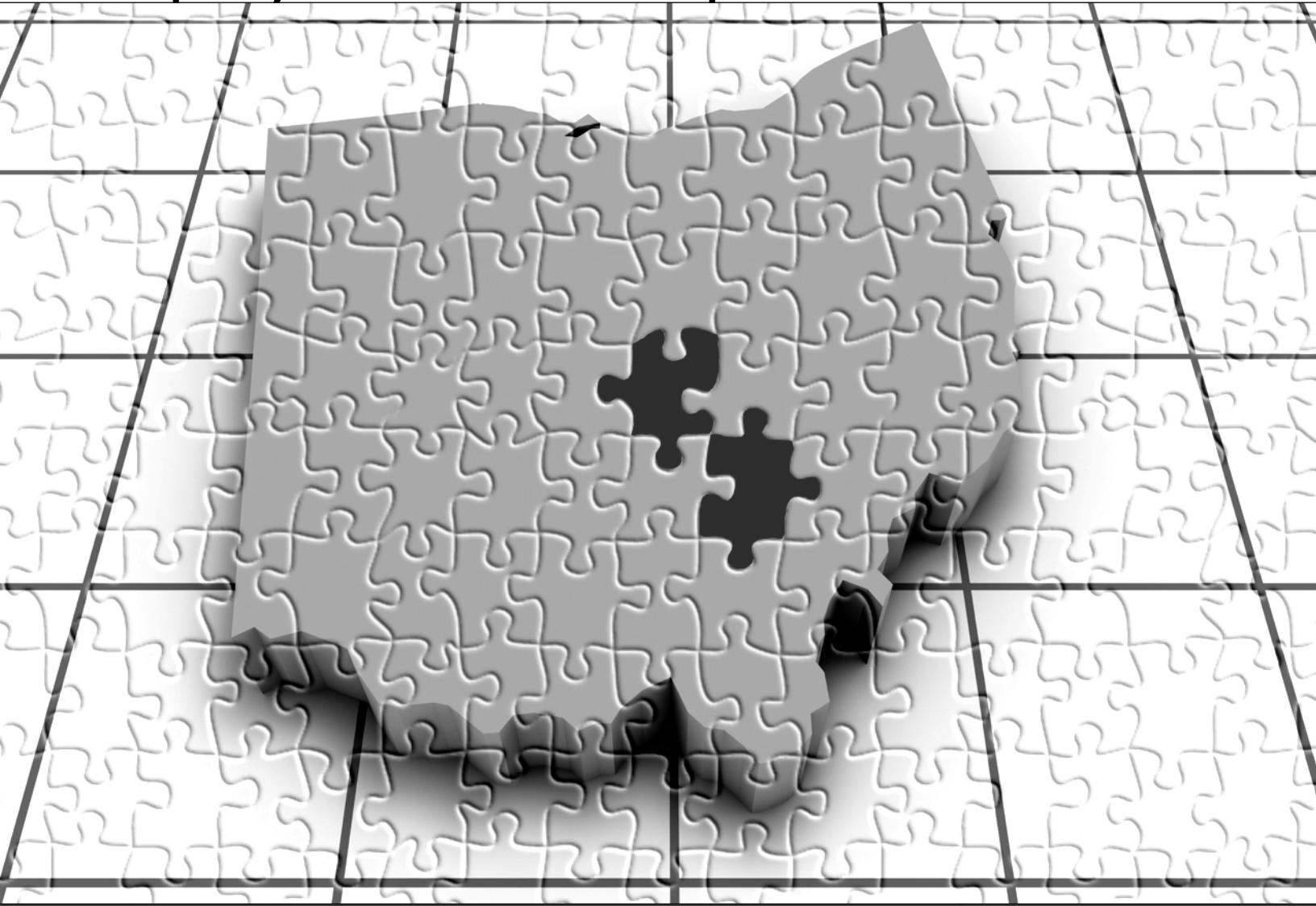


# OWNERS AT WORK

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## Employee Ownership



## Helping to Solve Ohio's Economic Puzzle



Martindale Electric  
Grand River Rubber and Plastics  
Casa Nueva Restaurant

AND..... A New Approach to Outside Offers  
A Veteran and a Novice Discuss Employee Ownership

# Protect Your Culture of Ownership with Reasonable ESOP Entry Dates

*Bill McIntyre*

One problem that many ESOP companies have is difficulty in getting their new employees excited about their ESOP. When ESOP companies spend much time in training and orienting new employees about the job, the company and the ESOP, they are often mystified that the effort seems to have minimal impact on new employees' attitudes about their ESOP. Why is this? One part of the answer is that other company practices can undermine those well-intentioned efforts. One of them is a little-known provision of the ESOP Plan document known as "Entry Date."

Let's look at how this happens.

First of all, we should clarify the distinction between an employee being eligible to be an ESOP participant by satisfying the plan requirements for eligibility and an employee actually entering the ESOP. It is common practice for an eligible employee to actually enter the ESOP only at the "Entry Date" that occurs after he or she becomes eligible.

After a required period of service, it is very common to designate January 1 and July 1 as entry dates. The existence of official "Entry Dates" is often not very well-known by participants, nor is it well-explained to new employees.

Adding to the confusion, many companies recognize new ESOP participants in a ceremony or celebration, based on their eligibility to become ESOP participants. The Entry Date is not discussed with the participant, even though an eligible ESOP participant is not actually in the ESOP until the Entry Date that occurs after the employee has become an eligible participant. Several months can pass when the employee thinks that s/he is eligible to receive stock allocations, but in fact is not in the ESOP at all. That is an unhappy experience that need not happen.

Let's consider the example of Harvey, who started work on July 15, 2010. On July 15, 2011, Harvey meets all the requirements (typically at least 12 months of employment, 1,000 hours worked and age 21) and becomes eligible to become an ESOP participant. On August 1, 2011, at the monthly company meeting, Harvey is introduced as being the newest ESOP participant. He receives applause from his co-workers. On October 15, 2011, all new ESOP participants for the July-September quarter are honored at the regular ESOP training and lunch organized by the ESOP Communications Committee. Harvey quite naturally assumes that he is now in the ESOP. But he isn't. And because Harvey's company has a December 31 year-end allocation and ESOP Entry Dates of January 1 and July 1, Harvey will have to wait a long time before he gets his first report of ownership. This reality appears to him slowly.

On April 30, 2012, the company has its Annual Participants' Meeting to announce the new stock price, review results and distribute individual ESOP account statements as of December 31, 2011. Harvey expects to receive his first individual ESOP account statement at the meeting. But he does not receive a statement.

At first, he thinks someone made a mistake, because he has worked at the company for 1 ¾ years and has been an ESOP participant since the previous July.

Someone on the company's ESOP Administrative Committee explains Harvey's situation to him. Yes, he was "eligible" to join the ESOP on July 15, 2011; however, the next Entry Date after that was January 1, 2012; and that date is after the last day of the Plan Year, December 31, 2011, when allocations are set for all ESOP accounts. Since Harvey had not "entered" the ESOP on December 31, 2011, he received no allocation. The ESOP Administrative Committee member says he is "very sorry" that Harvey misunderstood the ESOP procedures.

Naturally, Harvey feels betrayed. This ESOP "thing" that he had been hearing about is supposed to be good, but, now it seems to him that it was set up to maximize the length of time before he's allowed to benefit from it.

When will Harvey receive his first ESOP individual account statement? Not until the annual participants' meeting on April 30, 2013, nearly 3 years after he joined the company. By the time Harvey receives his statement, all his enthusiasm and sense of ownership may have drained away.

How can ESOP companies avoid this situation?

One common alternative is to have June 30 and December 31 as Entry Dates. Then everyone who becomes eligible sometime in the year will enter the ESOP before the annual allocation. If this had been the case for Harvey, he would have been eligible for an allocation. But he was only an ESOP participant for just one day. If Harvey's company allocates ESOP contributions based on compensation, and Harvey's eligible compensation is only that compensation after he had entered the ESOP on December 31, then his allocation would likely be so small that Harvey might have felt better if it was zero. Harvey might regard receiving something like a \$5.27 allocation as more insulting than receiving nothing at all.

To avoid the sense of loss that arises from a misunderstanding and erodes trust between employees and the company, there are some reasonable solutions. ESOP companies can include all compensation for the year for all participants eligible to share in the ESOP allocation. This represents the philosophy that "they contributed all year, they should receive an allocation based on their whole year's contribution." Alternatively, ESOP companies could include all compensation from the date on which the employees became eligible to join the ESOP. This represents the philosophy that "they were a participant on that date, so the allocation should be based on their compensation after that date." Or most simply, ESOP companies can remove the "Entry Date" issue by making the Entry Date be exactly the same as the Eligibility Date. This simple revision to the ESOP Plan could be approved by the board of directors, eliminating needless confusion and unpleasant surprises that can do a lot of damage to a new employee's sense of shared ownership in the company. **OAW**