



Ronald J. Gilbert

President

An ESOP Bill to Love!

“Louis Kelso would love Senator Ron Johnson’s proposed ESOP grant program. I worked for Louis Kelso, the father of the ESOP, and I do love it”

Kelso’s original intent was to provide workers with access to capital in the form of company stock. Senator Johnson’s bill, cosponsored by Senator Tammy Baldwin, would provide much needed capital NOW (a grant of \$20,000 per employee-ESOP participant and up to \$50,000 to cover some of the transactions costs) for companies that have or start a new ESOP. It is a game changer for the economy and for employee ownership!

Precedent

Precedent exists for this ESOP legislation. Senator Russell Long (D Louisiana) the legislative father of the ESOP, (who would love the bill too) was the driving force behind almost all of the early ESOP tax incentives, including the TRASOP, enacted in 1975, which was a tax credit ESOP designed to encourage the purchase of qualified property, mainly equipment and machinery. (A tax credit is the equivalent of a grant.) Now as then, ESOPs have strong bipartisan support in both the Senate and the House (Bipartisan support for any legislation is very rare nowadays).

The Enemy of the Good is the Perfect

Is the initial language perfect? No. (Which is true of all proposed legislation.)

Are some modifications or clarifications necessary to allow it to reach its full potential?

OF COURSE! Will the final version be perfect? No, but it can be better. A few thoughts.

Modifications/Clarifications Needed

Include 100% ESOP-owned Companies

Most privately-owned ESOP companies are 100% ESOP-owned. The bill appears to exclude them. They should not be locked out of a program that would apply to other 99% or less ESOP-owned companies. Grant money would increase the value of the ESOP participants’ account in a 100% ESOP in a similar manner as a partially owned ESOP.

Expand the Use of the Grant

Service companies need an expanded definition of eligible uses of the grant money. Adding health insurance, other health and welfare related expenses, and training, would go a long way to enable service companies to use the full amount of the grant, and make it easier to hire new employees.

A New Independent Valuation Requirement Is Not Necessary

There are very robust and well-defined valuation procedures and protections for ESOPs, with extensive guidance from the Department of Labor, for use by independent valuation firms and trustees to determine fair market value for ESOPs. The bill's current language should clarify reliance on established procedures for determining FMV in ESOP transactions.

New Jobs

An indirect result of the ESOP grants will be more jobs. The company that invests in new equipment or expands its facilities will be able to be more competitive, win new business, and need to hire more employees. One of our client's anticipates adding 45 employees, a 15% increase, once the grant money is invested in needed equipment and training.

Put a Ceiling on the Grants

In order to ensure that the money is used by companies that are truly small or mid-size, and that there is enough to go around, the grants should have a stated maximum. 75% of ESOP companies have 500 or less employees.

"Second Income" Plan

Kelso envisioned a second dividend income for all workers. Now is the perfect time to implement an ESOP dividend plan that numerous studies show can be very effective.

A small percentage of the grant money should be eligible for dividend payments, paid out through the ESOP to ESOP participants, subject to board of director approval. To facilitate this, additional legislative language would be required that would exempt an S corporation dividend, paid in cash to an ESOP participant, from the 10% excise tax applied to early distributions, which is the current IRS position. (C corporation dividends are not subject to the 10% excise tax.) Because the dividend is subject to ordinary income tax, paying a S corporation dividend is a "revenue raiser" for the federal government. Many of our ESOP clients would pay dividends to their ESOP participants immediately if this additional 10% tax were to be removed. What a great way to get some additional cash in to the hands of ESOP participants when it is needed the most!

Conclusion

The fundamental principal of Senator Johnson's bill, immediate access to capital for ESOP companies, is perfectly timed, true to the fundamental principles envisioned by Kelso and Long and should be an essential part of any new stimulus legislation.

Thanks to my colleagues Paige Ryan and David Binns and other anonymous contributors.

Ron

