

ESOP Companies Expand Globally

December 28, 2006

The economic realities of conducting business today are causing companies that sponsor employee stock ownership plans (ESOP Companies) to face the pressures of globalization, growth, diversification, competition, as well as management succession. In addition to these economic realities, the majority of the ESOP Companies in the United States are privately held corporations. As a result, these privately held ESOP Companies are obligated to repurchase their company stock held in the accounts of employee owners (ESOP Participants) who have become eligible to receive distributions from the ESOPs or to make contributions to the ESOPs to allow the eligible ESOP Participants to receive retirement benefits under the ESOP at the time that they become eligible for a distribution from the ESOP (ESOP Repurchase Liability Obligation).

In addition to managing their operations to meet the pressures of globalization and to satisfy their ESOP Repurchase Liability Obligations, ESOP Companies, like other non-ESOP companies, are constantly searching for new ways to become more efficient in their daily operations, to reduce overall costs, to enhance cash flow by increasing profits, and to increase cash reserves to remain competitive in a global marketplace. In response to these increasing pressures, many ESOP Companies have elected S corporation status for federal income tax purposes. By making the S election, these ESOP Companies have successfully accumulated large cash reserves as a result of the federal income tax savings resulting from the S election, and are looking for investment opportunities. These ESOP Companies are taking advantage of investment opportunities which include making acquisitions of, or entering into joint ventures with companies located outside of the United States, or outsourcing a portion of their business operations to companies outside the United States. As a result of ESOP Companies taking advantage of these investment opportunities, ESOP Companies are beginning to play an important role in the overall restructuring of businesses operating in countries outside the United States. Many of these countries are in the process of transitioning from an economy based on state-owned businesses to a market type of economy facilitated by these types of business investments (i.e., acquisitions, joint ventures, and outsourcing).

As countries continue to transition away from state-owned businesses and fragmented industries around the world consolidate, ESOP Companies are investing excess capital into these businesses to acquire low-cost manufacturing capacity and to obtain market share in the global economy. As ESOP Companies in the United States, like non-ESOP United States companies, make acquisitions of, or invest in, companies outside the United States, there are many business-related, social, and cultural challenges that arise, including employment, regulatory approval, and management style issues. For

example, (i) a state-owned enterprise might demand that its entire work force be guaranteed employment-like contracts for a specified period (e.g. 5 years), (ii) regulatory practices in a foreign country may require both local and national governmental approval (which can be a slow and expensive process), and (iii) the transition to a United States company management style may need to be modified and slowly implemented to avoid social and cultural disruptions and delays.

As globalization and the related investment opportunities continue, ESOP Companies will continue to expand and operate outside the United States in an effort to become stronger and more profitable, and thus able to compete in the global marketplace. The tax advantages of an ESOP used in conjunction with the S election represent a strategic tool that some ESOP Companies may be able to take advantage of with respect to these types of investment opportunities.

NEW ESOP BOOK JUST RELEASED

The newest edition of *Employee Stock Ownership Plans: ESOP Planning, Financing, Implementation, Law and Taxation*, published by the Beyster Institute at the Rady School of Management University of California, San Diego, is now being printed. We intend to complete a full book review in the next edition of "Morgan Lewis on ESOPs." This is the most complete reference work of its kind that has ever been published. With two volumes and more than 1,700 pages, there is a significant amount of current, useful, and critical information for everyone interested or involved in ESOPs. No ESOP library should be without one. Details are available at www.esopbook.org.

HOLIDAY WISHES

The Morgan Lewis ESOP Team wishes you and yours a wonderful Holiday Season and a safe and prosperous New Year.

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