



Inside this issue:

President's Corner

Bi-partisan Support for ESOPs Is Our Past and Future **2**

Ownership Advantage

Now Is the Time to Develop Leadership **3**

The Washington Report

Your Role in the Mid-Term Elections **5**

Advisory Committee on Administration

The Mechanics of Releveraging **7**

Foundation News

Institute Offers Free Employee Surveys **9**

Legal Update

How New Legislation Should Affect ESOPs **10**

ESOP Association Unveils New Look! *(See page 5.)*



2018 ESOP Company of the Year

Employee owners from Gardener's Supply accept the award for the 2018 ESOP Company of the Year during The ESOP Association's Awards Banquet in May.

Photo by Marty Lavor

Ownership Culture Runs Deep at Gardener's Supply Company

Employee ownership is deeply rooted in the culture at the 2018 ESOP Company of the Year, Burlington, VT-based Gardener's Supply Company. "It is part of who we are... it's our identity," says the company's Director of HR Christie Kane.

Even a brief look reveals how fully the employee owners—from top to bottom—and the company are committed to broad-based employee ownership. For example, Gardener's offers seasonal employees the chance to participate in the ESOP after their second year with the company.

Brad Bolton, who is Material Handling Lead at Gardener's Supply, got his start as one of those seasonal employees. Bolton could tell right away that Gardener's had a special culture: He could see it in the way employees interacted with each other.

The inclusive and motivated behavior of his colleagues spurred Bolton to become one of them, so he applied for a full time position. His understanding of and appreciation for the concept of employee ownership really kicked into high gear once he "became fully immersed in the culture," he says.

As Bolton began to grasp that the roots of Gardener's culture lay in its approach to living employee ownership, he became more involved in spreading the word.

Today, Bolton is the Chair of the Gardener's Supply ESOP Committee, which itself is a prime example of the company's cultural commitment. This 11-person group meets for an hour and a half every other week with the goal of "nurturing and sustaining the culture of employee ownership."

Gardener's investment in ownership reaches from its ESOP committee all the way to the top of the organization: The committee has an advisory board member who serves as the group's liaison to the board of directors. This ensures that employee owner interests are included in planning discussions.

Including an advisory board member on an ESOP committee is fairly unique, and it is just one of the ways that Gardener's has committed itself to living its ownership culture. The company has been an ESOP since 1987, and has invested years in refining its approach for educating employee owners and fine-tuning its interactive culture.

Examples of other approaches that have worked for Gardener's include:

A Brownie for Your Thoughts. Each year, Gardener's employee owners are personally invited to offer their ideas, questions, and concerns—in return for a fresh baked brownie. The questions are addressed and the answers are shared with the entire staff.

For Gardener's, this has been an effective way to open a line of communication with employee owners who might not otherwise feel comfortable asking questions about the organization.

Solstice Celebration. The anniversary of Gardener's transition to 100 percent employee ownership falls on the winter solstice. Each year, employees remember the day by gathering to celebrate.


What makes this event even more special is the fact that Gardener's includes customers in the experience: Its retail stores serve desserts to customers as a way of symbolically sharing a "piece of the pie."

This event helps open a dialogue between Gardener's employee owners and the community they serve. This kind of interaction can help employee owners better understand customers' needs and can help customers gain an appreciation for the passion and dedication of Gardener's employee owners.

Pride in the company's culture, and in the employee owners who embody that culture, is clearly something worth sharing.

This kind of interaction can help employee owners better understand customers' needs and can help customers gain an appreciation for the passion and dedication of Gardener's employee owners.

"We get a direct benefit for caring and doing our best, and it shows in our workforce," says Cindy Turcot, Gardener's President. "We have great employees, low turnover, and employees who offer ideas, constructive criticism, and solutions."

At Gardener's, the time invested in developing a home-grown culture of ownership and engagement certainly has paid off. 

ESOP Report



The Voice of The ESOP Association

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President's Corner

Bi-Partisan Support for ESOPs Is Our Past and Our Future

By J. Michael Keeling, ESOP Association President

E SOPs have survived thus far, and will survive far into the future, only if they continue to enjoy broad political support.

That kind of support already exists.

Want proof?

Read this statement from the [2016 Republican Party platform](#):

Republicans believe that the employer-employee relationship of the future will be built upon employee empowerment and workplace flexibility. We therefore endorse employee stock ownership plans that enable workers to become capitalists, expand the realm of private property, and energize a free enterprise economy.

And then read this statement from a May [policy brief](#) issued by the Progressive Policy Institute—a think tank

with long standing ties to the Democratic Party and with roots in the policies of President Clinton—which also offers a positive view of employee ownership. The report states that the federal government could encourage: “*the expansion of employee stock ownership plans (ESOPs) that would ensure that more of the fruits of economic growth flow to workers.*”

Why do I offer these two quotes, coming from sources that have different views on so many issues?

Because our community must never, ever forget that promoting ESOPs as a “Republican” policy or as a “Democratic” policy will move ESOPs into the present-day morass of partisan conflict that is stopping so many new proposals from improving our nation.

The ESOP Association recognized this concern as far back as 1982, at the first meeting I attended of this organization’s leadership. Our leadership further asserted the importance of broad political support when drafting our current [Strategic Plan](#), which includes the following provision:

The ESOP Association will take full advantage of the bi-partisan appeal of the ESOP business model, building on the broad based ownership model of all levels of employees advocating to protect and expand employee ownership in America.

One of the objectives of our Strategic Plan states our goal clearly, succinctly, and unambiguously: “Maintain and enhance bi-partisan support for all ESOPs.”

The Republican Party Platform, a Democratic-leaning think tank, and The Association’s Strategic Plan all are in sync: Broad based employee ownership via ESOPs is a good thing.

If The Association issues or even accepts a message that ESOPs are better when they are supported by Democrats or Republicans, then ESOPs will not survive into the latter years of the 21st Century.

Why am I preaching this message? Because I hear talk among outside pundits, campaign advisors, and a very few Democratic members of Congress who say employee ownership is “their” way of turning around Republican

favoritism for big business, capitalism, and C suite executives.

Having one party “own” employee ownership will lead to less, not more, of it. Why? Because no party stays in power all the time. Since ESOPs were formally recognized into law, control of the White House and the chambers of Congress see-sawed back and forth many, many times. If ESOPs were seen as a policy that belonged exclusively to one party or the other, they would have disappeared many years ago with the changing political tides.

But that didn’t happen because we continue to follow our Strategic Plan and focus on bi-partisan support.

And that has served us very well.


Think back to the 2017 tax law cut and remember that tax deductions once viewed as sacred—such as charitable donations, interest payments, and state and local taxes paid—were reduced, but no cutbacks were made regarding ESOP tax incentives.

Our community escaped negative consequences because our support is wide spread and bi-partisan. (Visit the list of [ESOP Advocates](#) on our web site and you will see plenty of Democrats and Republicans.)

More recently, our community gained new benefits thanks to the bi-partisan support marshaled by Senator Kirsten Gillibrand (D-NY).

How did the Senator get a pro-employee ownership bill through Congress and signed by a Republican President? She made sure the Republican chairs and the senior Democrats on the Congressional Small Business Committees supported the measure. She knew broad support was needed for her Main Street Employee Ownership Bill to become a law. (For more information on the new law, see the Legal Update on page 10.)

Mid-term elections are coming, and no one is saying you should be negative towards a candidate that you respect and admire from either party.

But you should be negative towards *any* movement that seeks to make broad-based employee ownership an issue that is “owned” by any one party. 

Ownership Advantage

Now Is the Time to Develop Leadership

By Victor Aspengren, Director, Prairie Capital Advisors, Inc.

Fortunately for businesses in general, the great recession was some time ago. Unfortunately for our businesses’ leaders, the lessons learned during that time of economic difficulty may now be fading as the economy continues to expand and unemployment continues to drop.

In these times of abundance, it is understandable that business leaders can be caught up in efforts aimed at growing value, pursuing new opportunities, and enjoying the financial success of the company. But that also means this is a time when it is easy to lose focus on the continual quest to improve one’s leadership skills.

It has been stated that great leaders spend more than 50 percent of their time honing their skills and awareness so they can take their leadership to the next level.

What amount of time are you spending on leadership development? No matter your position—whether you are the chair of the board or a team leader—you should be creating time to make this happen.

There is no ideal time, but being ready for the next economic downturn should motivate individuals and organizations to make the time.

The following leadership thoughts were presented a couple of years after the great recession. Presenting them again during good times may be the spark that initiates a renewed focus for your leadership development—for you personally and for your organization.

The Value of Consistency

In tough times, there is nothing worse than a Dr.-Jekyll-and-Mr.-Hyde style of leadership. Nothing is more exasperating to employees than trying to guess which leader is going to show up on any given day; they can never count on a consistent response.

No one—including leaders themselves—truly wishes for inconsistent behavior. Think of it in this way: Mother Nature has rhythms that vacillate between flood and drought, extremes in temperature, quiet days and violent storms. Everyone dislikes it, and sometimes a hefty price is paid for these great meteorological swings.

Everyone wishes for consistency, especially in their leaders.

Follow Through

Another attribute of weak leadership is a lack of follow through. When nothing gets done, company growth will fail to meet expectations. Leaders need to look in the mirror before they accuse anyone else of failure to follow through.

During economic turmoil, leaders need to set the example for those they lead. A lack of follow through by the leader is like salt in an organizational wound. Great leaders understand they must follow through, period.

Calendar of Deadlines and Important Dates

Oct. 1-31	Employee Ownership Month
Nov. 8-9	Las Vegas Conference & Trade Show
Nov. 11-14	Leading in an Ownership Setting: The Program for CEOs, Session II
Feb. 1	Deadline for Entering AACE and Employee Ownership Month Poster
Feb. 8	ESOP Professionals' Forum
May 22	ESOP Association Annual Awards Banquet
May 23-24	Annual Conference

To see all national and chapter meetings, visit us online at: www.esopassociation.org

Have Faith

Faith is a belief, duty, or trust in a concept that cannot be proven.

Leaders must have faith in the people they lead: Faith that their employees can and will become ardent champions in helping the company survive. Leaders believe in the good of people, not the negative.

They also believe that no matter what tough decisions the company may have to make, the fabric of the organization contains the faith that people are good.

When decisions are made that require the exit of an employee, they are done with dignity and without malice. Faith requires leaders to be resilient and support this faith in people, even when others may not.

Leaders must take the high road and avoid getting sucked into a mire of negativity.

Moving On

In time, all leaders must move on. *How* they move on is critical to the future of the company.

Great leaders begin working themselves out of a job from day one. They focus on a common vision shared by all, and communicate this vision relentlessly.


Leaders teach their employees how to think and act like owners by teaching them the business. This is done through open book management, involvement in strategy, and processes that allow employees to give input into business decisions.

Great leadership incorporates a succession planning process from day one. Leaders constantly are evaluating who is ready for a new leadership role, when it is the right time for new leadership, and what is in the best interest of the company.

There is ample opportunity for leadership training for the next generation through mentoring, training, and education. This is succession planning in its finest form. When done this way, it is easy for great leaders to say with complete calm and peacefulness that they have worked themselves out of job.

Carry On

During times of economic turmoil, leaders and those who wish to be leaders take pride in the consistent way they manage the successes and troubles of the company. They are zealots in following through on their commitments and the commitments of the organization. Leaders have faith in people, even when these people may have to exit the company for tough reasons. Great leaders understand how to exit gracefully and not by force.

The leaders who are admired and respected practice all these leadership traits. For those who wish to become leaders, this is just one small piece of the writing that reinforces what great leadership looks like. 

ESOP Association Unveils New Look

As you hopefully noticed in this issue of the *ESOP Report*, The ESOP Association is beginning to roll out a new look that features new, brighter colors and fonts that offer a more modern look and a faster and easier reading experience.

The new look is part of a larger effort that started in 2016. Under a program laid out by the board of directors, The Association conducted a communications audit to help assess our strengths and identify areas on which to improve.

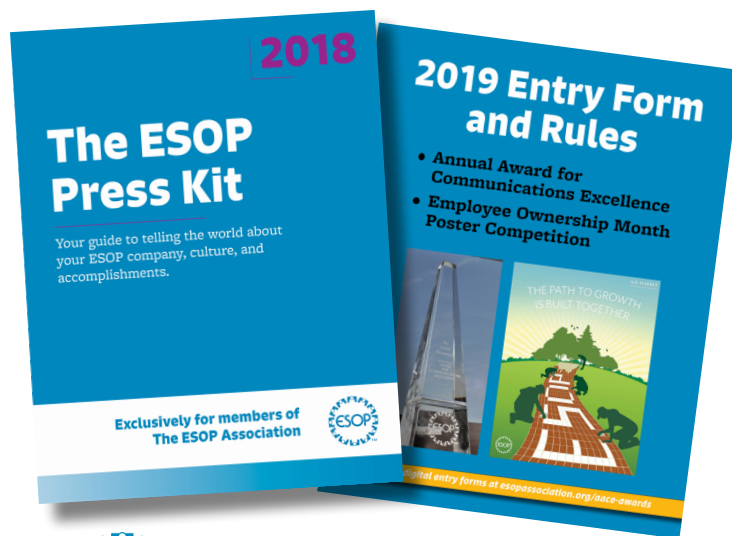
The following year, a brand audit examined The Association's overall efforts and offered suggestions for improvement.

This year, the results of those studies led to a new branding approach that we will be gradually rolling out to our members. In addition to this newsletter, other newly re-branded items include:

- Our logo, which can be found [on our website](#) and in this issue of the *ESOP Report*, and which now includes a version that combines our circular icon with the name of The Association.
- Our updated [Press Kit](#), which is available online and which helps our members communicate about their ESOP companies during Employee Ownership month and all throughout the year.
- The [rules and entry form](#) for the 2019 Annual Awards for Communication Excellence and Employee Ownership Month Poster competitions.

In time, our new branding will be expanded to include all Association materials, including our letterhead,

publications, signage, brochures, PowerPoint slides, and conference materials.



The ESOP Association

Keep any eye out for the updates as they are unveiled in the coming months.

If you have any questions or comments about our branding, please reach out to Communications Director Patrick Mirza at patrick@esopassociation.org. We would love to hear your thoughts. €

The Washington Report

Your Role in the Mid-Term Elections

By J. Michael Keeling, President, The ESOP Association

I speak to lots of members, on the phone and in person (typically at meetings held at our 18 chapters). And I frequently hear this question: “Who does The ESOP Association support in the election in [X location]?”

First, let me say that I respect these kinds of question, because the individuals who ask them want to vote for someone who will support positive ESOP law and push for more laws that encourage the creation and operation of ESOPs.

But, even though I appreciate the request, I still don't provide a straight answer. Why? Here are my five reasons

for not endorsing, even in casual conversation, any person running for office:

1. The Association—as I have emphasized recently in several columns in this newsletter—is neutral, politically speaking. We are neither pro-Republican nor pro-Democrat. This approach is in the best long term interest of The Association and the ESOP companies we serve.

2. Our ESOP PAC has a very clear cut, Board-approved policy dating back to the late 1980's and stating that we want elected officials—no matter their party—to know that we appreciate their public support of ESOPs.

3. In my experience, most people vote based on their personal views of the candidates seeking office, not on political party.

4. I frequently meet and interact with people from all walks of life, politically speaking. In some states I visit, people voted nearly two-to-one for President Trump and strongly endorse any candidate who supports the President. In other states, people voted nearly two-to-one for former Secretary of State Hillary Clinton and will endorse anyone who opposes President Trump.

5. I respect that voting is a deeply personal decision, one based on a variety of views—and that support of ESOPs is but one of the interests our members may possess.

The ESOP Association does not pressure our members to vote for any specific candidate. Voting is your right and your choice, and we believe you should vote your conscience based on the best information available to you.

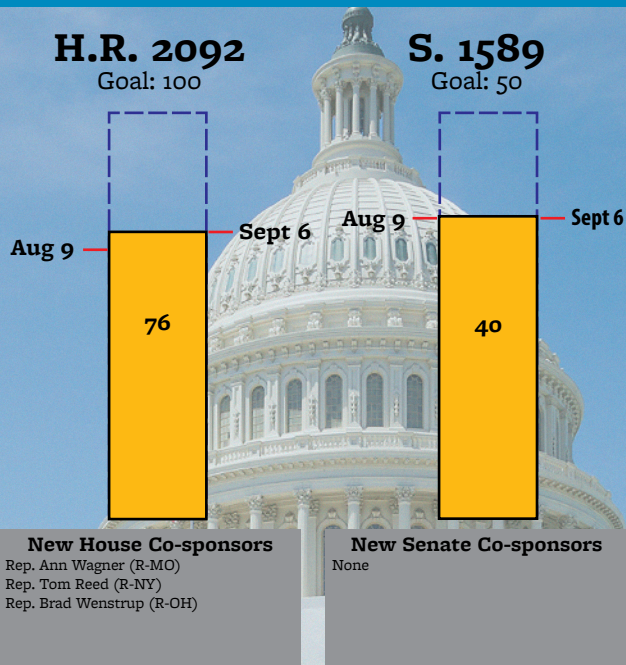
For that reason, we post on our website information—broken down by state, so it is easy to find—showing [which members of Congress support pro-ESOP laws](#). This may be only one point of data for you, but it is a data point we feel is important and should be available to you, if you wish to use it. That’s why we make a point of keeping this page ready and up-to-date.

We encourage you to use this resource as you see fit when voting.

Whomever you choose to vote for, we encourage you to interact with candidates and elected officials in your part of the country. Ask them: “What do you think about ESOPs and employee ownership?”

Many may not know what you are talking about. If so, consider that an opportunity to help educate them. Refer them to the list (on our website, listed above) of people in their party who are ESOP advocates. Send them the impressive information on the success of ESOP companies as a jobs policy, retirement savings policy, and boon for

ESOP Legislation



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company performance—all available in the [2018 Press Kit on our website](#).

Sharing your belief in ESOPs may help add a new supporter on Capitol Hill, or make a current supporter an even stronger voice for ESOPs in the next Congress.

We all want employee ownership to be available to every company, every household. And no one is a better spokesperson than you, who live the ESOP experience daily.

Whatever your political leanings or affiliations, don’t sit on the sidelines this election. Democracy, after all, is not a spectator sport.

Raise the Roof!

Don’t Wait! Register Today!

The Las Vegas ESOP Conference & Trade Show

November 8 - 9, 2018



Advisory Committee on Administration

The Mechanics of Releveraging

By Lisa A. Durham, Partner, Krieg DeVault LLP

Reviewed by Pete Prodoehl, Vice President, Principal Financial Group

You may have heard of the terms “releverage” or “repurchase loan.” The term releverage is sometimes used to encompass a partial or complete redemption of company stock from the ESOP by the company, which is then followed by the company selling the shares back to the ESOP and funding the ESOP’s purchase with an exempt loan.

However, the terms releverage and repurchase loan often are used interchangeably with a more common definition. They generally mean that an exempt loan is used to purchase shares from terminated participants or eligible diversification participants receiving payments from the ESOP.

In this article, we will discuss this more common transaction of releveraging or making a repurchase loan, which involves these steps:

- The ESOP distributes benefits (upon termination of the participant or due to diversification) to participants in the form of company stock.
- The participants must then “put” (see explanation below) the shares either to the company or the ESOP, as determined by the plan administrator.
- If to the company, the company then sells the shares back to the ESOP using an exempt loan for funding.
- If the put is to the ESOP, the company simply loans the ESOP the money to honor the put.

The Put Option

In a C corporation, participants must be allowed to take benefits in the form of company stock, and they may keep the stock or put it back to the company.

In the case of an S corporation, or a C corporation whose bylaws restrict legal and beneficial ownership of substantially all shares of company stock to active employees or to the ESOP, participants do not have the right to keep the stock that is distributed. They must immediately put it to the company or back to the ESOP, at the company’s discretion (subject to trustee approval), and either the company or the ESOP, as the case may be, issues a check for the fair market value of the put shares.

Repurchase loans are most often used by S corporation ESOPs because the participants are *required* to put the shares, thereby allowing an exempt loan to be used to purchase them. No stock certificates are issued for this put option transaction. The participant must give the trustee power to transfer the shares. (See “Documentation”

below.) In addition, payment in shares is not subject to the 20 percent mandatory withholding unless cash also is distributed with the shares.

Team Players

Because a releverage is a transaction between the company and the ESOP, it must meet certain rules to avoid being a prohibited transaction. Because the prohibited transaction rules are complicated, a releverage transaction should have the following experienced team members:

- Independent Trustee or Independent Fiduciary.
- Independent Appraiser.
- ESOP counsel (generally this is counsel to the ESOP trustee or fiduciary).

The other players in the transaction are:

- The company.
- Participants.

Requirements

An ESOP loan can be used only to purchase shares of company stock (or to repay another ESOP loan). Therefore, the stock must leave the ESOP in order to be purchased

An ESOP loan can be used only to purchase shares of company stock (or to repay another ESOP loan).

back. Distributions and diversifications may be paid in the form of company stock that is to be funded with a repurchase loan.

The following cannot be funded with a repurchase loan:

- Segregation or reshuffling does not include an actual distribution to the participant, so no stock leaves the plan. Segregations must be recycled, unless the company redeems the shares directly from the plan (requiring current valuation).
- Distributions that are paid without participant consent (e.g., involuntary cash outs of vested balances of \$5000 or less). This is because the participant must give his or her stock power to the trustee in writing to pay the distribution in company stock.


Documentation

In general, the following documents are necessary to releverage:

- Distribution forms that include a stock power section that must be completed by the distributee.

- ESOP loan documents (e.g., term note, loan agreement and/or pledge agreement) between the company and the ESOP.
- Board and committee resolutions authorizing the transaction and authorizing the trustee to enter into the transaction (if the trustee is directed).
- If the stock is put to the company, the company and trustee must enter into a stock purchase agreement to sell the shares back to the ESOP.
- In most circumstances, the trustee will require an adequate consideration opinion from the appraiser.

If the distributees' shares are recycled, instead of being handled through re-leveraging, then all shares are allocated to participants that year. With a repurchase loan, the shares are put in suspense and released over 10, 20, maybe 30 years or more.

In addition, if the distributee shares are much greater in a certain year (maybe because a highly compensated participant with a large balance is retiring), recycling may not be an option because of contribution limits. A repurchase loan does not count against Code §404 or 415 limits. 

Why Releverage?

Why do ESOP companies go to all this trouble to releverage? One reason is to slow down repurchase obligations.

This article was reviewed and approved by the Chair of the Administration Advisory Committee, Lynn H. DuBois, Partner, ESOP Law Group, LLP.

Employee Ownership Month Preparation

Are you ready to host a great month of celebration and education?

October is right around the corner—do you have your plans in place for celebrating, educating your employee owners about your ESOP, and hosting candidates and elected officials so you can gain their support for pro-ESOP legislation?

If you are a little behind, don't worry: We have plenty of tools to help you get started.

Poster. For starters, all corporate members have been sent a complimentary Employee Ownership Month poster. If you want additional posters (perhaps to hang at your various locations), you can order additional copies by using the form included in the packet mailed to you, or by [visiting the ESOP Store on our website](#).

This year's poster was designed by Julie Cressman, Roseline Bougher, Frank Dunsmore, and Rebecca Custer of A.D. Marble. Each year The Association holds an Employee Ownership Month Poster competition, which is open to all corporate members. The winning entry is selected by the five-person panel that judges the Annual Awards for Communication Excellence (AACE) competition.

To enter the competition for the 2019 Employee Ownership Month Poster, visit our website at www.esopassociation.org/aace-awards.

AACE Judges' Comments. Because many of the awards given in the AACE competition relate to events and communication efforts centered on Employee Ownership Month, there may be no better place to look for great ideas to use this October. See the [judges' comments](#) for this year (and years prior) when you visit our website.

Press Kit. If a company celebrates Employee Ownership Month and no one else hears about it, did it really take place? Putting aside the age-old question about trees and

forests, a celebration or event that isn't shared inside and outside of the ESOP community is a wasted opportunity.



For help sharing your great events with the world and telling your ESOP story, see our new and improved Press Kit. This guide is packed with new information on using social media, educating internally and externally, getting press coverage, and more. A copy of the Kit was sent out by e-mail in August, but if you didn't get yours, you won't be left out in the cold: Visit us online and search "2018 Press Kit" to [download your copy today](#).

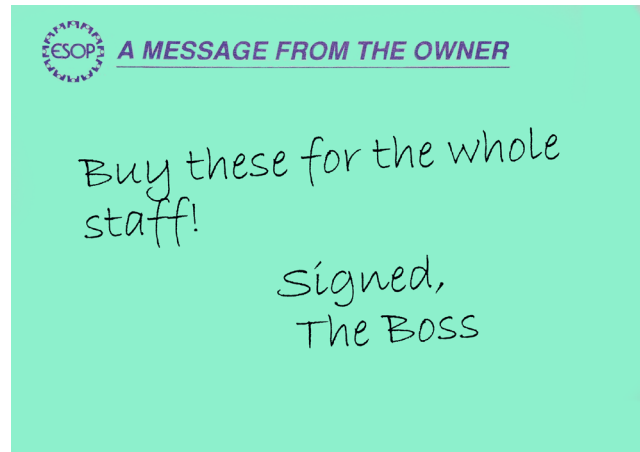
ABCs of ESOPs. As you consider ways to help your fellow employee owners deepen their understanding of your ESOP, don't forget about our online interactive training tool, the ABCs of ESOPs. Available for free to our members, this great teaching tool has multiple levels of instruction and is a fun way to help communicate some essential concepts of ESOPs. Visit our website and search "ABCs" to find this training module.

Issue Briefs. Stuck trying to figure out how to produce materials that your employee owners can keep and refer to down the road? Here's a suggestion: Stop trying. We've done it for you.


We have a host of Issue Briefs, some of which provide great introductory information for your employee owners. (Other Issue Briefs are more technical and are better suited to trustees and ESOP company executives.) Best of all, as ESOP Association members you can get copies for free!

If you have a little time before your event and want a professionally printed copy, visit the ESOP Store on our website to place an order. If you waited to the last minute and are short on time, we still have you covered: Visit us

online and search for the term "Issue Briefs" to download any of the Issue Briefs that meet your needs—just in time for that event that starts 20 minutes from now!



From the Owner notes. We all like swag. It's okay to admit it. There is a reason that the exhibitors at our [Las Vegas Conference & Trade Show](#) always have cool gadgets and trinkets at their booths—because those items grab our attention and we all like getting something for free.

The same holds true for your employee owners. So consider getting enough From the Owner sticky notes for each of them to have their own pack. (It is okay to share capital, but sticky notes are like toothbrushes—you really need to have your own.) 

Foundation News

Institute Offers Free Employee Surveys for ESOP Companies

The Rutgers University Institute for the Study of Employee Ownership and Profit Sharing—which the Employee Ownership Foundation has generously and long supported as a Founding Funder—is now offering ESOP companies a chance to get a complimentary survey of their employee owners.

The Institute is seeking to survey 10,000 employee owners; the aggregated data will update a seminal study conducted more than 25 years ago by the prestigious National Bureau of Economic Research.


That earlier study proved invaluable in showing that broad-based employee ownership is a win-win arrangement for ESOP companies, their employee owners, and our nation. It is hoped that the update of the study will prove equally valuable.

ESOP companies that participate in the study will receive results that are specific to their organizations. The only information released to the public will be aggregated data,

ensuring that employee owners' responses will remain confidential.

ESOP companies that are interested in participating are encouraged to contact ESOP Association President J. Michael Keeling at michael@esopassociation.org for additional information.

Funding academic studies and rigorous, independent research of this type is a primary function of the Foundation, which is an affiliate of The ESOP Association.

The Institute for the Study of Employee Ownership and Profit Sharing is the first organization that is affiliated with a major university and is devoted to gathering empirical research on employee ownership and ESOPs. The organization's mission and track record make it a worthy recipient for Foundation funding. (The Institute also administers the prestigious Kelso Fellowships for academics who study employee ownership, which the Foundation also funds.) 

Legal Update

How the Main Street Employee Ownership Act Should Affect ESOPs

By Lars Golumbic, Principal, Groom Law Group

Edited by: Julie Govreau, Senior VP and Chief Legal Counsel, GreatBanc Trust Company

Historically, ESOPs and ESOP-owned companies have made little use of the lending programs in place at the Small Business Administration (SBA). But that should change with recently-passed legislation designed to help ESOPs and their sponsor companies obtain and benefit from SBA loans.

The new law, which passed the House and Senate with bipartisan support, was introduced in the Senate in April 2018 by Senator Kirsten Gillibrand (D-NY) as the Main Street Employee Ownership Act. It was appended to a defense spending bill that was signed by President Trump on August 13, 2018.

The SBA, Generally

The SBA is a government agency that provides support to small businesses through various lending and development programs. Rather than lend to businesses directly, the SBA guarantees loans issued by approved lenders to encourage these lenders to loan to small businesses.

SBA loans typically have advantageous rates and low fees and can be used for a variety of purposes.

Relevant to ESOPs and ESOP sponsors, the SBA's 7(a) Loan Guaranty Program is a potential source of financing for an ESOP's acquisition of employer stock.

To qualify for an SBA loan, a business generally must, among other things:

- Be for-profit.
- Have invested equity or have reasonable equity to invest.
- Have exhausted its other financing options.
- Qualify as a "small" business.

Meeting the Small Business Criterion

To be considered a small business, a company either must meet the SBA's size standards, or its limits relating to the business's net worth divided by its net income.

Size Standard. The size standard test is industry-specific:

- In the services, retail, trade, or construction industries, qualifying businesses must average annual receipts of less than \$7 million.
- In manufacturing and mining (and similar industries) qualifying businesses must have no more than 500 employees, on average.

- In the wholesale trade industries, qualifying businesses must have no more than 100 employees.

Businesses may consult the SBA website and/or the regulations set forth in the Electronic Code of Federal Regulations (which also are accessible via the SBA's website) to determine whether they satisfy the standards for their industry. The relevant page can be found online at this location: www.sba.gov/document/support--table-size-standards.

Net Worth / Net Income Test. A business qualifies under the net worth / net income test if it has a tangible net worth of up to \$15 million and an average net income of no more than \$5 million after federal taxes over the past two full fiscal years.

Easing Restrictive Lending Rules

Historically, ESOP sponsors have not tapped the SBA's 7(a) loan programs, largely because the SBA's restrictive rules



Sen. Kirsten Gillibrand

made it challenging to do so.

For example, these rules, which have been in place since the late-1970s:

- Only allowed the SBA to loan directly to ESOPs, as opposed to the sponsor companies themselves.
- Required that ESOPs have full pass-through voting rights.
- Prevented sellers to the ESOP from maintaining an ongoing interest in the company

once an ESOP purchased a controlling interest.

The new law aims to increase the SBA's role in facilitating ESOP transactions by removing many of these restrictive rules.

A Look at the Lending Changes

One significant change is the SBA's new ability to make loans to ESOP sponsor companies that can then re-loan

to ESOPs. This change could considerably expand the potential for ESOP lending by, for example, allowing companies to pledge assets other than company stock as collateral.

As an added measure of flexibility, the law expressly states that the ESOP loan's terms and conditions (e.g., interest rates) need not match those of the SBA loan to the company. What is more, the new rules eliminate the prior requirement that the ESOP have full pass-through voting rights to qualify for an SBA loan, and no longer prevent selling shareholders from remaining involved as an officer, director, or key employee post-transaction. (Any seller who remains so involved, though, must personally guarantee the SBA loan.)

The law also now allows ESOP loans to be made via the SBA's Preferred Lenders Program (PLP). The PLP delegates loan approval, closing authority, and most service and liquidation authority to high-volume SBA lenders, and the SBA instantaneously assigns loan numbers for approved PLP loans submitted by those lenders. This enables PLP lenders to make loan decisions more rapidly, which in turn expedites the overall loan processing time.

Outreach and Education

Finally, the new law requires the provision of outreach and educational materials to small business investment funds and intermediary lenders to increase funding for


investments in, and loans to, employee-owned businesses, as well as to employee-owned businesses to inform them of SBA financing and contracting programs.

The new law also establishes the Small Business Employee Ownership and Cooperatives Promotion Program

The new rules eliminate the prior requirement that the ESOP have full pass-through voting rights to qualify for an SBA loan, and no longer prevent selling shareholders from remaining involved as an officer, director, or key employee post-transaction.

to offer technical assistance and training on the transition to employee ownership.

As part of this program, the SBA will work with small business development centers to conduct training and educational activities related to employee-owned businesses. This outreach is intended to encourage small businesses to consider employee-ownership, as well as support those that have already transitioned to the ESOP structure. The law also modifies a periodic report on the status of ESOP-owned businesses to include descriptions of these outreach efforts, as well as information about the number of ESOP loans made.

In all, the new SBA lending rules should make it easier for small businesses to acquire favorable financing to establish ESOPs for their employees. 

flag Publication Highlight

The ESOP Association Flag

Employee Ownership Month is nearly here: Are you ready to mark the occasion by flying your flag? This attractive flag is made of sturdy nylon and features The ESOP Association logo, and white lettering on a blue background. It makes a great addition to any company. Fly it next to your flag of the United States and your state.

One ESOP corporate member added an extra flag pole so they could display this flag proudly in front of their ESOP company!

Members \$68.00 / Non-Members \$500.00

Sign in to our website, www.esopassociation.org, or call (202) 293-2971 to purchase.





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