ESOP | Report

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

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A Year to Remember and to Give Thanks to You, Our Incredible Members

We Met the Challenges of 2020 Together, as a Community

For all members of the employee ownership community, 2020 has required unparalleled adaptation, resilience, and action. While this year has been difficult and challenging, it also has included many challenges we have met together head-on and much new success—all of which positions us well for the future.

We were all forced to adapt, and we did so together.

ESOP companies across the country modified production to make masks, tubing, ventilators, and more. Entire departments took voluntary pay cuts to ensure the success and survival of the company. Employee owners looked out for one another.

Here at TEA, we launched completely new initiatives to align with our member's needs—initiatives that will stick with us for years to come. Those initiatives were possible thanks to you, our members.

Our Board put in long hours analyzing information and helping us chart a path forward. Our Advisory Committee members, who were already logging long hours at work, took time to produce exceptional content that helped steer ESOP companies through confusing times. Our chapter officers rose to the occasion, helping to set up and promote new chapter activities while working hard to keep their ESOP companies safe and productive.

The HUB, By the Numbers

Logins: 25,756
Document Downloads: 10,820
Active Users: 3,107
Discussion Posts: 850

It all started in late February, as COVID-19 was starting to rear its head. TEA, The Board of Directors, and our Advisory Committees took quick action to gather and distribute timely materials for our members. Thousands of people used the COVID-19 Action Center on our website to find government resources and receive the latest alerts from Washington. As part

of that effort, we launched our first series of webinars—timed and positioned to provide maximum help when our members needed it most.

We launched a completely new digital networking portal, The HUB, which is the first and only platform of its kind. At a time when meeting in person became impossible, members had a new and exciting opportunity to interact virtually.

And interact you did. More than 14,000 of you have participated in this online community so far, engaging your fellow members, downloading files from ESOP Association webinars and conferences, and asking and answering questions. We couldn't be happier with the level of interaction and the quality of dialogue on this platform. Your collective insights, willingness to share, and mutual support have made this a powerful tool that will benefit all members for years to come.

> ***You have ensured that we will emerge from this pandemic as an intact community—one that is even stronger and better positioned for the future than when this year began.***

If you haven't yet participated, we encourage you to give it a try today, especially as some exciting new networks are about to come online.

We also took our events and conferences online. Our network of 18 chapters provided roundtables for ESOP leaders to share ideas and solutions. Our first ever virtual regional events attracted more than 1,300 attendees, who gathered for great content and networking.

To meet the demand for insights in rapidly changing times, we launched our first summer edition of the ESOP Professionals' Forum and added sterling keynote speakers Erica Dhawan and Drew Crouch. We also provided a new experience, ESOP 2020, to take the place of the Employee Owned Conference. Once again, members were treated to insightful and unique keynoters—Preston Rutledge and Chuck Todd. More than 700 attendees flocked to this event, which featured keynote sessions livestreamed from our new offices, only a few blocks from the Capitol.

We also expanded the educational credits available for all our national events, ensuring that your TEA conference experience will continue to help advance your career.

Our advocacy program grew this year and included ESOP Association testimony during an important hearing in the U.S. House Small Business Committee. Daniel Goldstein, CEO of Folience, did an outstanding job representing our community and its concerns, especially regarding the need for guidance on adequate consideration.

In 2020 we also created the Employee Ownership Action Network (EOAN), the primary grassroots effort promoting employee ownership in the public policy arena. EOAN provides an opportunity to present a concise, cohesive, and energized voice to policy makers urging their support of policies and positions that endorse employee ownership.

Our first EOAN campaign in Wisconsin was an impressive and successful initiative. In less than two weeks, our members sent 328 emails urging support of vital ESOP legislation to 58 Senators across 29 states. We thank all of you who participated in this initial effort. Your support of employee ownership is off to a great start and we look forward to seeing what this group can do in 2021.

To further bolster our advocacy capabilities, we moved our offices closer to Congress and will soon be opening the doors to the brand-new International Employee Ownership Center. This state-of-the-art facility will be the global headquarters for employee ownership. Just steps from the U.S. Capitol, it will provide new and unparalleled opportunities for advocacy and advocacy training.

For Employee Ownership Month we provided extra turnkey options to make it easier for our busy members to celebrate employee ownership and educate their employee owners. Backgrounds for video calls, items to share on social media, and tips for connecting virtually with elected officials were just some of the resources available. We also offered a series of free online quizzes that were taken by nearly 2,100 members of our community.

The Employee Ownership Foundation launched a new study examining how ESOP companies responded to the pandemic compared to other businesses. The results were amazing. ESOPs were more likely to retain staff and

ESOP | Report

The Voice of The ESOP Association

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working hours—even when other businesses received funding through the Paycheck Protection Program and ESOP companies did not. What's more, ESOPs did a better job ensuring employee safety, proving more likely to provide personal protective equipment and send employees home to work.

These amazing results will make it easier for us to argue on Capitol Hill that ESOPs deserve federal support, and they were possible thanks to all of you who shared your time and information with us.

While it may seem that 2020 was a year to forget, there are so many reasons to remember and be thankful. Most of all, we thank you, our members. Most of the accomplishments we enjoyed this year were possible because of your patience, time, and energy.

You created content for one another. You shared ideas and resources, making it easier for everyone to come through this pandemic together. You purchased sponsorships to support our educational efforts. You responded to requests for advocacy efforts and survey information. Most importantly, you continue to provide a safe, resilient, positive environment for your employee owners.

You have ensured that we will emerge from this pandemic as an intact community—one that is even stronger and better positioned for the future than when this year began.

From the Chair

The ESOP Association Creates a New Super Governance Committee, Begins a New Round of Changes to the Board

By Gary Shorman, Chairman of the Board, The ESOP Association

Earlier this month, The ESOP Association engaged in that difficult process we all take on before moving: sifting through materials we've had for years, deciding what should stay and what can go, and generally cleaning house. It is a process many of you may have experienced this year too, as months of COVID-19 quarantine led many of us to re-evaluate our personal spaces and how we use them.

The desire to clean up and get things squared away also is driving our Association to take on an important new challenge. Starting this month, several of your volunteer leaders are forming a committee to evaluate TEA's governance structure.

We are incredibly fortunate to have a veteran group of ESOP community leaders fill out this committee. The group will be chaired by Dave Fitz-Gerald, past Chair of the TEA board. Other members include Karen Ellis, Board Secretary/Treasurer; Derrick Vick, At-Large Board Member; and Lynn Dubois, former Chair of the Advisory Committee Chair's Council and a former member of the Board. I count myself lucky to be involved in this group too.

The members of this committee bring complementary skills, provide perspectives from different industries, and all have tremendous experience with TEA's governance. They also share a bold vision for how our organization can function in the future. This group represents our members well; it can provide an experienced view of where we have been, and a clear vision of where we can go next.

The work this committee will do is sorely needed and long overdue: Many TEA members probably don't know that some elements of our governance are left over from the late 1970s, when TEA was formed by the merger of two groups with different governance structures.

A lot has changed since those days, and it is high time to re-evaluate this structure and modernize and modify as needed. Doing so will give us the framework to plot the clearest course to the bright future that employee ownership deserves.

The plan is for this committee to provide recommendations by May 1, when most turnover on our board typically takes place. This will give our new board the chance to start fresh with a structure that is best suited to ensuring TEA's immediate and long-term success.

Turnover this year is marked by the departure of two members, who will rotate off the board as their terms expire.

Missy Pieske has done an absolutely tremendous job for the past three years as Chair of the State and Regional Chapter Council. Her first year she filled in for the previous Chair, who was unable to complete his term when he left the ESOP company where he had worked. Missy stepped in and hit the ground running, showing a skill and passion for the job, as well as the keen understanding of chapter operations she gained while working her way up to the role of president of the Minnesota/Dakotas chapter.

After completing her first term as Chair and Board Member, Missy came back and served another two-year

term. In her time as chair she has been the picture of even-handedness and grace under pressure, and her work on the board has garnered praise from staff and volunteers alike. Her contributions and good cheer have always been appreciated by the board and will be solely missed.

Missy, on behalf of the entire board, I with you a heartfelt thanks for all your good work!

Missy's role will be filled by Steve Earl, VP of Kitchen Operations at Mid-South Building Supply. Steve is a past President of the Mid-Atlantic Chapter, served as a judge for this year's Annual Awards for Communication Excellence, and is a past winner of the Employee Owner of the Year Award. We are thrilled to have Steve join the team and look forward to his contributions.

The second person who will rotate off the board is Dave Fitz-Gerald, whose term ends on May 1. Dave is TEA's Immediate Past Chair and has served on the Board in multiple roles for many years. As Vice Chair he led some truly invaluable initiatives, including chairing a task force that evaluated TEA conferences and offered recommendations for improving content and member engagement.

As Board Chair, Dave certainly took the recommendations of the task force to heart. He worked diligently to incorporate new elements into conferences—such as featuring the best sessions from TEA's chapter meetings. He also breathed new life into TEA events, in one case wearing a custom suit covered in hearts to match the conference theme, "I Love My ESOP."

One thing is clear: No one has ever doubted how much Dave has loved ESOPs or The ESOP Association!

Before joining the Board, Dave was extremely active in the New England Chapter, where he served as President. He also served on the Ownership Culture and Fiduciary Issues Advisory Committees, and as a Trustee of the Employee Ownership Foundation. Dave's accomplishments and contributions to TEA have been invaluable, making our organization stronger, better, and more engaging.

Dave, thanks so much for all the good work you have done, and for the good work you will continue to do heading up our Super Governance Committee!

We also have a few Board Members who will rotate out of their current roles but will remain on the Board.

Your Vice Chair, Ali Jamshidi, is nominated to become the new Chair. Secretary/Treasurer Karen Ellis is nominated to become the Vice Chair. At-Large Member Derrick Vick is nominated to become the Secretary/Treasurer. And as my term as Chair ends on May 1, I will take on the position of Immediate Past Chair.

In addition, two new folks have been nominated to join the Board as At-Large Members.

The first is Robyn Pollina, the CEO of Palmer-Donavin in Columbus, OH, where she has worked for more than 25 years. Robyn has served as the company's Assistant Controller, Controller, VP of Finance, CFO, and now CEO.

Missy Pieske, left, will rotate off the board on Jan. 1. Dave Fitz-Gerald will conclude his two year term and leave the board May 1, but not before chairing a committee that will be tasked with examining The ESOP Association's governance structure and offering recommendations.

She is a Trustee of the Employee Ownership Foundation and holds a BS in Accounting from Ohio State University.

The second person nominated to the Board is Daniel Goldstein, the President and CEO of Folience in Cedar Rapids, IA. Daniel serves on the boards of multiple organizations, and in February he did an outstanding job testifying on behalf of The ESOP Association at a hearing of the House Small Business Committee. Like Robyn, Daniel is an Employee Ownership Foundation Trustee.

Daniel has two degrees from Rensselaer Polytechnic Institute—an MS in Science and Technology Studies and an MBA in Finance—as well as a BA in Fine Arts and Economics from Colgate University. In 2017, he participated in the fantastic Leading in an Ownership Setting program, designed for leaders of ESOP companies. (Having been through the program myself, I can tell you it is the best investment ESOP leaders can make.)

As an organization we are lucky to have a treasure trove of skilled volunteers willing to share their energy, time, and

insights with our organization. On a personal level, I am especially thankful.

The volunteer leaders of this organization—especially the chapter officers, the Advisory Committee members, and the Board—have invested tremendous time and energy in TEA, especially this year. You have all made it possible for us to achieve so much in 2020, and you are laying the groundwork for an even brighter future for TEA and employee ownership. I can't wait to see what our future holds!

Remembering Jerry Kaplan

ESOP Pioneer Will Be Missed

It is with sadness that The ESOP Association learned of the passing of Jerry Kaplan, a tax attorney and pioneer in the employee ownership field.

Kaplan's involvement in ESOPs began in 1974, the year that the Employee Retirement Income Security Act codified ESOPs into law. Kaplan read an article about ESOPs, became interested, and started asking others about this new way to conduct leveraged buyouts. ESOPs were so new that no one had any experience with them, Kaplan said in an interview with ESOP Marketplace.

He attracted so much attention with his inquiries that he was asked to write the first paper on ESOPs, which he presented to the University of Chicago Tax Law Institute in 1985.

When tax law changes in 1984 made ESOPs even more attractive, Kaplan become more involved in helping clients set up these plans. Over the years he was instrumental in forming many ESOPs, including unusual arrangements such as the purchase of a controlling interest of United shares that was initiated by its employees.

Over the course of a long and impressive career, Kaplan served as the senior counsel at McDermott Will & Emery, and was the founder and CEO of Delaware Place Advisory Services, LLC.

He also generously contributed his time to nonprofit organizations. At The ESOP Association he served as chairman of the Legislative and Regulatory Advisory Committee from 1985 to 1990, and was on the Valuation Committee.

He also served on the Administrative Practice Committee of the American Bar Association's Tax Section, was a member of the editorial advisory board of Shannon Pratt's Business Valuation Update, and served on the board of advisors of the *Corporate Taxation Journal*.

In 2004, Kaplan was elected a Fellow of the American College of Employee Benefit Counsel, and in 2005 was named a Fellow of the American Bar Foundation.

Kaplan's contributions to the employee ownership community were substantial and will be missed.

Kaplan's family asks that in lieu of flowers, well-wishers honor him by donating either to their favorite charity or to the Chicago Symphony Orchestra, where Kaplan was past Chair of the Executive Committee of CSO Governing Members.

Ownership Advantage

Establishing an ESOP Communication Committee in the New Year

By Jason Wellman, Director of Ownership Culture, ESOP Partners
Edited by Ginny Vanderslice, Principal, Praxis Consulting Group Inc.

How do you establish an ESOP Communication Committee in 2021? Or maybe you already have an ESOP committee, but you need to refocus your time and resources in 2021. The members of an ESOP Communication Committee will focus mainly on ESOP education and training for fellow employee owners, along with basic financial literacy education. The committee also may assist in gathering information from fellow employee owners, create and provide ESOP related solutions, and track results.

There are five critical steps in the annual process for developing and maintaining an effective ESOP Communication Committee in the new year.

Strategic Planning

The first step in the process is to have a strategic planning meeting (or multiple meetings) with the senior leadership team to establish alignment for the committee with the company's initiatives. I would encourage the committee

Calendar of Deadlines and Important Dates

Jan. 6	Congress Sworn In
January	**State and Regional Chapter Council Meeting** *(tentative)*
Jan. 20	Presidential Inauguration
Feb. 3-4	**ESOP Professionals' Winter Forum**
Feb. 13	AACE and EOM Poster Entries Due
February	Spring Chapter Meetings Begin
March	Spring Chapter Meetings Continue
June	**Employee Owner Retreat**
June	Summer Webinar Series Launches
June	Chapter Summer Events Begin
July 18-23	**CEO Leadership Program, Part I** This event is for CEOs/Presidents of ESOP companies or their designated successors
Nov. 10-13	**Employee Owned 2021**
Dec. 5-9	**CEO Leadership Program, Part II** This event is for CEOs/Presidents of ESOP companies or their designated successors

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

to do an employee ownership engagement survey of their fellow employee owners to help understand which elements of the employee ownership benefit may need to be developed during the new year.

One of the byproducts of these meetings is the creation of a committee charter, that will provide the guiding principles for committee members, along with the committee's mission and vision statement. If you already have a committee charter, it will be important to review the mission and vision statement of your charter document to ensure it is in alignment with your goals for the committee in 2021.

The review should focus on evaluating the committee's charter document, which should include the following items:

- Mission statement.
- Eligibility requirements.
- Length of membership.
- Expectations of the chair and the committee members.

Part of the committee's strategic planning process is to have an annual regroup and/or retreat virtually or in person. A major component of this meeting is to review the survey results from ESOP participants to make sure the committee is making progress on key annual initiatives.

Committee Overview

The second step in the process is to announce the creation of the committee or re-announce the committee's existence for all employee owners.

This announcement should highlight the mission and vision statements for the committee. This announcement is providing individuals with an opportunity to gain more information and knowledge about the deliverables and inner workings of the committee.

Making a commitment of time is a key step all committee members must take to be effective in their roles. Time is the number one hurdle for most committees. Committee members have a "day job", but still need to allocate time to fulfill their committee responsibilities.

This is why it is so important to set clear expectations about the time commitment in the committee charter document. That way people will know what is expected before they apply.

Application Process

The third step in the process is to accept and review committee applications. This should be an annual process that enables small groups of individuals to drop off the committee and provides new participants a chance to join the group. This process can help ensure that new ideas continually flow to the committee.

The announcement process should include details about when, why, and how to apply for one of the open committee positions.

Education and Development

The fourth step in the process is training and developing the committee members each year to advocate for employee ownership.

Initial and ongoing training is critical for committee members and ESOP participants. This step often requires external resources to get the process jump-started.

Providing proactive educational materials can help make advocates out of ESOP participants and committee members, who can play a critical role in ensuring the ownership culture continues to move forward.

Identify the time commitment for the committee chair and members to make sure they are each trained and educated on the company's specific ESOP details. Then, outline a training schedule to review the "nuts and bolts" of the ESOP plan by attending webinars and seminars. Make sure to walk through hypothetical examples built around your specific ESOP plan document. Ongoing development and training can be achieved by attending (in-person or virtual) programming at the local, regional, and national level through The ESOP Association.

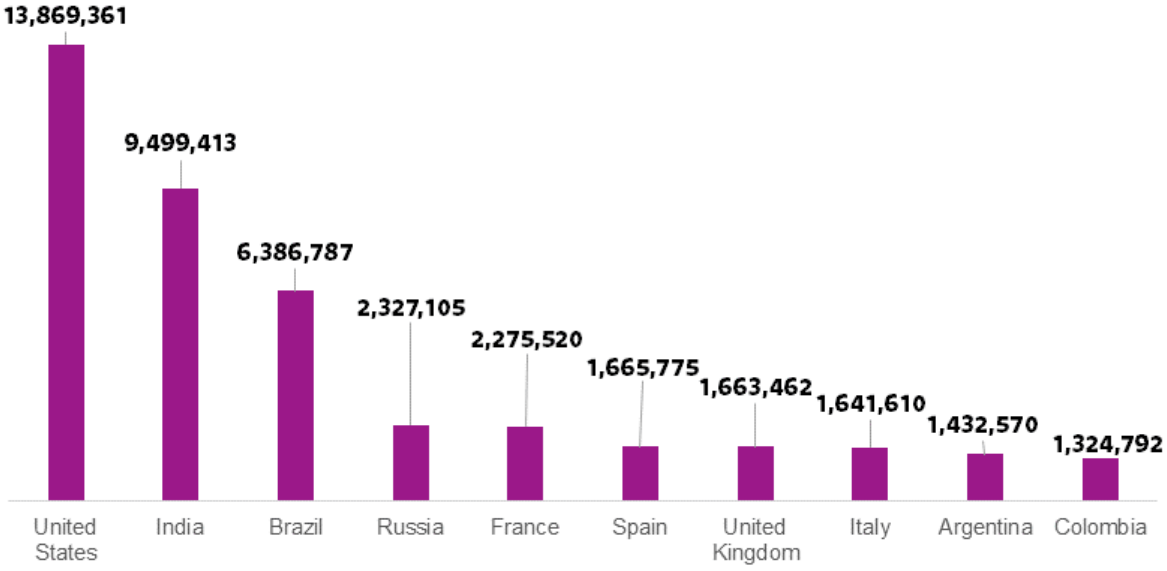
Execution of the Strategic Plan

The fifth and final step is to execute your mission and vision. One example could be producing a recurring newsletter for the company's employee owners throughout the year. The initial time commitment for committee members will be minimal, but this will add up over the year. Ensuring that committee members are available to carry out initiatives will be important to the committee's success.

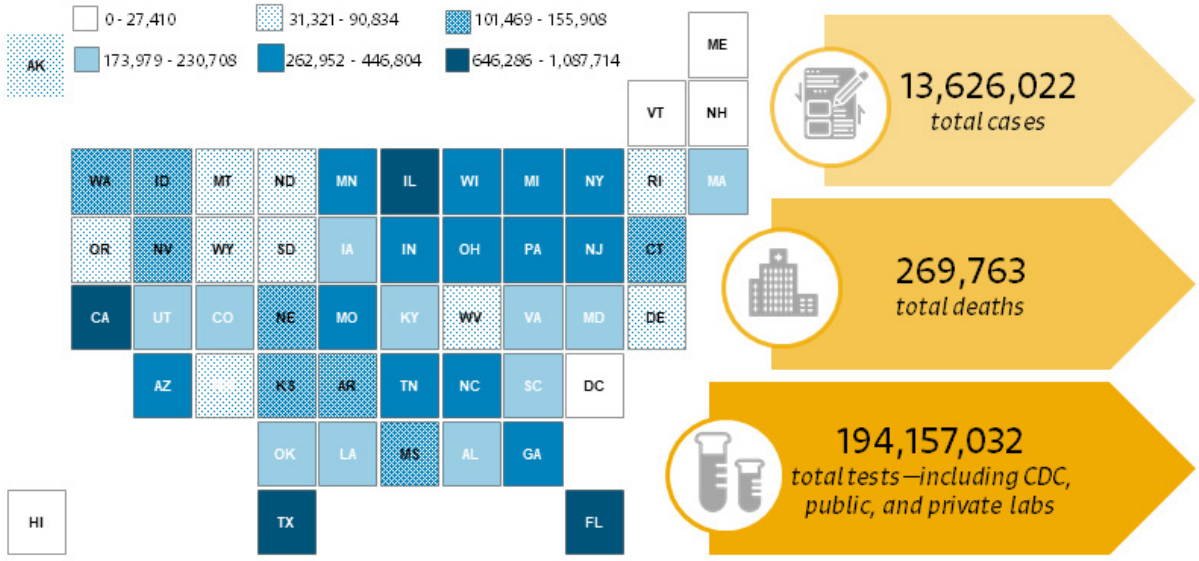
Below is a snapshot showing how COVID-19 cases have compared across countries and across states within the United States.

Countries with the Most COVID-19 Cases

Source: John Hopkins, data as of 12/2/2020



COVID-19 Cases Reported to the CDC*



Territories: AS | GU | MH | FM | MP | PW | PR | VI

*Data include confirmed and presumptive positive cases of COVID-19 reported to CDC or tested at CDC since January 21, 2020, except for test results for persons repatriated to the United States from Wuhan, China and Japan. State and local public health departments are now testing and publicly reporting their cases. CDC case counts and death counts include both confirmed and probable cases and deaths.

Sources: Centers for Disease Control and Prevention, The COVID Tracking Project, data as of 12/2/2020

Once the committee is set up, it will be important for the group to be well maintained. Here are some tips for ensuring your ESOP committee remains effective all year long:

- Maintain a positive attitude throughout the entire lifecycle of the committee.
- Stay focused on the mission statement and annual initiatives. Effective ESOP committees can and will be tasked with items outside their areas of responsibility. Be prepared to say no to the board of directors and/or senior management on specific projects that do not align with the committee's mission statement and annual initiatives.

To grow an identity as a committee, answer these questions:

- How are you going to provide solutions to pain points and concerns?
- What will the committee's decision process look like?

By following this process, your company can and will have a high performing ESOP communication committee in 2021, but it won't be easy. Maintain your focus on achieving you're the committee's mission statement in all it does throughout the year. Also, do not be afraid to try something new when you're planning for 2021 and beyond, especially if you are challenging your ESOP participants to learn more about your company's ESOP plan.

Chapter Sponsorships Updated, Aligned

New Annual Option Makes It Easier to Buy and Track Sponsorships, Ensures Your Brand Is Seen Throughout the Year

Purchasing a sponsorship at one of The ESOP Association's 18 chapters is now an easier and potentially faster process, thanks to changes implemented just this month. The new changes fix some longstanding issues and can provide a better, faster experience for members.

The Association's leadership realized that sponsorship options and benefits varied from one chapter to the next, as did pricing structures and deadlines. As a result, companies that wanted to purchase more than one sponsorship throughout the year—whether at one chapter or multiple chapters—had to conduct multiple purchases and track multiple receipts.

That is no longer the case.

Chapter sponsorships now have consistent levels of benefits and consistent naming. What's more, all sponsorships are for the entire year, saving time and effort for all involved and making it easy to ensure that your

Annual Chapter Sponsorship Levels

Benefits	Leader	Promoter	Supporter	Contributor
Pre-conference attendee list (w/o emails)	X			
Post-conference attendee list (w/o e-mails)	X	X		
Company name listed as a sponsor on Chapter events - **main registration page for events** (excludes roundtables)	X			
Listed on all chapter events registration page - **sponsorship tab**	large logo (includes roundtable events and networking events)	medium logo	name	name
Included on the conference brochure (pdf or digital)	large logo	medium logo	name	name
Sponsor recognized in e-mail to chapter meeting **registrants thanking sponsors**	large logo	medium logo	name	
Company logo and website link placed on the **chapter website sponsorship page**	large logo	medium logo	name	name
Company announced and logo displayed, or name listed all chapter meetings **(virtual/print materials/signage)**	large logo	medium logo	name	name
Logo displayed for chapter **roundtable** events	logo			
Posting on the **chapter HUB** thanking the sponsors	large logo	medium logo	name	name
Badge ribbon for in person meetings	X	X	X	X
Display table for in person meetings	X	X	1/2	

message is consistently visible to members of the chapter or chapters you choose.

These sponsorships will apply to events that are virtual, in person, or a hybrid. The table on the preceding page shows the benefits for each sponsorship level.

Note: Annual chapter sponsorships do *not* apply *to* 2021 Regional Conferences, which range in price from $750 - $6,000 and may be purchased separately starting in April.

For more information and to see prices for the options listed below, visit the web page for your chapter.

How Much Insurance Is Enough?

New Benchmarking Data Can Help You Determine How Much Corporate Liability Insurance Your ESOP Company Should Carry

By Jeffrey Gelburd, Vice President and Program Administrator, Murray

ESOP companies often wonder if they are holding the right amount of corporate insurance. It is, of course, an important question: While no executives want to find at a time of crisis that they are under insured, neither do they want to overspend on a level of protection that does not match their needs.

While there are no formulas or ratios to help answer this question, it is helpful to look at data offering a high-level view of the amounts of coverage being purchased by other ESOP companies, based on their employee count, corporate asset size, and ESOP plan asset size.

These data come from an executive liability insurance program offering Directors and Officers (D&O), Fiduciary, and Employment Practices Liability (EPL) insurance for ESOP companies.

The program—which is endorsed by The ESOP Association and is entering its 32nd year—currently insures more than 350 employee-owned companies. The data used to develop these results are taken from reports generated by the insurance companies providing the coverages in our program.

Separate vs. Shared Limits of Liability

Companies that purchase insurance have the option of applying policy limits separately to each coverage type (D&O, Fiduciary, and EPL) or spreading out the limits on a "shared" basis across all three insurance types.

Sharing coverage limits generally results in a lower premium for the policy holder. Having a policy with separate policy limits is an alternative to increasing your overall policy limit on a shared basis.

Based on our data, most policy holders opt to apply limits separately. Among purchasers of EPL insurance, a majority opt for separate policy limits. This trend is even more pronounced in D&O and Fiduciary coverages, where 59% and 63%, respectively, purchase policies with limits on a separate basis.

Average Limits of Liability

The average limits of liability for D&O and Fiduciary insurance are trending upward, the data show. Compared to the most recent study, which was done in 2018, the average

> ***The average limits of liability for D&O and Fiduciary insurance are trending upward, the data show.***

Fiduciary limit increased nearly 26%, from $1.99 million to $2.5 million. For D&O insurance the limit increased even more substantially, jumping nearly 42% from $1.975 million to $2.8 million.

We believe this trend is a result of the following factors:

- A continued increase in activity against ESOP companies by the Department of Labor.
- The number of ESOP transactions within a company in which the ESOP increases its ownership.
- Stability of premium costs for the additional limits of liability (although overall premiums continue to rise).
- Policies that have their limits apply on a shared basis are more apt to have higher limits than otherwise.
- Should there be a claim on the policy, defense costs (i.e., attorney fees) are paid within the policy limit, thereby eroding the policy limit to pay for an award or settlement.

Unlike D&O and Fiduciary insurance, the average limit on EPL insurance stayed roughly the same over the past three years.

D&O and Fiduciary Limits

Below is a breakdown of the limits of liability being purchased for D&O insurance and Fiduciary Liability

insurance, based on common underwriting data of corporate or plan assets.

Corporate or Plan Assets <$10 million.

D&O Liability Limits—75% of ESOP companies had D&O policy limits of $1 million. The remaining 25% in this category had limits between $2-$5 million.

Fiduciary Liability Limits—70% of ESOP companies in Category I had fiduciary policy limits of $1 million; 21% in this category had $2 million in limits and the remaining had limits of $3-$5 million.

Corporate or Plan Assets $10 million - $25 million

D&O Liability Limits—46% of ESOP companies in Category II have $1 million policy limits. 25% had $2 million limits and 27% has D&O limits of between $3 million - $5 million. No company had more than $5 million in this category.

Fiduciary Liability Limits—29% had fiduciary limits of $1 million while 35% had limits of $2 million. The remaining 36% had fiduciary limits of between $3 - $5 million.

Corporate or Plan Assets between $25 million - $50 million

D&O Liability Limits—41% of ESOP companies had limits of $1 million; 21% had limits of $2 million and 39% had limits of between $3 million - $5 million.

Fiduciary Liability Limits—32% in Category III had $1 million in limits while 28% had a $2 million limit. The remaining had limits of at least $3 million.

Corporate or Plan Assets > $50 million

D&O Liability Limits—41% of the ESOP companies in category IV had $5 million or above in D&O limits. Otherwise, a little more than half had at least $2 - $4 million in limits.

Fiduciary Liability Limits—Only 10% of ESOP companies in this category had a $1 million limit; 43% had limits of either $2 or $3 million, while another 43% had $5 million or more.

Employment Practices Liability Limits

To properly compare limits of liability for Employment Practices Liability, we have categorized ESOP companies by employee count, according to the data below.

Fewer Than 50 employees. At this size, 82% of ESOP companies had policy limits of $1 million; 14% had a $2 million policy limit. The remaining 4% had limits of $3 million or more.

Between 50-100 employees. At this size, 58% of ESOP companies had $1 million in policy limits and 14% had a policy limit of $2 million. The remaining 28% had policy limits of $3 million or more.

101-250 employees. At this company size, 41% of ESOP companies had policy limits of $1 million; 40% had a $2 million limit. The remaining 19% had limits of $3 million or more.

More than 250 employees. In this category, 33% of ESOP companies had a $1 million policy limit while 17% carried a $2 million limit. The remaining 50% had $3 million or more in policy limit.

More Information

Murray, an independent insurance agency located in Lancaster, PA, administers an affinity insurance program placing executive liability insurance (D&O, Fiduciary, and Employment Practices Liability) for ESOP companies. The program also offers cyber liability and crime insurance and is endorsed by The ESOP Association. Coverage can be accessed directly from Murray or through a local insurance agent.

Legal Update

Three New Opinions Relevant to ESOP Fiduciaries

By Larry Goldberg, Partner, ESOP Law Group
Reviewed by Julie Govreau, Senior Vice President and General Counsel, GreatBanc Trust Company

This month's Legal Update examines three new opinions in court cases that provide insight into subjects facing ESOP fiduciaries.

The three cases are New England Biolabs v. Miller, Lysengen v. Argent Trust, and *Burke v. Boeing*.

New England Biolabs v. Miller

In *New England Biolabs v. Miller*, (USDC. Mass 11-23-2020) the court considered a case in which a plan administrator

believed it overpaid an ESOP participant for his benefit distribution, and the ESOP sought reimbursement.

Under the terms of the plan, retiring participants were to receive a distribution in cash based on the stock's value immediately prior to their termination of employment. The plan did not permit participants to defer their retirement distributions.

Miller retired after retirement age and alleged that he was told by an NEB employee that he did not have to take his retirement distribution. Miller did not return the distribution forms and received no distribution for two years. During that time, the stock value increased.

The ESOP was amended to require accounts of all terminated employees to be converted to other investments. Upon being informed of the change, Miller agreed to a distribution; payment was made using the valuation for the year-end immediately preceding distribution.

Although the plan administrator took no action during the two years after Miller's retirement, the ESOP claimed Miller was overpaid and should have received the (lower) stock price that existed at the time of his retirement, in accordance with the plan.

The ESOP moved for a preliminary injunction, to prevent Miller from disposing of the plan assets until the case could be decided.

In determining whether preliminary injunction was appropriate, the court first concluded that NEB had standing to sue Miller to collect the funds that would otherwise belong to the other participants in the ESOP.

Next, the court determined that Miller would be treated as a fiduciary in judging his actions. The court looked to the ERISA definition of a fiduciary, which includes one who "exercises control over plan assets." The court stated the definition would include a person who unlawfully receives and retains plan assets.

Third, the court dismissed NEB's state law claim of "unjust enrichment" as being preempted by ERISA.

Finally, the court granted a preliminary injunction preventing Miller from disposing of the overpayment prior to resolution of the case.

Certainly, when the case moves to full trial on the merits of the plan's position, the court ruling that the participant is an ERISA fiduciary will make it much more difficult for Miller to defend his position. It is important to note that the opinion does not provide enough facts to be clear that the ESOP made a mistake. What is important is that the court found that a participant who receives an overpayment may be treated as a fiduciary as to those plan assets.

Lysengen v. Argent Trust

Lysengen v. Argent Trust, et. al. (USDC Cent. Illinois. 11-3-2020) involves claims by plaintiffs that the ESOP trust paid more than fair market value for stock in connection with the establishment of the ESOP. The court denied the defendant's motion to dismiss.

The case follows very much in line with *Allen v. GreatBanc Trust* in which the 7th Circuit denied a similar motion to

dismiss and was satisfied with very limited factual pleadings by the plaintiffs.

In moving to dismiss, the *Lysengen* defendants first asked the court to take judicial notice of the fact that the transaction had already been the subject of a financial fairness determination in state court involving a claim by the minority shareholders. The court refused.

In reviewing the plaintiff's statement of facts to support the allegation of an overpayment by the ESOP, the central facts are simply that the transaction price paid at the May 2017 closing was $75.25 per share and the year-end value at December 2017 dropped to $33.78. The court cited *Allen* for the position that this allegation is basically sufficient to avoid a motion to dismiss.

In *Lysengen*, there was a little further confusion over the stock price because there was apparently a prior ESOP and a stock value of $58.04 was determined as of December 31, 2016, which the company stated was in error and was later corrected to $72.57 per share. The court concluded the plaintiffs made a sufficient showing to avoid a motion to dismiss and reaffirmed the 7th Circuit precedent, which states that the statutory exemption to prohibited transaction rules is an affirmative defense.

The defendants also were unable to obtain a motion to dismiss on the alleged breach of loyalty claim under ERISA Section 406(b)(2) as the court believed the allegation of an overpayment supported the claim the fiduciary was disloyal to the plan participants. The court also held that the drop in stock value justified further discovery on the breach of fiduciary duty claims.

The court also refused to dismiss the plaintiff's claims that the indemnification provisions violated ERISA, and instead, asked for further findings on the subject.

Burke v. Boeing

In *Burke v. Boeing* (USDC Eastern Division. Illinois. 11-12-2020) we find a silver lining as it relates to the delegation of fiduciary duties. This case involves breach of fiduciary duty claims against the fiduciaries for the Boeing Voluntary Investment Plan—a combination 401(k)/ESOP—in connection with the offering of Boeing stock in the backdrop of the Boeing 737 Max accidents and groundings.

As a publicly traded company, Boeing offered its plan participants the opportunity to purchase Boeing stock through the ESOP-sub fund in its 401(k) plan. An Employee Benefit Investment Committee (EBIC) composed of officers of Boeing had the responsibility for investments under the plan and had the authority to appoint an investment manager to have fiduciary control over the investment of plan assets.

Further, an Employee Benefit Plans Committee (EBPC) had the fiduciary responsibility to administer the plan but no investment authority over plan assets.

Based on a trend begun after the *Dudenhoeffer* decision, the fiduciaries of the Boeing Plan delegated all discretionary authority over the Boeing stock fund to an independent fiduciary. The EBIC entered into an investment manager agreement with Newport to provide Newport with the exclusive authority over the investment of assets in the Boeing stock fund in the plan. The *Burke* lawsuit named both the EBIC and the EBPC as defendants.

As a threshold matter, the court had no hesitation in concluding that neither the EBIC nor the EBPC were ERISA fiduciaries with respect to the Boeing stock fund assets, as that authority had been delegated to Newport, and Newport alone was the responsible fiduciary.

Some recent cases involving privately held company ESOPs have concluded that a board of directors or selling shareholders are co-fiduciaries with the entity they empower with investment authority over ESOP assets. While the circumstances of a publicly traded company's stock are somewhat different, perhaps courts will consider the straightforward approach of the Boeing court before extending fiduciary status to delegating parties in a manner contrary to the plain reading of ERISA.

Advisory Committee on Administration

Interplay of Contribution Limits Under Code Sections 404 and 415

By Barbara M. Clough, QPA, QKA, Director, ESOP, Newport Group
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Plan sponsors often ask, "How much is our company allowed to contribute to the ESOP?" The answer is more complicated than it may seem at first glance and is based on two important code sections that govern the maximum deductible employer contribution and the maximum annual additions allowed.

Code Section 404 applies limits to *employers*; Code Section 415 applies limits to *employees*. Whether a contribution is too high will depend on decisions made at the employer level as well as decisions employees have made regarding deductions from their paychecks to a qualified plan sponsored by the employer.

Code Section 404

Code Section 404 allows plan sponsors to make deductible contributions to the qualified retirement plans they sponsor; in general, these contributions cannot exceed 25% of eligible compensation. (C-corporations may be able to exceed this limit in very specific situations and on the advice of counsel.)

Eligible compensation refers only to the compensation given to participants receiving an employer contribution. This total is referred to as the total eligible compensation. For 2019 plan years, the maximum compensation per participant is $280,000. For 2020, this limit has been increased to $285,000.

Now that we have determined the total eligible compensation, we need to apply the 404 limit, which is 25% of total eligible compensation. The employer contributions that count toward this limit are:

- Employer matching contributions.
- Employer safe harbor contributions (non-elective and matching).
- Employer discretionary contributions.
- Employer money purchase contributions.
- Prevailing wage contributions.
- Cash contributions in an ESOP.
- Stock contributions in an ESOP (valued at the fair market value on the last day of the plan year).
- Contributions to fund ESOP loan payments. (For C-corporations, this applies only to payments on principal; for S-corporations, this applies to principal and interest payments.)

If contributions exceed the 25% limit, a plan sponsor may declare that any amounts paid after the close of the plan year are attributable to the next plan year. These amounts will be allocated in the next plan year and will count towards the applicable limits in the following year.

Contributions exceeding the maximum allowable amount are subject to a 10% excise tax, which is reported on Form 5330. Additionally, any excesses must be included in the deduction limits in the following plan year.

Code Section 415

Code Section 415 is the annual additions limit. As mentioned previously, this is an employee limit. The maximum annual addition is the lesser of 100% of a participant's compensation, or $57,000 for 2020 ($56,000 for 2019). In other words, the limit for employees who earn under $57,000 in 2020 is their annual compensation.

Annual additions consist of the following items:

- Employee 401(k) deferrals, not including catch-up contributions.
- Employee Roth deferrals, not including catch-up contributions.
- Employee after-tax contributions to a qualified plan.
- Employer matching contributions.
- Employer safe harbor contributions (non-elective and matching).
- Employer discretionary contributions.
- Employer money purchase contributions.
- Prevailing wage contributions
- Reallocated forfeitures, other than to the ESOP.
- Cash and stock contributions made to an ESOP.
- Contributions to fund ESOP loan payments. (For C-corporations, this applies only to payments on principal, provided that highly compensated employees—or HCEs—do not receive more than one third of the allocation. For S-corporations, this applies to payments on both principal and interest.)
- ESOP reallocated forfeitures, which are valued at the fair market value on the last day of the plan year. (For C-corporations, forfeitures related to leveraged shares may be excluded if HCEs don't receive more than one third of the allocation. For S-corporations, these forfeitures include the value of the stock reallocated, plus the cash reallocated.)

HCEs are defined as individuals:

- Whose compensation exceeded the threshold in the prior year—$130,000 for 2020, or $125,000 for 2019.
- Who have *direct* ownership in excess of 5% in the current or prior plan year.
- Who are certain lineal ascendants and descendants of the individuals described above.

Always refer to your plan document for specific provisions relating to HCEs.

Your plan document will specify the provisions for testing ESOP allocations under Code 415 (the annual additions limit test). If provided, principal and interest payments related to the ESOP acquisition loan may be valued at the lesser of the fair market value of the shares released or the payments made for the plan year.

This provision typically is beneficial in the early years of an ESOP, when the fair market value is depressed due to the debt on the corporate books.

Correcting Contributions that Exceed 415 Limits

In the event the 415 limit is exceeded, a correction must occur. The correction method will be detailed in the plan document and should be consistent across all the sponsored plans.

Generally, there are two methods available for plan sponsors to make these corrections.

Method 1 is to limit allocations to affected individuals within the ESOP; the excess is reallocated to all remaining eligible participants. This approach allows participants to maintain their personal retirement savings approach within the 401(k) plan and to control their retirement investments as they did prior to the ESOP.

A word of warning, though: The effective contribution rate to participants may vary. For example, say the total contribution made to the ESOP, including loan payments, was 20% of pay, and that three individuals needed to be limited; the effective contribution rates could be different for each limited individual, and the net for all others might be 22% (for example).

This is sometimes difficult to communicate when relaying general information about the health and welfare of your ESOP.

Method 2 is to correct the excesses in the 401(k) plan by first refunding Roth or 401(k) contributions; this will result in the match on those contributions being forfeited.

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The language in a plan document generally states that the correction is being made under the Employee Plans Compliance Resolution System, or EPCRS.

This approach provides the greatest possible ESOP benefit to participants. Corrections to participants from deferrals will results in a taxable event that must be reported on Form 1040 the following year. In addition, the ADP and ACP tests must be reworked to reflect the adjusted contributions credited to participants for the plan year to ensure that no testing excesses occur in the current or future plan years.

This approach can be difficult to communicate to affected participants. Under the guidance of EPCRS, the IRS directs that excesses be avoided when possible.

How Much Is Too Much?

Returning to the question posed at the beginning of this article, there isn't a set answer on what constitutes a contribution that is too small or too large. The reality is that many ESOPs make large contributions based on generous contributions, loan payment obligations, and repurchase obligations.

When this happens, plan sponsors must work closely with their advisors when determining the contribution amount and allocation to make sure they comply with Code Sections 404 and 415.

Plan sponsors who carefully consider their participant retirement goals and benefit levels—as well as who pays for the benefits, the participants or the employer—can create an annual benefit package that meets the needs of all parties.

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