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Property, Ownership, and Employee-Ownership: Employee Control in ESOPs

Purpose: Most people associate ownership with the ability to control something. In the U.S., ESOPs are one of the principal forms of employee ownership. However, most ESOPs give employees very limited rights of control over the company they own. This paper explores this conflict by examining theories of property and ownership to determine whether the right to participate in decision-making is inherent in the idea of ownership as it is generally understood. Ultimately, I argue that the law governing ESOPs should be revised to give employees a larger role in the governance of their companies.

Design methodology/approach: This paper considers the concept of ownership both historically and analytically. I examine the roots of property theory in the work of John Locke and contemporary theorists, as well as contemporary theorizing about ownership.

Findings: There are two kinds of ownership: legal ownership and psychological ownership. In legal ownership, the right to participation is inherent but alienable, so one can legally be an owner of something but have no right of participation. Psychological ownership primarily arises from a sense of control. Legal ownership confers some part of the bundle of rights associated with property. Psychological ownership conveys a feeling of efficacy, responsibility and control, but no formal rights. I argue that, in order for employee ownership to be more than mere property-holding, it must include meaningful participation in decision-making, including governance.

Research Limitations/Implications: This essay is only concerned with ESOPs in

the U.S. Although the findings may be applicable, it does not address other forms of employee ownership or employee ownership outside of the U.S.

Practical Implications: People associate ownership with the ability to control something, so when workers are told they own their company but then find they have few control rights, it may undermine their sense of ownership. This then has negative implications for the company's success. In order to ensure meaningful levels of governance rights, policy-makers should revise the laws governing ESOPs to require greater involvement by employees.

Social Implications: Clarifying ambiguities around ownership will help support arguments for affording employee-owners greater control rights in their companies, which will have various spill-over effects.

Originality/value: Practitioners and scholars alike deploy the term, “ownership” but ascribe different meanings to it. The distinction between legal and psychological ownership is largely lacking in the ESOP literature. Clarifying this distinction will help to move the discussion forward regarding employee participation in ESOPs. In addition, the paper provides an original analysis of property that demonstrates the importance of the right to control, showing that traditional ESOP structure may violate important aspects of that right.

Property, Ownership, and Employee-Ownership: Employee Control in ESOPs

Introduction

Employee ownership, often dismissed as a fringe practice in the world of business, has been receiving greater attention in the U.S. in recent years. Reasons for this include the Great Recession, concerns about the growing disparity of wealth, and the increasing pressures of the so-called “Silver Tsunami,” an “ownership crisis” arising from the millions of Baby Boomers who own small businesses and are beginning to look toward retirement (Thorpe 2016). The most common form of employee ownership in the U.S. is the Employee Share (or Stock) Ownership Plan, or ESOP. About 14 million Americans, a little under 10% of the workforce,¹ work at ESOPs and ESOP-like companies (NCEO 2021).

An ESOP is, in essence, a kind of retirement plan, although the reason for establishing an ESOP may have more to do with the financial interests of the person transferring ownership (Rosen 2017) than the interests of employees.² Employees in an

¹ Pre-coronavirus pandemic, that is. This number is from 2018. In an survey of its members, the National Center for Employee Ownership found that over 65% said, “being employee-owned has had a positive effect on their ability to respond to COVID-19” (NCEO 2020).

² Kaufman (1989) notes that while it is defined as an employee benefit and regulated under the Employee Retirement Income Security Act of 1974, which governs retirement and pension plans in the U.S., “IRS regulations view the ESOP as a tax-beneficial capital financing tool.” According to the Menke Group, one of the oldest and most highly-respected ESOP advisors in the U.S., ESOPs are not primarily retirement plans, but “a tool of corporate finance that is used as an alternative to a sale or merger as a way of creating

ESOP receive grants of stock from the company which are held by a trust. Employees don't own the stock directly and cannot access the asset until they either leave the company or the company is sold. The proportion of the company held by the ESOP varies. According to recent estimates, about half are majority-owned by the employees; of these, most are one hundred percent ESOPs (Rosen 2017). Most ESOPs are privately held.³ The trust is managed by a trustee who, in most cases, is selected by the company's board of directors.⁴

Existing Employee Control Rights

By law, the ESOP trust must be accorded the highest degree of voting rights given to shareholders in the company, regardless of whether the company is publicly traded or privately held. The trustee, in their fiduciary capacity, votes on behalf of the beneficiaries of the trust (the employees). In publicly-held companies, plan participants (employees) are "permitted" to instruct the trustee on how to vote their stock; in privately-held companies, trustees are required to allow pass-through voting where participants express their preferences to the trustee for how to vote their stock for mergers, acquisitions, buyouts, and

liquidity and investment diversification for owners of privately-held businesses" that also comes with "tax advantages [that] maximize the tax savings to the sellers" (Group, "Misconception #2").

³ However, most ESOP employees are at publicly traded companies. A slight majority of ESOPs are S corps, but the vast majority of ESOP employees work for C corps. This makes sense, since S corps are much more likely to be small businesses (<https://www.nceo.org/articles/employee-ownership-by-the-numbers>, accessed 11/19/2020).

⁴ The Menke Group seeks to reassure potential clients by saying, "In most cases, the existing Board of Director members serve as the ESOP Trust fiduciaries" (Group, "Misconception #5").

other major fiscal actions (26 USC 409[e]). However, the trustee is required by law to override the employees' instructions if they consider the employees' vote to be contrary to their financial interests as plan beneficiaries (Steiker 2004).⁵ Indeed, courts have ruled that trustees must consider the interests of the employees "in the *abstract* as beneficiaries" of the plan (Kaufman 1989). So, for example, if in the judgment of the trustee it is in the financial interest of employees to accept an offer of a sale that would involve widespread layoffs and the employees themselves vote against the sale, the trustee may be legally bound to ignore the result of the employees' vote and vote the employees' stock in favor of the sale.⁶

Given the very limited degree of control that employees have in ESOPs, the question I wish to explore is whether what they have can really be considered ownership, as opposed to merely property-holding. As one critic of the typical ESOP structure puts it, "in most cases, when applied to the actual employee stock owners, 'ownership' is a hollow word" (Kaufman 1989). Unlike worker cooperatives, another form of employee ownership where employee-owners have full governance rights and often operational control as well, ESOPs are not inherently a form of democratic business. That said, unlike worker cooperatives, which are largely unregulated, the law does require at least a limited degree of democratic

⁵ When it comes to matters not directly related to their financial interest, such as "environmental, social, and governance metrics," trustees may override an employee vote if it promotes a "non-pecuniary benefit" that is "unrelated to the financial interests of the plan's participants and beneficiaries" (Federal Rule 29 CFR 2550.404a-1, quoted in Rosen 2020).

⁶ Rosen notes, however, that "it is exceedingly rare for employees to vote no on a good offer" (Rosen 2020).

control by workers in the form of pass-through voting, as noted above.⁷ Of course, ESOPs “may grant plan participants broader voting rights than provided by law,” such as for members of the board of directors, “although that is not a common practice” (Steiker 2004). Still, a “democratic ESOP,” while uncommon, can be every bit as democratic as a worker-owned cooperative (or more).⁸ However, most of the time, except for the fact of

⁷ As Kaufman (1989) puts it, “the ESOP structure itself cannot create a democratic workplace.” This is not the place for a full-on discussion of the differences between ESOPs and worker co-operatives, which I explore elsewhere (Kaswan 2013). Some important points may be made. The first is that ESOPs are highly regulated in the U.S., while worker cooperatives are largely unregulated, although some states have recently adopted regulations governing them (Oatfield 2015). Second, democratic governance is an essential part of the identity of cooperatives in a way that it is not for ESOPs (for cooperatives, see <https://www.ica.coop/en/cooperatives/cooperative-identity>). However, democratic governance on paper is different from democratic governance in practice (Kaswan 2021). There is an extensive literature on what’s called the “degeneration thesis,” which has to do with the tendency in worker cooperatives for democratic practices to decay over time (summarized in Bretos et al. 2020). In large worker cooperatives, worker participation may be limited to periodic votes for members of the board of directors, and it is not uncommon for worker cooperatives to employ non-member labor, people who are not co-owners either by choice or because certain classes of workers are ineligible for membership. Although worker cooperatives may have a flatter organizational structure than many businesses, they are not immune from managerialism (Kaswan 2014), and some hire outside managers, which can put significant power in the hands of non-members (NCF 2006). In contrast, a democratic ESOP may involve its employees in governance more than do some worker cooperatives, and all employees of an ESOP “normally” participate in the ESOP (Rosen 2017), making them more inclusive than worker cooperatives.

⁸ Kaufman (1989), in offering a model for a “democratic ESOP” details several ways that traditional

employee ownership, ESOPs are virtually indistinguishable in terms of governance and management from traditionally owned companies (Blasi and Kruse 2006).⁹

Distinguishing Property and Ownership

The absence of meaningful opportunities to participate in governance may come as something of a surprise for casual observers. Ask a random person on the street what they think ownership means, they will likely say that it means the right to control something. “Control of an object appears to be a key characteristic of the phenomenon of ownership” (Pierce et al. 2001). Or, as Logue and Yates write in *The Real World of Employee Ownership*, “Ownership of property and the right to make decisions about its use go hand in hand in American economic thought” (2001). This implies that in property theory, if not in law, decision-making rights are inherent in the ownership of property.

An ESOP share may be property, but since many ESOPs fail to provide opportunities for participation, just because it is referred to as “employee ownership” we cannot assume that employees are able to exercise control of their firm. Rather, there seems to be a disconnect between the idea of ownership as associated with the right to control, and the practice of employee ownership.¹⁰ The question then is, if the right of control is an

ESOPs are structured that inhibits worker control of the enterprise.

⁹ It appears that, for some ESOP advocates, such as the Menke Group, this may be a major advantage, as too much worker control may scare off potential conversions (Group 2021).

¹⁰ Indeed, a prominent and influential member of the ESOP community—an attorney who has been involved in establishing ESOPs since even before they were formally established in 1974—reacted very

essential element of ownership, but most ESOP employees have only limited ability to exercise control or participate in decision-making, can ESOPs really be understood as a form of ownership?

Property and ownership are closely related, but, as will be made clear in what follows, there are important differences. As we will see, having property is a formal, legal condition, which we sometimes call ownership. But when we think about ownership, we usually refer to a broader conception of ownership that is rooted in a social and psychological condition that may or may not involve having property. Indeed, the ambiguity in the term gives rise to a paradox, as it is possible to have property but no sense of ownership, and to have a sense of ownership without having property. The existence of this paradox reveals that property and ownership may not be as intrinsically connected as we tend to think.

In examining this question, I start by taking a look at property theory. There is a large literature on this, and I will only engage with it enough to lay a foundation for an understanding of what property is and the basis and nature of property rights. I will start with the work of John Locke, whose work in the 17th century strongly influenced our modern ideas of property, followed by a discussion of a few more contemporary theorists. As will be seen, the legal form of ownership is fairly thin and arcane. After problematizing the relationship between property and ownership I will discuss a broader, stronger

negatively to an earlier draft of this paper, arguing directly that control rights had nothing to do with ownership.

conception of ownership, psychological ownership, which is primarily rooted in the capacity to control an object. The essence of my argument is that, for employee ownership to be meaningful for an ESOP, a property-rights framework is not enough. If we want to give more than lip service to the idea of ownership, the strong form associated with control rights needs to be present. Workers need to have a sense of control, at least to some meaningful degree.

Formal Ownership: Property

If we are to understand how the formal or legal right to property may be distinguished from ownership understood more broadly, we need a clear idea of just what property is. Our contemporary ideas about property, in the Western world at least, owe a great deal to the work of John Locke, particularly his *Second Treatise on Government*.¹¹ This, then, is a good place to start.¹²

Locke's starting point for his theory of property is two-fold: the natural reason of the need for subsistence, and the divine reason of God's gift to the world to humanity "for the

¹¹ Near the end of his life, Locke wrote to a friend, "Property I have nowhere found more clearly explained, than in a book entitled, Two Treatises of Government." He did not, however, claim authorship of the work, which had been published anonymously. His authorship was uncovered after his death (Laslett 1960).

¹² There is a substantial secondary literature on Locke that I will largely ignore. My intention here is merely to use Locke to help provide some clarity on the concept. It does not help that Locke himself was famously contradictory and cloudy, leaving much room for conflicting interpretations. My interest here is not to sort out those conflicts, so I will primarily stick to Locke's text and not engage the literature on it.

support and comfort of their being.” (Locke 1988 II. §25). However, in order to use what we have been given we must acquire them first: That is, we must make them our property. The way we do this, Locke argues, is by applying our labor to them. Those objects become our property because our labor is an extension or application of the “property” each person has in his or her “own *Person*” (1988 II. §27). Because “property in the person” is a natural condition, property rights are considered natural rights. Locke’s theory is often referred to as the “labor theory of property,”¹³ and it remains the fundamental premise of property rights.¹⁴

There are other ways one might come to have property (inheritance, for example), which need not concern us here. The point is that, in Locke’s theory, the fundamental means by which one acquires a property right is through one’s labor. Locke himself complicates this a few lines after asserting this theory by saying that he would have a property right to “the Turfs my Servant has cut,” which suggests that the servant’s own labor is not a sufficient condition to establish his claim (1988 II. §28). And Locke himself may have enjoyed property rights in things he did not labor to make, such as his home, his carriage, and the clothes on his back (assuming he did, indeed, own a carriage and a house).

¹³ Not to be confused with the labor theory of *value*, which Locke also articulates later in the same chapter. The two are often confounded but are, in fact, quite different.

¹⁴ This, despite Marx’s pointing out that, in fact, “primitive accumulation” of the sort Locke describes is but a myth, and that the reality is “written in the annals of mankind in letters of blood and fire” (Marx 1967). White (2017) provides a trenchant critique of the way the Lockean idea of primitive accumulation is perpetuated in the work of Robert Nozick.

How could he claim them as his property if he had not contributed his labor to them? For us, the answer is fairly obvious: they occur within a currency-based system of exchange of labor for wages. In other words, he merely exchanged some of the labor we may assume he did perform—the representation of labor value stored in the form of money—for the labor of the persons who made the goods he then considered his own. As Locke puts it later, a “Free-man makes himself a Servant to another, by selling him for a certain time, the Service he undertakes to do, in exchange for Wages he is to receive...[which] gives the Master but a Temporary Power over him, and no greater, than what is contained in the *Contract* between ‘em” (1988 II. §85). The terms of the contract, in effect, are what give the “owner” of the servant’s time the ownership of the produce of the servant’s labor.

In Lockean terms, then, workers transfer (or alienate, to use the Marxian term) the produce of their labor through a contractual agreement, usually with whomever is paying their wages. Strictly speaking, in a one hundred percent worker-owned firm, there is no alienation of labor as there is no capitalist to whom property rights have been alienated.¹⁵ While this is, in some respects, no different from how it works in a traditional capitalist firm, the difference is in the direct property relation of workers to the assets of the firm (capital) and the produce of their labor. In both cases the owners of the firm own the produce of the

¹⁵ If workers are not full owners then it is little different from a traditional company except that the workers have a claim to a portion of the surplus value of their labor. Here I’m only referring to the property structure of the firm, not to its governance or management, which could be quite different from a traditional firm.

labor performed; in the worker-owned firm it is the workers, while in the capitalist-owned firm, it is the stock- or shareholders.¹⁶

If Locke's labor theory of property helps us understand how we acquire property, what does it mean to have property? In other words, what rights follow from having property? Locke defines property as such a thing "that without a Man's own consent it cannot be taken from him" (1988 II. §193; see also II. §140, where Locke makes reference to the "Fundamental Law of Property"). One of his essential points is that the reason for claiming ownership is to be able to enjoy the benefits that come from the use of it. The ability to enjoy those benefits means that the owner of property must be able to dispose of (i.e., use) it in the manner he or she chooses, up to and including "a right to destroy any thing by using it" (1988 I. §39). The right to destroy (by using) would seem to imply the right to control its use. Various questions may then arise from this, including what constitutes control, how control may be manifested, the limits of that control, the ability to delegate or alienate control, and the responsibilities that may be associated with the right to control what one owns. These are all included to some extent in the contemporary literature on property, but it would appear, at least, that we have identified that the right to control is an intrinsic part of property rights—a right that is present only to a limited degree in ESOPs.

Contemporary Perspectives: Property Rights and Control Rights

Most contemporary theories are, essentially, refinements of Locke's theory of

¹⁶ Technically, in an ESOP the employees are shareholders in the trust, which owns the shares of the firm. I will explore this issue later.

property as natural rights. Many of these take as their starting point the idea that property is a “bundle of rights” (e.g., Pennock 1980). Becker identifies 4,080 possible bundles (1980) based on a collection of 13 categories.¹⁷ The idea of a “bundle” means that these rights may be severable, and it means that someone may be identified as the owner of some property but for one reason or another not be able to exercise all of the rights associated with that property. So, for example, the owner of a piece of land may lease it to someone to build a factory but have only limited control over what the factory owner does on that land (for example, a contract may limit the factory owner to certain kinds of activities or, more likely, forbid certain activities). The factory owner might build a factory on the leased land but then lease out the factory itself to an enterprise that actually carries out the operations. Subcontractors, with their own employees, might be brought in to perform specific functions for a firm; these employees might work side-by-side with employees from a different firm. The ownership of each or any of these enterprises might be distributed among any number of persons, some of whom may not even be aware that they are part owners (especially if their ownership stake is in the form of stock held through a mutual fund). Ultimately, the determination of the exercise of any particular property rights, including that of control, is determined by law. So, a conception of ownership based on property rights is certain to be confusing and unstable, as the idea of property rights itself is confusing and unstable.

The key point to notice here is that property is a set of legal relations which are based on certain kinds of social relations inscribed in law. Ultimately, legal relations are relations

¹⁷ Similar to Becker’s 13 categories is Honoré’s 11 “incidents” of private ownership, usefully summarized by White (2017).

between people: “since the purpose of the law is to regulate the conduct of human beings, all jurial relations must...be predicated of such human beings” (Hohfeld 1964). In other words, it is too easy to fall into the mistake of treating these concepts as pure abstractions, when in fact they are bound to various forms of actual human action. As Hohfeld reminds us, legal concepts such as property rights are, in the first instance, ways of understanding social relations between people with respect to things, and in the second instance a means through which those social relations are governed and adjudicated. So, “property” is not the relation itself, but a conceptual category for certain kinds of relations that exist between actually-existing people.

If we understand property as a means for establishing and administering certain kinds of relations between people, then to control property is to exercise a kind of control over a set of social relations. So, what does it mean to exercise control? While, as Logue and Yates write, ownership may commonly be associated with the right of control, Ellerman (1992) raises the question of just what sort of control that entails. He argues that the formal legal relation only involves a negative control right: no one may use my property without my consent. But, as Ellerman would have it, this is a simple binary: either I do or I do not consent to someone’s use of that property. It does not imply that I have the ability to decide exactly *how* that property will be used. Rather, the contrasting “positive control right to tell others what to do is not a part of property ownership” (Ellerman 1992). Instead, Ellerman argues, positive control rights come from contracts. However, I am not convinced: positive control rights do not simply appear out of thin air to be inscribed in contracts. They must come from somewhere. I would argue that in fact, the positive control rights *are* a property

right, but they can—and may often be—alienated (or assigned) through contract. If part of the right of property involves the ability to control that property, then surely the right to control the property must ultimately rest with the owner. They cannot originate with a user other than the owner, although the owner may assign them to someone else.

For example, imagine a piece of land that is owned by an individual. Ellerman notes that the owner's negative control rights can "make a worker into a trespasser" if the worker uses the land without the owner's consent; similarly, the owner becomes "a kidnapper" if she forces the worker to labor without his consent, and he argues, correctly, that what gives the owner the ability to tell the worker what to do is a contract (1992). But the positive right doesn't just appear out of nowhere. In the first instance, the owner has the right to control what is done on her property. This positive control right is maintained in the employment contract, as the positive right of control (within legal limits) is extended to the labor power rented (to use Ellerman's term) by the property (or business) owner—that is, the property owner can tell the worker what to do. The worker also has a positive control right to his labor, which is part of the property he may be said to have in his person: the ability to control what he does. It doesn't disappear in the labor contract, nor does the property owner magically gain a right that did not previously exist. Rather, the positive control right is part of what is alienated by the worker to the owner by contract. So, contract does not create the positive control rights, but it makes them explicit in transferring them from one party to the other.

Pateman (2002) hints at, but does not directly address, this positive aspect of ownership in her essay comparing the notion of property in the person to self-ownership.

Reviewing recent writing on self-ownership, she characterizes its central point as the idea that people would be able to have “a significant say in their own life...to pursue their own goals...and [have] control over their actions” (2002). The ability to make decisions about one’s self—the object of property in self-ownership—is clearly an integral part of what it means to own one’s self. We can extrapolate from this that the ability to make decisions about what one owns is an integral part of ownership generally.

Pateman goes further into property theory, however, and makes clear another important element about the relationship between ownership and property (or, the property that is owned): One of the elements of self-ownership that distinguishes it from property in the person has to do with the ability to alienate elements of the property that each person has in themselves. This is an important part of what it means to have control over one’s self (2002). In other words, as noted above, part of the function of ownership is the ability to alienate rights with respect to property—to control to whom the rights are alienated. But while one of the features of property is its alienability, ownership itself cannot be alienated. If, as Locke puts it, the “fundamental law of property” is that it cannot be alienated without the owner’s consent (the negative control right Ellerman refers to), then one must be able to make decisions about the alienation of one’s property (a positive control right). In cases where one’s property is an indivisible part of a larger object also owned by others, as in a joint stock company, then to consent must mean the right to participate in decisions about that object.¹⁸

¹⁸ The option of exit, however, is not alienable nor is it something that requires the consent of the

As has been noted, control rights, or the ability to make decisions about one's property, can be alienated, but even this requires consent on the part of the owner. Such consent must, for reasons Locke makes clear, be revocable.¹⁹ It would be fairly easy to go further down a Lockean road here and point to the idea of "tacit consent." When workers become members of an ESOP it may be said that they tacitly—and maybe even expressly—agree to alienate control rights for their shares to the ESOP trustee. However, unlike the hypothetical conditions of state-formation Locke describes in the Second Treatise in which autonomous individuals in the state of nature join together in the social contract to form a legal government, ESOPs are often imposed on workers, who are faced with the option of accepting the terms or finding another job. Even if they approve of the ESOP, however, they usually have no voice in the selection of the trustee who will exercise what limited rights to control of the enterprise the employees may have.

Psychological Ownership

Legal ownership, from this reading, appears to be fairly thin. The line connecting the property owner to the object itself may be strong, inscribed in contracts and enforceable in courts of law, but it may have little in terms of actual content. The idea of an "ownership culture," popular in the ESOP literature, invokes a broader, more substantive conception of

other property-holders. Nonetheless, some limits may be placed on how exit is performed—for example, in the case of an ESOP, the shares must be sold to the company and their value may be paid out over a number of years.

¹⁹ As Ellerman points out, an irrevocable labor contract is accurately referred to as slavery.

ownership that rests much more on the *feeling* of ownership than on the existence of a property claim. Indeed, the dominant theme in that literature is that the mere existence of a property claim is insufficient to give rise to a sense of ownership, which arises primarily from the establishment of practices that promote participation in decision-making. In addition to being a legal relation, then, ownership can be a state of mind. This is known as “psychological ownership.”

The notion of psychological ownership is not new—Pierce et al. (2001, 2003) reference work stretching back over 100 years. They identify three types of psychological ownership rooted in particular human motivations: the roots of psychological ownership can be found, in part, in three human motives: (a) efficacy and effectance, (b) self-identity, and (c) having a place” (Pierce et al. 2003). I will focus on the first of these as being most relevant to my argument, although I will briefly touch on the second later.

In their work they distinguish, as I am, between psychological ownership and legal ownership. Legal ownership, they note, is something recognized by society, whereas psychological ownership is something recognized by the individual(s) involved. And, just as “psychological ownership can exist in the absence of legal ownership,” people can have a legal claim to an object but lack a sense of ownership (Pierce et al. 2003). Thus, the concept of ownership is ambiguous—when someone says they own something we do not know if they mean legally, psychologically, or both. Exploring this ambiguity reveals some important elements of our understanding of ownership.

Both property (legal ownership) and ownership (psychological ownership) indicate a

kind of social relation between people with regard to objects of one kind or another.²⁰ Property is a formal legal relation enforceable through the particular social institutions of the state and courts of law. Ownership is also a social condition in that it establishes a similar sort of relation—between people with respect to objects—but it must be recognized by the individuals involved in it in order for it to have meaning. It is, in effect, a state of mind.

Ownership Without Property

When something is our property, we usually say that we own it. But we can say that we have ownership of something without it necessarily implying that it is our property. I may have a feeling of ownership over my desk in an office, even though I have no formal property right to the desk or even the space where it sits, because I exercise exclusive control (within prescribed limits) to that space. This points again to the social and informal character of ownership, which has to do with my relation to an object with respect to other people, separate from the property relation.

The example of the desk tells us that psychological ownership may be quite weak: my claim to the exclusive use of my desk may be denied to me by the person or entity that has a property right to it, for example if I am relocated, reassigned or fired. By the same token, the sense of ownership that comes from having property rights may be quite thin, as I may have little sense of connection to an object that I own. For example, if I inherit some

²⁰ Mostly, the distinction is between tangible and intangible objects. A house is a tangible object, a share in a corporation is intangible (even though the corporation has assets, which are tangible). Intellectual property is another form of intangible property.

land that I have never visited, I may have no sense of ownership over that land. Or, if I own shares in a mutual fund that owns shares in various companies, I may technically have a property right with respect to those companies but lack any sense of ownership (or, in many cases, even the knowledge of what companies are included in the fund). Like the mutual fund, ESOP employees also have an indirect ownership in their company (they own shares in the trust, which owns shares in the company). The difference between the ESOP employees and the mutual fund, though, is that, as employees, they have a direct connection to their property. The irony here is that while the employees have a direct and meaningful connection to the property they own because they work there, it is possible that they may lack a sense of ownership if the factors that support psychological ownership are absent.

Dan-Cohen (2001) also points to the psychological dimension of ownership by distinguishing between the “pragmatic” aspect of ownership, which pertains to specific kinds of benefit or value, and “constitutive” ownership, which refers to the ontological incorporation of an object into the self. This constitutive element of ownership is reflected in our use of personal pronouns such as *I*, *mine*, etc., and suggests a performative aspect to ownership that is missing in the formal property-centered understanding. For Dan-Cohen, *property* (the pragmatic aspect of ownership) pertains to value, whereas *ownership* (the constitutive element) pertains to attachment. The constitutive aspect of ownership also points to the second of Pierce, et al.’s analytical categories: self-identity. As they explain, possessions “serve as symbolic expressions of the self since they are closely connected with self-identity and individuality” (Pierce et al. 2001). The use of possessive pronouns, whereby we consider a possession as either a part of ourselves or as reflective of who we are, is

indicative of a psychological condition.

Psychological Ownership and the Culture of Ownership

The value orientation of Dan-Cohen's pragmatic ownership reflects that the main point of owning property is that we obtain some kind of benefit from it. The question is whether the benefit that is derived from owning property is sufficient to produce the feeling of ownership. Can a culture of ownership at an ESOP develop based solely on the benefit one derives from the property?

Pierce, et al. suggest that simply obtaining benefit would not be sufficient. It is worth noting that financial benefit does not factor into their analysis of the motives that lead to psychological ownership. Rather, "The motive for possession is in large part being in control" (Pierce et al. 2003). We seek to have possessions precisely because this enables us to control them. So, "ownership basically means the ability to use and to control the use of objects.... control exercised over an object eventually gives rise to feelings of ownership toward that object" (Pierce et al. 2001). They explain that the ability to control objects is how we come to see them as constituting part of our identity, as part of the self, and, "the greater the amount of control, the more the object is experienced as part of the self." This leads them to argue that, "There is a positive and causal relationship between the amount of control an employee has over a particular organizational factor and the degree of ownership the employee feels toward that factor" (Pierce et al. 2001).

Both Pierce, et al. and Dan-Cohen place emphasis on the use of possessive pronouns in identifying psychological ownership, but this runs the risk of muddying the waters. We may use the terms "my" and "mine" and so on to refer to things we identify with or that

give us a sense of belonging in a way that is quite different from the kind of psychological ownership in the way I have been discussing it. For example, many people feel a strong sense of attachment to professional sports teams yet have neither any rights of control nor property claims. Similarly, people might have a strong attachment to elements of their identity, including their religion, ethnic heritage, or their family lineage. However, important features of ownership are noticeably absent in both of these cases. The attachment one has to a sports team does not confer any rights whatsoever; the same could be said, for the most part, to the various elements of identity.²¹ These are much more like what economists would call public goods than private ones—they are non-exclusive, and the expansion of the number of people who share the feeling of attachment does not diminish the enjoyment of the connection for the others. With few exceptions (for example, a right of way to a public beach), public goods cannot be objects of ownership. In Dan-Cohen's terms, while elements of the constitutive aspect of ownership may be present, the pragmatic aspect, which has to do with the value of the object, is absent in these cases.²²

²¹ The only exception to this would be the kinds of socially-prescribed (or even legal) rights attendant on members of particular dominant classes, such as, until recently, the exclusive claim of heterosexual couples to the right to marry. As Haney Lopez (1996) details, until well into the 20th century, the category of who could be considered white, and therefore eligible for various benefits, was something that had to be protected against contestation by people who were excluded.

²² There is something of a curious use of the concept of psychological ownership in the marketing literature (e.g., Peck and Shu 2009; Kirk 2017). The question of whether merely touching an object may impart a kind of psychological ownership, as in Peck and Shu, seems quite attenuated from much of the sort of

It could be said that the example of the desk to which I am assigned in the company where I work is also not properly understood as ownership because, based on a Lockean argument, I have neither applied my own labor to acquiring it nor have I engaged in exchange such that I would be able to claim a property right to it. But this is precisely the point of the example: The sense of ownership comes in the absence of a property claim. By the fact of the desk having been assigned to me (or to me in addition to others), it becomes *mine* in a sense, in that I have some kind of exclusive claim to it. It is clearly a private good: if other people are assigned to the same desk, it diminishes the value I may derive from it by limiting my use of it in either a temporal or spatial sense, or both. But, if that desk has been assigned to me but I am severely limited in my ability to use the desk in a way that I choose—in other words, exercise control over it—then I am unlikely to have a sense of ownership. What gives me the feeling of ownership is the ability to control what I do with it.

The point of this is not to suggest that we should stop thinking about employee ownership as a property relation. Rather, it is to suggest that this is not enough. If employees are truly to be understood as owners, they need to be able to exercise control to some degree, because a sense of control is intrinsic to our understanding of ownership. The legal relation is important in terms of the material benefits that come from it, but this does not impart a sense of ownership, which does not rely on the existence of the legal relation. The

ownership being considered here. However, Kirk's finding that giving customers a sense of being able to exercise some control over the product they are buying, whether through customization or by voting on potato chip flavors, further reinforces the argument that control is an essential element of ownership.

feeling of ownership comes from the capacity to control. Indeed, the ability to control is intrinsic to both forms of ownership, but it may be alienated in the case of legal ownership. Once alienated, however, the feeling of ownership will likely evaporate.

Complications: Mixed and collective ownership

The question of ownership is clearest in the case of individuals, as it is possible to make a direct association between individual and object, ability to control and the object under consideration.²³ But although individuals own individual shares in ESOPs, the ESOP itself is collectively owned.²⁴ A 100% employee-owned ESOP is collectively owned by the employees. In most ESOPs, however, ownership is mixed, and the ESOP shares ownership with whomever owns the rest, whether an individual, a family, a partnership, or stockholders. If, as I am suggesting, the right to control an object is part of ownership, how does that work when the object is collectively owned?

The classic discussion of the connection between ownership and control rights in corporations is Berle and Means' 1932 book, *The Modern Corporation and Private Property*. They argue that in large, publicly-traded corporations (a relatively new phenomenon when they published their study), the absence of a clear and direct owner who is able to exert

²³ It should be noted that the ability to control is, generally speaking, always exercised within legal and social/cultural limits. There may be few objects of ownership for which anyone may be said to have absolute control, no matter how much they may think they have it.

²⁴ As has been noted, the employees own shares in an ESOP trust, which then owns a share of the company.

substantial control over the enterprise, and the delegation of control to managers (managerialism), means that the connection between ownership and control had effectively been severed. Their work has been subject to much criticism, especially in recent years (see Cheffins and Bank (2009) for a review of the recent literature). In one respect, the validity of their claim is not relevant here, because few (if any) large, publicly-traded companies are ESOPs. However, the question does not entirely go away, as it raises an issue that is a matter of concern when dealing with any sort of collective object. Indeed, this is the point at which economic or business theory meets political theory, for which this question—collective control of an object—may be understood as a central concern. The introduction of political theory provides a different sort of lens for thinking about the question of control rights in a collectively-owned object.

It is not uncommon in the literature to see an analogy being made between corporations and states, but in some ways the connection is closer than that. If we simply understand both states and corporations as different sets of associations or collectively-controlled objects, we can see that the same sorts of principles may apply to each,²⁵ at least as concerns the argument being presented here.²⁶

²⁵ In fact, Dahl (1985, 1998) takes this approach in his work.

²⁶ There are, certainly, differences. One has to do with the ability of the state to make and enforce law (including the capacity for the legitimate use of violence). Another is that the division between workers and owners has no parallel for the state, although, because the topic of this paper has to do with worker-owners, this difference is not, in fact, relevant.

In laying out the classic liberal case for the development of the state, Locke argues that, through the social contract, individuals give up the liberty they enjoy in the state of nature (right of control) to a governing authority that will act in their interests.²⁷ To understand this in a corporate sense, in the transaction in which stockholders purchase shares in a company, individual property owners give up their right to control their property (their money) to the corporation which then, like the state, is a fiduciary that acts in the financial interest of the owners. The owners occupy the same position as citizens in the social contract in the sense that it is by bringing them together (in a literal contract) that the corporation is formed, and they exercise a limited sort of sovereignty (within the bounds of law and the share purchase contract). By electing the members of the board of directors they elect representatives (albeit typically on a one-vote-per-share basis rather than one-vote-per-person) who then exercise governance, which is delegated to an administrative body that exercises day-to-day control. One difference is that, in a corporation, the members of the board are expected represent the interests of all shareholders and not just those from a particular constituency, but the important point here is that their function is to be elected representatives. To flip Dahl (1985) on his head, if the people are recognized as being

²⁷ To be sure, this is a simplification of a complex and nuanced argument. In fact, Locke identifies three different types of liberty (natural liberty, liberty of man in society, and liberty of man under government) (1988, II. §22), and the last two of these can be understood as products of the social contract. Nonetheless, the “perfect freedom” enjoyed in the state of nature is limited only by what Locke calls the “law of nature,” which he identifies as “reason, which is that law” (1988, II. §§4, 6), which is clearly far more extensive—yet also more unstable—than what people enjoy under the social contract.

self-governing in a representative democratic system, then corporate shareholders can be said to govern the corporation; if corporate shareholders cannot be said to govern the corporation, then on what basis may we say that the people are sovereign in a representative democracy?²⁸

Still, Berle and Means' argument may have merit in large corporations where voting is based on the size of one's holdings, most shareholders have virtually no direct involvement in the company, and the election of members of the board of directors is effectively controlled by the existing board through fixed slates of candidates and the use of proxy voting. However, it surely does not hold—or should not hold—in the case of an employee-owned firm, where the employees are directly involved in the life of the firm. While the epistemic distance of a typical shareholder may be great, no such distance exists for employees. Arguably, in terms of the day-to-day operations, the involvement of employees is far greater than that even of the board of directors. But this also points to an important distinction seldom made in discussions of control rights: the difference between governance and managerial (operational) control.

Governance and Operational Control

In most businesses, formal managerial decision-making is strictly hierarchical, although some elements of democracy such as group deliberation and even voting may be incorporated. However, in such a system there is usually a line of authority that ends with

²⁸ This claim may say more about the weakness of representative democracy than that power of corporate shareholders, but I will leave that discussion for a different paper.

the person of the CEO. In other words, managerial decision-making is not collectivized, although authority may be distributed. The lower down in the chain any individual is, the less their sense of control, both in terms of the scope of their decision-making and in terms of the degree to which their authority is final. Within this formal hierarchical structure collective decision-making may take place, for example in work teams or among managers and executives, but while these may have many of the hallmarks of democratic participation, it must be remembered that they are taking place within a hierarchical structure that places ultimate decision-making authority in the hands of the CEO, who is him- or herself answerable to the board of directors which, ultimately, governs the company. So, even though those lower in the hierarchy may have the ability to participate in decision-making, their degree of control is limited to the scope of their authority, and subject to ultimate acceptance by the CEO and board.²⁹

Governance functions differently. It is generally accepted that ownership conveys a right to participate in governance, for example by partners or stockholders. It is not uncommon for there to be categories of owners, such as silent partners, who do not have control rights, but, following from my argument, I would say that these owners without control rights are best understood as having property rights but not full ownership. Also, the governance process (in a traditional firm) may (but usually doesn't) include opportunities for

²⁹ In some cases, such as in union contracts or works councils such as are fairly common in Europe, employee participation in managerial decision-making may also be formally established in a way that counterbalances or limits the power of the CEO.

participation by non-owners such as the workers or any of the other stakeholders associated with the firm. If this participation does not include voting rights then it is merely advisory, or it may be incorporated into firm governance through, for example, employee seats on the board of directors.

Where there are multiple owners, there are usually bylaws or articles of incorporation that determine the control rights of the owners. As I noted above in my response to Ellerman, these contracts assign positive control rights. Normally, the collective owners share governance rights based on the size of their investment (i.e., the number of shares owned). There is no hierarchy—either one has rights or not, and then, if one has rights, the question is the degree to which their participation counts. Those with more shares have more control, but this does not function as a hierarchy—those with more shares cannot tell those with fewer what to do or how to vote their shares. Rather, those with more shares have more votes, with the consequence that they are generally able to get their way.

Most of the time, the governance activity of the owners is limited to voting for the members of the board of directors, who are the ones who are more or less actively engaged in governance. The board of directors acts as fiduciary on behalf of the owners, and the owners are expected to be able to hold the directors accountable. These owners may exercise their control rights in two ways: by changing the composition of the members of the board, or by divesting themselves of ownership in the company by selling their shares.

How ESOPs are Different

Unlike regular shareholders, ESOP employees often do not vote for members of the board of directors. In addition, it is much more difficult for employees in an ESOP to divest

themselves of ownership if they are unhappy with the direction the board or management is taking with the company, because doing so means giving up their employment. Also, unlike typical stockholders, most ESOP plans don't allow departing employees to withdraw the full value of their shares right away. Furthermore, as with any retirement plan, there may be substantial penalties for early withdrawal and a waiting period of several years before they can even access the money.

There are other ways ESOPs differ from traditionally-owned companies. As with traditional businesses, employees are themselves fulfilling the functions of the company, engaged in its day-to-day operations. Therefore, the ability to participate in managerial decision-making will often be more immediate and important to them than governance. Their desire to participate, however, comes not only from their interests as employees, but also from their interests as owners. Indeed, to a degree the distinction between governance and management breaks down because the interests of employees are usually assumed to be in conflict with the interests of owners. If the workers are owners, then those conflicting interests can more easily be reconciled. However, as has been noted, employees only have very limited ability to exercise control of an ESOP.

Despite the rather negative tone of this essay it is important to recognize that democratic control by employees is not entirely absent in ESOPs. The right of employees to participate in pass-through voting on fiscal matters is important. In a way, this reflects a form of direct democracy (where citizens—or in this case, employees—vote directly on a matter of policy rather than having representatives represent their interests) that is otherwise completely absent in the corporate world. It means that even the least-democratic ESOP is

more democratic than any traditional corporation when it comes to employee participation. However, we must also recognize the limits to this: trustees are usually chosen by the board of directors instead of the employees (or the board serves as trustee themselves); there is no requirement that they allow employees to vote on any matter not strictly related to a limited set of fiscal matters; and trustees are required by law to override the votes of employees if, in their judgment, the employees are subordinating “the interests of the participants and beneficiaries in their retirement income or financial benefits under the plan to any non-pecuniary objective, or promote non-pecuniary benefits or goals unrelated to these financial interests of the plan’s participants and beneficiaries” (Federal Rule 29 CFR 2550.404a-1, quoted in Rosen 2020). The fact of *some* democratic participation, however, should not be confused with a meaningful sense of control.

Policy Implications

The argument I am making in this paper, that ESOPs should provide employees with meaningful opportunities to exercise control over the companies they own, is not new. It has been made in various ways for decades.³⁰ In most cases, the argument is made on the basis of firm performance. The argument, however, has largely fallen on deaf ears: the National Center for Employee Ownership reported in 2010 that 83% of ESOP companies responding to a governance survey reported that employees had “no role at all in the election of the board of directors” (Magowan 2010). One might expect that legal mandates would not be

³⁰ Winther and Marens (1997) provide a useful overview. Note that their review is from over 20 years ago.

necessary, and that the financial rewards of increased participation would be enough to compel firms to give employees meaningful mechanisms for participation. However, as McHugh et al. (2005) find, managers do not perceive that employee participation in governance contributes to firm performance. They note that managers recognize that employee participation may be valuable at the operational level, but they fail to recognize its value when it comes to “strategic level decisions” (i.e., governance). This leads them to argue, “the primary motivation for a more democratic ESOP structure would be for social, rather than economic reasons. Thus, socially important ESOP structural issues are likely to be neglected by organizations. Therefore, there is clearly a role for policy makers not only to encourage practices that enhance ESOP firm performance, but also to create safeguards so that ESOPs are structured in ways that meet employee-owner interests” (McHugh et al. 2005).

I fully endorse McHugh, et al.’s call for policy reforms to ensure a role for employees in the governance of a firm. There are many ways that could be done, and both Magowan (2010) and (Murphy 2005) offer some good ideas.³¹ Kaufman (1989) notes that there have been legislative attempts to limit the tax benefits of ESOPs to those that meet certain criteria for democratic participation, but it seems that these have not been successful. Murphy cautions that pushing too hard on democratic participation may reduce the number of

³¹ It is not my intention to offer an explicit set of proposed reforms, but one that I have not seen mentioned is the idea that the selection of a trustee must be ratified by the employees. This seems to me to be a fairly minimal step that would establish that employees consent to the agent who will act on their behalf.

companies adopting the ESOP model,³² but he acknowledges that the increased tax revenue from companies that fail to meet the participation standards could be used to help promote the law's adoption (Murphy 2005).

What distinguishes my approach from these, however, is that in my view employee involvement in governance should not just be done because it is a good idea, but as a matter of right. As currently structured, the law, divided between the tax code and ERISA, ignores the interests of ESOP employees, concerning itself only with the interests of the selling parties and the employees in a future state as retirees. The tax breaks for selling owners seems like a reasonable accommodation to encourage a practice that has significant social benefits by distributing wealth more broadly. It also seems reasonable to treat an ESOP as a retirement plan, since employees tend to discount the future and not save enough for retirement. What is not reflected is the interests of the employee-owners of a going concern, understood as both employees *and* as owners. Simply put, employees, understood as owners, should be able to exercise the rights that come with ownership. But this is denied

³² One of the reviewers of this paper has suggested that the absence of democratic control helps to explain why ESOPs are much more common than worker cooperatives, which the Democracy at Work Institutes estimates only number about 1,000 with around 10,000 total employees in the U.S. (Prushinskaya 2022). In the worker cooperative literature, the untraditional governance structure of worker cooperatives is often cited as a significant hinderance in obtaining financing from skeptical funders (Abell 2014). In addition, business owners may feel more comfortable converting their business to an ESOP than a cooperative because they feel more comfortable with the more-traditional structure. Thus, the Menke Group's efforts to deemphasize employee participation is a strategic move to reassure potential clients.

them when they have no say in the creation of the ESOP, they have no say in the selection of a trustee, they cannot vote for members of the board of directors (let alone have employees elected to the board), they only have pass-through votes on a limited set of matters, and their votes, when they do vote, may be overridden by the trustee.

Conclusion

In the course of writing this paper I happened to be sitting on a plane next to an intelligent young man in his early twenties who worked on a Southern California farm. He asked me at one point how my work was going and I explained that I was having difficulty drawing a very fine line through a grey area. And so I asked him: “What does ownership mean to you?” His response: “It means the ability to control something.” I thanked him. Clearly, the idea that there is a strong connection between ownership and control runs deep in our society. This understanding of the essential character of ownership, however, is at odds with the practices of many employee-owned companies that afford employees no meaningful opportunities to control the companies where they work—enough so that their *lack* of control is offered reassuringly to owners who might be considering using an ESOP as a way to extract value from their business (Group 2021, Misconception #8).

A company is property, and an ESOP is a mechanism by which the employees of a company may claim ownership of a portion of that property. Their claim is attenuated: they own shares not in the company itself but in a trust that owns shares in the company. In a typical ESOP, their interests are exercised by a trustee, a position often occupied by the existing board of directors of the company. Employees have limited rights to voice their preference on certain existential matters pertaining to the company, but the trustee can

override their preference if in their opinion their expressed preference is not in their interests as beneficiaries of the ESOP understood as a retirement plan. They have little effective control over the company.

As it turns out, the term, “ownership,” is ambiguous. We refer to the condition of having property as ownership, but we also use ownership to describe a psychological condition where we have a sense of control over the object in question. While often intertwined, they are distinct. While the capacity for control is intrinsic to both legal and psychological ownership, control rights may be alienated in the former although, as I have argued, that alienation requires consent that may be absent in most ESOPs. For its sake, psychological ownership derives from a feeling of control, so it cannot be irrevocably alienated or assigned.

A result of this is that the image of employees having control over their workplace that often accompanies the idea of “employee ownership” is based on the notion of psychological ownership—but this turns out to be false in the case of the typical ESOP. Employees have little more control than they would if the company had no ESOP at all.

Democratic ESOPs exist, but they are fairly rare. The ESOP literature is littered with appeals for the development of an “ownership culture” that often but not always includes recommendations for the inclusion of participatory practices. Usually, these appeals rely on the interests of those with the most to gain, as the primary reason given for inclusion is that it results in improved firm performance. This seems to have had little effect. I suggest, then, a shift in approach. Employee participation in ESOPs should be ensured through the adoption of policy that recognizes it not merely a matter of interest but as a matter of right.

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