SB 561Capital Forest Products Bryant O'Kane 02-15-

Uploaded by: Bryant O'Kane
Position: FAV

February 14, 2022

The Honorable Guy Guzzone
Chair, Senate Budget and Taxation Committee
3 West Miller Senate Office Building
Annapolis, Maryland 21401

Dear Chair Guzzone,

On behalf Capital Forest Products, Inc, I am submitting this letter in support of Senate Bill 516 which would eliminate Maryland tax on the sale of shares to an Employee Stock Ownership Plan ("ESOP"). My testimony reflects the financial transactions and culture of mid-sized ESOP company located in Annapolis for over forty years.

I wish to thank the committee for hearing my testimony in strong support of SB 561, which I believe will encourage more ESOP formations, retain jobs in Maryland and increase tax revenue dollars. In my time here today, I wish to focus on the significant benefits my company and its employees have experienced since becoming an ESOP.

By way of background, Capital Forest Products was founded by Michael Tichenor in his hometown Annapolis, Maryland circa 1981 (hence the name Capital). Over the next 40 years, Mr. Tichenor and his wife Barbara grew from a two-man wholesale lumber operation to over fifty plus employees nationally. Mike instilled an entrepreneurial mindset among many lumber traders, ambitious to start their own business but lacking the resources. Capital Forest's model attracted the top tier in the lumber trader industry. Today, we are a quarter of a billion-dollar sales annually with double digit growth year over year. Mike and Bobbie Tichenor sold a 20% tranche of company to the employees in 2016 and becoming 100% owned last year. Capital's entrepreneurial model was extended to all employees of company. In Mr. Tichenor's own words, "I wanted to give back to those who helped Capital Forest grow over the last 40 years".

<u>Capital Forest Products, a 100% Employee-Owned Company.</u>

Great ESOPs like Capital Forest Products promote a culture of inclusion where all team members have a voice, and those voices are empowered. Since our company's recent transition into a 100% fully owned ESOP, the enthusiasm generated by my team members to participate in the financial growth of the company is palpable. The owner mindset fostered by the ESOP has increased everyone's commitment to the company. This is leading to inspiration for new product lines and improved operational efficiency in all areas of the company.

Unlike other companies, we are experiencing the opposite of the so-called great resignation. Out of fifty employees, only one voluntary resignation of a newly hired member has occurred in the last year.

The ESOP provides team members with an equity interest and a direct stake in the economic benefit of the company's performance. The profits ultimately go into their pockets through increase share value, not just the owner. It's a living example of the famous motto from the Three Musketeers – one for all and all for one.

As CFO, it is my duty to share financial information – a concept known as open book management -- and encourage team members to engage in the ESOP and the company. To use a sports analogy – it would be unfair to play in a game where you don't know the score or the rules. Unfortunately, that is the case today for many workers at American companies.

That is not the case at Capital Forest where team members know both the rules and the score. Accordingly, they feel empowered knowing that their input and opinions are both sought and valued. My ESOP team members are more motivated than ever and hold other team members accountable to perform at their best.

Who has benefited from our ESOP?

The answer is everyone. Our founder who sold his shares has benefited by receiving fair market value for his stake after a lifetime of building the business. I note that he may have enjoyed the sale even more if this tax advantaged bill provision had been previously enacted. Importantly, our founder is remaining with the company after the transaction. Additional he helped financed much of the sale by taking back a seller note from the company for his shares. The ESOP is the best exit strategy for many sellers to remain associated with and involved with the company they created.

The team members benefit because in addition to their 401(k) accounts, they now have a meaningful equity interest in the place where they work. The diversification prevents team members from putting their eggs in one basket. There's also the corollary, since the team members have skin in the game, they monitor the company very carefully. That's what employee-owners at an ESOP do. They are very involved in the day-to-day operations. When employees eventually retire or leave, the company the company has an obligation to buy back those shares at the last annual value as determined by the independent appraiser. These funds can then be rolled over to an IRA or taken into income. This is no different from other retirement programs.

The community benefits because ESOP companies stay where they were founded. They are not relocated out of state or have corporate staff downsized following a strategic acquisition. The company and its employees continue to lease office space, support local merchants, and pay applicable taxes. It's clearly a win-win for all.

Past, present, and future.

A good ESOP company also goes above and beyond for its team members. For example, in March of 2020, as the pandemic was ramping up with fear of the unknown, Capital's management team stepped up to protect our own. The executive team was concerned about institutional closures, the banking, payroll, and mail services would be interrupted or come to a complete stop. Therefore, we prepaid our employees three weeks of salary before being earned to ease any financial burden caused by the pandemic. At the same time, executives also volunteered to suspend their salary for three months until economic conditions improved. It turned out that these concerns for the company's livelihood did not materialize, but our team members knew that by its actions Capital Forest cared about them.

I hope after hearing my remarks you now can appreciate the ESOP concept as much as I do. I now welcome any questions you may have.

Bryant R. O'Kane
Chief Financial Officer
Capital Forest Products, Inc.

SB561 Income Tax Subtraction Modification Employee
Uploaded by: Charlotte Davis
Position: FAV

Rural Maryland Council

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John Hartline, Chair *Charlotte Davis, Executive Director*

Testimony in Support of
Senate Bill 561 - Income Tax - Subtraction Modification - Employee-Owned Businesses
Senate Budget and Taxation Committee
February 16, 2022

The Rural Maryland Council supports Senate Bill 561 - Income Tax - Subtraction Modification - Employee-Owned Businesses. This bill creates a subtraction modification against the State individual and corporate income tax for any income from a qualified transfer of stock or membership interest of a Maryland corporation or limited liability company (LLC). If the qualified transfer is to a direct share ownership plan, the subtraction is limited to the lowest amount of stock or membership interest transferred to any tenured employee during the taxable year multiplied by the number of all tenured employees. The promotion of more Employee stock ownership plans (ESOPs) will ultimately benefit the rural and underserved areas of Maryland.

ESOPs are worker owned cooperatives, meaning the business is owned and managed by the workers. Being a worker for a cooperative comes with specific advantages. For example, cooperative workers generally receive higher wages than non-cooperative workers. Through collaboration and building economies of scale, this solution is able to work in all underserved communities of the State, not just rural communities.

Much of rural entrepreneurship exists of family owned and operated businesses. As our rural population is aging, succession and exit planning for family businesses are vital to ensure the businesses' future continuation and vitality. Succession and exit planning will help ensure that these businesses do not cease to exist when the owners decide to retire or move on to other endeavors.

In Fiscal Year 2017, the Rural Maryland Council awarded a grant to Frostburg State University Office of Research Sponsored Programs to conduct a feasibility study to investigate the need for business succession and exit planning strategies in western Maryland. The University investigated two business succession and exit planning programs, one in Kansas and another in Pennsylvania. As a part of the grant scope of work, the University interviewed 20 businesses regarding succession planning and identified 5 alumni interested in pursuing such opportunities. While it determined that there is a need to offer succession and exit planning services, there were not enough alumni interested in taking over such businesses. Employee stock ownership plans are a viable alternative to ensuring the retention of our rural small businesses and their continued vitality.

The Rural Maryland Council respectfully requests your favorable support of Senate Bill 561.

The Rural Maryland Council (RMC) is an independent state agency governed by a nonpartisan, 40-member board that consists of inclusive representation from the federal, state, regional, county and municipal governments, as well as the for-profit and nonprofit sectors. We bring together federal, state, county and municipal government officials as well as representatives of the for-profit and nonprofit sectors to identify challenges unique to rural communities and to craft public policy, programmatic or regulatory solutions.

CKC Testimony in Support of SB 561.pdf
Uploaded by: Christopher Croft
Position: FAV

Maryland Center for Employee Ownership

6211 Falls Road, Baltimore, Maryland 21209

Committee: Senate Budget & Taxation
Testimony on: HB 561 "Income Tax - Subtraction Modification - Employee-Owned Businesses"
Position: Support
Hearing Date: February 16, 2022

The Maryland Center for Employee Ownership requests a favorable report for SB 561.

Thank you Mr. Chair and Members of the Committee. My name is Christopher K. Croft. I am the Executive Director of the Maryland Center for Employee-Ownership (MDCEO). I was recently an adjunct professor and research fellow of International Studies and Sustainable Communities in the School of Public Policy at the University of Baltimore.

With the passage of 2018 federal legislation, the Main Street Employee Ownership Act[1], I am hopeful we can build upon this framework to make all of Maryland an "Opportunity Zone" through Employee Ownership (EO).

My commitment to employee-ownership is due to my granddaughter and my students. I want them to have the same opportunities that I enjoyed growing up. Many of my past students worried about how they are going to pay their mounting student debt after graduation with today's meager salaries that often pay less than a living wage.

My Sustainable Communities classes conducted research with case and feasibility studies throughout semester-long courses. Students immersed themselves in learning about local economic and environmental issues. They examined challenges like malnutrition in Baltimore's "food deserts" with an eye to recommend solutions to the problems. Invariably, at the end of each semester, team papers were turned in with student's urging the incentivizing and growing of local businesses run and managed by those in our communities - employee owners.

1 https://smlr.rutgers.edu/sites/smlr/files/Documents/Faculty-Staff-Docs/3-21-18_main_street_employee_ownership_act_summary_5_copy.pdf

In rural areas of Maryland many people are also struggling to put food on the table, which costs more-and-more, with jobs that pay less-and-less. Something must be done immediately to ground opportunities locally for our citizens. Broad-based employee-ownership is a proven strategy to build teamwork, create assets for workers, retain jobs in our neighborhoods, and build nest eggs for retirement plans[2]. In fact, a 2019 NCEO study highlighted the impact of EO in struggling communities - showing that employee-ownership in distressed areas is good for employees, their communities, and the firms.

Employee-ownership is also an important tool for business succession planning. Thirty-three percent of Maryland business owners have no exit or succession strategy. Employee ownership is a vital tool to keep jobs and businesses functioning and flourishing in Maryland. According to the Small Business Association, Maryland lost approximately 35,000 jobs due to the permanent closure of businesses with more than 20 employees between 2001 and 2010. With sixty percent of small businesses owned by baby boomers, job losses associated with the generational transition are expected to increase. Employee-ownership is a natural solution to this “Silver Tsunami” of retiring boomers.

Nationally, we can see from the long list of successful employee-owned businesses, that it is not only possible, but it can work for everyone while promoting localism, self-reliance, and pride. Further, In states such as in Wisconsin, where introduction of similar legislation has occurred, fiscal analysis has shown revenue neutrality.

In conclusion, my students' reports usually reflected that much of our community’s problems are exacerbated by the lack of employment opportunities. SB 561 is an important step in halting the loss of businesses in Maryland, and will provide benefits for our communities by allowing business owners’ legacies to live on after them in the form of living wage opportunities, while giving Maryland businesses a competitive advantage over neighboring states in the Chesapeake region.

The National Center for Employee Ownership[3] has a considerable amount of information on the largest employee-owned businesses in the US[4] and the facts about how employee-owned companies out compete traditional businesses[5]. I urge you to explore their website and learn more about employee ownership in America today.

I have personally committed my time and efforts to promoting Employee Ownership in Maryland. My organization, MDCEO, supports SB 561 and strives to make all of Maryland an “Opportunity Zone.” through Employee Ownership. I urge this Committee to do the same.

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[2] https://www.nceo.org/articles/esops-too-risky-be-good-retirement-plans
[3] https://www.nceo.org/
[4] https://www.nceo.org/articles/employee-ownership-100
[5] https://medium.com/fifty-by-fifty/stocks-from-employee-owned-companies-outperform-s-p-ac375706124b

SB 561 Oral Statement.pdf
Uploaded by: Christopher Croft
Position: FAV

SB 561 Oral Statement:

Mr. Chairman and Committee, thank you for this opportunity to weigh in with my support of SB 561. My name is Christopher Croft. I am the Executive Director of the Maryland Center for Employee-Ownership. I was recently a professor of Sustainable Communities and Research Fellow at the University of Baltimore.

I have submitted written testimony for the record, but I want to emphasize the importance of this bill in a larger context. Chairman Guzzone, as a previous sponsor of this bill in 2019, I know you appreciate the opportunities this bill can create.

What the bill does is simple, when a business owner is ready to retire, the State of Maryland will waive the capital gains tax if the owner sells to the employees; thereby, keeping the jobs and revenues in Maryland. This opportunity is an *option*, not a mandate. The state of Iowa has had a 50% cap gains tax exemption for several years.

Looking at a larger picture, the following developments tell an important story:

- A recent study by the National Center for Employee Ownership shows that employee-owned businesses have fared better during this pandemic than other forms of business.
- Yet, past Labor Secretary, Robert Reich, has sounded the alarm that while working Americans are losing financial ground, "during the first 19 months of the pandemic, US billionaires added $2.1 trillion dollars to their collective wealth and that number continues to rise".
- The 2021, the Pandora papers revealed how the top 1 percent continue to avoid taxation through overseas havens.
- Recently the Rand Corporation study on the transfer of wealth over the last forty years from the working classes to the top 1 percent is in the order of *50 Trillian Dollars*.

When I was born, the American middle class was the envy of the world. Today, too many are struggling to survive paycheck to paycheck and, according to Noam Chomsky, even trivial social safety net efforts are impossible to get through the US Congress. It's time to help working- and middle-class Marylanders.

Our fiscal and policy note says that there will be a one-time expenditure increase of $68,000 in fiscal 2023, but it will come at a higher cost to our treasury when venture capitalists buy Maryland companies, strip them of their assets, lay off workers, and pocket the profits.

Let's give more Marylanders a *chance* at business ownership and an *opportunity* to build community wealth through passage of this bill. I urge you to vote favorably for SB 561.

Thank you -

Employee Ownership with a High_Involvement Culture
Uploaded by: Frank Shipper
Position: FAV

Honors, Fellowships, & Grants for Work on Employee Ownership

Co-author of the runner-up entry in the 2020 Emerald Best Case Award Competition. "John Lewis Partnership Approaching 100 Years – What Now?"

Invited contributor in 2020 to Oxford Bibliographies in Management. Ed. Ricky Griffin. New York: Oxford University Press,

Winner of the 2018 John Molson M.B.A. International Case Writing Competition, Shipper, F. & Hoffman, R. C. "John Lewis Partnership and Brexit or Not – What Now?"

Shared Entrepreneurship: A Path to Engaged Employee Ownership featured on the Aspen Institute website

USM Regents' Faculty Award for Research/Scholarship/Creative Activity 2014

Kevin E. Ruble Fellowship by Rutgers University 2013-2014

A Rosen Ownership Opportunity Fund (ROOF) Grant, January 2012

"Everyone a Team Leader: Shared Influence at W. L. Gore & Associates" reported by ScienceDirect to be one of the Top 25 Most Downloaded Articles for the 2009-2010 Academic Year

Louis O. Kelso Fellowship by Rutgers University, 2010-2011

← Open

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Shipper, F., Manz, C. C., Nobles, B., & Manz, K. P. (2014). Shared entrepreneurship: toward an empowering, ethical, dynamic and freedom-based process of collaborative innovation. *Organization Management Journal,* 11(3), 133-146, DOI: https://doi.org/10.1080/15416518.2014.949613

Salisbury UNIVERSITY

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Employee Ownership with a High-Involvement Culture A Win-Win-Win-Win Proposition

by

Frank Shipper, Ph.D.

Professor Emeritus of Management

Regents' Research Award Winner

FRANKLIN P. PERDUE SCHOOL OF BUSINESS

Open →

Employee Ownership with a High-Involvement Culture, A Win-Win-Win-Win Proposition for

Profits

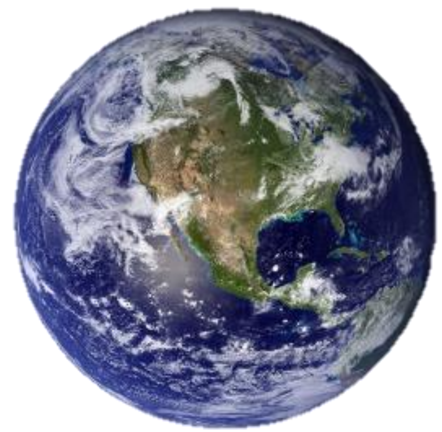
- Higher Profits
- Faster Growth
- Higher Innovation
- Higher Productivity
- Lower Susceptibility to Recessions
- Faster Recovery from Recessions
- Tax Advantages

People

- Greater Job Stability
- Higher Compensation
- Greater Wealth
- Larger Retirement Nest Eggs
- Higher Engagement
- Broader Prosperity
- Values Orientation
- More Vibrant Culture

Planet

- Environmentally Friendly Practices
- Recycling
- Leaders in Energy and Environmental Design
- Physical Stability



Politics

- More Vibrant Economy
- Greater Involvement
- More Tax Revenue
- Lower Need for Taxes
- Less Economic Inequality
- Bipartisan Support

Frank Shipper_s Testimony on Senate Bill 561 Sprin

Uploaded by: Frank Shipper

Position: FAV

Frank Shipper's Testimony on Senate Bill 561

Hello, distinguished members of the Maryland Senate. My name is Frank Shipper. I am a Professor Emeritus of Management at Salisbury University. I have researched, written, and taught about them both domestic and foreign employee-ownership for close to 40 years. Largely for my studies of employee-owned enterprises, I received the University of Maryland System Regents' Award for Research In addition to the Regents' Award, I have received multiple awards, grants, and fellowships for this work. Furthermore, I have made multiple invited presentations from the Haier Group in China to Oxford University in the UK.

Before proceeding, I want to make two points. First, let me clarify that employee-ownership does not have to be 100% for it to be effective. Some of the best-known, employee-owned companies such as Southwest Airlines, Herman Miller, Lincoln Electric, and NUCOR are also publicly traded. Other well know companies such as Intel, Google and many other high-tech companies also are partially employee-owned. Second, the benefits from employee-owned companies are too numerous to cover all of them in this brief, so I have enclosed a hand out that lists many others than I will cover.

When combined with a high engagement culture, employee-ownership represents a win-win-win-win form of enterprise. In short, the shareholders win because these companies are more profitable and faster growing than traditional ones. The worker-owners win because they have higher compensation both short and long-term and they are laid off less frequently than those in traditional companies.

The planet wins because they tend to be more environmentally conscious than traditional organizations. For example, Herman Miller designs cradle to cradle products from recycled material that can be recycled again at the end of its useful life. NUCOR Steel and SRC Holdings are two of the largest recyclers of ferrous products in the US. Maryland's own EA Engineering was honored in 2017 with the Outstanding Corporate Leadership Award from the Maryland Recycling Network. In addition, its corporate headquarters won a LEED's Platinum certification from the U.S. Green Building Council**.**

The community and its leaders win because employee-owned companies build a more vibrant economy than traditional companies. In the US, this has happened in Silicon Valley, Grand Rapids, MI, Twin Fall, ID, and Springfield, MO. In Spain, this happened against all odds in the Basque region and in Italy, around Bologna.

Employee-owned enterprises with a high-engagement culture provide an opportunity where every worker can be an owner, a leader, and an entrepreneur. Employee-ownership represents an alternative approach to business that works for all.

It is only logical that the State of Maryland supports employee-ownership for three reasons. First, other states such as New Jersey, Pennsylvania, New York, Ohio, Virginia, and California are doing so. The two states with which Maryland shares long borders -- Pennsylvania, and Virginia -- have 312 and 302 employee-owned companies, respectively. By contrast, Maryland has only 135 based on 2019 data. The competition for employee-owned companies nationwide was escalated by the President signing the Main Street Employee Ownership Bill in August 2018. Therefore, in the interstate competition for good paying and stable jobs for Maryland's citizens, it makes sense to support the bill.

Second, employee-ownership (EO) helps to moderate income and wealth inequality by enlarging the economic pie, not by redistributing portions of the pie. It works under a variety of socio-economic conditions. A nationwide study released in 2018 found that EO had positive impact on distressed communities that "… are disproportionally rural, nonwhite, and concentrated in the South and East of the U.S.; they were also hit hardest by the recession that began in 2007…"

Thus, I ask you to support Senate Bill 561 to enhance the growth of Maryland's economy, and increase the wealth and well-being of all.

Ian MacFarlane testimony Feb 2022.pdf
Uploaded by: Ian MacFarlane
Position: FAV

Mr. Chair and members of the committee, thank you for your time and your service. I am Ian MacFarlane, CEO & Chair of EA Engineering, Science, and Technology, an environmental consulting firm headquartered in Hunt Valley with 600 employees nationally of which 40%, including 'back office' headquarters staff work out of Maryland offices (Hunt Valley, Ocean Pines, Abingdon). [I am also the former Chair of the Maryland Higher Education Commission, MHEC, appointed to the board in 2012 and retiring as Chair in 2020.] EA serves government and industry with scientific consulting and engineering, and example Maryland agency clients include SHA, MES, MPA, and MAA. EA was founded in 1973 by a JHU professor, and after a stint as a publicly traded company, has remained independent, that is resisting offers to be bought out by non-Maryland firms, by going private, gravitating to employee ownership. We became a partial ESOP in 2005, then went 100% ESOP, and legal benefit corporation, in 2014- so we are very keen on providing value to all our stakeholders, which include our employees, the clients we serve, and local communities.

I am living 'the dream' as an employee-owned firm leader, as our employees, being owners too, care deeply about doing well as a business, doing top quality work for our clients, and truly being part of the community. What leader wouldn't want that? An ESOP culture makes for a very healthy, collaborative, and caring work environment and fair treatment of our stakeholders. We believe ESOPs and employee owned firms should be promoted by State policy because they not only make great business partners for us, they are good for Maryland citizens, good for Maryland's economy, and good for the nation.

Good for Maryland's citizens because ESOP-owned firms focus on building retirement wealth. And I mean focus. This is a main goal of the firm, to assure our employee-owners have sufficient retirement wealth to live well in their communities. EA's stock growth as an ESOP (with employees as owners) has been about double the S&P 500. Employee-owners of ESOPs also experience greater continuity and certainty of employment. We are long-term focused, and lay-off reluctantly. ESOPs have done comparatively very well (survival, growth, retention of employees) over the Great Recession and COVID Pandemic relative to conventionally owned firms. To sum up in one metric about the employment relationship, EA's employee tenure is over double that of our industry in general, with significantly less employee turnover and a competitive advantage at attracting professional employee candidates. Further, ESOP management and employees work hard at making fellow employees' jobs meaningful, in part because we are doing this for ourselves….we strive to develop employee satisfaction and engagement, which leads to greater fulfillment, which leads to better health and well-being, less stress, and more productivity. It's a wonderful virtuous cycle. EA's employee engagement is about triple the engagement of average U.S. workers, with envious safety performance.

Good for Maryland's economy because ESOPs promote independence, which for Maryland means keeping firms headquartered here at home. Similarly, for the US, it means keeping equity ownership and the workforce patriated, and directly counteracting our society's growing wealth disparity. Maryland could have lost EA's 60 or so income-tax-paying corporate positions, and perhaps more, if EA had not gone ESOP to retain independence. Also good for our economy because ESOPs breed collective entrepreneurship and quality work. A collective ownership culture enhances innovation and empowers employee-owners to improve the organization, and value allocation to its stakeholders, in myriad ways. On service quality, I would compare EA's client ratings, and those of our fellow ESOP firms, to anyone's in our industry. As a citizen, I'd be proud to enhance Maryland's wealth-building, wealth-equality, innovation, and high-quality brands with more ESOP firms. Speaking of other ESOP firms…5 of the 150 largest US engineering design firms are Maryland based; 3 of those 5, including EA, are 100% ESOPs. ESOPs are making a difference in Maryland, and we believe all efforts should be made to promote more forming, such as through the subject legislation, and their future growth, for instance through procurement preferences.

In closing, thank you, and please consider this legislation favorably.
2/16/2022

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Ian D. MacFarlane, President, CEO, & Chair

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EA website, My Biography

EA is a 100% Employee-Owned Public Benefit Corporation

IMPROVING THE QUALITY OF THE ENVIRONMENT IN WHICH WE LIVE, ONE PROJECT AT A TIME®

Paul formed WorkPlace Consultants, LLC in 2007 to assist clients with their ESOP and benefits-related issues. He has served as Chair of The ESOP Association's Ownership Culture Committee, and as a member of The ESOP Association Board of Governors, the Employee Ownership Foundation Board of Trustees, and the NCEO Board of Directors. Paul is a frequent author and speaker on ESOPs and other benefits topics.

Paul received a BA degree in mathematics and a minor in business from the State University of New York at Binghamton in 1980, graduated from Boston University School of Law in 1983, and earned a Master of Laws in Taxation from Georgetown University Law School in 1987. Paul is a member of the Massachusetts and California Bars, and also has earned the SPHR certification from the Society for Human Resource Management.

Respectfully submitted,

Paul Horn
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HOUSING SECURITY:

- *No* ESOP respondents reported being behind on their rent or mortgage, compared to *more than 25 percent* of their non-ESOP peers.

3. 2020 Aspen Institute Report. ESOPs are helping to narrow the wealth inequality gap, according to a Report that draws on multiple studies funded by the Employee Ownership Foundation.

One study compared the wealth of employee owners at a group of ESOP companies to national averages. It found that employee owners earning low- and moderate-incomes had ESOP accounts with a median value of $165,000—far outpacing the typical median American household, which had only $17,000 in savings.

Employee owners who were closer to retirement fared even better: Of the low- and moderate-income employee owners surveyed, those ages 60 to 64 had *10 times more wealth* than the typical American in the same age group.

4. ESCA Survey. A 2018 survey of S corporation ESOPs conducted by the NCEO with support from the Employee-Owned S Corporations of America (ESCA) found that ESOP participants have more than twice the average total retirement balance of Americans nationally, and that those making less than $26,000 a year also have on average more than double the retirement savings compared to similar workers nationally.

C. Paul Horn Biography

Paul has been actively involved in the employee benefit s field since beginning his career as an attorney with the IRS Office of Chief Counsel in 1983. He litigated retirement plan cases before the Tax Court, worked on tax rulings, and coordinated IRS positions with other government agencies such as the DOL, PBGC, DOJ, and EEOC.

Paul then worked at major law firms in San Francisco and Washington, D.C. He returned to government service as FDIC Benefits Counsel, serving as the national coordinator for all employee benefits and tax matters involving FDIC bank receiverships.

Following completion of his FDIC appointment, Paul joined American Systems, where he had responsibility for all benefit and compensation programs. He played an integral role in the organization's transition to one of the country's largest 100% S Corp. ESOP companies in 1997. Paul served as President of The ESOP Association's Mid-Atlantic Chapter for six years, was named ESOP Chapter Officer of the Year in 2003, and helped the Chapter win the ESOP Association Chapter of the Year Award.

- <u>Improving company performance</u> – Studies like the ones below show that ESOP companies out-perform comparable companies, while exhibiting more resilience during economic downturns.

1. <u>Rutgers/SSRS Study</u>. During the pandemic, ESOP companies are dramatically outperforming other firms in such key areas as securing employees' jobs, and maintaining work hours, salary, and workplace health and safety. (Study conducted by Rutgers University and SSRS, funded by the Employee Ownership Foundation.) Key study findings show that, compared to other businesses, ESOP firms were:

- 3-4 times more likely to retain non-manager and manager employees.
- 3.2 times more likely to retain staff—*even when other businesses received funding through the Paycheck Protection Program and the employee owned firms did not.*
- Significantly less likely to reduce employees' hours or pay.
- More likely to send employees home to work during the pandemic—and did so earlier.
- More likely to provide employees with personal protective equipment, such as gloves and masks.

From an economic perspective, the study found ESOP companies "kept considerably more money in employees' hands—and in the economy" than other firms.

2. <u>John Zogby Strategies</u>. Zogby surveyed a sample of mid- and lower-level employees at employee-owned private companies and a sample of other non-ESOP employees and "found a world of difference between the two groups" in key measures during the pandemic, including:

JOB RETENTION:

- Non-ESOP employees reported experiencing job losses or downsizing at *six times the rate* of their peers at employee-owned companies.

FINANCIAL SECURITY:

- Non-ESOP workers have been adversely affected by the pandemic economy at *more than three times the rate* of employees at ESOP companies.
- *Twice as many* non-ESOP respondents as ESOP respondents are concerned about their ability to pay down debt.
- *Three times as many* ESOP employees say they are able to cover an emergency $500 expense, compared with their non-ESOP counterparts.
- *Twice as many* ESOP workers expect to retire by the age of 60 compared with workers at non-ESOP companies.

Recent National Center for Employee Ownership (NCEO) data chart shows 114 ESOPs in Maryland covering 25,866 participants.

Many "baby boomers" who own private Maryland businesses will be retiring in the near future -- the so-called grey tsunami. If they sell the business to a third party, the buyer may consolidate corporate staff via layoffs, move the headquarters out of state, and/or close certain operations. In contrast, these issues can be avoided if the owner sells to an ESOP and current management continues to run the company. This can benefit all parties – the seller, the employees, the community, and Maryland and local governments.

The seller may be subject to significant capital gains tax on the sale of shares to a third party buyer. SB 561 would encourage the sale of shares to an ESOP because this capital gains tax would no longer apply.[1]

Importantly, tax is not "avoided" but can be viewed as being deferred. Why? Eventually, employees will receive distributions from the ESOP which will be taxable or, if rolled over to an IRA, ultimately taxable when distributed therefrom. Moreover, the ongoing ESOP-owned business will continue to pay employment and other taxes, and its employees will of course continue to pay their applicable taxes on their paychecks.

By enacting SB 561, Maryland will keep pace with other states that have already enacted, or are considering enactment, similar rules to promote ESOPs.[2]

B. Recent Research Documents ESOP Success

The key benefits of ESOPs are noted below and followed by some recent supportive studies.

- Preserving jobs and community impacts – ESOP companies keep jobs in the communities where they are rather than moving or losing them.
- Helping companies attract and retain good employees – ESOP companies have engaged cultures and higher retention rates.
- Improving wages and benefits – ESOP companies tend to have higher wages and better benefits.
- Enabling employees to build wealth over time – ESOP companies give employees a meaningful equity stake in the future growth and success of the business.

[1] Section 1042 of the Internal Revenue Code provides an exemption from federal tax on the sale to an ESOP, but only if numerous requirements are met. These requirements can be quite restrictive and, consequently, limit the widespread utility of this provision.

[2] These efforts include legislation and/or regulations (a) in the form of subsidized or guaranteed loans, tax credits, or other incentives for implementing an ESOP, and (b) tax credits and contractual set asides like those now existing for minority owned and similarly disadvantaged companies.

WorkPlace Consultants

February 15, 2022

To: Chair Guzzone and the Members of the Budget and Taxation Committee

From: Paul Horn, President, WorkPlace Consultants, LLC

Re: Support for SB 561 / Hearing Date February 16, 2022

I am pleased to provide the following written, personal testimony **in strong support** of SB 561 which would eliminate Maryland tax on the sale of shares to an Employee Stock Ownership Plan ("ESOP"). This provision would encourage more Maryland business owners to create ESOPs which would be positive for their employees, the business owner, the community, and the government. This is because employee-owners at an ESOP company work with each other, not for someone else.

This testimony has three parts:

A. ESOP Background
B. Research Supporting ESOPs
C. Paul Horn Biography & Contact Information

A. ESOP Background

An Employee Stock Ownership Plan (ESOP) is a tax-qualified retirement plan with an accompanying trust which buys shares from the company's owners via loaned funds and/or cash contributed by the company.

Shares held in the ESOP trust are allocated on annual basis as the loan is repaid to individual employee accounts with the shares typically allocated on the basis of relative pay. Unlike a 401(k) matching contribution which is predicated on employee contributions, employees only need to contribute their time and effort to receive annual ESOP share allocations. As in any retirement plan, employees vest in their account based on years of service. When employees leave the company, they receive the value of their shares which are paid for by the company. ESOP companies must have an annual independent valuation to determine the price of their shares.

Based on recent IRS Form 5500 filings, there are over 6,500 ESOPs holding total assets of over $1.4 trillion and covering over 14 million participants. ESOPs are the most common and successful form of employee ownership in America.

SB0561-BT_MACo_OPP.pdf
Uploaded by: Kevin Kinnally
Position: UNF

Senate Bill 561

Income Tax – Subtraction Modification – Employee-Owned Businesses

MACo Position: **OPPOSE**

To: Budget and Taxation Committee

Date: February 16, 2022

From: Kevin Kinnally

Tax Incentives and Local Government Autonomy

Counties are eager and committed partners in promoting economic growth and creating opportunity – and prefer local autonomy in determining the best way locally. The Maryland Association of Counties (MACo) opposes state-mandated reductions in local revenue sources, but county governments welcome flexible and optional tools to serve and react to local needs and community priorities.

The General Assembly routinely considers broad or targeted tax incentives to stimulate economic growth, encourage beneficial activities, or attract and retain residents. These proposals sometimes focus exclusively on the state's tax structure, but often extend to local revenues as well.

In general, MACo stands for local self-determination. Counties, led by locally elected leaders directly accountable within the communities they serve, are best positioned to govern local affairs – ranging from land use to fiscal matters. MACo steadfastly guards this local autonomy and consistently advocates against one-size-fits-all policies that override local decision-making.

State tax incentives should be enacted as "local option" offerings to allow counties maximum flexibility in tailoring local policies to meet local needs and priorities. The State and its local governments already work together here – where the State routinely grants a state-level property tax credit, but then enables county governments to enact their own as a local option.

MACo urges the Committee to primarily consider state income tax credits as the best means to incorporate local tax relief as part of a broader policy. MACo and county governments stand ready to work with state policymakers to craft flexible and optional tools to deliver broad or targeted tax incentives, but resist state-mandated changes that preclude local input.