

Growing Investment Capital for Employee Ownership Can Fundamentally Change the Face of Ownership in The U.S. and Address Racial Wealth Gaps

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Abstract

The employee ownership (EO) field sits at the precipice of massive economic and social change in the United States. There is an unprecedented opportunity to advance EO to serve as a counterbalance to the forces in our economy that are driving wealth concentration, and investment capital is a critical component to drive this growth.

Employee ownership is a bipartisan, market-based, research-backed, and proven solution to addressing the racial and wealth gaps in the United States. Today, there is a unique opportunity to scale its impact, given the Great Wealth Transfer of \$124 trillion paired with the wave of retiring business owners—dubbed the silver tsunami—that represents nearly 3 million companies needing to find buyers that could be transitioned to employee ownership.

Employee ownership has myriad documented benefits at the individual, family, and community levels and for society at large, including creating quality jobs, building wealth for employee-owners, strengthening and more resilient businesses, and preserving local business ownership. Scaling this highly impactful business model addresses many issues that nonprofits and foundations work hard every day to address.

The nonprofit Ownership Capital Lab plays a critical market-making role in the EO capital marketplace. It has the ambitious goal to support the growth of EO by increasing EO investment capital by \$1 billion by 2030, to create tens of thousands more employee-owners in the United States, and then to 10x employee ownership capital from there.

There is vast potential to increase capital for EO amidst generational shifts that change who owns wealth and how that wealth is held. This includes through the Great Wealth Transfer, which will create a more diverse set of wealth holders, with more female and younger wealth

holders who are more impact-oriented and aligned than any group that has come before; through unlocking investment and grant capital from donor-advised fund capital (currently at \$252 billion and could increase by \$3 trillion over the next two decades); and through public policy that unlocks guarantees, public investment dollars and other supports for EO.



MN Builders, a 100% employee-owned construction company based in Oakland, CA, creates quality jobs and wealth-building for its entire team.

Introduction

The Ownership Capital Lab is a nonprofit initiative with the ambitious goal to support the growth of employee ownership through growing employee ownership investment capital by \$1 billion by 2030, to create tens of thousands more employee-owners in the United States, then to 10x employee ownership capital from there.

Employee ownership is a bipartisan, market-based, research-backed, and proven solution to addressing the racial and wealth gaps in the United States. Today, there is a unique opportunity to scale its impact, given the Great Wealth Transfer paired with the wave of retiring business owners—dubbed the silver tsunami—that represents nearly 3 million companies needing to find buyers. The Great Wealth Transfer forecasts \$124 trillion to move into the hands of heirs and philanthropists with potentially different (including more impact-focused) investment priorities that could open up the scale of financing needed to transition silver tsunami businesses to EO.

What is Employee Ownership and Why Does it Matter

Broad-based employee ownership (EO), in which every employee can become an owner of the company where they work, has a long and important tradition in the United States. EO creates a path to accessing the financial and professional benefits of entrepreneurship for the average small business employee, even for individuals who themselves may not have the “entrepreneurial bug.” Most EO is created through ownership transitions of profitable, longstanding businesses that employ between 10 and 100 workers (which collectively represent an estimated 25% of all businesses that employ workers with low wages). This approach skips over the risky small business start-up phase, helping workers become business owners more quickly and with less risk. When targeted at companies with a majority of frontline workers, EO becomes a powerhouse strategy for economic mobility.

EO has myriad documented benefits at the individual, family, and community levels and for society at large. EO is a wealth-building tool: employee-owners have a higher household net worth, higher income, better benefits, and greater job tenure than their non-owner employee counterparts. By creating wealth for frontline workers, EO can also create intergenerational wealth for families. When assessing overall strategies that can increase individual and family economic mobility, the report *Life Experiences that Power Economic Mobility* outlines 28 “mobility experiences” that have a significant impact on people’s lifetime income—and as a result—their economic mobility. Owning a business is in the top 10 (ranked #8), based on the percent impact on lifetime earnings, nearly tied with the effect of completing a high school education. EO is also a tool to build a healthier workforce, improve the quality of jobs across the country, and create more sustainable and durable businesses. With a healthier workforce comes healthier businesses: many studies have demonstrated that EO companies have higher sales and productivity, grow faster, and lay people off at meaningfully lower rates than comparable businesses.

This solution is needed today more than ever, with income and wealth gaps choking the majority of American families. Over half of U.S. households have expenses that exceed—or that just barely meet—their incomes. That means that if an unexpected expense comes up or there’s a drop in income, it becomes impossible to make ends meet. Black and Hispanic households each own under 3% of our country’s overall wealth (but make up 27% of households), while White households own 87% of the wealth (and are 68% of households).

Ownership can change this equation. Employee ownership is a low-risk way for the average worker to become a part owner of the business where they work and have access to the wealth-building potential of business ownership.

There are many forms of EO that deliver meaningful impact for workers, with the most common forms being ESOPs (Employee Stock Ownership Plans), EOTs (Employee Ownership Trusts), and worker cooperatives. All are important options for businesses to have available; which form is the right one is all about its fit with the goals of the selling owner and the business. All share the following characteristics:

- All employees have access to ownership;
- Employee voice in the workplace (which increases engagement and associated positive business outcomes);
- Quality jobs (better pay, benefits, and workplace culture); and
- Wealth building is achieved through one or more profit sharing, stock ownership, and retirement plans.

While many people may be unfamiliar with EO as a household term, most Americans are familiar with EO companies, perhaps unknowingly. EO companies operate in most industries, from manufacturing and engineering to media and consulting to construction and service businesses, and are inclusive of both consumer-facing and business-serving companies.

As of 2021, if we count both privately held and publicly traded companies, almost one in five (18%) U.S. employees have some form of ownership stake in the company where they work.ⁱ Narrowing to just workplaces where the employee ownership stake is at least 30% of the business, there are more than 5,000 companies that employ over 1.5 million American workers.ⁱⁱ Some of the larger and more familiar brands include Wawa, Davey Tree, Litehouse Foods, and Publix Supermarkets, which, with more than 225,000 workers, is the largest employee-owned company in the U.S..

In my work, I have seen frontline workers—even in low-margin industries (like bakeries, restaurants, and housecleaning)—earn individual profit sharing in their first years of being employee-owners in the \$10,000-20,000 ranges, which can effectively increase annual hourly earnings by 30% or more. EOs can also generate hundreds of thousands of dollars in retirement accounts for employee-owners, in both ESOP accounts and 401(k)s, with employee-owners having household net worths nearly twice as high as their peers in similar non-EO companies.

How Does Employee Ownership Come About?

Few EO businesses start as such. Most transition to EO at the time of retirement or other ownership succession as an alternative option to selling to a single buyer or a private equity firm. As this is a sale of the business, financing is required to pay the selling owner and to create the ownership stake for the employees. In simplest terms, the business takes out a loan that is paid back out of future profits. The employees themselves don't take out loans in their names or need to have assets (like a house) to borrow against through this shared ownership approach.

There are two main approaches to transitioning companies to EO. Most existing EO companies were created when EO consulting firms (nonprofit or for profit) market EO to business owners and their advisors, then work with the business to structure and facilitate the transaction, including helping to line up financing, which can be challenging. Some banks finance very large transactions of one form of EO (ESOPs), and a handful of CDFIs (Community Development Financial Institutions) and nonprofit loan funds exist that specialize in lending for EO.

The approach to EO transitions that is growing—and that has the biggest scale potential—involves participating more directly in the capital markets. Every day, businesses are bought and

sold by large corporations or private equity firms that have raised funds (a pool of investment capital) to finance these transactions. These types of funds can also be set up to finance EO transitions. Over the past five years, there has been significant growth in the number of specialized EO funds that do just this. It is an exciting trend with tremendous potential to grow broad-based EO much more quickly.

Leveraging the Capital Markets to Grow EO

Capital is the single greatest barrier to scale for EO, cited by both businesses and EO funds established to finance these transactions. In interviews with 27 fund managers, 90% cite lack of capital as the primary factor limiting their growth.ⁱⁱⁱ

Compared to the capital being deployed to buy and sell companies in the mainstream marketplace, the amount of capital targeting EO transitions is barely even a drop in the bucket. Today, there is only ~\$500 million of assets under management (AUM) for all existing specialized EO funds combined,^{iv} yet the silver tsunami opportunity for transitioning companies into this deeply impactful business model measures well into the trillions. Today, the imperative is to attract scalable sources of capital to grow the sector further. If just 10% of the 2.9 million silver tsunami companies could be transitioned to employee-owned and preserved, this would sustain an estimated 57,000 small businesses and 2.6 million jobs, supporting families and communities across the U.S.^v It would also preserve six hundred billion dollars in economic activity by American-owned firms, flowing these firms' profits into workers pockets.^{vi}

There is vast potential to increase capital for EO amidst generational shifts that change who owns wealth and how that wealth is held. This includes, but is not limited to, the following sources of capital, for which initial research shows promise:

(1) The **Great Wealth Transfer**, which will create a more diverse set of wealth holders, with more female and younger (often called NextGen) wealth holders who are more impact-oriented and aligned than any group that has come before. Due to the same generational shifts that create the silver tsunami, the U.S. economy is at the beginning of the Great Wealth Transfer, in which \$124 trillion is transferring to new generations.^{vii} These new generations of wealth holders and investors are more diverse, with rapid wealth transfer to women and younger generations unfolding. These new investors are increasingly values- and impact-aligned and a great match to support EO funds. Additionally, values-aligned women and younger wealth holders who inherit wealth could strongly connect with investing in EO because small business ownership often generated their own family's wealth.

(2) The potential of **donor-advised fund capital**. There is a largely untapped and growing pool of donor-advised funds (DAFs), which hold \$252 billion in assets.^{viii} The Ownership Capital Lab has calculated that DAF capital will increase by as much as \$4.5 trillion over the next two decades due to the Great Wealth Transfer, which would be a nearly seventeen-fold increase of an already enormous number. DAFs are arguably well-positioned to provide the most catalytic and patient capital. These are dollars set aside for charitable purposes that have already been

granted a government tax deduction and that could be invested for impact, but today, they mostly sit in mainstream investment portfolios.^{ix}

(3) Guarantees or **public investment dollars** can be obtained through programs like the SBA's SBIC program to finance EO. Public policy and legislation at the federal and state levels support, provide capital for, and incentivize the growth of EO. Importantly, EO receives bipartisan and widespread support, with EO legislation typically gaining unanimous support by legislators from across the aisle. That we need more broad-based employee ownership—and that the opportunities for EO growth presented by the silver tsunami are important to our local economies—is one of the rare issues that everyone seems to agree on.

Ownership Capital Lab's Theory of Change

The Ownership Capital Lab was founded in 2024 to leverage the current unprecedented opportunity for employee ownership (EO) to scale with the silver tsunami of retiring business owners and the Great Wealth Transfer, recognizing that capital is a barrier to—and the biggest opportunity for—the growth of EO. The Ownership

Capital Lab focuses on capital as a growth and scale lever for EO, with a vision to grow capital to finance employee ownership by \$1B in its first 5 years, then 10x it from there. The Lab focuses on strategies for financing EO with capital that allows for a slice of the value and return to accrue to the employees to address structural inequality in the U.S.

OWNERSHIP Capital Lab

What is needed is a focus on market-making in the capital markets and mergers & acquisitions (M&A) space. The Ownership Capital Lab's strategy has three levels:

First, we **build connective tissue among investors and EO funds**. Today, it can be challenging for investors new to EO investing to understand the space, identify the funds, and quickly get up the learning curve to be able to assess the investment opportunities. By providing educational resources and spaces for investors to learn and share with each other, as well as serving as a clearinghouse of a depth of information about EO investing and EO funds, we champion the specialized EO funds and bring new investors into the space.

Second, our Innovation Lab **assesses, pilots, and potentially launches new vehicles** or other approaches that are necessary to unlock scale or overcome barriers faced by funds investing in EO. We look for opportunities to tap increasingly more mainstream capital or strategies with the potential to tap subsidized capital at a greater scale.

Third, our Action Lab **unlocks the potential in untapped sources of scalable capital**, like the wealth being passed to new wealth holders through the Great Wealth Transfer, DAF capital, and subsidized government capital. Through market research, structured testing, and pilot strategies, we gain an understanding of the barriers (logistical, technical, psychological, systemic) to EO investment from these sources to design successful approaches to unlocking them.

Role of Philanthropy

Foundations, family offices, and high net worth individual philanthropists and investors play critical roles, especially at this stage in the growth of the EO capital marketplace, by providing grants, investments, and guarantees.

Grant capital. Grants support the development and growth of the EO funds by supporting new funds and emerging managers, as well as helping smaller CDFIs and nonprofit funds maintain their presence and community connections. Grants are also crucial for supporting the education and field-building needs of the EO investing space, policy work, and broad and targeted awareness of EO.

Emerging and diverse fund managers need start-up funding before they launch to hire staff to raise investment capital, build a pipeline of companies to transition to EO, and cover legal, accounting, and other service provider costs. Grant capital for new funds is critical to support emerging and diverse fund managers who may not be able to self-fund this stage.

Smaller EO funds (community-based CDFIs and nonprofit funds) may also require grant capital on an ongoing basis to support their operations and maintain their low cost of capital for their borrowers.

Catalytic investment capital or PRI investments. Catalytic investments are critical for smaller, community-connected funds (which are mostly CDFIs or nonprofit funds) as well as for emerging fund managers bringing their first or second funds to market. PRI investments can play an important role for managers' first and even second funds, recognizing that transitioning them to an MRI or market-rate bucket after their Fund I is of strategic importance to help them grow beyond PRIs.

Guarantees. Guarantees can play critically important roles because most government-backed guarantees that bridge lending risk for mainstream financial institutions are not available for most employee ownership (e.g., the Small Business Administration's 7(a) loan guarantee).^x The result is that most lenders require a personal guarantee, something that doesn't make sense in the EO context: Which of the 50, 100, or 500 employees should sign the guarantee on behalf of the whole group? Philanthropy can play a guaranteed role not only for the EO funds but also in helping bridge the personal guarantee requirements for the EO businesses that need lines of credit, working capital loans, credit cards, leases, bonds, etc., which also typically require personal guarantees. This can help unlock capital from more risk-averse investors and from financial institutions whose regulatory limits restrict their lending flexibility. This can also reduce barriers to EO transactions since the selling owner is often asked to maintain personal guarantees even after they sell their company, making EO less appealing than other options they may have for selling their company.

Conclusion

The employee ownership field sits at the precipice of massive economic and social change in the United States. There is an unprecedented opportunity right now to advance EO to serve as a counterbalance to the forces in our economy that are driving wealth concentration, and investment capital is a critical component to drive this growth.

Scaling capital to finance the growth of EO is central to the Ownership Capital Lab's mission. People often quip, "He who has money makes money." By enabling more investment capital to flow to employee ownership, we can fundamentally change who controls our small business wealth generators and fundamentally change the face of ownership in the U.S.

End Notes

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^{iv} *Ibid.*

^v Lingane, Alison. "[Retiring Baby Boomers Can Turn Workers Into Owners: Securing American Business Ownership Through Employee Ownership.](#)" *Federation of American Scientists*, Dec. 17, 2024.

^{vi} *Ibid.*

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^{ix} Beasley, Stephanie. "[The \\$230 Billion Donor-Advised Fund Industry Gets an IRS Hearing.](#)" *Yahoo Finance*, May 8, 2024.

^x For more information about the SBA loan guarantee issue and need, see: Lingane, Alison. "[Retiring Baby Boomers Can Turn Workers Into Owners: Securing American Business Ownership Through Employee Ownership.](#)" *Federation of American Scientists*, Dec. 17, 2024.