## SMC MEMBERS' ISSUES

# EMPLOYEE OWNERSHIP BILLS GAIN MOMENTUM

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Two bills have been recently introduced in the United States Congress to promote employee ownership to perpetuate American businesses and provide retirement security to the American workforce. Both H.R. 2096 and S. 1212 bills are titled "Promotion and Expansion of Private Employee Ownership Act of 2015" and aim to enhance the already significant tax-advantages of Employee Stock Ownership Plans (ESOPs).

**Employee Stock Ownership Plan (ESOP):**

An ESOP is a tax-qualified retirement benefit plan that provides an immediate buyer of company stock at fair market value for owners desiring liquidity with many personal and corporate tax advantages while providing significant retirement benefits to all eligible employees. ESOPs allow a selling shareholder to indefinitely defer federal capital gains taxes on the sale of stock, provides a 100% corporate deduction of the value of the stock sold, may result in corporate profits being 100% federal and state income tax exempt, does not disturb corporate control and keeps the business in the family or with key management who generally can't buy the business on their own.

**How an ESOP works:**

Typically, the ESOP borrows funds from a bank and/or the seller takes back a note. The company makes tax-deductible contributions to the ESOP which uses the funds to repay the loan incurred to buy the stock. The shares purchased by the ESOP are allocated to employees of the company as the loan is repaid. The employees "cash in" their shares upon retirement or other qualifying event.

**Proposed Legislation:**

H.R. Bill 2096 was introduced on April 29, 2015 and as of this writing has fifty-three co-sponsors (36-R/17-D). S. 1212 was introduced on May 6, 2015 and has twenty-six co-sponsors (14-R/10-D/2-I).

Both bills allow sellers of S Corporation stock to enjoy the same indefinite capital gains tax deferral currently available only to sellers of C Corporation stock to an ESOP under IRC 1042 provided the sale proceeds are reinvested into qualifying U.S. stocks and bonds. Current effective federal capital gains tax rates are up to 23.8% plus applicable state rates.

Both bills also address the provisions of the Small Business Act that threatened the preferential status of certain businesses such as women-owned and minority-owned businesses if more than 49% of the stock is sold to an ESOP. The bills propose that if the other qualifying provisions regarding racial, gender or other criteria are met, preferential status treatment will not be lost solely due to a sale to an ESOP.

H.R. 2096 additionally seeks to replace a similar, previously expired provision that incentivizes banks to lend for ESOP purposes. Banks will not have to pay tax on 50% of the interest income they collect on loans extended for ESOP purposes if passed.

In summary, ESOPs are gaining momentum due to the continued bi-partisan support for employee ownership as well as the tremendous numerous tax and other advantages making an ESOP worthy of your exit planning consideration.

*Dan is a nationally recognized practitioner, author and speaker on ESOP matters. Dan is Past-President of the Society of Financial Service Professionals (Pittsburgh), Past-Chair of the Pittsburgh Business Ethics Awards and a member The ESOP Association and the National/ Pennsylvania Centers for Employee Ownership. For more information, visit www.ESOPGUY.com or call Dan at 724 -766-3998.*