The Impact of Employee Ownership and ESOPs on Layoffs and the Costs of Unemployment to the Federal Government

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Unemployment is expensive for the federal government. It pays unemployment benefits and forgoes payroll tax revenue. Based on the estimated cost of each unemployed worker, the implied federal savings from the lower layoff rates for employee owners is $23.3 billion for the recession year 2010 and $13.7 billion per year for the longer 2002-2010 period. The implied savings for ESOPs and stock bonus plans alone is $13.7 billion for 2010 and $8.1 billion per year for the 2002-2010 period.

The analysis was conducted in partnership with the Employee Ownership Foundation. Dr. Douglas Kruse, an economist at Rutgers University's School of Management and Labor Relations, reviewed and advised on the analysis.

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Unemployment has been the central economic issue for the last four years in the U.S. Major federal programs and expenditures have been created to reduce it, tax rates have been cut, and unemployment insurance benefits extended, among other steps. There has been little or no discussion, however, about how the form of business ownership affects unemployment. That is unfortunate, because it turns out that people who work for companies with employee ownership plans are vastly less likely to be laid off than those who do not.

Data from the General Social Survey, widely regarded as the single best national survey data on social trends, shows that in 2010, for instance, 12.1% of all working adults in the private sector report having been laid off in the last year, compared to just 2.6% of those respondents who says they own stock in their company through some kind of company-sponsored employee ownership plan. In other words, if employee ownership companies behaved like conventional companies, they would have laid off 2.28 million people in 2010. In fact, they laid off 488,000, meaning 1,787,000 more people were employed in 2010 because they were employee-owners.

It might at first blush seem that these differences are an artifact of the fact that to be in an employee ownership plan, employees generally have to have one or more years of tenure. So if they have been laid off in the last year, they may have been less likely to qualify and be in the plan at the time of the survey. That would only be true, however, to the extent their layoffs were not temporary and they were able to return to their jobs.

Fortunately, the data allow us to address this concern directly, and the dramatic differences still hold up. If we look at respondents with one year or less of tenure, about twice as many people who are not employee owners report being laid off compared to respondents with one year or less of tenure who are employee owners. If we look at those with one year or more of tenure, employee owners are about five times less likely to have been laid off as non-employee owners with one year or more of tenure. Given the sample sizes of these groups, the tenure-based differences are not large enough to indicate that tenure is a determining factor in whether employee ownership has an impact on turnover, although if we only looked at the one year or more of tenure layoff data, the results would be somewhat (but only) somewhat less impressive than what this report will find for the overall impact of employee ownership on federal costs of unemployment.

The differences in 2010 were also not a fluke occurrence. In fact, the same magnitude of difference occurs in each the prior GSS quadrennial surveys going back to 2002, the first time questions about employee ownership were asked. During that period, employee-ownership companies retained 1.5 million jobs per year more than they would have if they behaved like other firms.

Table 1 provides details:

Table 1: Layoff Rates for Employee-Ownership and Other Companies
2002, 2006, and 2010 Cross-Sectional General Social Surveys Data on Layoffs and Employee Ownership

	All private sector		
	2002 (1)	2006 (2)	2010 (3)
Laid off in past year			
All private sector employees			
Employee ownership			
Yes	3.0%	2.3%	2.6%
No	9.3%	8.6%	12.1%
Less than one year of job tenure			
Employee ownership			
Yes	6.4%	7.4%	14.2%
No	16.3%	17.5%	25.3%
One year or more of job tenure			
Employee ownership			
Yes	2.7%	1.9%	1.4%
No	6.3%	3.9%	7.1%

This differential layoff experience has major implications for federal government costs. This paper tries to estimate an order of magnitude for what these costs might be. We report both the data on the whole sample as well as the more conservative sub-sample of employees with one year or less of tenure.

The 2010 data are especially important given the high levels of unemployment that year, but note that the large differences remain even if we sum the three surveys and take an average. The total number of people laid off is less in 2002 and 2006 than in 2010, but the employee ownership retention advantage across the years is still at about four times the rate for the overall population and 2.7 times the rate for those with one or more years of tenure:

- Mean rate of layoffs for those not in plans overall: 9.9%
- Mean rate of layoffs for those in plans overall: 2.6%
- Mean rate of layoffs for those with one year or more of tenure and not in plans overall: 5.4%
- Mean rate of layoffs for those with one year or more of tenure and in plans overall: 2.0%

Varieties of Employee Ownership Plans

There are a variety of ways employees might become owners through stock plans in their company. The GSS data reported here look at whether employees say they own company stock through a company stock ownership plan. The ownership plans would include employee stock ownership plans (ESOPs), a plan typically funded by company contributions to a trust that holds shares for employees meeting basic eligibility requirements (generally one year of full-time service), stock bonus plans (very similar to

ESOPs), and 401(k) plans with company stock as one of the investments. There are about 11 million ESOP and ESOP-like plan participants nationally (we include stock bonus plans in this calculation). Precise data on how many employees own company stock in 401(k) plans are not available, but probably is in the range of about four million. Employees can also be owners by buying stock through discounted employee stock purchase plans or can be given stock options or similar grants. Nationally, we estimate that about another 15 million people are covered by one or more of these plans.

The GSS data break out ownership by all categories of plans and specifically options and similar grants (the "own company stock" category includes any form or ownership), as reported in Table 2:

Table 2: Employee Ownership Data 2002-2010

	% of all private sector employees			**employees in for-profit companies**	**employees in companies with stock**
	2002	2006	2010	2010	2010
Own company stock (%)*	21.2%	17.5%	17.4%	20.8%	36.0%
Own company stock (millions of employees)	23.0	20.0	18.7	18.7	18.7
Number of responses the in GSS	1242	1173	795	690	394

*Includes ESOPs, 401(k) plans, and ESPPs.

The data suggest that there are 18.7 million participants in ESOPs, stock bonus, 401(k) and ESPP plans. We know that ESOP and stock bonus plan participation accounts for conservatively about 11 million participants, or about 59% of the total. Some of the people in that 59% with ESOPs or stock bonus plans may also participate in 401(k) plans or ESPPs.

Impact of Employee Ownership Participation on the Total Number of Unemployed

In calculating the impact of employee ownership on unemployment, we will assume that ESOP participants would be no more or less likely to have been laid off than people who own stock in other ways. The GSS data do not allow us to break out the data by ESOPs, so we cannot assess this precisely. We do know from existing research on employee ownership and corporate performance, however, that ESOPs appear to have a much more significant impact on corporate performance than other kinds of plans. There are a variety of reasons for this that are beyond the scope of this paper, but readers can consult the summary of research on this topic, "Research on Employee Ownership, Corporate Performance, and Employee Compensation," on the NCEO Web site. Consequently, our analysis of the specific impact of ESOPs on federal costs for unemployment should be viewed as very conservative.

Table 3 projects how many more workers would have been laid off if they were not employee owners. It calculates the actual number of laid off workers in employee ownership plans compared to how many would have been laid off if those employee-owners had the same rates of layoffs as non-employee owners. We look at both 2010 and the mean data for the three surveys. The data assume a total private sector workforce over this time of 109 million employees.

Table 3: Actual and Projected Layoff Rates by Employee Ownership Status

	Layoff rate, employee owners/non-employee owners	Number of employee owners	Number of projected laid-off workers using rates for employee owners	Number of projected laid-off workers if they had the same rates as non-owners	Total number of private sector workers reporting being laid off in last year
2010	12.1%/2.6%	18.8 million	488,000	2,274,800	11,620,000
Mean for all three samples	9.9%/2.6%	20.6 million*	535,600	2,039,400	11,449,800

*This is an estimate based on different numbers for the total sector work force over this period and the different rates of plan participation.

In what follows, we estimate how large the impact of the lower rate of layoffs for employee owners, including ESOPs, is to the federal government.

Elements of Costs of Unemployment

Calculating just how much revenue the federal government foregoes as a result of the difference in unemployment between those in employee ownership plans and those who are not requires a number of assumptions. To make a more precise estimate, we would need data for each survey respondent on at least their length of unemployment, their annual compensation subject to tax, and whether their state is one that qualified for extended unemployment benefits paid for by the federal government. We do not have that kind of detail, however. We only know whether people report having been laid off.

Recognizing that a precise measure is not possible, we can at least suggest reasonable estimate for the costs. While the real number may be off significantly from our estimate, we believe that by relying on typical rates of unemployment duration, taxation, and unemployment contributions from the federal government, we can derive an estimate that is in the ballpark of the actual costs.

Base Assumptions

Using data from the Bureau of Labor Statistics, the Social Security Administration, and the Census Bureau, we can construct the relevant numbers for our analysis. Where relevant, we use both the median and mean numbers, but because the federal cost per unemployed worker is the sum of all costs divided by the number of out of work people, means are generally more appropriate than medians. The one area where we believe using means overstates the case is in calculating foregone federal taxes.

Table 4: Base Data Used for Calculations

Average length of unemployment 2010	30 weeks
Average length of unemployment 2001-2008	16 weeks
Federal cost annual costs of private sector unemployment, 2008-2010	$82 billion
Federal annual cost of unemployment, 2005-2007	$25 billion
Average wage 2010	$39,959
Median wage 2010	$26,363
FICA/FUTA tax rate, 2010	7.65%
Median federal income tax rate paid by married couples	5.6%
Average federal income tax rate by married couples	11.8%
Number of private sector workers 2010	108 million

It is important to understand the components of these costs and how they vary from year to year. 2010 was at the height of the recession, and the average length of unemployment was almost twice as long as in non-recession years. We have calculated costs on both the 2010 data alone and the mean annual rates for the 2002-2010 period.

The federal costs of unemployment are even more variable. Normally, unemployment is handled by the states. Normally, the federal government becomes involved only to the extent of paying certain administrative costs and loaning money to states whose unemployment reserve funds have run out. The Extended Benefits (EB) program typically provides an additional 13 or 20 weeks of compensation to jobless workers who have exhausted their regular benefits in states where the unemployment situation has worsened dramatically. This program exists regardless of the country's economic situation. The 2009 American Recovery and Reinvestment Act authorized temporary full federal funding, which remains in effect as of this report, dramatically increasing federal costs.

During 2010, about 4.5 million people were receiving federal unemployment benefits under this program, while about 8.5 million overall were unemployed at any one time and, based on the GSS data, . In short, the additional unemployment insurance costs to the federal government from layoffs would be very small in normal years (about $31 billion in the pre-recession period) but a great deal larger during recessions.

Of course, not all of these people were in the private sector, which is the focus of this study. Data are not broken out on unemployment costs by sector, so we have applied the ratio of the private sector workforce to the total workforce to reduce the total costs of unemployment benefits to an estimated private sector only cost.

The median and average wage data we report may seem surprisingly low, but the number that most people see when income levels are reported is from total household income, not total wage income.

For 2012, the FICA tax rate is 4.2% and the Medicare tax rate is 1.45%. The maximum wage limit subject to FICA tax (4.2%) in 2012 is $110,100. There is no limit on wages subject to the Medicare (1.45%) tax. This reflects a 2% reduction in FICA obligations, however. In 2010 and prior years, the combined number was 7.65%. Both the employer and employee pay these taxes, so the normal combined rate is 15.3%. Because there is no reason to think that the 2% reduction will be permanent, we use the 15.3% number for the analysis. However, because a very small number of employees will reach their maximum taxable limit for FICA, we have used a more conservative total foregone revenue estimate of one percentage point lower (14.3%). Census data estimate that the sum total of employee income exceeding 110,000 is 11% of all employee income, so this adjustment appears reasonably reliable.

A married couple in the exact middle of the income spectrum pays about 5.6% of its income in taxes. The average income tax rate was 11.8% for a married couple. We assume these rates for this study, although the actual rates would vary by filing status. We calculate foregone taxes both on the mean rates because the total government layoff costs is a function of that number, but it could be that layoff rates differ by income level, so there may be some skewing of the results from this in a way we cannot estimate.

Finally, we base the data on the private sector workforce only (108 million). In other words, a 9% difference in the rates of the two studied groups would account for an additional 9.72 million people on layoff during the 2010 period.

Results

In the table below, we show the estimated federal foregone revenues from layoffs costs differences for employee owners overall and for ESOP and stock bonus plan participants. The core assumption here is that, as reported in Table 1, employee owners are almost four times less likely to have been laid off than non-employee owners. In the Table below, we look at what the total estimated costs of layoffs would be for the estimated layoffs over the survey period per employee.

In the table that follows, we look at what the estimated costs per employee would be in each group. Finally, the last table looks at what the added cost would be for the federal government if employee owners had the same rates of unemployment as non-employee owners.

The table uses the percentage of total costs attributable to each group based on their percentage of total laid off workers based on the data reported at the outset of this paper. Because total costs to the government are based on total wages, we use the means to calculate the costs, but we also report the median wage data as an information point.

Table 5: Estimated Federal Costs for Unemployment per Worker Laid Off

Measure		**Costs per worker laid off any time in the last year based on GSS data**
Federal cost annual costs of private sector unemployment, 2008-2010*	$82 billion	$7,056
Federal annual cost of private sector unemployment, 2005-2007*	$25 billion	$2,251
Average wage 2010	$39,959	
Median wage 2010	$26,363	
Foregone FICA/FUTA taxes, recession year at mean annual wage of $39,959, 30 weeks of unemployment	14.3%	$3,296
Foregone FICA/FUTA taxes, non-recession year at mean annual wage of $39,959, 15 weeks of unemployment	14.3%	$1,648
Foregone federal income taxes based on rate paid by average income married couple, 30 weeks of unemployment	5.6%	$1,275
Foregone federal income taxes based on rate paid by mean income married couple, 30 weeks of unemployment	11.8%	$2,662
Foregone federal income taxes based on rate paid by median income married couple, 15 weeks of unemployment	5.6%	$638
Foregone federal income taxes based on rate paid by mean income married couple, 15 weeks of unemployment	11.8%	$1,331
Total cost per worker, recessionary periods based on mean wage data, 2010		**$13,014**
Total costs per worker, mean of recessionary and non-recessionary period (2002-2010)		**$9,122**

***Only some laid off employees receive federal unemployment benefits. This calculation is based o the total dollar amount paid divided by the total number of people laid off during the year, not the total number actual receiving benefits, which would be higher.**

Based on these estimates, we can construct how much the federal government saves among workers in the employee ownership sector. Assume that the rate of layoffs is four times that of employees in the non-employee ownership sector. In that case, there would not be 2.8 million employee owners laid off during the recessionary period of 2010, or 1.5 million for the 2002/2006/2010 average, but 3.85 times that number (10.8) in the recessionary period and 4.4 times the rate (6.6 million) in the non-recessionary period. Assuming a private sector workforce of 110 million, the resulting costs would be as described in the table below:

Table 6: Implied Revenue Benefits to the Federal Government from Lower Layoff Rates

		2010 (Annual Rate)	2002 to 2010 (Annual Rate)
Actual number of layoffs by employee-owned companies	a	488,000	536,000
Number that would have been laid off, if employee-owned companies had the same layoff rates as conventional companies	b	2,275,000	2,039,000
Layoffs avoided because of employee-ownership	c = b - a	1,787,000	1,503,000
Costs to the federal government per unemployed worker	d	$13,014	$9,122
Federal government savings from employee ownership (thousands)	e = c*d	$23,256,000	$13,710,000
Federal government savings from companies with ESOPs and stock bonus plans alone (thousands)	59% *e	$13,721,000	$8,089,000

Conclusion

The analysis relied on the most conservative realistic assumptions. This analysis focuses exclusively on federal government revenues and expenditures related to unemployment. It does not cover a number of other factors relevant to an overall cost-benefit analysis of employee ownership. On the cost side, the analysis does not consider the foregone taxes related to federal government tax incentives for employee ownership.

On the benefits side, it does not include some of the other effects widely attributed to employee ownership, most notably an increase in new hiring, higher compensation per employee, and higher firm survival rates. The undocumented tendency for employee-owned businesses to be more innovative could also increase the jobs advantage of employee ownership, further increasing its positive impact on federal government revenues.

This study does, however, indicate that in 2010, the implied federal savings from the lower layoff rates for employee owners is $23.3 billion and $13.7 billion per year for the longer 2002-2010 period. The implied savings for ESOPs and stock bonus plans alone is $13.7 billion for 2010 and $8.1 billion per year for the 2002-2010 period mean data.