

Choosing Between Government Procurement Preferences and Employee Ownership

By Camille Kerr

In 2010, Adworkshop - a 33-percent employee-owned marketing agency based in Lake Placid N.Y. became a certified women-owned business. The firm applied for the certification through a state-level program offered by the Empire State Development Agency of New York and New York State's Division of Minority and Women-Owned Business Enterprise. As a result of its women-owned status, Adworkshop has benefited from new business opportunities and built valuable new relationships.

As Adworkshop and other firms have experienced, government contracts can accelerate the revenues and growth of a business. In the U.S., the federal government alone awards \$500 billion in contracts annually. Procurement preferences, like those offered by the Empire State Development Agency, also are offered by most states, as well as local and federal agencies, and provide a significant advantage for qualifying small businesses looking to compete.



Founded by Adele and Tom Connors in 1977, Adworkshop has grown to more than 30 employees

Unfortunately, employee stock ownership plan (ESOP) companies have encountered obstacles when trying to participate in procurement programs. For example, majority employee-owned companies are not eligible to be certified as a women-, minority-, or service-disabled veteran-owned small business under current federal policy. Furthermore, logistical requirements, such as having to enter each of the company's shareholders (including individual ESOP participants) through an online form, have made it difficult for many ESOP companies to participate in programs, even though they are eligible to participate.

Adele Connors, majority owner and CEO of Adworkshop, now faces such an obstacle. Adworkshop currently is considering a transition to 100 percent employee ownership over the

next 10 years. According to the policy in New York, which is more ESOP-friendly than the policy in many states, Adworkshop would have to show that at least 51 percent of the stock is allocated in female participants' accounts to maintain its women-owned certification. Because the company hires without regard to gender, it may lose its status. Although the company does not rely on those contracts for its business to be successful, it would not be an inconsequential loss to the organization.

Federal policy

The Small Business Administration (SBA) is the federal agency responsible for small business procurement programs, with regional and district offices throughout the country. The SBA registers companies that meet certain industry-specific size requirements to compete for the percentage of federal contract dollars that must be awarded to small businesses—currently set at a minimum of 23 percent. The agency also certifies businesses to be eligible for contracts that are set aside for disadvantaged groups through the 8(a) Business Development Program, the Women-Owned Small Businesses program, and the Service-Disabled Veteran-Owned Businesses program.

For a small business to qualify for one of these programs, not less than 51 percent of the company stock must be unconditionally and directly owned and controlled by individual(s) of the disadvantaged group. The agency has interpreted this to mean that a majority ESOP-owned company would not qualify as women-owned, for example, even if 100 percent of employees at the company, the trustee, and the board of directors were women. Many of the state and local procurement offices have programs similar to those offered by the SBA, and follow similar policies.

Because majority employee-owned companies cannot qualify for these federal procurement programs, small businesses that would otherwise have become majority employee-owned have chosen to remain at least 51 percent owned by individuals outside the ESOP. Other companies have chosen to become majority employee-owned and have lost their preferential status as a result. To eliminate this dilemma, U.S. Senator Benjamin Cardin of Maryland introduced the *Promotion and Expansion of Private Employee Ownership Act of 2013*, section 5 of which would grandfather in companies that have previously qualified for the program, as long as a majority of stock ownership was held by the disadvantaged group through the ESOP.

Diversified supplier programs

Companies that are not eligible for public procurement programs may also consider participating in diversified supplier programs. Many of the largest U.S. companies have programs to promote diversity in their contracting and suppliers. Certification organizations, such as the Women's Business Enterprise National Council (WBENC), will certify majority employee-owned companies. WBENC's eligibility requirements for ownership specifically mention ESOPs, permitting the certification of companies whose securities are "owned by women who are participants in an employee stock ownership plan...and held in a trust where all of the trustees are women, provided that, a financial institution may act as trustee."

Conclusion

According to the most recent Census Bureau data, there are more than 600,000 women-owned

and 200,000 minority-owned companies with owners above the age of 55. Many currently receive preference in federal government contracts for their contribution to the diversity of the business community, but will soon have to choose between their preferential treatment and providing a lasting benefit to their employees. By expanding the definition of ownership to include indirect ownership through an ESOP trust, the certification would no longer discourage companies from providing their employees with the long-term financial benefits of an ESOP. However, even if such a change to the federal policy is not effected, many majority ESOP-owned companies can take advantage of state, local, and private procurement programs that provide valuable business opportunities.

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