ESOP | Report

September 2020 | The Voice of The ESOP Association | *Serving the Entire ESOP Community*

Inside this issue:

TEA, EOF to Open New International Center for Employee Ownership

State of the Art Facility Will Dramatically Expand Conferencing, Advocacy, Education, Capacity in Service of Employee Ownership

The ESOP Association and the Employee Ownership Foundation are thrilled to announce the establishment and December opening of the International Center for Employee Ownership—an all-new headquarters, advocacy, education, and conferencing facility for the employee ownership community. Located just blocks from the United States Capitol, the new facilities will include an education center capable of holding more than 200 attendees for classroom style learning sessions; a cutting edge full-production digital audio/video studio for online and virtual education and content; facilities for hosting and convening groups of lawmakers, staff, and scholars; and staff offices for the larger operations envisioned over the next decade for both organizations.

The Center is located in the recently developed Capitol Crossing complex on Capitol Hill and within walking distance of the United States Capitol as well as the U.S. Department of Labor, the primary regulatory agency for ESOPs.

TEA and EOF will use the facilities to host member companies, employee owners, members of Congress and their staff, and other leading government agency officials. The organizations also intend to convene meetings with international guests and domestic leaders in the not-for-profit and think tank communities in collaborative sessions to advance employee ownership.

One of the available meeting/reception areas in the new International Center for Employee Ownership is an enclosed, rooftop space with a view of the nearby Capitol (artist's rendering).

The facility will also become the new home-base for advocacy-day and frequent lobbying activities of TEA's new Employee Owner Action Network (EOAN) comprised of employee owners from across the nation.

"Over a year ago we began to examine the feasibility of a facility like this and what it could mean for the employee ownership community," said Gary Shorman, Chairman of the TEA Board of Directors. "It has been thrilling to bring this from idea to reality, but even more exciting is what it will mean for Employee Ownership in the years to come. These facilities can be transformational for Employee Ownership in Washington, DC and TEA's ability to deliver the highest possible value to our current and future membership."

TEA and EOF will move into the new International Center for Employee Ownership on December 15, 2020, marking the end of a nearly 18-month process that involved close collaboration with the Board of Directors and other leaders.

As this artist's rendering shows, the new International Center for Employee Ownership includes flexible, configurable meeting spaces that, when fully opened, are capable of accommodating more than 200 individuals. The space is intended to be used for business, education, advocacy, and thought leadership gatherings.

"From a programmatic and operational standpoint, we needed different facilities to meet our membership's needs. We were out of space in an outdated and poorly located building. So, we made a list of everything we could imagine the Employee Ownership movement could become in the next decade—and that is what we built for," said James Bonham, President and CEO. "I simply cannot wait for the first convening of the community in Washington early next May at our National Conference. These are facilities worthy and reflective of the size and importance of the employee ownership movement in America today."

Association leadership evaluated the project both before and during the current COVID-19 pandemic, and all operational and aspirational drivers to move forward with the project remained valid, even in a COVID and post-COVID environment.

"After COVID hit, we of course took a beat and asked if this continued to be the right move for the future of TEA and EOF. The unanimous conclusion was to build for our community's future," Bonham continued. "Across all metrics, the main drivers for the facility remained valid regardless of COVID—expanded advocacy, learning and education, development of our own digital and on-line content, the need for a gathering place for academic and policy thought leaders. It is all necessary for the future.

"Because we will have our own space, we can become much more innovative and expansive in how we conduct outreach and education," Bonham continued. "We can be much more forward leaning in imagining ways to bring our community, and those who hold sway over our futures, together."

On Capitol Hill. The new Center is located on Capitol Hill, four blocks from the US Capitol. Beyond the conferencing and educational spaces, the expansive rooftop terrace of the building complex is built to host meetings and world-class events in the shadow of the Capitol dome. Expect these spaces to be leveraged for political action, education, scholarship and other high-level events to benefit employee owners across the nation.

Expanding Multimedia Content Capabilities. The new center will include a fully equipped digital production studio, enabling TEA and EOF to efficiently and cost-effectively produce original audio/video content,

programming, and communications. With a recognition of the dominant role played by digital media in today's online world, this studio will provide new capabilities for enhancing our live and virtual events, member-focused educational content, and advocacy efforts.

Growing Capacity. The new International Center for Employee Ownership and Advocacy will enable TEA and EOF to grow over the next decade while expanding our efforts in advocacy, education, and content production, among others.

Hosting Meetings Onsite. One of our largest needs each year is renting space for meetings of all kinds—the new center drives to the heart of solving this problem for both TEA and EOF and creates huge new opportunities for collaboration and leadership.

A Grand Opening and welcome is in early planning stages, likely to take place during the May 2021 ESOP Association National Conference and Advocacy Day next spring. Also stay tuned for additional upcoming news about how you or your company can help with the new International Center for Employee Ownership and receive permanent recognition at the Center for your contribution.

> *We can become much more innovative and expansive in how we conduct outreach and education.*

TEA Announces New Virtual Event—ESOP 2020: Resilience and Renewal

Conference Offers Technical Content Usually Offered in Las Vegas, with Stellar General Sessions on the Business and Political Climates

Those familiar with ESOP Association programming know that Employee Owned—our live event held each year in Las Vegas—is an amazing, interactive conference with top-notch technical content, unparalleled networking, and an unmatched live experience.


Nicolle Wallace


Preston Rutledge

Health and safety concerns—coupled with meeting restrictions imposed due to COVID-19—forced us to postpone Employee Owned until 2021. While we are disappointed that we won't be able to share this great experience with you in person, we also know that you depend on the technical and strategic insights our Vegas show offers.

As you work to close out this year and begin preparing for 2021, you probably need those insights more than ever. To meet your needs, we are launching a new, virtual event—ESOP 2020: Resilience and Renewal.

This event will fortify you for the future, renewing your spirit and helping you keep your ESOP company buoyant and bouncing back, no matter what lies ahead.

Held Nov. 11-13, this conference will offer multiple General Sessions featuring important keynote speakers and presentations on major national topics, including:

- The 2020 national elections and what the results will mean for ESOP companies.
- An analysis and overview of the U.S. and global economies and what businesses can expect in 2021.
- An important dialogue regarding the future of ESOPs, our Association, and the decade ahead.

The first two keynoters have already been announced.

Nicole Wallace—anchor at MSNBC, former White House Communications Director under George W. Bush, and *New York Times* best-selling author—will join us for a live and interactive session of post-election analysis and discussion on what the results may mean for our economy, governance, and the new year.

Preston Rutledge—who until recently served as the head of the Employee Benefits Security Administration, the group with primary responsibility for enforcing ESOP laws and regulations—will be featured in one of the event's four general sessions. Rutledge's unique insights will be available *only* at this live and interactive event.

What about that technical content? ESOP 2020 will also offer three amazing tracks that are perfectly suited to leaders of ESOP plans and companies:

- **Board Member & Executive Track**—covers topics critical to corporate governance.
- **ESOP Fundamentals**—offers a solid grounding in the fundamentals of managing an ESOP, adapted to today's current events and situations.
- **Trustees Track**—covers the waterfront for ESOP trustees, from the basics to essential information even the most experienced trustees will value.

This great content qualifies you for the following educational credits: CPE, SHRM PDC, or a certificate of attendance.

Early bird registration is now open, with discounts available through Sept. 29. Registration will remain open until the event ends, but rates will increase as we draw closer to the conference. Visit us online for more information or to register today.

ESOP Association Announces Calendar of Key Activities Through June 2021

Virtual and Live Events Planned Through June 2021

The ESOP Association is announcing its planned schedule of events and activities that will carry the employee ownership community through the end of this year and into 2021. While all plans at this time are necessarily subject to change—no one can anticipate exactly when or how the COVID-19 pandemic may affect our nation in the future—we feel it is important to share this schedule now, so our community can plan to engage in these important activities.

October 2020

Employee Ownership Month—October is famous for celebrating employee ownership, and to help make your celebrating a little easier, we have done some of the work for you. The latest addition: Five free quizzes for you and your fellow employee owners to take! These are great ways to help everyone sharpen their knowledge related to:

- ESOP Facts
- ESOPs and Employee Owners
- How ESOPs Work
- ESOP Advocacy
- ESOP Association History

After taking each quiz you will receive feedback on your answers and be directed to a special web page with additional related online resources, so you can keep learning. All five quizzes are available now in the Employee Ownership Month network on The HUB.

AACE Winners to be Announced—Judging for the Annual Awards for Communication Excellence is nearly complete, and winners and runners up will be announced in late October.

EOM Poster—The winning entry in the Employee Ownership Month Poster competition has been selected. (See page 7 for more information.) All corporate members will receive one free poster. Want another copy? Limited quantities are available for sale in the ESOP Store.

November

National Election—Our elected representatives use voter registration lists to know which of their constituents

ESOP Report

The Voice of The ESOP Association

The *ESOP Report* is published on a monthly basis by The ESOP Association, the national non-profit association of employee-owned companies and ESOP practitioners, located at:

1200 18th Street, N.W., Suite 1125, Washington, D.C. 20036-2506.
Phone: (202) 293-2971 • Toll Free: (866) 366-3832 • **Fax:** (202) 293-7568
E-mail: media@esopassociation.org • **Internet:** http://www.esopassociation.org

Subscriptions are included in annual membership dues.

The articles within represent the views of the authors and may not be the views of The ESOP Association.

actively vote, and which ones don't. This is one reason why nothing is more important to employee ownership advocacy efforts than casting your vote. Don't forget to request your ballot and send it in, or vote in-person, on Nov. 3.

ESOP 2020: Resilience and Renewal—TEA's new virtual event provides the technical content you've come to expect from us in November and would usually receive in person in Las Vegas. (See the article on page 3 for more about this conference.)

December

EOF/UPenn CEO Leadership Program, Part I—This unique, two-week program is designed especially for leaders of ESOP companies and their designated successors. The first week typically takes place in the summer but was moved to December in response to the COVID-19 pandemic. A few slots remain for this program but are going fast, so we encourage you to register today.

International Center for Employee Ownership—The ESOP Association and Employee Ownership Foundation will move into their new headquarters on Dec. 15. Planning has begun for a Grand Opening in spring 2021. To learn more about the amazing new capabilities this facility will offer for enhancing and expanding the employee ownership movement, see the cover story in this issue.

Winter Webinar Series Begins—Stay tuned for more information on the latest round of top-notch virtual content available from The ESOP Association.

January

Congress Sworn In—On Jan. 3, all new and returning members of Congress will take the oath of office. Mark the date, and make plans to congratulate your elected officials.

State and Regional Chapter Council Meeting—The first 2021 meeting of TEA's 100+ chapter officers is tentatively scheduled for January 10-11. This meeting provides chapter officers the tools and training they use throughout the year to provide our members with top-notch programming and service. We are hoping to hold this event in the new International Center for Employee Ownership in Washington, D.C.; if conditions are not favorable for an in-person gathering, this event will take place virtually.

Presidential Inauguration—The winner of the November presidential election will be sworn into office on January 20.

February

Professionals' Forum—With a special focus on education, collaboration, and providing our professional advisors with the tools they need to service the ESOP community, this annual gathering of professional advisors to ESOP companies is unique in the employee ownership community.

Keep an eye out for an invitation—this event sells out quickly. Specific dates and location will be set soon, based upon evolving conditions.

AACE and EOM Poster Entries Due—Entries for the 2021 Annual Awards for Communications Excellence and Employee Ownership Month poster competitions will be due at The ESOP Association's new headquarters location on Feb. 13.

Information on updated requirements for entering both competitions will be forthcoming.

Calendar of Deadlines and Important Dates

Sept. 22-23	**Great Lakes Regional Meeting** Michigan, Indiana, and Ohio/KentuckyChapters
Sept. 24-25	**Southeast Regional Meeting** New South, Carolinas, and Mid-Atlantic Chapters
Sept. 29-30	**Northeast Regional Meeting** New England, Pennsylvania/Delaware, and New York/New Jersey Chapters
Oct. 1-31	**Employee Ownership Month**
October	EOM Posters Received by Corporate Members
October	AACE Winners and Runners Up Announced
Nov. 3	National Election
Nov. 11-13	**ESOP 2020: Resilience and Renewal**
Dec. 6-11	**CEO Leadership Program, Part I** This event is for CEOs/Presidents of ESOP companies or their designated successors
Dec. 15	**International Center for Employee Ownership**
December	Winter Webinar Series Begins
Jan. 3	Congress Sworn In
Jan. 10 -11	**State and Regional Chapter Council Meeting** *(tentative)*
Jan. 20	Presidential Inauguration
Feb. 13	AACE and EOM Poster Entries Due
February	**Professionals' Forum**
February	Spring Chapter Meetings Begin
March	**CEO Leadership Program, Part II** This event is for CEOs/Presidents of ESOP companies or their designated successors
March	Spring Chapter Meetings Continue
May 5 -7	**National Conference and Advocacy Day, Awards Celebration and Gala**
June	**Employee Owner Retreat**
June	Summer Webinar Series Launches
June	Chapter Summer Events Begin
Nov. 10-13	**Employee Owned 2021**

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

Spring Chapter Meetings Begin—Keep an eye on your email and on The HUB for announcements of the spring events taking place in your chapter.

March

CEO Leadership Program, Part II—The second week of this program, originally scheduled for December, will take place March 21-25.

Spring Chapter Meetings Continue—Our 18 chapters typically produce more than 100 events each year, and spring is when it all gets started. Whether virtual or in person, these promise to be exceptional opportunities to learn and gather with local ESOP companies and advisors.

May

May 5-7, 2021, National Conference and Advocacy Day, Annual Awards Celebration and Gala—Held annually in Washington D.C., this year's event will be a special opportunity for our community to gather once again. The 2021 gathering will be especially important because of changes resulting from the 2020 fall elections and the national policy implications that could follow. Get your advocacy shoes ready! Make your plans today to participate in this critically important event that benefits *all* employee owners through advocacy and engagement with our leaders in Washington.

Next year will offer a much more intensive advocacy focus, with additional advocacy training and coordinated interaction with elected officials. We will also be moving to a newly renovated, more spacious venue—the Renaissance Washington, D.C. Downtown Hotel.

Finally, keep an eye out for announcements regarding the grand opening of the new International Center for Employee Ownership on Capitol Hill, your new home-base for employee ownership advocacy and education.

June

Employee Owner Retreat—This event, designed especially for educating employee owners, is expected to take place in June. Final details on location and dates are still being determined.

Summer Webinar Series Launches—Get ready for another round of outstanding content, just a mouse click away.

Chapter Summer Events Begin—We hope that by summer our chapters will be able to meet in person so we can gather for education, networking, golf, and barbecues.

The Rest of 2021

We continue to work on developing events to be added to the calendar later in the year. Last year's inaugural Professionals' Forum Summer Edition was so well received that we are working on plans for a second installment in mid summer 2021. And, as always, we will have a round of fall chapter meetings and our Employee Ownership Month celebration in October.

Next year, we look forward to a return of our premiere fall conference, Employee Owned, which is slated to take place Nov. 10-13 in the revamped Caesar's Palace Conference Center.

Need a Hand with Your EOM Planning?

Let Us Help You Spread the Word On Employee Ownership

This article appeared originally in The ESOP Association blog. See our website for more blog posts.

Recently, we were talking to one of our members about her ESOP company's preparations for Employee Ownership Month (EOM). She shared some of her concerns:

- She was not sure how much bandwidth her fellow employee owners would have for EOM activities, especially since many have school age children who will be home while attending classes remotely this fall.
- She was concerned about spending too much of her own time—and too much of her ESOP company's money—on festivities that might be seen as frivolous during such a distressing time.
- She wanted to be sure her company's EOM activities were safe.

That conversation was a huge help in shaping our own plans for EOM this year.

Like the member mentioned above, we know many of you are stretched thin, trying to develop new products or ways of working while adapting to constantly changing conditions. For many of us, tasks that once were established and easy to manage are now complex and complicated.

If that describes your planning for EOM, then let us help you out.

This year we are offering a suite of turnkey products you can share directly with your employee owners—all designed to make your EOM events easier, less stressful, and less expensive, while hopefully remaining enjoyable and educational.

Plus, the place where you can find all these tools is a resource of its own—the special Employee Ownership Month network on The HUB! Visit today to share EOM ideas with your peers, ask questions, bounce suggestions off each other, and do what employee owners do best—collaborate on solving problems and making things work better.

While you are there, get access to great resources like:

- Five free online quizzes (**just added!**) you can share with your employee owners! When you are done, all the quizzes will provide feedback on your answers and direct you to additional, relevant resources online.
- EOM backgrounds you can use in your office video chats.
- Signs to printout, take selfies with, and share on social media during October.
- Fact sheets about ESOPs.
- The 2020 Press Kit, with tips on communicating to employee owners, the press, and your community.
- Links to educational ESOP Association webpages.
- And more!

These new materials have already been downloaded more than 1,000 times! And more resources will be added regularly between now and Oct. 1. So, visit the EOM Network today and let us help you ensure your fellow employee owners have a great October.

EOM Poster Winner, Runner Up Announced!

Congratulations to Hisco, which submitting the winning entry in this year's Employee Ownership Month competition! (See the photo above.) A free copy of the poster will be mailed to all corporate members of The ESOP Association. Additional copies may be purchased in the ESOP Store.

Congratulations also go out to Human Kinetics, which submitted the runner up entry (shown at right)!

Ownership Advantage

What's Changed with COVID-19?

By Mike Frommelt, CEO/Owner, KeyStone Search
Edited by Matt Hancock, Consultant, Praxis Consulting Group Inc.

Being an executive recruiter, I've always gotten questions about the talent market. However, with COVID-19 totally disrupting our economy, these questions are now coming fast and furious: How's the market right now? Are more people out there and available? Is this a good time to hire or not?

After enduring six to seven months of this pandemic, the best answer I can give is that COVID-19 has changed everything...and it's changed nothing.

Almost everything regarding how we recruit, interview, select, and even on-board talent has changed. Zoom and MS Teams rule the day, and to be honest, I've almost forgotten what it's like to interview an executive candidate in person.

Yet, when it comes to the availability and interest level of leadership candidates to make a job move, very little has changed. What we hear from candidates in our recruiting calls falls into one of three camps:

- COVID-19 has driven our business downward and yes, I'm open to hearing about other opportunities.
- COVID-19 has driven our business down and thus, I need to stay here and see this through.
- COVID-19 has either not affected our business or has driven our business upward, and I am planning to stay put.

Net-net, it's the same it has been for the last 10 years. There is a relatively small percentage of qualified leaders who are open to considering a change. And, those who are

GDP growth is expected to rebound in Q3 and Q4 but unemployment is projected to remain above 10%

Notes	Source	2020				2020 Annual	2021 Annual
		Q1	Q2	Q3	Q4		
Real GDP % Change (seasonally adjusted annualized rate)	CBO*	-4.8	-37.7	21.5	10.4	-5.6	4.2
	Conference Board	-5.0	-38.9	20.6	0.8	-7.0	1.0
	BEA*	-5.0 (actual)	-32.9 (actual)				
Unemployment rate (% of all civilian, seasonally adjusted)	CBO*	3.8	15.1	15.8	11.5	11.5	9.3
	Conference Board	3.8	13.0	10.6	10.8	9.6	9.4
	BLS*	4.4 (actual)	11.1 (actual)				

Sources: Congressional Budget Office, Conference Board, Bureau of Labor Statistics, Bureau of Economic Analysis

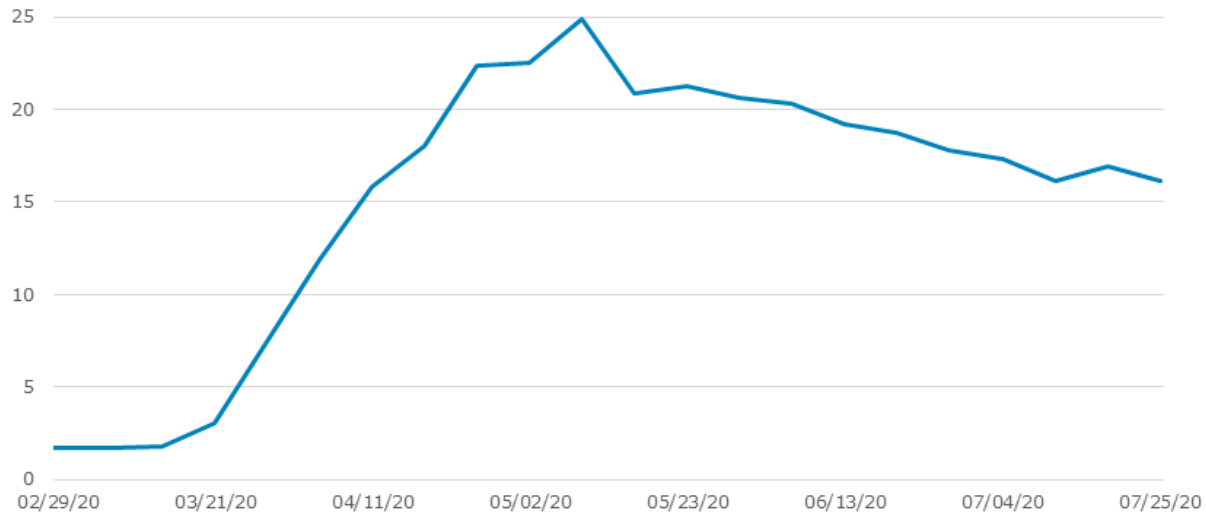
Slide updated August 11, 2020

3

While the number of unemployed Americans continues to fall, it remains well above the levels reported prior to the pandemic

Continued Claims (insured unemployment, seasonally adjusted)

WEEKLY CLAIMS, ENDING SATURDAY; FEBRUARY 1, 2020 – JULY 25, 2020



Sources: Department of Labor.

Slide last updated on: August 3, 2020

4

open still need to be presented with a strong opportunity to consider a move.

Basically, there just aren't a lot of high-quality leaders wandering around looking for work. Add to this the fact that only a small percentage of leaders in other companies are really capable of leading in an ESOP culture, and we find ourselves in the same position we were seven or eight months ago.

Great leaders are *still* hard to find.

The truth is we've been enduring a business leadership crisis in this country for years, not because of the economy but because of our demographics. The baby boomer generation (ages 56-74) accounts for nearly 72 million people in the U.S. The next generation, Gen X (ages 40-55) includes just over 65 million people.

To add a little more context, 10,000 people in this country turn 65 every day. As more and more baby boomers retire, there simply are not enough qualified people behind them to take over and lead.

So unfortunately, at least at the leadership levels, the battle for talent rages on. The good news here is the companies that recognize this and double down on internal leadership development, and hire thoughtfully from the outside when necessary, will come out of this stronger than the competition.

One thing is certain: This upheaval will end, it's just a question of when. And, just like everything else in business and life, our actions now will dramatically affect our future results.

KeyStone is an executive search and consulting firm serving ESOPs across the country. Mike and his team have assisted numerous ESOPs through CEO transitions, as well as other high-level hiring/transition initiatives.

DOL's PRO Good Guidance Rule

Rule Clarifies Which Materials Are Binding, Which Are Not

By Ted Becker and Rick Pearl, McDermott, Will & Emery LLP

On August 19, 2020, the Department of Labor (DOL) published the Promoting Regulatory Openness through Good Guidance Rule, which will become effective 30 days after it is published in the *Federal Register*.

This rule sets forth the DOL's policies and procedures for complying with the Executive Order issued by the President on October 9, 2019 and entitled "Promoting the Rule of Law through Improved Agency Guidance Documents."

This Executive Order (EO) prohibits agencies from imposing legally binding requirements without first setting forth the requirements in either legislation or properly promulgated rules issued in accordance with the Administrative Procedure Act (APA).

Consistent with the APA's purpose, the EO directed federal agencies to:

- Create an open and fair regulatory process.
- Permit public comment on guidance materials.
- Halt the practice of enforcing—or threatening to enforce—standards set forth in non-binding guidance materials.

The crux of the rule is that the DOL may attempt to enforce only properly promulgated laws, rules, and regulations. The rule clarifies which materials may be considered binding on the public (referred to as "regulated persons"), which materials are not binding, permissible uses for non-binding materials, and the processes for issuing non-binding guidance and inviting the public to comment.

What Is Considered "Guidance?"

Non-binding materials are referred to as "guidance" in the rule. Guidance generally is not binding on regulated persons and cannot be used by the DOL as a basis for alleging that a regulated person violated the law.

Even though guidance is not binding, the DOL acknowledges the importance of guidance and the effect it can have on the conduct of regulated persons. Before guidance can be issued, it must be reviewed and approved by a designated DOL official and, if released, identified as non-binding with disclaimer language.

Guidance includes any agency statement that sets forth a policy on a statutory, regulatory, or technical issue. It also includes an interpretation of a statute or regulation, which is also publicly available and is of general applicability.

Guidance generally cannot use mandatory language—such as "shall," "must," "required," or "requirement."

Guidance should be written in plain and understandable language, and include effective dates, citations to implicated legal provisions, a description of the persons to whom it might be relevant, and an indication if it revises prior guidance.

Documents that are not available to the public are not guidance. Guidance does not include rules that have been promulgated through proper rulemaking channels, which typically requires notice-and-comment procedures (with

some exceptions for certain military or agency-operation rules).

Certain internal agency documents—which are unlikely to have a substantial future effect on regulated persons—are not guidance. DOL legal briefs and court filings are not guidance. Advisory opinions, legal opinions, and other statements of "specific applicability" are not guidance.

Specific documents, however, can become guidance if they are published and cited by the DOL in other contexts. Pre-enforcement rulings and written communications that respond to a request about compliance issues can be guidance, but they are exempt from procedures for issuing guidance.

The rule recognizes that certain guidance may have a more significant impact than routine guidance. Significant guidance is defined as guidance that is reasonably expected to:

- Lead to an annual effect on the economy of $100 million or more, or materially and adversely affect economic, environmental, health, or state/local governments.
- Create serious inconsistency with another federal agency.
- Materially alter certain grant or loan programs.
- Raise novel legal or policy issues arising out of legal mandates, the President's priorities, or principles of a 1993 EO on reviews of certain regulatory actions.

Uses of Guidance

Guidance may not be used prior to the effective date of the rule. Guidance that is non-binding may never be used by itself to create binding requirements, and enforcement actions must be based on violations of applicable legal requirements, not mere non-compliance with guidance.

Guidance may not be used to suggest that it sets forth the only acceptable standard or means of complying with law, nor can guidance be used to threaten enforcement action. The DOL cannot use guidance to reward those who comply with it by decreasing the frequency of audits or investigations.

Non-binding guidance can be used for certain purposes. Guidance that describes existing legal requirements can be used as evidence that a person had knowledge or notice of the legal requirements, presumably if the DOL shows that the person knew of the guidance. Guidance can be used to rebut a claim that the DOL has changed its position over time.

In the Supplementary Information portion of the rule, the DOL acknowledges that the APA prohibits a federal agency from using guidance to impose binding, new standards on regulated persons, and that the APA requires formal rules or regulations to meet certain procedural requirements, including notice-and-comment periods.

The DOL also acknowledges that even if it ceased any attempt to issue new legal requirements through non-binding guidance, this would not be enough to comply with the EO or respond to concerns about federal agency enforcement of non-binding guidance materials. Indeed, the rule states that guidance inherently affects regulated persons' conduct and can persuade courts, and "coercive guidance" can cause regulated persons to modify their conduct just to avoid the threat of governmental inspection or enforcement action.

Implications for the ESOP Community

The rule should discourage the DOL's aggressive efforts against ESOPs. Although ERISA requires the DOL to promulgate regulations, 46 years after ERISA was enacted, the DOL still has not promulgated a regulation on adequate consideration.

Nevertheless, in recent times the DOL has aggressively litigated to attempt to enforce its own interpretation of the adequate-consideration exemption. This is what a prominent career official at the Employee Benefits Security Administration—the DOL group that enforces many laws related to ESOPs—has referred to as "regulation through litigation."

A word of caution: The rule contains language that signals that the DOL might try to use guidance materials in ways that violate the spirit, if not the text, of the EO. Guidance can be made binding by force of some other law, or against a party to a contract if incorporated in a contract or agreement.

The rule states that guidance can be used "to show that a party has failed to meet professional or industry standards when those are relevant to statutory or regulatory requirements."

It is unclear why the DOL believes it may use guidance to establish professional or industry standards. If professional or industry standards exist or existed, then the DOL should be required to prove such standards with evidence of such standards other than the DOL's own, non-binding guidance documents.

Legal Update

Beneficiary Designations In ESOPs

By Jay Van Heyde, Shareholder, Dean Mead
Edited by: Julie Govreau, Senior Vice President and General Counsel, GreatBanc Trust Company

On June 26, 2020, the Eleventh Circuit Court of Appeals decided the case of *Crowder v. Delta Air Lines, Inc., et. al.*, 963 F.3d 1197, 2020 WL 3481497 (11th Cir., June 26, 2020).

Although the decision involved the account balance of a deceased participant in a 401(k) savings plan, not an ESOP, the lessons learned from this case have significant application to ESOPs.

Namely, plan sponsors should review the beneficiary designation and distribution provisions of their ESOP document to make sure they have properly taken into account the impact of divorce on beneficiary designations.

Background

Marvin Crowder was a long-term employee of Delta Air Lines and a participant in the Delta Family-Care Savings Plan, a defined contribution plan subject to ERISA. In this regard, the plan is identical to an ESOP.

Marvin and Wanda Crowder were married in 2004. Marvin never designated his wife as his beneficiary (which required filing a written beneficiary designation form), but once the couple was legally married, as a matter of federal law and the terms of the Delta plan, Wanda Crowder became the participant's automatic, sole beneficiary.

Seven years later, the couple separated and on June 23, 2014, Wanda Crowder filed for divorce. On July 16, 2014, while still legally married, Marvin Crowder submitted a beneficiary designation to Fidelity (the plan's record keeper) naming his sister (Chappie Prince) as his sole beneficiary. The divorce was finalized 26 days later. Mr. Crowder never changed the designation of his sister as his beneficiary.

Mr. Crowder died on January 23, 2016. On February 26, 2016, pursuant to a claim filed by Mr. Crowder's sister, Fidelity distributed the account balance to the "beneficiary" listed on file.

Wanda Crowder, the former spouse, later filed suit claiming she was entitled to the account because the one beneficiary designation on file (Mr. Crowder's sister) was submitted while the couple were still married. Fidelity took the position that under the plan document, the spouse was an "automatic" beneficiary, but only during the time the couple was married.

The Role of Plan Language

The plan language in this case stated that the automatic spousal designation applies "if the participant is married" and only "during the marriage." Wanda argued that the automatic beneficiary designation should survive divorce unless and until the participant affirmatively designates a beneficiary *after* divorce.

Both the District Court and the Appellate Court refused to extend the Treasury Department's Regulation 14.03 that far and found that Wanda Crowder was the automatic spousal beneficiary only as long as she remained married to Marvin Crowder.

Most Summary Plan Descriptions (SPDs) will advise participants to be diligent about naming a beneficiary and updating their designation whenever there is a change of family status. This case highlights that importance. ESOP documents should include detailed language to cover this "automatic spousal designation" during the marriage, but ESOP sponsors would be well served to review those provisions to make sure that when a divorce occurs, the beneficiary status changes as well.

This case brings to mind another problematic situation involving divorce and the status of the former spouse as a beneficiary. What happens when a participant, during the marriage, affirmatively names his/her spouse as the primary beneficiary—then divorces, but fails or forgets to affirmatively change the beneficiary designation?

Most divorced participants do not intend their former spouse to continue as their designated beneficiary. Will that be the result, though, if nothing is done after the divorce and the ESOP document does not deal with the situation?

Most, but not all, ESOP documents contain a provision essentially stating that if a participant affirmatively designates a spouse as the primary beneficiary of the ESOP account before or during the marriage, but then divorces, the divorce will *automatically* revoke the prior designation. The exceptions: If a qualified domestic relations order (QDRO) provides otherwise, or the participant makes a new, affirmative beneficiary designation after the divorce that again names the former spouse as the designated beneficiary.

Absent this type of plan document language, if the former spouse was designated as the primary beneficiary before or during the marriage, and no changes were made after the divorce, the former spouse will continue to be the designated beneficiary of the ESOP account. That old designation likely will be the "latest beneficiary designation" on file and will be honored.

State Law Is Not Enough

Many state legislatures have attempted to deal with these beneficiary designations that were made prior to divorce, but *not* revoked after the divorce, by enacting statutes that make the designations void upon divorce. The problem with relying on those types of state statutes in these cases is that the U.S. Supreme Court has held such state statutes to be pre-empted by ERISA—and therefore ineffective.

The lead case is *Egelhoff v. Egelhoff,* 532 U.S. 141 (2001). In this case, a state of Washington statute provided for automatic revocation, upon divorce, of any prior designation of a spouse as the beneficiary for all types of plans, assets, and accounts. The Supreme Court held that the state statute was preempted as it applied to ERISA benefit plans (such as 401(k) plans, ESOPs, pension plans, employer provided group life insurance, etc.) because the statute directly conflicted with the ERISA requirement that plans be administered, and benefits paid, in accordance with plan documents.

The Washington statute would interfere with a nationally uniform plan administration scheme, the court ruled, and would prevent administrators from making payments by simply identifying the beneficiary specified in the plan documents.

Instead, the court found, administrators would be required to familiarize themselves with state statutes to determine whether the named beneficiary status had been revoked by operation of law. This would impose a burden that was intended to be avoided by ERISA, the court determined.

Prevent Confusing Designations

This type of litigation can prove costly to the ESOP sponsor and the beneficiaries of the deceased participant. Thus, great care should be taken to make sure the language in the ESOP document (including the SPD) is carefully crafted to produce the intended result.

In addition, systems should be put in place to identify when a divorce occurs, and to notify the ESOP administrator, who can then offer new beneficiary designation forms to the plan participant.

Often, an employer is first made aware of a divorce in connection with the administration of the group health plan or flexible spending account (Section 125 plan). A "change in family status" update or change is requested or filed. When that occurs, the ESOP administrator should be made aware of the situation and should actively work with the participant to obtain an updated beneficiary designation.

Advisory Committee on Administration

Sensible Assumptions for Repurchase Obligation Studies

By Nicole Medgaarden, QKA, ESOP Consultant, FuturePlan by Ascensus
Reviewed by Lisa J. Tilley, CPA, President, Lisa Tilley Consulting, LLC

Privately held ESOP companies are required by Section 409(h) of the Internal Revenue Code to buy back shares of company stock held in vested participants' accounts for various qualifying reasons.

As such, many ESOP sponsors choose to have a repurchase obligation study performed to help forecast that liability. The assumptions modeled in a study are the decisive factors that determine the magnitude of the projected liability.

Meaningful studies start with pragmatic and statistically relevant assumptions. Establishing assumptions might seem like a simple task at a first, but the devil is in the details. Applying thoughtful consideration when developing study assumptions will result in quality projections.

In general, assumptions should be reasonable, cohesive, and consider internal and external business and economic factors. Understanding the relationship among the variables will help in the development of reasonable and unified assumptions.

This article outlines variables impacting a study and discusses concepts to consider while cultivating relevant assumptions to model.

Employee Groups

The employee demographics of a company are the foundation of a study and are used to establish employee groups for analysis. How employee groups are characterized—when integrated with salary, turnover rates, and workforce predictions—will impact the timing and repurchase liability being projected.

Groups can be defined by job classification, compensation and/or length of service, division, or geographic location. The goal is to develop employee groups based upon similar

actuarial and demographic trends. Each group should have similar statistical probabilities related to length of service, age, compensation, turnover rates and workforce growth rates.

The demographic data gathered from these groups will, among other things, determine at what age and at what compensation a new and/or replacement hire will enter the study.

Turnover Rates

Once employee groups are defined, an analysis of each group's historical turnover trend should be performed. The objective of this analysis is to identify general trends related to the age and length of service at which employees tend to terminate (i.e., turnover average). These statistical turnover averages may vary by employee group; consequently, they should be integrated into the study accordingly.

Aside from supplying turnover averages by employee group, an examination of a company's employment history will provide the framework for selecting a relevant turnover table. Flat rate, age-based, and service-based tables are the most common types of turnover tables used.

Flat turnover tables show the same percentage of employees leaving each year. An age-based or service-based table might be used if, for example, the analysis of a company's turnover trend reveals higher turnover rates among younger employees with fewer years of service.

It should be noted that, although this is a historical analysis (typically three to five years), the information should be indicative of prospective turnover behavior. Singular circumstances of attrition—such as past layoff or downsizing events—will need to be scrutinized, as they inflate turnover and distort averages. Overall weighted turnover averages may need to be adjusted for years in which these uncommon events occurred.

The actuarial data obtained during this examination will provide the foundation for determining when the repurchase liability will occur in the forecast.

Defining Retirement Age

The plan document provides the definition of Normal Retirement Age (NRA). However, if the probable age of retirement differs from what is described in the plan document, alternative NRA assumptions should be modeled.

When a company has a population of employees that work beyond NRA, it is challenging to project at what age those participants will retire. It might be helpful to apply some simplifying assumptions (i.e., participants 65-70 will retire at age 70; participants age 71-75 will retire at age 75, etc.). This can spread out the projected repurchase liability for this group.

As an alternative, a historical retirement analysis can be performed, i.e., turnover analysis by age, including participants past NRA. Then, an age-based or a combined table could be used.

Death and Disability

The factors influencing the use of death and disability assumptions in a study include, but are not limited to, the nature of the industry and historical occurrences. Utilizing these assumptions in a study decrements a portion of each participants account every year and reflects it as a repurchase liability associated to death and/or disability.

In reality, however, these occurrences are unpredictable and when they do transpire generally are paid over a short period of time (rather than stretched throughout the forecast). Furthermore, the impact of these events occurring are only magnified when it relates to a participant with a significant share balance.

Therefore, it might be more pragmatic to plan for the repurchase obligations of those participants with significant share balances, in lieu of projecting a fraction of each year's repurchase obligation related to death and/or disability using mortality or morbidity tables.

Payroll Growth

Comprised of compensation and workforce growth assumptions, growth in payroll should be indicative of the long-term projections (i.e., what is expected to occur) of the company, including economical and financial trends of the industry. Similar to turnover, major corporate events (i.e., mergers, acquisitions, etc.) may need to be considered if such an affair is pending or predicted.

The assumptions applied to compensation and workforce growth will determine total covered compensation. When developing workforce growth rates and salary growth assumptions, the appropriate relationship between total payroll growth and enterprise value of the company should be considered.

Stock Value Growth Rate

A discussion with key members of the management team and involvement of the appraiser is recommended when determining what stock value growth assumptions to model in a repurchase obligation study. As with total payroll assumptions, the growth rate assumptions applied to share value should align with the business' financial projections. Sometimes it is desirable to forecast changes in share value by integrating the ESOP repurchase obligations into a comprehensive financial model of company. This allows executives to see a company's repurchase obligations in the context of its projected income and cash flow; it also creates a tool for forecasting share value.

However, it is important to note that this contractual obligation of the plan sponsor is not recorded on the corporate balance sheet as a liability for GAAP reporting

purposes. The assumptions applied to share value growth rates determine the value of the future liquidity requirements.

Funding Strategy

The source of cash used to fund repurchase obligations can impact how the shares that are repurchased are redistributed to participants.

Funding repurchase obligations with contributions will ensure that only active employees are eligible to participate in the recirculation of the shares. Projections that assume ongoing contributions equivalent to a percentage of covered compensation will provide a specific level of benefit to participants. A pay-as-you-go funding strategy results in contributions being driven by repurchase obligations, which can produce uneven benefit levels and correlated contribution requirements.

Funding repurchase obligations with cash dividends or S distributions will recirculate a greater proportion of the shares to participants (actively employed or terminated) with large share balance because dividends and S distributions paid on allocated shares are allocated pro rata based upon share balances.

Long term use of dividends and S distributions as a funding source will concentrate shares in accounts of long-term participants with larger account balances, thereby magnifying any "haves vs. have-nots" situation within the ESOP. However, the use of S distributions as a funding source might be unavoidable if the ESOP owns less than 100 percent of the company.

Diversification Election Rate

Diversification election rate assumptions determine the repurchase obligations related to diversification and can be difficult to predict. A review of the company's historical diversification elections is a good place to start. However, if the ESOP is less than 10 years old, companies might need to consider other factors that affect employees' diversification decisions. Those might include:

- Historical performance of company stock.
- How valued a diversified retirement portfolio is to a participant.
- Whether participants are aware of their diversification rights and what it means to diversify.

All these factors can be considered when deciding what diversification election rate to assume.

Other Considerations

ESOP's owning less than 100 percent of the company might need to include future acquisitions of shares if a stock purchase transaction is expected to occur within the forecasted period. If in-service distributions are an option from the ESOP, or the company is contemplating offering a one-time distribution opportunity to "actively employed" participants, election rate assumptions should be incorporate into the projections.

> ***Funding repurchase obligations with contributions will ensure that only active employees are eligible to participate in the recirculation of the shares.***

Furthermore, ESOP's with 401(k) features will have additional modeling considerations to develop, i.e., employer match formula, employee deferral rates, etc.

Conclusion

All things considered, the validity and accuracy of the projections are only as sound as the assumptions they are based on. As reality starts to deviate from key assumptions, it might be time to consider updating your study.

Consider running contrasting repurchase obligation scenarios to:

- Stress-test key assumptions—such as, share value growth, payroll growth, and diversification election rates—to determine how sensitive the results are.
- Understand the impact of financial, strategic, and/or policy changes.
- Account for the effect of different retirement assumptions for participants with significant share balances.

Best practice is to obtain consensus on the assumptions from the executive team, Board of Directors, and ESOP trustees, in addition to the service providers (i.e., appraiser, legal counsel, TPA, etc.).

The ESOP Association
1200 18th Street, NW
Suite 1125
Washington, D.C. 20036-2506

Phone: (202) 293-2971 • **Fax:** (202) 293-7568
E-mail: esop@esopassociation.org
Website: http://www.esopassociation.org
Blog: http://www.esopassociationblog.org
Follow us on: Facebook, LinkedIn, Twitter, YouTube, Flickr

Serving the Entire ESOP Community

Want the *ESOP Report* by e-mail? Send your name, company info, and email address to: **media@esopassociation.org**