Blowups at Vatex's Employee Ownership Lab

Solving the legacy problem is Jerry Gorde's obsession. How do you sell your company without selling its soul? It's harder than anyone might imagine, but Gorde is determined to turn his company into a laboratory modeling a solution.

Vatex—a Richmond, Va. maker of T-shirts and promotional apparel with $7 million in revenues—is now on its third experiment. After creating an Employee Stock Ownership Plan in 1980, Vatex moved to a worker cooperative in 1995, then in 2001 went back to an ESOP. "It's blown up each time," Gorde said with a laugh. "This time I don't think it will blow up."

A key aim of Gorde's experiment is the redistribution of wealth and power. He wants to put company wealth in the hands of those who help create it, employees. He wants to create a democratic structure to carry on the social mission of the firm, while also ensuring good management. And he wants to cash out of his 30 percent ownership stake at about $2 million, so his own financial future is secure.

As Gorde puts it, he has equal concern for legacy, succession, and exit strategy. "Exit means getting your money out," he explained. "Succession is how the company can sustain itself," with competent leadership. "Legacy means preserving the values, the core values."

The form Gorde has settled on is an ESOP, whereby an employee trust uses company cash flow to buy out the founders' shares. The company can take a tax writeoff, which "can bring your tax liability to zero," Gorde said. Plus the founders take cash tax-free. "I can make more money selling to an ESOP than to Attila the Hun," he said.

If Gorde is now enthusiastic about the ESOP, in the mid-1990s he was disillusioned with it. "If you can't read an income statement and balance sheet, you'll be a lousy capitalist," he told Business Ethics in a 1996 interview. Because Vatex is in a disadvantaged area and offers entry-level work, its employees are "at the bottom of the food chain," Gorde said. Vatex had to break T-shirts out of twelve-packs into packs of ten before packing slips started to be accurate, he explained. "We put signs all over the plant, 'Think 10.' That's how basic things are here." He also found the ESOP created an incentive for employees to leave, since they couldn't cash out unless they quit or retired. Fed up, Gorde dropped the ESOP in 1990. The company began buying employees out, to the tune of $700,000. That was blowup No. 1.

After five years the smoke cleared and the buyout was complete. That led Gorde in 1995 to launch experiment No. 2: the worker-owned cooperative, where employees would be taught economic democracy. Common stock was converted to non-voting preferred stock, and employees each got one ownership share in the company. "That's what creates the democratic structure," Gorde told us in that same 1996 interview, a few months into the experiment. The bylaws of Vatex became its constitution, with every right enumerated—a detailed grievance process, procedures for workers to elect the board, a committee structure whereby employees set up wage scales and employment policies, plus a stated goal of passing 30 percent of profits to workers. It seemed ideal.

"My theory is if capitalism is the most potent economic form, and democracy is the most potent political form, why not put them together?" Gorde said in a 2003 interview. "Except when you do both in an orthodox way, it's like oil and water. Capitalism is nimble. Democracy is cumbersome." With so much focus on process, "the organization becomes internally myopic," he said. "It forgets the customer." The constitution was so over the top it became a distraction. Hence came blowup No. 2. The worker co-op was terminated in 2000.

"Now we're going for a little less democracy, a little more nimble," Gorde said about his third experiment, ESOP redux. Created in 2001, the ESOP over 10 years will acquire 100 percent of the company. With no stars in his eyesabout employee governance, Gorde says he won't hand employees control untilthe ESOP owns over 50 percent.

This time employees must earn their ownership. Instead of being paid for learning time, as under the co-op, employees learn about employee ownership on their own time. They can learn about company financials by attending quarterly town meetings, where attendance is not required but is noted in appraisals and is rewarded with door prizes like toaster ovens and lava lamps. Vatex also instituted cliff vesting, so employees earn shares over time but they don't vest for five years. If in that time employees have not demonstrated a capacity to be owners, they'll be terminated before vesting, Gorde said. "I will not spoon feed you concepts of responsibility. It's what you're doing to earn the equity being given you."

You might call it an experiment in tough love. More than two years into it, Gorde seems to be right: this time it's not blowing up.

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