

After the Dust Settles, You have an ESOP. Now What?

Presented by

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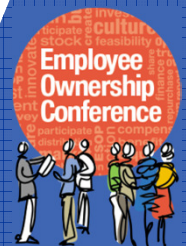
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President



Agenda: Mapping a Path Forward



- Communications and Culture
- Getting organized
- Strategic and Governance Essentials
- How Policies & Procedures Mapped Out in the Beginning Can Matter Years Later



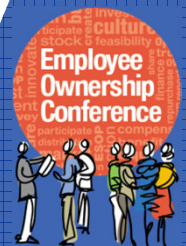
Communications and Culture



Employee Communications and Culture

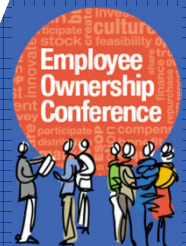


- Introductory
- Ongoing
- New Hires
- Integrate with strategic plan
- Fire hose vs small sips



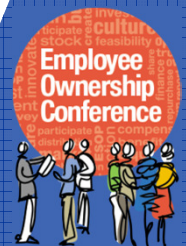
Communications and Culture

- Foot Path or Train?
- Vision and Written Plan
- Staff time and resources
- Committee or no Committee?
 - Educating Committee Members (Train-the-Trainer)
- What's your style?



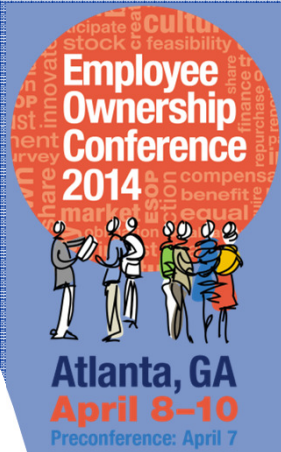
Communications and Culture

- Timing
- Delivery methods
 - Personal, Meetings, Mentor, Community
 - Email, webinars, intranet
 - Videos
 - What are other's doing?
- Remember Board, Leadership, Customers, Vendors, Community, **Legislators!**



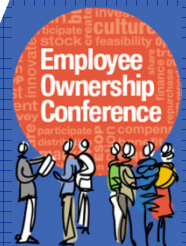
Get organized!

Closing Binder
Parties and Responsibilities
Post Closing Action Items
Annual Administration



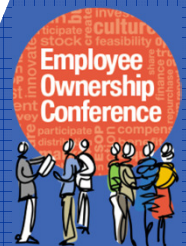
Get Organized: Closing Binder

- Documents govern actions.
- Request a closing binder from counsel.
- You want executed hard copies!
- **Read** your documents.
- **Follow** your documents.
- **Ask** if you don't understand!



Closing Binder: What to Include

- Tab:1 Parties and Responsibilities
- Tab 2: Narrative of final transaction
 - What actually happened. Who got what. How cash flows moving forward. Include a diagram of flow of funds and/or the feasibility study.
- Tab 3: ESOP Documents (Plan, Trust, etc.)
- Tab 4: Transaction documents (SPA, Notes, etc.)
- Tab 5: Guidelines
 - Post-closing and annual
 - Guidance for when to go to Board, Trustee, and /or Counsel
- Tab 6: Meeting and call notes



Parties and Responsibilities

Summary sheet for all parties.
Understand roles and responsibilities.
Identify overlapping roles



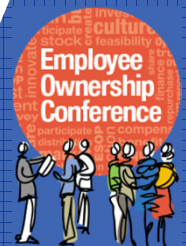
Company
Board
Shareholders
CFO/Controller
Communications
Committee
Sellers



ESOP
Trustee(s)
Appraiser
ERISA Counsel
ESOP TPA

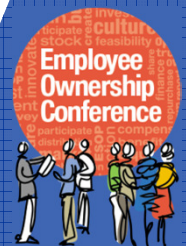


Other Advisors
CPA
Corporate Counsel
401(k) TPA
Insurance Agent
Financial advisors



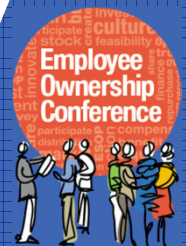
Get Organized: Post Closing

- Request Post-deal value: Year-end or update?
- Schedule Note Payments
- Calculate and schedule ESOP contribution / dividends / S distributions. Coordinate with CPA on tax implications.
- **Extend Tax Return if necessary**
- Open trust account, if not done with transaction
- Update D&O, Fiduciary Liability Insurance
- Communicate with CFO/CPA: Complexity
- **Schedule Employee Communications**
- See samples. Create your own checklist.

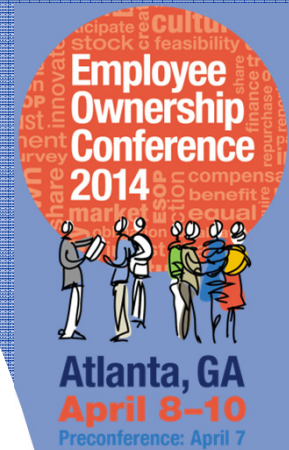


Get Organized: Annual Admin

- Review and update checklists
- Communicate with board on ESOP issues
- Reengage advisors: Trustee, appraiser
- Schedule a call with Appraiser, Trustee, Third-Party Administrator, CPA to review action items and timeline
- Make contributions, distributions to ESOP
- Communicate with employees
- Coordinate payouts with Trustee and TPA
- **First year is always the most difficult!**

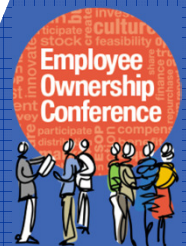


Identify Strategic and Governance essentials



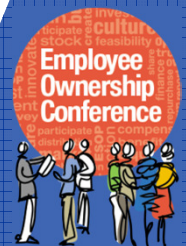
Strategic and Governance Essentials

- Incorporate the ESOP into Strategic Plan
- Develop Board (Or Advisory Board)
- Marketing your ESOP
- Lobbying for ESOPs!
- Monitor and Update Financial Plan
- Plan for Transition of Leadership
- Focus on Ownership Culture



Strategic and Governance Essentials

- Developing Board
 - Independent outside directors
 - Nomination/selection process
 - Recruiting, compensating and insuring outside directors
 - Difficulties for small companies

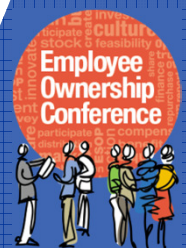


Board Candidates

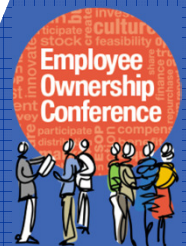
- Industry expert
- Accountant (retired)
- Attorney (retired)
- Banker (retired)
- Business person
- ESOP expert
- Other

Alternatives

- Guests
- Advisory Board
- Peer Groups

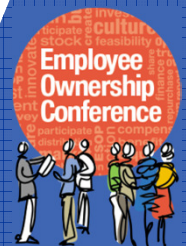


A well structured, competent and involved Board of Directors is one of the most effective means of protecting the interests of employee-owners in an ESOP company



Special Considerations for ESOP Companies

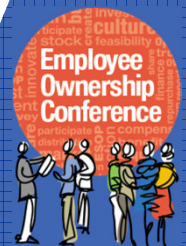
- Voting of company stock and “pass-through”
- Valuation of company stock
- Effects of ERISA on corporate governance
- Role of ESOP fiduciary (Trustee) in governance
- D&O and fiduciary liability insurance
- Fiduciary conflicts
- Managing committees



Compliance and Maintenance



- Board
- Management
- Shareholders
- CPA
- Appraiser
- Financial advisor (for 1042 and cash flow planning for investments.)
- Marketing your ESOP



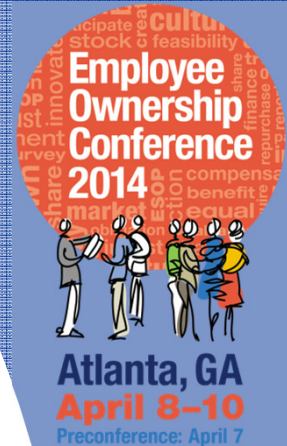
Your ESOP “Road Trip”

How Policies & Procedures Mapped Out in the Beginning Can Matter Years Later

Presented by

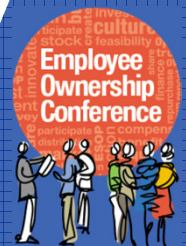
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Mapping the Way Forward

1. Major concepts supporting the best ESOP operation & decision making.
2. Questions you should ask.
3. Why, When, Whom.

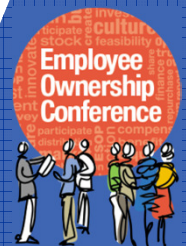


Guideposts

Five Important Things to Remember for the Road Ahead



- **Coordination of your advisors**
- **Meeting/Managing Participant Expectations**
- **Reaction vs. Proaction**
- **Having an “owner” of the process in the company.**
- **You cannot know it all, but you can know whom to call.**



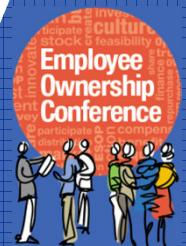
Those Are Nice General Things to Consider, But...

Can we be specific?

To illustrate the important principle of a coordinated ESOP operation, let's look at the pros and cons of a seemingly simple example:

How do we handle vested stock account balances of terminees?

- Lump sum payouts?
- Installment payouts?
- Convert stock accounts to OIA in the plan and pay later?
- Does it matter?

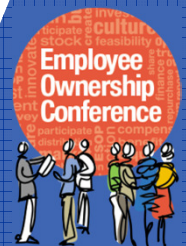


Keeping On Track

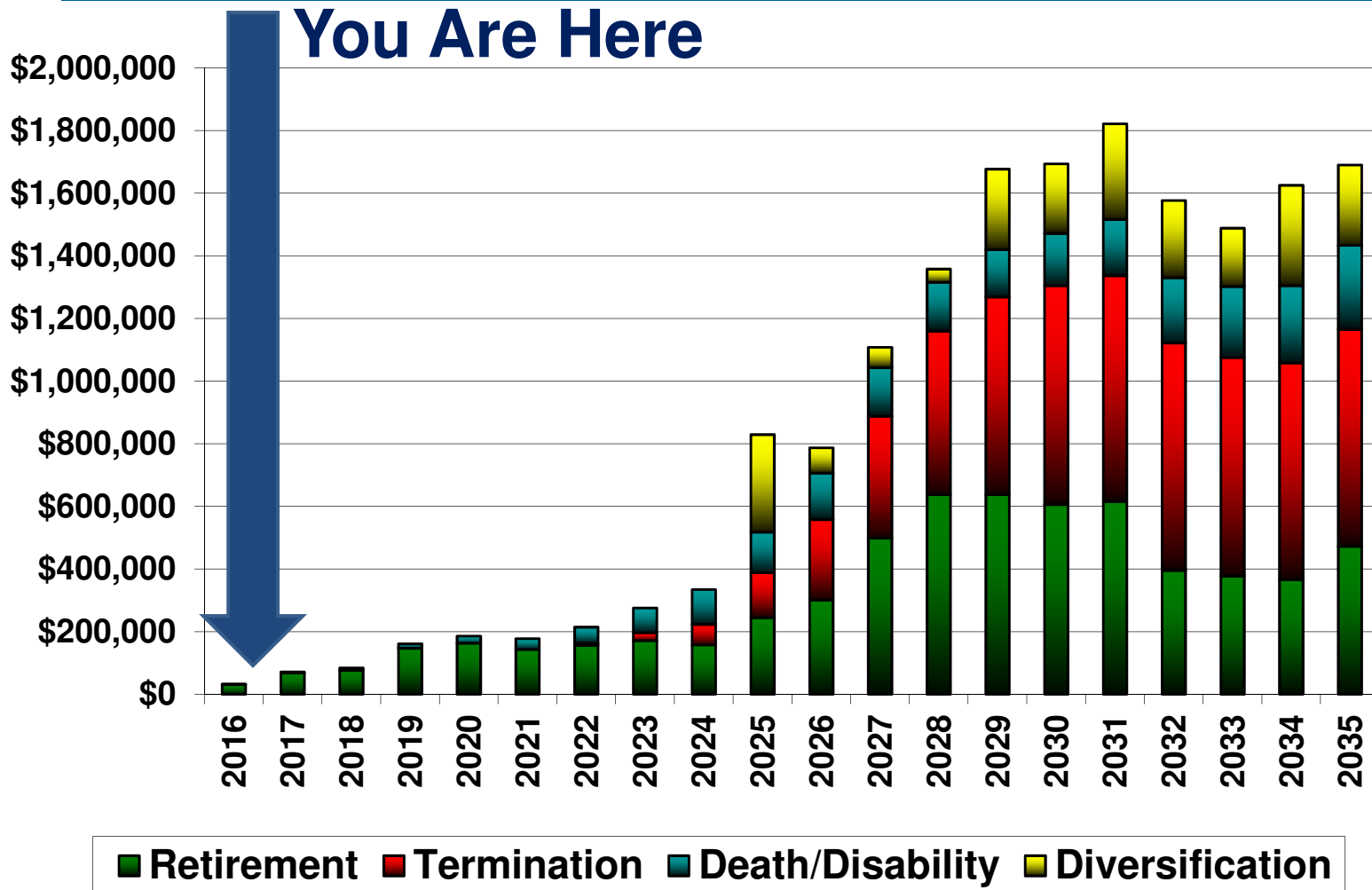
How you pay folks out (or not) can make a very big difference in two ways:



- 1. You set a precedent for employee expectations with the manner of payout, and**
- 2. These “distribution rules” can have a greater effect on the long term buyback obligations than even the share price appreciation.**



ESOP Stock Repurchase Obligations - What Should We Do and When Should We Do It?

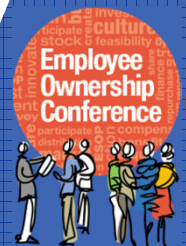


A Real World Case

Cumulative Payouts Through Years==>	2016	2021
I. Restrictive Rules 3% Growth Baseline	\$ 232,099	\$ 743,530
II. Liberal Payouts 3% Growth Baseline	\$ 615,155	\$ 1,121,222

NOTE THAT THE ONLY DIFFERENCE IN THE TWO SCENARIOS IS THE MANNER OF PAYOUT TO FORMER PARTICIPANTS

1. The conversion of stock to other investments means a faster reallocation of shares when stock is recycled in the plan...faster buyback of all shares.
2. This acceleration of the recycle rate can be costly and detrimental to long-term sustainability.
3. When should you have restrictive rules? Liberal rules?

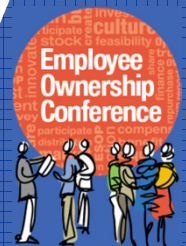


Why Strategy Matters

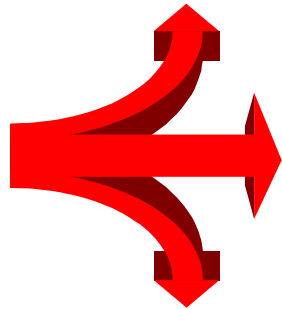
Suppose The Stock Grows at 7%? (Immediate Liquidity Can be Costlier Than High Stock Prices)

Cumulative Payouts Through Years==>	2016	2021
I. Restrictive Rules 3% Growth Baseline	\$ 232,099	\$ 743,530
II. Liberal Payouts 3% Growth Baseline	\$ 615,155	\$ 1,121,222
III. Restrictive Rules 7% Growth	\$ 262,573	\$ 954,552

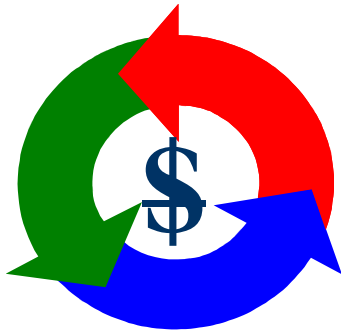
1. The important idea here is that there is a general principle of ESOP operation to apply: If you focus on just one objective (such as lump sum payouts), without understanding all the consequences, you may have a suboptimal plan operation.
2. Note that administrative distribution rules (non-discriminatory and well-documented) external to the plan provisions can be changed periodically to balance both expectations and repurchase costs. This assumes the plan language is restrictive.



What This Example Shows: The Need for Coordination

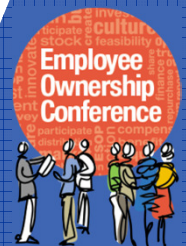


A decision in an ESOP company reached with only a narrow focus can have unintended consequences, dissipating dollars and employee good will in disparate directions.



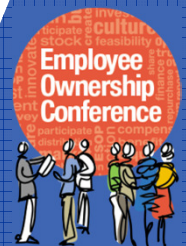
A decision which ties together all the loose ends can contain costs and maximize participant perceptions of the plan.

1. This implies the existence of coordinator or coordinating group – someone who can “own the process.”
2. This person will know the players and their roles. Most importantly, when to ask them questions!



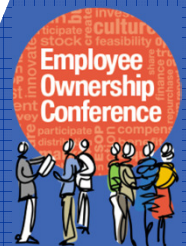
Examples of Good and Not-So-Good Coordination

1. A company CFO did what Paige & Victor warn against: He stacked the plan & compliance documentation in the corner and forgot it.
2. When the record keeper needed the census and plan information for the annual recordkeeping, he hurriedly pulled it together. He omitted the 125 cafeteria plan data, with the result that the annual allocations were wrong.
3. Discovered the following year, the results were: Costs to re-do the plan accounting, upset participants and need to amend a tax return.
4. The CFO has since hired a controller who also is the point person for checking all the boxes for all the practitioners supporting their ESOP.

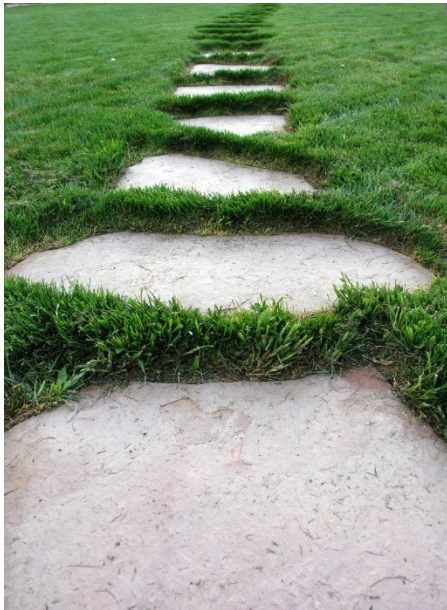


Examples of Good and Not-So-Good Coordination

1. The HR head of an S corporation with a newly leveraged minority interest S ESOP sent all of the requested information in a timely manner to the record keeper.
2. She requested a trial allocation run for her review before finalizing participant statements.
3. The ESOP had purchased shares with some cash accumulated in the plan and an ESOP loan.
4. The company had made both a deductible contribution to the plan and also paid some earnings on S stock in the plan “dividends.”
5. However, the record keeper had used all the “dividends” on all shares for loan payments. A mistake, since only earnings on the leveraged shares could be so used.
6. Further, the record keeper overlooked a deferred compensation agreement for a 409(p) test.
7. Due to the diligence of the HR lady, the corrections were made in time and accurate plan accounting was done.



Your Map



- Have a written plan
- Follow the plan
- Review and update periodically!



Seek help when you are not sure which way to go.

