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Economic Performance Survey Results

Shift in How Rewards Are Structured, New Insights in Employee Owner Involvement in Cost Management Revealed in 2019 Study

The results of this year's Economic Performance Survey (EPS) show that, once again, companies belonging to The ESOP Association have experienced positive corporate performance. And, once again, they are sharing those gains with their employee owners.

But the 2019 version of this study does offer new insights into how well some companies performed, how responding companies structured their rewards, and how involved employee owners are in managing expenses.

A History of Strong Performance

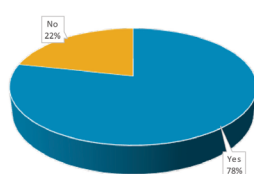
ESOPs are able to share the wealth with employee owners only if there is wealth to be shared. This year's results show that responding ESOP companies continue to perform well, generating wealth that keeps companies financially strong and that is, in turn, distributed to employees.

Of particular note: The percentage of companies reporting that profits rose 50 percent or more leaped this year from 10.6 percent to 18.9 percent—a jump of nearly 80 percent. This is the largest year-over-year increase we have seen since we started asking this question in 2016. Moreover, 18 percent is the highest percentage of companies reporting this level of profitability in our history of asking this question.

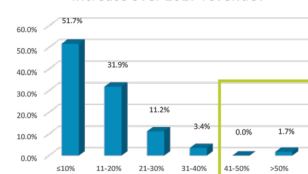
Since the EPS was launched in 2000, the majority of respondents have reported increases in profits for every year but two (2002 and 2010) and increases in revenue for every year but one (2010). The exceptions noted above

Revenue

Did revenue increase in 2018 from 2017?

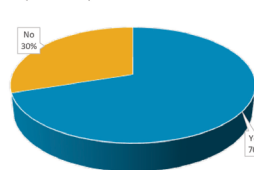


By what percentage did 2018 revenue increase over 2017 revenue?

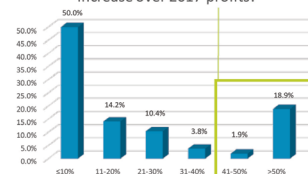


Profits

Did profitability increase in 2018 from 2017?



By what percentage did 2018 profits increase over 2017 profits?



reflect the nationwide economic downturns of the prior years (2001 and 2009). Even in those challenging economic times, 29 percent or more responding ESOP companies reported that profits and/or revenue increased.

ESOPs and Wealth Inequality

This year's results reveal a change in how corporate gains are being shared: Funds appear to have been shifted, in some measure, away from ESOP contributions and toward employee owners' salaries.

Companies responding to this year's survey offered their employee owners wage increases higher than last year's

respondents, and higher than the national average of 3.1% (as reported by [World at Work](#)).

Nearly half (48.3 percent) of the ESOP companies responding to our survey offered salaries of 3 percent. More than a third (34.6 percent) offered pay increases of 4 percent or more—substantially higher than the national average.

This suggests that ESOP companies are doing better than conventionally-owned businesses at combating wealth inequality among our nation's working population. Since this is only the second year we have asked for data on wages, these findings are preliminary.

Employee Owners as Expense Managers

Last year we reported an interesting trend: For three years, responding ESOP companies reported that profits rose at rates greater than revenue. That trend continued this year as well.

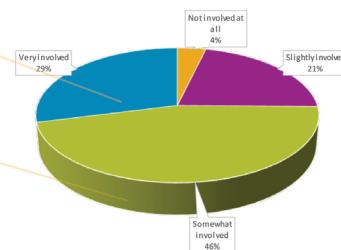
We speculated that these companies were excelling at paring costs, and that employee owners—who tend to be highly engaged in the business—might have a hand in these efforts. To delve more deeply into this issue, this year we asked respondents how involved employee owners are in managing costs. The results reveal that three out of every

Managing Expenses

This year, for the first time, we asked respondents how involved employee owners are in managing expenses.

The results show that 75% of respondents report that employee owners are Somewhat or Very Involved in managing company expenses. Employee owners appear to be helping companies wring out greater profits—and, in return, are sharing in the rewards. (See page 4.)

To what degree are your employee owners involved in managing company costs?



four employee owners are involved to a significant degree in keeping costs down.

More Information

Members of The ESOP Association can download a free copy of the [Economic Performance Survey Report](#) by visiting our website.

We wish to thank the 162 company representatives who took the time to answer the survey and to offer a glimpse into their organizations.

The Economic Performance Survey is made possible thanks to the generous support of the [Employee Ownership Foundation](#). €

ESOP Report

The Voice of The ESOP Association

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Cindy Turcot Elected Foundation Chair

Established ESOP Champion Will Succeed Mark Lomele

The Employee Ownership Foundation (EOF) has elected a new Board Chair—longstanding employee ownership leader Cindy Turcot.

Turcot is the president of Gardener's Supply Company, a 100 percent employee owned business based in Burlington, VT. She has served on the Foundation's Board of Trustees since 2005 and is a past Board Chair of The ESOP Association.

"This is a very exciting time for employee ownership and I am thrilled to be stepping back into a leadership role at the Foundation," said Turcot. "At Gardener's Supply Company, becoming 100 percent employee owned has permanently changed the lives of our employee owners for the better. I can't wait to start working with the rest of the

Foundation Board to make sure others receive the same opportunity to become owners where they work.”

“I am thrilled to welcome Cindy, who brings tremendous energy, experience and a passion for the Foundation’s central mission of growing the number of Americans who own a stake in the place where they work,” said James J. Bonham, Foundation President. “Cindy is a person who not only has vision but puts her shoulder down and does the hard work, too.”

Turcot takes over as Chair from Mark Lomele, who has served in the role since 2015. Typically, the EOF Chair is limited to serving no longer than two terms, or four years. Lomele, who retired from a 30-year career with California based Recology, Inc. in 2018, will continue to serve as a member of the EOF Executive Committee. Last year, Lomele was recognized with the Life Service Award by The ESOP Association for his contributions to the employee ownership community.

Since its founding in 1991, the Employee Ownership Foundation has operated in pursuit of a single overarching goal: to help more individuals become employee owners.

The Foundation has raised and donated millions of dollars to collect data used by academics, encourage objective research, and to facilitate dialogue about employee ownership between thought leaders.

Going forward, the Foundation will also place a larger emphasis on raising awareness of the employee ownership model among business owners and on funding more applied



research that can further improve the market advantage held by well-run employee owned businesses. [E](#)

Employee Owned 2019 Ready for Launch

Final Details Are Rounding into Shape for the Premiere Education and Networking Event for Employee Owned Companies

In only a few weeks, the biggest event in the employee ownership community will take place—[Employee Owned 2019](#). There are many exciting additions and details being finalized for this event, so here is a quick rundown of all the latest news and updates that you will want to know about.

Innovation Stage Schedule

The schedule for the Innovation Stage—the new area in the center of the Trade Show where attendees can hear presentations from Corporate and Professional members—has attracted great interest and is nearly full.

As a result, attendees will have a host of new options for listening to content and gathering insights from a variety of individuals in the employee ownership community.

The current roster of presenters for the Innovation Stage includes:

Katharine Manning will offer five tips on listening to victims of trauma in a way that is both compassionate and effective.

ESOP Economics will offer a live demonstration of the company’s repurchase obligation software.

Ginny Vanderslice will discuss the ESOP CEO Leadership Program, which is offered by the University of Pennsylvania and supported by the Employee Ownership Foundation.

Blue Ridge ESOP Associates will offer a presentation about its customized 20-year Repurchase Obligation Studies.

ProAct, Inc.—the country’s only employee owned Pharmacy Benefit Manager—will discuss managing pharmacy costs and benefits.

Jay Vincent will discuss using a modern approach to external affairs to achieve better outcomes in the communities where businesses operate.

Welcome Reception

New this year, the conference will start off with a bang at the Wednesday evening welcoming reception. Come register for the conference and get a head start on meeting old friends and making new ones as you network away. The reception takes place from 4:00 to 6:00 PM—leaving plenty of time afterwards for you to schedule a business meeting, have dinner with colleagues, take in a show, or try your luck on a game of chance.

Don't miss it! This reception promises to be a lot of fun and should include a fun surprise or two.

Schedule for Chief Executive Sessions

The schedule for the first ever Chief Executive Sessions has been released and features exclusive presentations from the conference's three keynote speakers (see below), as well as additional experts speaking on a variety of leading-edge business topics. For a full and up-to-date description of speakers and topics, see the [Chief Executive Sessions](#) page for the [Employee Owned 2019](#) conference.

The first ever Chief Executive Sessions are fast filling up, with more than 110 ESOP company CEOs and presidents already signed up.

Three Keynoters

This year's Las Vegas conference features three world-class keynote speakers who have been chosen specifically for the way their expertise meshes with the needs of ESOP companies.

Sekou Andrews will help you find and tap your poetic voice to be a genuine, powerful, and persuasive speaker—one who inspires others to action. All employee owners—especially those in the C-suite and on Employee Ownership Committees—will benefit from finding more powerful ways to express their passion for employee ownership to customers, job applicants, and elected officials.

Seth Mattison will help you adapt to the world's lightning-fast digital transformation so you and your fellow employee owners can be more agile, innovative, and customer focused. Getting on the cutting edge of this essential evolution will help your business find a new competitive edge—one all employee owners can engage in and benefit from.

Erica Dhawan will show you how to unlock the power of your connections to increase share value and drive elite performance. Wouldn't any employee owned company want to learn about strengthening human connections and maximizing return for shareholders? [E](#)

A Special Evening for Employee Owners

Foundation Fundraiser in Las Vegas Will Help Pave the Way for Exciting New Initiatives Aimed at Boosting Employee Ownership

Next month, during the Employee Owned 2019 Conference and Trade Show in Las Vegas, a very special event will be held to support a potential new wave of growth in employee ownership. Thursday evening, more than 500 employee owners and professionals are expected to gather with Trustees and major donors of the [Employee Ownership Foundation](#) (EOF) at the Eiffel Tower restaurant to celebrate the start of an exciting new initiative.

The focus for the evening: The *new* roaring 20's—the 2020's—and the opportunity to exponentially grow employee ownership during the coming decade. The evening will mark the beginning of a determined effort to convert millions of businesses, currently owned by Baby Boomers, into employee-owned enterprises.

Doors will open at 7:30 pm for a cocktail and dessert reception high above the Las Vegas strip. Attendees will be treated to live entertainment and the best view in town of the iconic Bellagio Fountain Show.



In the next 10 years, more than 1.7 million privately held businesses will need a succession plan as their founders and owners prepare for retirement and the crucial decision of how to sell their businesses. Known as the "Silver Tsunami," this retirement bulge has caught the imagination and attention of leaders in the employee ownership community, as well as the lawmakers who support

ESOPs. This wave of retirements is an obvious opportunity to create more job and economic security for millions of Americans. This is a one-time opportunity to catalyze a new wave of ESOP formations, and the EOF is preparing to seize that opportunity.

This first-ever evening reception in Las Vegas supporting the Foundation is sure to become a mainstay of the Las Vegas conference experience. Tickets can be purchased in advance through the [EOF website](#), at the conference registration, or at the EOF booth in the conference exhibit hall.

As a 501(c)(3) charitable organization, contributions are tax deductible. Venue space is limited, so those wishing to



Employee owners at ESOP Association member Proponent hosted Rep. Gilbert Cisneros (D-CA-39) at their Brea, CA facility on Oct. 9. Two days later, Rep. Cisneros supported pro-ESOP legislation for the first time, co-sponsoring H.R. 2258. Rep. Cisneros is in the center, with a white shirt and jacket.

be part of this important evening are encouraged to secure a ticket early.

Through its nearly three decades of operation, EOF has advanced its mission to educate and grow employee ownership by funding rigorous, independent academic research and by increasing the number of university scholars interested in studying employee ownership. By also funding and providing logistical support for data collection, the EOF has been instrumental in establishing the availability of critical research inputs for ongoing research for years to come.

Moving into the next decade, the EOF will continue its vigorous support of research for employee ownership as a model for business. But the retirement of millions of

Baby Boomers mandates a more diversified agenda with an increased focus on the active recruitment of these businesses into ESOP formation. Using the most cutting-edge digital marketing techniques, combined with business and consumer marketing data, EOF is making plans to specifically target these business owners with advertising, outreach, and education efforts.

All too often, selling a business to employees is not presented as a serious option, or is not considered at all because close advisors, sometimes with limited depth of understanding, dissuade owners or clients. The EOF's mission is dedicated to raising awareness and educating Americans about the economic, societal, and individual merits of employee ownership. [E](#)

Ownership Advantage

Creating an Impactful ESOP Communication Committee

By Jason Wellman, Senior Relationship Consultant, ESOP Partners

E SOP Communication Committees are critical for ESOP companies to move forward with an ownership culture. Members of committees do more than just plan company cookouts and celebrate Employee Ownership Month through games. They focus on providing proactive educational materials so ESOP participants become advocates for this unique benefit. I have been asked numerous times during round table discussions and in conversations with ESOP companies: “How can I create an impactful ESOP Communication Committee?”

The first item of business is making sure your committee has an updated charter. The charter should be reviewed

annually and should provide guidelines and principals for the committee chair and members to ensure they're meeting and exceeding the expectations of senior managers and the board of directors.

The charter should provide a mission statement and eligibility requirements for committee members, along with a general outline of expectations.

Once you have completed your charter, start the application process for committee members. Send an invitation—perhaps in video form—explaining the mission statement of the ESOP Communication Committee. Include a link to an application.

The invitation message should be direct and upbeat about the committee's vision because new members—through their work on the committee—can help create many ESOP advocates among their fellow employee owners.

Committee members should be held to a term limit. I have seen term limits anywhere from one year to eight years. Committee members should be at different stages within their ESOP life cycle and should be from different departments (and locations) throughout the organization.

Place an additional limit on committee participation: Allow only one committee member per department. This way your committee will have representatives from multiple departments throughout the company.

Once you receive your applications for prospective committee members, have the committee chair and the outgoing committee members review the applications. Once the reviews are complete, nominate the prospective committee members who align with the committee's mission statement and hold an election.

I have seen companies go all out with these elections, with campaign posters and open forums where candidates tell their fellow ESOP participants about their passion for employee ownership.

Once the ESOP Communication Committee has been formed through the election process, the real work begins. All committee meetings should have a set calendar of action items for the next 12 months. Each action item should be focused on meeting the committee's mission statement.

The calendar also should include at least four touchpoints throughout the year, at which time results can be reviewed with management.

Ideally, committee meetings should be held monthly. But quarterly meetings can work well too if your company has only a few annual activities on which to focus. All meetings

should have an agenda with minutes. Meeting minutes should be provided to senior management to keep them up to date on the annual calendar and action items.

Feedback after events will be critical to ensure that your ESOP-related messages are truly impacting your company's participants. Many companies use SurveyMonkey with six or fewer questions to solicit this information. If completing this type of survey is too difficult initially, start with a survey that is conducted annually. This can be held before the application process and can help to ensure your committee is creating meaningful materials and events for your company's ESOP participants.

Your company can and will have an impactful ESOP Communication Committee with this annual process, but it will not be easy. Maintain your focus on achieving your ESOP Communication Committee's mission statement in everything you do throughout the year. Also, do not be afraid to try something new—especially if you are challenging your ESOP participants to learn more about your company's ESOP plan.

I am 100 percent certain that if I talked to all the owners who have successfully created and sustained an ownership culture, they would say it was worth the effort. I'm also 100 percent certain the employees would say the same thing. €

Calendar of Deadlines and Important Dates

Oct. 1-31 [Employee Ownership Month](#)

Nov. 13-15 [Employee Owned 2019, the Conference and Trade Show for ESOPs](#)

Dec. 1-4 [Leading in an Ownership Setting](#)

Feb. 6-7 [ESOP Professionals' Forum](#)

May 20-22 [National Conference](#)

To see the full list of ESOP Association meetings, visit us online at: www.esopassociation.org.

At Miklos, an ESOP Runs Through It

Ownership Culture Is Central for 2019 ESOP Company of the Year

At Miklos Systems Inc., the 2019 ESOP Company of the Year, an ESOP is more than just an employee benefit: It is an extension of the management style established by founder Betsy Miklos, a core part of the culture, and a key to the company's competitive advantage.

What effect does a strong ownership culture have on the business? "That's why we've been here for 25 years," says President & CEO Roland Burdett, III.

Burdett has personally seen most of that longevity in person, having joined the company more than 24 years ago. "I'm employee number two," he says with a laugh.

Employee number three is Beth Dyer, the current chair of the Employee Ownership Committee (EOC). The culture

may have kept the company going, but it encouraged Dyer to stay put. "It's the reason I'm still here, almost 25 years later," she says.

That kind of longevity is impressive for just about any business, but perhaps more so for a company in the federal contracting space.

Creating Connections

Miklos is a technology contractor that provides software development, systems engineering, and project management services to clients primarily in the federal government. It is the nature of the business that employee owners work at



Employee owners at Miklos Systems Inc. receive the award for ESOP Company of the Year during the awards ceremony at the National Conference.

their clients' offices; Miklos employees work in teams that are as small as one or two and as large as eight.

Since a widely dispersed workforce has few naturally occurring opportunities to interact, it can be challenging to build and maintain a strong corporate culture.

It is a challenge Miklos does not shy away from. The company offers opportunities to interact that are both regular and varied. Each month Miklos holds a meeting of the whole company (which is approaching 50 people) or sets up lunch gatherings at rotating locations and times. The meetings are designed to make it convenient for employee owners to attend at times and locations that fit their schedules.

Meetings typically have two parts—one designed to address employees as employees, and one designed to address them as owners. The first segment might include information on benefits, forms, or new contracts. The second part might include financial information presented in an open book format, or discussions of the company's future path.

The goal: "Every meeting, you should walk out knowing 'I'm an employee owner of the company,'" says Burdett.

Dyer says that meeting invitations are handled online, and all employee owners can see who plans to attend. She believes this helps spur participation because employee owners sometimes make a point of attending so they can ask a specific colleague for help with a technical challenge.

In-person gatherings are supplemented with regular digital interactions. The company shares information and news via a SharePoint site, and sends out lots of e-mail updates.

If You Build It, They Will Come

While regular interactions are great for maintaining a strong corporate culture, Miklos doesn't rely on them to build the culture. To accomplish that, the company has implemented a complete education system that starts when individuals first come into contact with the business.

Applicants learn about the ESOP and the ownership culture in their first conversations with a recruiter, and again in interviews with Burdett, who discusses how the

"The ESOP is a way to keep everyone connected, from an employee point of view, and from a customer point of view it really has contributed to our great reputation out there because everyone is pulling together."

**—Roland Burdett, III
President and CEO**

ESOP and culture influence the company. Applicants also receive a document written by the EOC that describes the ESOP and what it means.

Once they are hired, Burdett takes new employee owners out to lunch; the topic of the ESOP is sure to be covered.

New hires also attend a series of training sessions, described as ESOP 101, 201, and 301. The courses are taught by members of the EOC, and a member of the C-suite attends to answer questions. "It is very interactive," says Dyer, who adds that the interpersonal approach enables EOC members to get a sense for who is grasping the information and who might need additional help.

The ESOP “absolutely is a huge part of our recruiting process,” says Burdett. “It’s there from the start, in everything we talk about.”

Pay to Play

Like any contractor, billable hours are key to Miklos’ success. To underscore that point, the company offers a bonus based on the number of billable hours employees accrue.

And to underscore the importance of the ESOP, any time spent at company meetings is included in those billable hours for purposes of the bonus.

When Burdett explained that to a new employee over lunch recently, she understood the significance right away. “Oh, I get it,” she said, “you want me helping both the customer and the company all the time.”

Miklos’ willingness to put its money where its mouth is extends to EOC as well, which has a budget for carrying out its mission. Says Burdett: “If the company is going to ask you to do it and the company thinks it is important, then the company ought to be paying for it.”

Once a budget has been set for an ESOP committee, he adds, executives should avoid micromanaging—just get out of the group’s way and let its members do their job.

Benefits for the Business

The time, energy, and money Miklos invests in its ESOP and ownership culture are paying worthwhile dividends. For example, the company covers snow days for its employee

owners: If the federal government closes, Miklos closes too. (“I don’t want people to get out on the road and have accidents,” says Burdett.) But employee owners are encouraged to make up the lost billable hours, if they can.

A few years ago, a heavy snow storm caused the company to lose an entire week’s worth of billable hours. Over the remainder of the quarter, the employee owners made up nearly 70 percent of those lost hours.


Miklos tells customers about its ESOP, and sees a benefit there too. “Even when the customer doesn’t understand the whole ESOP culture, they see the teamwork that we have... and they like that,” says Dyer.

“The ESOP is a way to keep everyone connected from an employee point of view,” says Burdett, “and from a customer point of view it really has contributed to our great reputation out there because everyone is pulling together.”

The teamwork and collaborative spirit the company has built also give it a competitive advantage when it comes to attracting and retaining employees. The company excels at moving employee owners to situations where they can be happy and can succeed. Knowing that the company is looking out for their well being makes a big difference to employee owners, says Dyer.

In comparison, when the company hears about its competitors, it is told that employees there feel like they get a paycheck—nothing more.

“A lot of government contractors hire for the contract and, because we are an ESOP, we hire for the company,” says Burdett. “We want people to stay here.”

If the tenures of Burdett and Dyer are any indication, Miklos has certainly succeeded. 

Advisory Committee on Administration

DOL Ramps Up Scrutiny Regarding Missing Plan Participants

By Kjersti Cory, Senior Vice President, GreatBanc Trust Company

Reviewed by Lynn Archer, Esq., Senior Vice President, GreatBanc Trust Company

It is not uncommon for ESOP participants to be non-responsive or impossible to locate when it’s time to make ESOP distributions. One common reason is that ESOP plans typically have a waiting period that must pass before participants who leave the company are eligible to receive distributions. Often, this waiting period is a minimum of one year and could be as long as five years.

During this time, participants may move, pass away, or forget that they are owed a distribution.

The U.S. Department of Labor (DOL) is increasingly scrutinizing plans that have “missing” participants. DOL conducted a pilot program out of its Philadelphia office by reviewing Forms 5500 for plans with a high number of terminated participants who had not received payments.

When the DOL attempted to contact these “missing” participants they were able to locate a number of them. Because of the success of the Philadelphia program, the DOL is now making this a national initiative. The agency intends to monitor plan fiduciaries’ attempts to locate missing participants; failure to locate or contact participants may be considered a breach of fiduciary duty under ERISA, as amended.

In 2014, the DOL provided guidance related to locating missing participants in terminating plans in Field Assistance Bulletin 2014-01. While these steps apply only to terminating plans, many Plan Sponsors have adopted these search methods to locate missing participants in active plans. The steps include:

- Using certified mail.
- Checking related plan records.
- Checking with beneficiaries.
- Using free electronic search tools.

In addition to the DOL guidance, the IRS issued a memorandum on October 19, 2017 pertaining to missing participants and Required Minimum Distributions. The guidance explained what steps a plan sponsor should take to locate missing participants in order to avoid challenge by the IRS. These steps include:

- Using certified mail.
- Searching related plan, sponsor, and publicly available records for alternative contact information.
- Using a commercial locator service, credit reporting agency, or a proprietary Internet search tool.

It is not clear if the DOL will consider these search methods as “adequate” when trying to locate missing participants. Until new guidance regarding locating missing participants is available, the DOL has said that plan sponsors should undertake the following steps:

- Contacting by phone (since many people keep the same cell phone number).

- Using certified mail.
- Keeping good records of terminated participants.
- Contacting co-workers to see if they know how to get in touch with terminated participants.

Plan sponsors should check their ESOP Plan Document as it may contain a provision regarding steps to take when locating missing participants. It is important to keep good records of attempts to contact participants; doing so can head off scrutiny from the DOL if the agency should audit your plan.

You also may want to check with your Third-Party Administrator, since many of these firms have tools to help search for missing participants.

Finally, upon retirement or termination, it is helpful to stress to former employees the importance of keeping their contact information current with the Plan Sponsor. This simple conversation can be an important step in keeping track of them.

This article was reviewed and approved by the Chair of the Administration Advisory Committee, Dolores Lawrence, Managing Director at Blue Ridge ESOP Associates. 

Washington Report

ESOP Enforcement: New Rules for the DOL

By James J. Bonham, President and CEO, The ESOP Association

For the last decade it has been a stated priority of the Department of Labor (DOL) to aggressively investigate ESOPs and the companies that form them. Along the way, the agency has pursued numerous enforcement actions—ranging from settlement agreements to full prosecution of cases—in which DOL alleged that companies sold shares to ESOPs at prices that were too high.

As the watchdog protecting employee owners, it is not unreasonable to expect DOL to keep an eye out for unusually high company valuations. That is, after all, *part* of their job. But DOL is not just an enforcement agency, it is also a regulating agency. As such, the DOL is obligated to clearly state what the rules are.

In the 45 years since the Employee Retirement Income Security Act was signed into law, the agency has failed to issue any regulations showing companies who operate in good faith *how* to value their shares.

Two new Executive Orders (EOs) signed this month by President Trump have both good news and bad news for the ESOP community when it comes to DOL regulation and enforcement actions. One EO may limit the DOL’s ability to pursue legal action without first issuing the kind of regulatory guidance our community desires. But the other

EO, issued at the same time, may make it more difficult for the agency to issue the clear guidance that is needed.

The two EOs apply to all Federal Agencies—not just DOL—and are titled the *Executive Order on Promoting the Rule of Law Through Transparency and Fairness in Civil Administrative Enforcement and Adjudication* and the *Executive Order on Promoting the Rule of Law Through Improved Agency Guidance Documents*.

Transparency Order

The first EO requires federal agencies to “establish a violation of law by applying statutes or regulations.” This would seem to limit the DOL’s enforcement in the absence of regulations, which of course would be welcome news to companies, trustees, and founders who feel unfairly persecuted for their good faith efforts to properly value company shares.

The EO places other limitations on agencies as well.

Agencies can apply standards of conduct only after they have been publicly stated in a way that would not cause “unfair surprise”—which the order defines as a position or policy that does not provide reasonable certainty or fair warning of what the agency required.

Further, agencies must publish guidance documents in advance in the *Federal Register* or in the searchable database on their websites if they wish to cite them in enforcement actions or adjudications. In the event a document or rule arises out of litigation—as has been the case in a few instances related to ESOPs—an agency must explain the implications of that document when it is published.

The EO includes other helpful elements, including the chance to be heard and to contest findings *before* an agency takes any action that may have legal consequences; the establishment of procedures for administrative inspections and the establishment of investigation control numbers; and a system of self-reporting in exchange for reduced penalties.

Guidance Order

The second EO appears to attempt to make it more difficult for agencies to issue rules or regulations without substantial political and procedural oversight. The EO states that agencies “may impose legally binding requirements on the public only through regulations and on parties on a case-by-case basis through adjudications, and only after appropriate process, except as authorized by law...”

The order imposes these new procedural requirements on agencies issuing certain guidance documents:

- Existing sub-regulatory guidance must be reviewed by the Office of Management and Budget.
- Guidance documents that agencies want to keep must be included in one searchable, indexed database on their websites.

Other new procedures basically will give the public a chance to comment before new rules take effect. As a result, in the event DOL begins to issue guidance documents, ESOP companies will have more opportunity to petition DOL to make changes or remove specific draft guidance documents.

The new requirements do not appear to apply to written agency responses to inquiries concerning compliance, which

likely includes EBSA Advisory Opinions or IRS Private Letter Rulings.


Impact on ESOP Enforcement

Although the full impact of these new EOs remains to be seen, they could result in changes to DOL’s enforcement positions, particularly those related to valuation practices. The language relating to “unfair surprises” in the first EO seems tailor-made for the ESOP community and should limit DOL’s ability to pursue companies without first issuing regulations.

On the other hand, the second EO may make it harder for DOL to issue helpful guidance with respect to ESOPs. Although Advisory Opinions do not appear to be affected by the new procedural requirements, the order does limit DOL’s ability to issue broadly applicable sub-regulatory guidance, including Field Assistance Bulletins and Information Letters. Historically, DOL has used that type of guidance to help inform plan sponsors, plan fiduciaries, and plan service providers on how to interpret ERISA.

DOL’s enforcement division would argue their actions for the last decade have been pro-employee, not anti-ESOP. Their view is that by pursuing an action, they are fulfilling their responsibilities to protect the retirement accounts of employees.

However, the travesty is that these actions—especially when taken without the context of regulatory and procedural clarity—have chilled the formation of new ESOPs, thereby denying potentially millions of Americans of greater economic and retirement security.

The DOL touts the money it has “recovered” from enforcement actions as evidence of its good work. Unfortunately, those numbers fail to tell the stories of the millions of American families who were never given the opportunity to own shares in the companies where they work, because the founders dismissed forming an ESOP for fear of a fickle investigatory risk down the road. 

Legal Update

How Labor Department Changes Might Affect ESOPs

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Recent and significant changes at the U.S. Department of Labor (DOL) could have an effect on ESOP enforcement. The changes: Eugene Scalia succeeded Alexander Acosta as the new Secretary of Labor, and the Employee Benefits Security Administration (EBSA)—the agency within the DOL that is tasked with regulating ESOPs—is being reorganized.

Secretary Scalia’s Background

Eugene Scalia, age 56, is the son of late U.S. Supreme Court Justice Antonin Scalia. Formerly, he focused on labor, employment, and ERISA litigation as a partner in a large corporate law firm. In that role, he represented employers

and was a member of a team representing the U.S. Chamber of Commerce, the Securities Industry, the Financial Markets Association, and other groups in successful challenges to the DOL's fiduciary rule.

In 1992 and early 1993, Scalia was Special Assistant to the Attorney General. In 2001, Scalia was Acting Solicitor of Labor, and from January 2002 to January 2003, he was the Solicitor of Labor. The Solicitor is the legal officer responsible for all DOL litigation and legal advice on administrative law and rule making.

Scalia has experience with cases involving ESOPs.

As Acting Solicitor of Labor, he—along with the Solicitor General of the United States—submitted a brief that successfully opposed review by the U.S. Supreme Court of a case in which the lower courts found that an ESOP had overpaid for company stock.

As Solicitor of Labor, he and the Solicitor General, successfully opposed review by the U.S. Supreme Court of a case involving ERISA preemption of state law claims for breach of fiduciary duty relating to the sale of shares to an ESOP in a leveraged buyout.

With Timothy Hauser, then Associate Solicitor of the DOL Plan Benefits Security Division (PBSD), Scalia, as Solicitor of Labor, submitted a brief opposing the dismissal of a case brought by Enron workers who alleged that their retirement accounts (including an ESOP) lost millions of dollars when Enron collapsed in a wave of accounting scandals.

The Reorganization of EBSA

In 2017, Preston Rutledge was nominated by President Trump and confirmed by the Senate as Assistant Secretary of Labor for EBSA. Before joining the DOL, Rutledge served as senior tax and benefits counsel on the Majority Tax Staff of the U.S. Senate Finance Committee.

Jeanne Klinefelter Wilson was appointed by President Trump as EBSA's Deputy Assistant Secretary for Policy in 2017, and in May 2019 was named EBSA's Principal Deputy Assistant Secretary. Wilson is the first in line of succession to Assistant Secretary Rutledge, and as stated on the DOL's website, "is the Assistant Secretary's alter ego and principal advisor." Before her appointment, she served as counsel to plan sponsors and fiduciaries for more than 15 years.

Timothy Hauser joined the DOL in 1991 as a trial attorney for the PBSD, representing the DOL in federal district court and appellate litigation. In 2000, he became the Associate Solicitor of PBSD, responsible for all of the DOL's legal work under ERISA. In 2013, he became the Deputy Assistant Secretary for National Office Operations, the COO of EBSA.

In late August, 2019, Assistant Secretary Rutledge e-mailed EBSA staff announcing that effective October 1, 2019, EBSA would be reorganized. A key change is that there are now three, rather than two, deputy assistant secretaries who report directly to him. The reorganization will result in Deputy Assistant Secretary Wilson, a political appointee, taking on oversight of the Office of Exemption

Determinations as well as the Office of Regulations and Interpretations. These are core regulatory oversight functions that had been performed by Hauser, a career staffer, not a political appointee.

Under the reorganization, Hauser will take on the role of Deputy Assistant for the National Office and have oversight for the Office of Enforcement, the Office of Technology and Information Services, and the Office of Outreach, Education, and Assistance. The third Deputy Assistant Secretary will be a career staffer and will oversee EBSA's 10 regional offices.

Potential Impact of These Developments on ESOPs


ESOP companies wonder whether these changes will result in the DOL relaxing the aggressive enforcement activities it has pursued against ESOPs for more than a decade. This remains to be seen. Secretary Scalia was a pro-business lawyer in private practice who opposed regulations, but when he previously served in the DOL, he advocated against plan sponsor companies and ERISA/ESOP fiduciaries who allegedly breached their duties to ERISA plans and ESOPs.

Under the reorganization, responsibility for rule-making oversight will be put into the hands of Wilson. An amended fiduciary rule is expected to be released in the near future, and this release now will be under the auspices of Wilson rather than Hauser. There has been some speculation that the reorganization was initiated partly because the DOL was not meeting the goal of President Trump's Administration to provide faster-paced guidance and regulations.

Hauser, who has aggressively pursued investigations and litigation against ESOP companies and fiduciaries, retains responsibility for the Office of Enforcement. It will be interesting to see if the creation of the third Deputy Assistant Secretary position will result in more uniformity in enforcement activities at the regional level. Historically, regional directors have had broad discretion in deciding whether to pursue investigations, and regional offices have operated somewhat autonomously.

If the enforcement agenda is set by the National Office and remains consistent with the past agenda implemented by Hauser, it is possible that regional enforcement will become more uniformly aggressive.

Since ERISA was enacted in 1974, there have been few regulations put into effect on important issues relating to ESOPs. A proposed regulation on valuation introduced in 1988 was never issued.

For many years, the ESOP community hoped that the DOL would introduce constructive regulations and provide guidance to ESOP companies, their fiduciaries, and advisors that would make compliance easier by fostering a more predictable regulatory environment. The hope was that the DOL would make its expectations clear and regulate by regulation, rather than by litigation. The reorganization of EBSA has this potential, and this would be welcomed by the ESOP community. 



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