

Date of Hearing: April 29, 2021

ASSEMBLY COMMITTEE ON BANKING AND FINANCE

Timothy Grayson, Chair

AB 1319 (Lorena Gonzalez) – As Amended April 21, 2021

SUBJECT: The Cooperative Economy Act

SUMMARY: Establishes the Cooperative Economy Act (Act) which creates a private, nonprofit mutual benefit corporation called the Federation of California Worker Cooperatives (Federation), to serve as a voluntary membership organization for worker cooperatives.

Specifically, **this bill:**

- 1) Requires the Labor Commissioner (LC) to organize a corporation under the Nonprofit Mutual Benefit Corporation Law, as specified. The Governor must appoint the initial board of directors, to serve for one year or until the first regular meeting of the members, whichever comes later.
- 2) Provides that the Federation is a non-public entity, does not constitute a public agency or state employer for any purpose, and that once the LC organizes the Federation as a nonprofit mutual benefit corporation, and the Governor appoints the first initial board of directors, there shall be no further involvement in the operation of the Federation by any governmental entity.
- 3) Requires membership in the Federation to be restricted to legal entities that comply with all of the following:
 - a) Have uniform hiring and ownership eligibility criteria and for whom a majority of the work is performed by worker-owners.
 - b) At least 51 percent of the workers are worker-owners.
 - c) A majority of the voting ownership interest is held by worker-owners.
 - d) A majority of voting power is held by worker-owners.
 - e) Worker-owners exercise their vote on a one-person, one-vote basis.
 - f) The majority of earnings is distributed or allocated based on the quantity or value of work performed rather than ownership interest.
- 4) Requires members to be allocated voting power proportionate to their worker-owner's share of the total federation workforce, provided that no member shall have greater than 30 percent of the voting power, as specified.
- 5) Requires the initial board of directors to have three voting directors, and for one of them to be a worker-owner.

- 6) States that the initial board of directors shall set forth rules in the bylaws for the composition of future boards of directors and requires those rules to provide, at a minimum, all of the following:
 - a) That there is an odd number of voting directors.
 - b) That following the term of the initial board of directors, no voting directors can be appointed by the Governor, the Legislature, or other governmental entities.
 - c) That nonmembers and nondirectors shall not have voting power with respect to election of directors, amendment of the bylaws, amendment of the articles of incorporation, or any other decision of the members or board of directors.
 - d) Directors shall be elected by member votes weighted, as specified.
- 7) Requires the Federation to set the labor policy and provide all management to the members, as specified.
- 8) Applies the tax exemption available to state-chartered credit unions to both the Federation and a member for the duration of its membership.
- 9) States that a member shall not directly employ its own managers. Any manager shall be an employee of the Federation, as specified.
- 10) Provides that the member is the employer under federal law and that the Federation and the applicable member are both employers of the workers for purposes of state law.
- 11) States that provisions of this act are severable.

EXISTING LAW:

- 1) Establishes the Nonprofit Corporation Law that recognizes the following:
 - a) Public benefit corporations;
 - b) Mutual benefit corporations; and
 - c) Religious corporations.
- 2) Establishes the Nonprofit Mutual Benefit Corporation Law and provides that a corporation may be formed as a nonprofit mutual benefit corporation for any lawful purpose, provided that it is not formed exclusively for charitable purposes, as specified.
- 3) Establishes the Division of Labor Standards and Enforcement (DLSE) under the direction of the Labor Commissioner (LC) and authorizes the LC to investigate employee complaints and enforce labor laws, as specified.

FISCAL EFFECT: Unknown. This bill is keyed fiscal by Legislative Counsel.

COMMENTS:

1) PURPOSE

According to the author:

Employee ownership and worker cooperative models help workers build wealth, while allowing them to participate in the management of the business. When workers are also owners, they can prioritize stronger worker protections and benefits, instead of profits. The lack of awareness of this business model and its benefits has been a major barrier in forming worker co-ops. AB 1319 would incentivize employee ownership by creating a Federation of worker co-ops to serve as a membership organization and resource that can provide technical assistance and administrative support. The creation of more worker co-ops will help move the state towards an inclusive and resilient economy by centering on worker ownership and investing in local communities.

2) BACKGROUND

A cooperative corporation (or co-op) conducts its business primarily for the mutual benefit of its members as patrons of the corporation. The earnings, savings, or benefits of the co-op are legally required to be used for the general welfare of the members. Whereas a traditional corporation generates earnings for its owners or shareholders, a co-op is required to proportionately and equitably distribute earnings to some or all of its members or its patrons, based upon their patronage of the corporation.

Consumer co-ops and worker co-ops are two general classes of cooperative corporations. A consumer co-op is organized for the benefit of its members who purchase goods or services from the co-op. A worker co-op is organized for the benefit of its members who provide their labor in the production of the good or service sold by the co-op.

Both consumer and worker co-ops are required to distribute their earnings, savings, and benefits to their members. For worker co-ops, these distributions are typically based on the amount of hour worked or wages earned and often take the form of a share in year-end profits.

In recent years there have been renewed interests in promoting worker cooperatives and addressing the obstacles owners (or future owners) face in trying to grow or start the business. An August 16, 2019 informational hearing hosted by the Assembly Labor Committee explored the challenges faced by worker cooperatives. The Assembly Labor Committee identified the following challenges in the purview of this committee:

- a) *Finding investors.* Cooperatives face difficulty in finding investors or financial institutions willing to assist with start-up costs and thus become more reliant on internal financing.
- b) *Lack of legal expertise.* The legal framework for establishing a cooperative is not widely taught and potential owners navigate a myriad of tax and corporation laws related to formation.

3) THE UNIQUE STRUCTURE OF THE COOPERATIVE FEDERATION

This bill proposes a unique organizational structure with the intended goal of allowing more worker cooperatives to form and thrive in California. As drafted, the Federation provides member organizations with management professionals to help execute the Federation's labor policy, which will include policies around hiring, firing, compensation, and assignment of work. Though not explicit in the bill's language, member organizations will also receive other types of technical assistance and administration support from the Federation as well as a tax exemption detailed in Comment #4.

While there is no direct comparable project in state government, there are other mutual benefit nonprofits formed by governmental bodies whose purpose is to perform certain functions on behalf of member stakeholders.

For example, the California Travel & Tourism Commission (now called Visit California) promotes California as a tourist destination and works in partnership with the travel industry to develop and maintain marketing programs. Formed by the California Tourism Marketing Act (Tourism Marketing Act), industry stakeholders pay an assessment collected by the California Office of Tourism.

The Federation also differs substantially from other worker cooperative umbrella organizations. For example, at first glance the United States Federation of Worker Cooperatives (USFWC) shares some similarities with the proposed Federation: USFWC is a member organization that provides consulting and technical assistance to member cooperatives. However, unlike the Federation, USFWC does not develop labor standards for member organizations and does not provide member organizations with management professionals.

There remain unanswered questions about the exact structure of the Federation and the nature of the relationship between it and member organizations. Many of these questions are not in the purview of this committee. For example, what type of labor standards will be required for membership? Or, what is the intended purpose of making an employee of a member organization also an employee of the Federation? As the bill moves through the legislative process, these details will likely need to be filled in.

4) TAX EXEMPTION

This bill applies a tax exemption available to state-chartered credit unions to the Federation and its members. Under current law, a state-chartered credit union is "exempt from all other taxes and licenses, state, county, and municipal, imposed upon those credit unions" except specified taxes such as sales and use taxes, local utility user taxes, and taxes upon their real property.

It is unclear what the full impact of this credit union tax exemption will be. Proponents indicate that one motivation for this is to reduce the impact of license fees such as alcoholic beverage license fees as well as secretary of state filing fees to reduce the start-up burdens for new worker cooperatives. However, there may be unintended consequences from applying a broad tax exemption designed for a type of financial nonprofit entity like a credit union to the Federation (a nonprofit) and member organizations (presumably for-profit). How would this exemption affect the tax treatment of distributed profits? What happens if a member organization leaves

the Federation and how do appropriate government bodies know the tax exemption no longer applies?

As this bill moves forward, greater clarity on the scope of this proposed tax exemption will be needed. There are some similarities between credit unions and worker cooperatives, but credit unions' tax exempt status is an artifact of history related to a their unique role in the financial system. The author may wish to consider specifying which taxes are exempt instead of applying the existing credit union tax exemption to the Federation and worker cooperative organizations.

REGISTERED SUPPORT / OPPOSITION:**Support**

California State Council of Service Employees International Union (SEIU California) (Sponsor)
Worker-owned Recovery California (WORC)

Opposition

None

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