well to other external organisations that are also tasked to *"do good"* such as philanthropic, development aid, or other helping organizations in general.[2] As John Dewey (1859–1952) put it:

> The best kind of help to others, whenever possible, is indirect, and consists in such modifications of the conditions of life, of the general level of subsistence, as enables them independently to help themselves. (Dewey and Tufts 1908, p. 390)

The aim of a helping organisation should not be to *"do good"* in any direct sense. Instead, the central role of government should be to set up and maintain the conditions for people to be empowered and enabled to do good for themselves. This approach could range from providing transparent information to citizens about the candidates in a democratic election race, to establishing and enforcing the private property prerequisites for the functioning of a market economy.

Much of the classical liberal literature uses the model of the individual as a sovereign actor in the marketplace, e.g. the shopkeeper, farmer, or worker. But the goal of increasing people's agency to do good for themselves is not restricted to the marketplace. The goal should be to increase people's autonomy, organisational efficacy, and effective social agency so they can do good for themselves—individually in the marketplace or, more likely, jointly in their own organisations. That is how the virtues of individual self-regarding activity in the marketplace (the usual setting for classical liberal imagery) generalise to the virtues of collective activity by people in their own organisations.

The democratic classical liberal normative framework that emphasises this autonomy and self-efficacy is perhaps best stated by James M. Buchanan (1919–2013):

> The justificatory foundation for a liberal social order lies, in my understanding, in the normative premise that individuals are the ultimate sovereigns in matters of social organization, that individuals are the beings who are entitled to choose the organizational-institutional structures under which they will live. In accordance with this premise, the legitimacy of social-organizational structures is to be judged against the voluntary agreement of those who are to live or are living under the arrangements that are judged. The central premise of individuals as sovereigns does allow for delegation of decision-making authority to agents, so long as it remains understood that individuals remain as principals. The premise denies legitimacy to all social-organizational arrangements that negate the role of individuals as either sovereigns or as principals. (Buchanan 1999, p. 288)

It should be particularly noted that Buchanan goes beyond the common image of the sovereign individual acting in the marketplace to the individual acting in an organisation which allows *"for delegation of decision-making authority."* Then the legitimacy of the *"social-organizational arrangements"* depends on the individuals being principals in their own organisations, meaning that they hold in their hands the power to give and take the power from their representatives.

In this paper, we will develop a brief intellectual history of this democratic classical liberalism through Tocqueville, Mill, and Dewey, who, as the reader will see, all promoted democratic organisation of a workplace, and, finally, we will show that classical liberalism has a functional counterpart in the special employee-ownership programme in the USA, which could be extended and generalised into other market-based private property economies.

The implications for today's social-organisational structures

We have taken James M. Buchanan's description of the normative basis for classical liberalism as the foundational framework, which we are going to apply to in thinking and understanding about the classical liberal approach to "doing good". Buchanan's mature thought moved beyond the conventional liberal idea, expressed in his *Calculus of Consent* (Buchanan and Tullock 1962), about the consent being a sine qua non for a legitimate human conduct. He made a stronger requirement that people should always be sovereigns or principals who delegate decision-making authority in an organisational setting. Buchanan's strictures imply democratic self-governance in contrast to the contemporary currents of libertarianism and Austrian thought that accept the consent of the governed as conferring legitimacy on non-democratic governance, e.g. startup or charter cities (Freiman 2013).

In many modern discussions of associative and deliberative democracy (e.g. in the tradition of Tocqueville), there is a curious *"dog that didn't bark"*. The emphasis is rightly on the associative activities of citizens who come together for discussion, dialogue, deliberation and responsible action to address problems that they cannot resolve at the level of the individual or the family. People create many associations for collective action: church groups, charities, issue-oriented non-profits, unions, social clubs, hobby groups, political parties and *ad hoc* special-purpose groups. People might participate after-hours in these various Tocquevillean associations to try to accomplish together what they cannot accomplish individually.

But that list of non-governmental associations leaves out the one organisation that dominates most people's lives outside the family, namely, the workplace.[3] Of course, some people work for themselves or in small family firms, so those workplaces are only a marginal extension of family life. But most people work in larger organisations requiring the concerted associated activities of many non-family members. These work organisations provide the primary sites, outside the family, where people acquire mental habits and social skills and where they engage in effective collective activities.

Almost all workplaces today are organised on the basis of the employment contract. In common usage, to have an income-producing job is to be *"employed."* Indeed, in his iconic paper *The Nature of the Firm*, Ronald Coase (1910-2013), a

Nobel prize-winning economist and one of the pioneers of the theory of the firm, identifies this relationship as the *"legal relationship no*rmally called that of 'master and servant' or 'employer and employee'" (1937, p. 403).[4]

With the employment contract, the employees are not Buchanan's principals. They are not the owners of the things they produce; they are simply hired hands, paid in a similar way as the employer pays for the electricity or other 'inputs' for production. Despite the fact that they enter the employment relationship on a voluntary basis, this does not by itself guarantee the legitimacy of the relationship. To argue for this would be analogous to the libertarian argument in favour of voluntarily entering the autocratic state and saying that the consent itself legitimates the autocracy of the government.

When evaluating according to the principles of classical liberalism, it becomes clear that workers in a conventional business enterprise do not delegate decision-making authority to the employer. The employer is not the representative or delegate of the employees; the employer does not manage the organisation in the name of those who are managed. The employees are not directly or indirectly part of the decision-making group; the employees have alienated and transferred to the employer the legal discretionary decision-making rights over their activities within the scope of the employment contract.

The form of workplace organisation that would satisfy the strictures of Buchanan's Principal's Principle is one where all the people working in a firm are the principals, members or co-owners in the workplace and have a democratic governing right.

Brief intellectual history of the classical liberal alternative:
Tocqueville, Mill, and Dewey

To see the context and corroboration for Buchanan's normative framework, we might consider the work of three earlier liberal philosophers, Alexis de Tocqueville (1805–1859), John Stuart Mill (1806–1873) and John Dewey.

Today, the welfare rights movement would be seen as a progressivist movement aimed at increasing public welfare programmes and getting better access to existing programmes—not on the poor using their agency to remove their need to access such programmes. Tocqueville, however, thought along classical liberal and civic republican lines. For instance, government programmes of land reform might make individual parcels of land available to landless agricultural workers or larger parcels available to agricultural cooperatives. But, even in his time, the economy was becoming more industrial than agricultural. In our opinion, the crux of the problem to be solved is this:

> To find a means of giving the worker the small farmer's spirit and habits of property ownership. (Tocqueville 1837)

Thus, government programmes might foster individuals and families starting their own small businesses, groups of individuals starting cooperative businesses, or the conversion of existing firms with the *"aristocratic form"* (*Ibid.)* into employee-owned companies. Such government programmes would assist existing wage workers to acquire shares in their company to eventually become more *"owner"* than *"employee."* In contrast, progressivist government programmes would focus more on labour unions and industrial legislation to better protect and care for wage workers.

Tocqueville explicitly notes the need for large capital to exploit returns to scale but he infers that this requires "large" owners.

> Until now, experience has shown that in order to engage in most commercial enterprises with any hope of success, large capital concentrated in a small number of hands is necessary. Thus, we find a few individuals who possess great wealth and who put to work on their behalf a multitude of workers who possess nothing themselves. Such is the spectacle that French industry presents nowadays. It is exactly what happened here in the Middle Ages, and what we see still happening to agricultural industry over much of Europe. (*Ibid.*)

Today, with the development of the public equity markets in the late 19th and early 20th centuries, we see that "large capital concentrated in a small number of hands" is not needed to exploit returns to scale. The largest publicly traded companies will have the largest number of owners. But the small passive owners in public security markets are not the industrial analogues of the small farmers actively working their own land who are promoted in classical liberalism and civic republicanism. Day-trading on the stock market is hardly an anti-poverty programme for the poor.

As already noted, the "crux of the problem" is "To find a means of giving the worker the small farmer's spirit and habits of property ownership." But Tocqueville ends up focusing, in the latter part of his unfinished memoir, on individual savings accounts.

Tocqueville recognises that the "most efficacious" means of improving the situation of the industrial worker is for them to have:

> an interest in the factory. This would produce effects in the industrial class similar to the division of landed property among the agricultural class. (*Ibid.*)

But he considers that the only way for workers to acquire such an interest in an existing factory is for the:

> industry's capitalist entrepreneurs…to give their workers a proportionate amount of the profits or to contribute to the company small sums which could be shared with the workers. (*Ibid.*)

While Tocqueville thinks that the employers should make such gifts in their own interest, he finds little inclination for them to do so. Despite his previous argument about large capital requiring large owners, Tocqueville also recognises the possibility of workers' industrial associations. But he notes their largely unsuccessful experience in his time. He sees that as an option for the future but as not being ripe for his own time.

> Nevertheless, I am led to believe that a time is approaching when a large number of industries might be run in this manner. As our workers gain broader knowledge and as the art of joining together for honest and peaceful goals makes progress among us, when politics does not meddle in industrial associations and when government, reassured about their goals, does not refuse them its benevolence and its support, we will see them multiply and prosper. In democratic ages like ours, I think that associations of all sorts must gradually come to take the place of the commanding action of a few powerful individuals.
>
> It thus seems to me that the idea of workers' industrial associations is bound to be a fertile one, but I do not think it is ripe. (*Ibid.*)

In today's world, Tocqueville's scepticism and suggestion about savings accounts are unnecessary. There are many possible ways of organising labour into worker-associations, and many of them have proven to be very successful through the decades (see below). Before going to the alternative models of economic organisation, let us see what other classical liberals had to say about the normative principles of "doing good".

John Stuart Mill argued that social institutions should be judged in large part by the degree to which they "promote the general mental advancement of the community, including under that phrase advancement in intellect, in virtue, and in practical activity and efficiency…" (Mill 1972, Chapter 6). Mill saw government by discussion as an "agency of national education" and mentioned "the practice of the dicastery and the ecclesia" in ancient Athens as institutions that developed the active political capabilities of the citizens.

In his *Principles of Political Economy*, Mill considered how the form of work would affect those capabilities and how the workplace association could become a school for the civic virtues if it progressed beyond the employment relation.

> But if public spirit, generous sentiments, or true justice and equality are desired, association, not isolation, of interests, is the school in which these excellences are nurtured. The aim of improvement should be not solely to place human beings in a condition in which they will be able to do without one another, but to enable them to work with or for one another in relations not involving dependence. (Mill 1899, Book IV, Chapter VII)

Previously those who lived by labour and were not individually self-employed would have to work *"for a master"*, i.e., would not be a principal in their work activity.

> But the civilizing and improving influences of association, …, may be obtained without dividing the producers into two parties with hostile interests and feelings, the many who do the work being mere servants under the command of the one who supplies the funds, and having no interest of their own in the enterprise except to earn their wages with as little labor as possible. (Mill 1899, Book IV, Chapter VII)

One halfway house in this direction would be various forms of association between capital and labour.

> The form of association, however, which if mankind continue to improve, must be expected in the end to predominate, is not that which can exist between a capitalist as chief, and workpeople without a voice in the management, but the association of the labourers themselves on terms of equality, collectively owning the capital with which they carry on their operations, and working under managers elected and removable by themselves. (Mill 1899, Book IV, Chapter VII)

Under this form of cooperation, Mill sees an increase in the productivity of work since the workers then have the enterprise as "their principle and their interest."

> It is scarcely possible to rate too highly this material benefit, which yet is as nothing compared with the moral revolution in society that would accompany it: the healing of the standing feud between capital and labour; the transformation of human life, from a conflict of classes struggling for opposite interests, to a friendly rivalry in the pursuit of a good common to all; the elevation of the dignity of labour; a new sense of security and independence in the labouring class; and the conversion of each human being's daily occupation into a school of the social sympathies and the practical intelligence. (Mill 1899, Book IV, Chapter VII)

What Mill sees as happening in the democratic workplace echoes what he earlier found in Tocqueville's description of the educational effect of the New England township. In Tocqueville's words:

> Nevertheless, local assemblies of citizens constitute the strength of free nations. Town-meetings are to liberty what primary schools are to science; they bring it within the people's reach, they teach men how to use and how to enjoy it. A nation may establish a system of free government, but without the spirit of municipal institutions it cannot have the spirit of liberty. (Tocqueville 1961, Chap. V, p. 55)

As Mill expanded on the point:

> In this system of municipal self-government, coeval with the first settlement of the American colonies…our author (Tocqueville) beholds the principal instrument of that political education of the people, which alone enables a popular government to maintain itself, or renders it desirable that it should. It is a fundamental principle in his political philosophy, as it has long been in ours, that only by the habit of superintending their local interests can that diffusion of intelligence and mental activity, as applied to their joint concerns, take place among the mass of the people, which can qualify them to superintend with steadiness or consistency the proceedings of their government, or to exercise any power in national affairs except by fits, and as tools in the hands of others. (Mill 1961 (1835), p. xvii)

Thus, Mill agrees with Tocqueville that organisational self-governance develops the democratic capabilities of the people. A century later, John Dewey emphasised the formative implications of people's daily activity in an industrial society.

> For illustration, I do not need to do more than point to the moral, emotional and intellectual effect upon both employers and laborers of the existing industrial system. ... I suppose that every one who reflects upon the subject admits that it is impossible that the ways in which activities are carried on for the greater part of the waking hours of the day, and the way in which the share of individuals are involved in the management of affairs in such a matter as gaining a livelihood and attaining material and social security, can not but be a highly important factor in shaping personal dispositions; in short, forming character and intelligence. (Dewey in: Ratner 1939, 716-7)

Do these primary sites for outside-the-family socialisation and development foster the virtues of associative democracy? While "democratic social organization makes provision for this direct participation in control: in the economic region, control remains external and autocratic." (Dewey 1916, 260)

> Control of industry is from the top downwards, not from the bottom upwards. The greater number of persons engaged in shops and factories are "subordinates." They are used to receiving orders from their superiors and acting as passive organs of transmission and execution. They have no active part in making plans or forming policies—the function comparable to the legislative in government—nor in adjudicating disputes which arise. In short their mental habits are unfit for accepting the intellectual responsibilities involved in political self-government. (Dewey and Tufts 1932, 393-2)

Here, Dewey is talking about the employees, who are, in Buchanan terms, not sovereigns within the scope of the employment contract, but rather *"passive organs of transmission and execution"*, subjects of authority, who have no say in putting this authority in place and having a capability of removing it from there. From his earliest writings in 1888 to his mature years, Dewey's liberalism saw democracy as a norm applicable to all spheres of human activity, not just to the political sphere.

> (Democracy) is but a name for the fact that human nature is developed only when its elements take part in directing things which are common, things for the sake of which man and women form groups—families, industrial companies, governments, churches, scientific associations and so on. The principle holds as much of one form of association, say in industry and commerce, as it does in government. (Dewey 1948, 209)

It should not be too much of a surprise that the normative framework of James M. Buchanan's classical liberalism has the same implications for Tocqueville's *"science of associations"* in this regard as Mill and Dewey[5] even though the full implications were not explicitly drawn.

Contemporary corporate ownership

There have been a few social commentators who have pointed out the institutionalised irresponsibility of the *absentee-owned* joint stock corporation. The first to theorise about *absentee ownership* and to actually coin the term was an eccentric economist Thorstein Veblen, who was, in his book Absentee Ownership (1923), one of the first to explain and problematise the economic returns on merely owing capital. His analysis was quickly supplemented by the classic from A. Berle and G. Means, who in their 1932 book *The Modern Corporation and Private Property* argued that in the modern economy ownership have been separated from control. Some years later in a 1961 book aptly entitled *The Responsible Company*, George Goyder quoted a striking passage from Lord Eustace Percy's *Riddell Lectures* in 1944:

> Here is the most urgent challenge to political invention ever offered to the jurist and the statesman. The human association which in fact produces and distributes wealth, the association of workmen, managers, technicians and directors, is not an association recognised by the law. The association which the law does recognise—the association of shareholders, creditors and directors—is incapable of production and is not expected by the law to perform these functions. We have to give law to the real association, and to withdraw meaningless privilege from the imaginary one. (Percy 1944, 38; quoted in Goyder 1961, 57)

As argued at the outset, *"doing good"* in the classical liberal sense means creating the capacity enabling institutions. Government policy should promote social structures so that people can take associative collective actions to address their own problems and the problems of their communities. People are involved in effective collective action all day long in their work associations. But today the structure of most companies of any size—namely, the employment relation with the employer being the absentee owners on the stock market—institutionalises irresponsibility by disconnecting the far-flung shareholders from the social and environmental impact of their "corporate governance." Or viewed the other way around, that employment structure prevents the local managers and staff in widely held companies from being the principals to use the main outside-the-family organisational involvement to address local problems.

3 Practice: employee ownership and social responsibility

Family firms and social responsibility

Family-owned small and medium-sized enterprises (SMEs), which are arbitrarily defined as companies of up to 250 employees, but could be much larger, do not have serious problems of corporate social responsibility for a very good reason—everyone has a natural incentive not to foul their *“own nest.”* The family typically lives in the community containing the enterprise and has a tradition of respect for creating jobs in and otherwise supporting the local community.

However, the family business is not sustainable on its own. It needs an ownership and control succession plan. Founders pass on and the children may have little interest in running the family business, so these companies are often sold to a competitor or to a larger industrial or financial conglomerate. In any case, the firm then becomes absentee-owned, and the new owners have a very different set of incentives than commitment to the local community. The enterprise may continue to operate for a time while the customers are switched to other facilities, while the value of the assets is *“milked out”* by not undertaking replacement investments, and with less attention to costly pollution controls. Eventually the enterprise is closed, citing high labour costs and increased competition from cheaper foreign or domestic labour.

SMEs in Europe currently employ around 65% of the total workforce (European Commission 2016), and are a major contributor to local jobs, to sustaining local communities and municipalities, and often dedicate some of their funds to socially responsible programmes (Werther Jr & Chandler, 2010). It is in the interest of European citizens to keep these companies locally owned, and locally governed. This may, however, soon become a serious issue; a baby-boom generation of entrepreneurs is now reaching a retirement age, which may lead to a substantial withdrawal of family businesses from operation if there is no systemic succession plan in place.[6] We can only imagine the social consequences of the mass retirement of SME founders, if there is no alternative in place.

Fortunately, there is a way out. This way out builds on the values of classical liberalism as exposed above. There is a time-tested alternative—replace family-ownership by employee-ownership—that has proven successful in some 7000 enterprises in the United States (covering 10% of the private workforce), and this alternative can readily be adapted to other private property market economies. But objections arise immediately; the employees do not have the money to buy out the family owners and they are well-advised not to risk their own savings and mortgage their own homes on such a venture. These objections are well-taken. The 7000 firms with partial or whole employee ownership did not arise from employees risking their own private savings or assets. They arose from a new legal mechanism, the Employee Stock Ownership Plan (ESOP), which allows a partial or 100% employee *"leveraged buyout,"* while avoiding the old problem of employees risking their own savings and assets.

The ESOP mechanism directly addresses the old problem of family ownership giving way to absentee ownership and the resulting downward spiral in corporate social responsibility to the local community.[7] The ESOP mechanism is, however, not limited to solving family succession problems; it can also be used to partly or wholly spinoff corporate subsidiaries which are no longer part of the core business strategy. In any case, some significant employee ownership brought about by the ESOP mechanism changes the mix of incentives for corporate management and establishes a more natural alignment between corporate and social responsibilities.

It is our belief that the ESOP is an important "social invention" compatible with classical liberalism that is too little known in Europe and other market economies. The question is, how to implement ESOP, which is legally a fairly complex institution, into European economies?

What is an ESOP?

It is firstly important to say what an ESOP is not. The acronym *"ESOP"* is often used to denote any form of employee ownership no matter how it was established. In particular, an ESOP is quite different from the relatively common Employee Share Purchase Plans (ESPPs) where employees set aside a portion of their wages and salaries on an individual basis to purchase shares at a discounted price. Such plans rarely amount to a significant percentage of corporate ownership. The slow increase in employee shares through an ESPP seems to have little effect on either employee or management perceptions or incentives. In contrast, the ESOP leveraged buyout involves a loan to buy a significant amount of ownership at one time, although the employees only gain control over the shares as the loan is paid off over a period of years.

The key to the ESOP leveraged transaction is an Employee Stock Ownership Trust (ESOT) separate from the company with the employees of the company as the beneficiaries of the trust; indeed, it is a special type of private pension trust. The ESOT then approaches a bank or other financial institution to take out a loan to buy shares from the exiting owner (e.g. the family or corporate owner) or to buy newly issued shares.

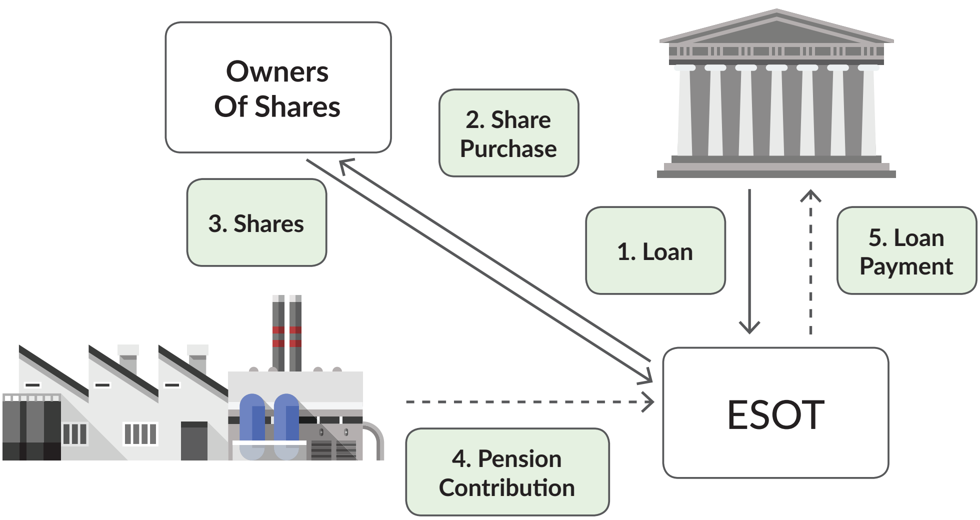

Figure 1: The ESOP Mechanism for an Employee Leveraged Purchase of Shares

The purchased shares are initially held in a special 'suspense account' in the trust and they will be forfeited if the loan payments are not made. But banks and financial institutions do not want to hold shares in a privately held company so the real security is that the company commits to make the loan payments (as in an ordinary loan) except that the 'loan payments' leave the company as pension contributions to the ESOT, which are then passed through to the lender. This creates a significant tax advantage for the company since the whole pension contribution is deducted from taxable income as deferred labour compensation—whereas ordinarily only the interest portion of the loan payment is deductible. Then, shares, equal in value to the loan payment, are distributed from the suspense account to the individual employee share accounts in the trust in proportion to their compensation.

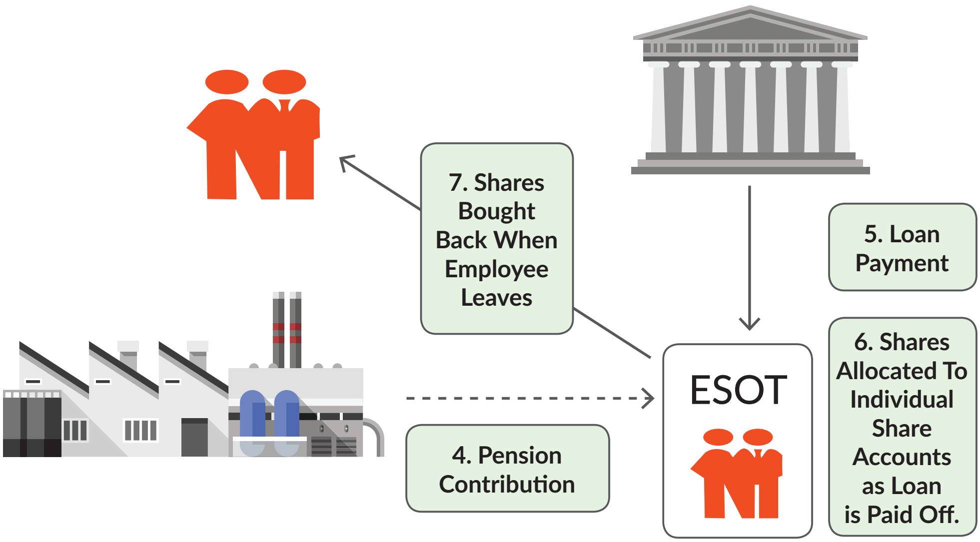

Figure 2: Shares allocated to individual accounts and repurchased on exit

When the employees retire or otherwise leave the company, the ESOT repurchases their shares over a period of time, and the repurchased shares are reallocated to the individual accounts of the employees still with the company. Unless the company is a publicly traded company, the company is obliged to repurchases the shares of the exiting employees since there is no external public market. That repurchase liability of the company can be financed out of current earnings transferred to the ESOP as a pension contribution or by another loan paid off in the same manner. In that manner, the employee ownership is stabilised over time.[8]

Legislative History of ESOPs

In an ordinary American private pension fund associated with a company, the pension contributions would be used to buy other shares or securities with at most 10% allowed to be invested in employer securities. Hence the legislative route to create the ESOP mechanism was to 'carve out' the ESOP as a special type of pension trust that was different in two respects: 1) it could be invested 100% in employer shares, and 2) it could be 'leveraged,' i.e., could take out a loan, guaranteed by the company, to buy shares for the trust.

It is particularly interesting that the ESOP legislation and amendments over the years has been supported both from the Right ("turning workers into capitalists") and from the Left (*“moving towards the old idea of workplace democracy and worker ownership”*). Now, around 10% of the private workforce in the USA (around 14 million workers) work in the 7000 companies with ESOPs, while, in comparison, only about 7% of the private workforce is unionised. The major accounting and finance firms have departments devoted to ESOPs in addition to many smaller ‘boutique’ firms specialising in ESOP transactions.

4 The Next Steps

It is now possible to set up a generic Coop-ESOP in any European or other democratic country (Ellerman et al. 2019) that has worker cooperative legislation and normal corporate laws. However, special legislation would be needed to provide a standardised tax-favoured model. Unfortunately, the label “ESOP” is used very loosely in Europe to mean most any type of employee ownership scheme from marginal and partial Employee-Share Purchase Plans (ESPPs) to Employee Stock Options Plans for just the managers and a few key employees. The Coop-ESOP model is an “ESOP” in the strict sense that: (1) all employees (beyond a probationary period) must by law be included and (2) the buyout of the old ownership is based on contributions from the company to the ESOP, not on the personal assets of the employees. Moreover, by using a worker cooperative as the ESOP mechanism, the governance of the employee portion of the ownership is democratic (one person, one vote), a rare feature of US ESOPs.

One of the forms of democratic social enterprise is the worker cooperative. But worker co-ops have always had the **‘problem’** of being all or nothing without any transition mechanism from a conventional firm. ESOPs address that problem which is one of the reasons why in the whole of the USA, there are about 300 worker cooperatives and 7000 ESOPs. The Co-op-ESOP model addresses that problem of both the transition and of democratic governance of the worker cooperative that holds some percentage of the ownership of the otherwise conventional company. Thus, democratic and locally oriented green values can begin to inform company policy long before the transition to 100% cooperative ownership is complete. When the percentage of cooperative ownership reaches 100%, then the company can be folded into the worker cooperative which would then fully take over the business operations as a Mondragon-style worker cooperative.

The Mondragon cooperative complex gives a good example of how worker co-ops also sponsor other social enterprises as a part of the complex:

- the Mondragon University (including an internal manufacturing cooperative to introduce students to co-op principles) which grew out of the original polytechnical high school and college;
- the Mondragon Bank that serves both the cooperatives and the general population in the Basque region and surrounding provinces in Spain;
- the associated social insurance and medical cooperatives since the cooperative members are not considered as "employees" in the Spanish social insurance system;
- the hybrid worker/consumer supermarkets that have spread out of the Basque region into other parts of Spain;
- the associated technical research centres to do the preliminary 'spadework' research into new technologies to see what marketable products might be developed; and
- small business development and support centres.

The whole Mondragon system developed using only the 100%-or-0% co-op model without any ESOP-like transition mechanism. Hence, the development of the Co-op-ESOP transition mechanism has the potential for a much larger uptake with corresponding multiplier effects. The question that is very important is how can European institutions help to realise the potential behind the ESOP model in Europe?

Awareness campaign and research

While the EC is already discussing the negative consequences of the 'silver tsunami' or the wave of the retirement of business owners in the EU, not many practical and socially conscious solutions have been proposed to address this problem. Employee ownership in the form of the ESOP model is one potential solution. A general campaign informing European business owners about the succession planning and the employee ownership as a way out would be an important strategy on the part of the EC. Financial support should be given to the decentralised institutions and initiatives, which are equipped with in-depth knowledge and technical know-how, so that they individualise the campaigns and adapt them within the individual Member State's cultural context. In addition to this, EC should finance research that legitimises the employee-ownership agenda in Europe. In the USA, there is a 40-year-old research tradition that focuses on studying the effects of ESOPs on business indicators, job stability, worker satisfaction and wealth inequality. Most of the literature agrees on the positive effects of employee ownership. This is a first step to a sympathetic public and political opinion towards economic democracy.

EU directive on adopting appropriate legislation

The ESOP model in the USA was a success because it was institutionalised through appropriate legislation. ERISA is a retirement act that defines a special legal vehicle called ESOT (*Employee Stock Ownership Trust*), which receives tax benefits on different levels. ESOT may be a 100% owner of the contributing company, while the company may transfer money to the ESOT without it being taxed, if the money is used to buy the company stock in the name of the employees, who are members of the ESOT. All employees must be included in the ESOT if it is to be recognised for the tax breaks, and the buyout must be financed with the company's revenues and not the savings of the individual employees. Owners may postpone the tax on capital gain by selling their stock to ESOT if they invest the received capital in the American economy. Finally, banks, who are financing the ESOP buyout, receive tax breaks on the interests that charge to the receiving end of the loan. Each individual EU Member State should adopt laws adapted to the existing state's legislation to recognise a special ownership vehicle, which would function as the employee ownership and employee governance participation entity.

Thinking about the supporting industry

There would not be 7000 ESOPs in the USA if there were not supporting consultant businesses with the knowledge about employee ownership, the ESOP model, and the general business expertise. The consulting and engineering part is crucial, because you need people with specialised knowledge to restructure the companies correctly, otherwise either nothing gets done or it gets done in an incorrect way. Both are a problem. In addition to this, there are educational institutions in the USA that teach management and employees about the ownership culture. The management of a democratic enterprise has to internalise new and progressive values of leadership, which does not only allow employee participation but also encourages it. Employees, on the other hand, should be educated on what it means to be a business owner, and to have a basic understanding of the financial statements, annual reports and other business-related material. The EU should encourage and finance the creation of the consulting and educating institutions to help newly democratised enterprises up to the point where the business picks up, then one can leave it to the market competition.

Thinking about the supporting financial institutions

There would be many more ESOPs in the USA if there were more capital available for the restructuring of the companies in the direction of employee ownership. While ESOPs in the USA are a success story, there is much potential unleashed. We should learn from the American experience and build national financial institutions that could either (i) complement the loans with business banks, which are to be used for the employee buyouts, or (ii) provide collateral for the loans with business banks.

5 Concluding Remarks

Our point is simple. If all this can happen in forty-odd years in the most labour-hostile industrialised country, there is no reason why it can't happen on even a larger scale in the industrialised democracies of the European Union with appropriate legislation fully in accord with democratic classical liberal principles (e.g. Tocqueville, Mill, Dewey, and Buchanan).

A systematic programme to promote employee ownership with cooperative values and an ESOP-like transition mechanism would have a concomitant impact on:

- improving the income and wealth distribution in a direct pre-distributive manner[9] as opposed to after-the-fact redistributive policies[10];
- improving productivity normally promoted by trying to get employees to "act like owners" whereas in an ESOP, they are owners[11];
- counter-cyclical income stabilisation since firms with significant employee ownership would in the face of a downturn or recession tend to foster the 'belt-tightening' of all the members rather than laying off some of the members;
- community stabilisation by avoiding absentee ownership and eventual closures in the business succession of local firms—which requires a prior public education programme to inform SME owners of the employee ownership opportunity; and
- overall improvement in corporate social responsibility by aligning the incentives of the owners and the local social/green concerns.

FOOTNOTES

[1] *This juxtaposition of two philosophies is not meant to be a binary dichotomy. Depending on the design, many progressive programmes can be seen as empowering rather than displacing decentralised agency and initiatives.*

[2] *The phrase "external organisation" does not apply to associations where people join together to apply their collective efficacy to address some problems of their own; it applies to organisations, particularly those with paid staff, tasked to help others. The aim of a helping agency should be to do itself out of a job—which is rather difficult for a professionally staffed organisation of any type. See Ellerman (2005) for a development of this theme along with a philosophical analysis of why it is so difficult for such external helping organisations to actually "help people help themselves."*

[3] *Cornuelle (1991) is a welcome exception to the rule.*

[4] *The older name of the relation was the master-servant relation but, aside from a few law books on agency law that use the master-servant language as technical terms (e.g. Batt 1967), that usage was slowly replaced in the late 19th century and early 20th century with the Newspeak terms of "employer" and "employee."*

[5] *Note how the implications of Buchanan's Principal's Principle gives essentially the same results as Dewey's democratic "principle (that) holds as much of one form of association, say in industry and commerce, as it does in government."*

[6] *See Duh 2012; Malinen 2001; Močnik et al. 2019; Pendleton et al., n. d..*

[7] *See Brill 2017 and http://www.nceo.org/articles/esop-business-continuity and Frisch 2002.*

[8] *For more information, see the literature of the National Center for Employee Ownership such as: Gordy et al. 2013 or Rosen and Rodrick 2014.*

[9] *"Property-owning democracy avoids this, not by the redistribution of in¬come to those with less at the end of each period, so to speak, but rather by ensuring the widespread ownership of productive assets and human capital (that is, education and trained skills) at the beginning of each period, all this against a background of fair equality of opportunity. The intent is not simply to assist those who lose out through accident or misfortune (al¬though that must be done), but rather to put all citizens in a position to manage their own affairs on a footing of a suitable degree of social and eco¬nomic equality." (Rawls 2001, p. 139). See also: O'Neill and Williamson 2012 and Thomas 2017.*

[10] *In a comprehensive review of the literature on ESOPs and inequality, Jared Bernstein (economic advisor to former US Vice-President Joseph Biden), argued that ESOPs': "impact on inequality reduction could well be significant. In part, I argue that this is a result of transferring wealth in the form of stock in their companies to workers who, because they own little such wealth, reside in the lower reaches of the wealth distribution." See also National Center for Employee Ownership 2017.*

[11] *See Kruse 2002; Kruse et al. 2010; and O'Boyle et al. 2016.*

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