34:1B-30 to 34:1B-35

LEGISLATIVE HISTORY CHECKLIST

NJSA: 34:1B-30 to 34:1B-35

(Employee stock ownership plans — Labor & Industry to study means of encouraging such plans)

LAWS OF: 1981

CHAPTER: 82

Bill No: A1021

Sponsor(s): Schwartz and Patero

Date Introduced: Feb. 21, 1980

Committee: Assembly: Labor

Senate: Labor, Industry and Professions

Amended during passage: Yes // Amendments during passage denoted by asterisks

Date of Passage: Assembly: Nov. 10, 1980

Senate: Feb. 9, 1981

Date of Approval: March 25, 1981

Following statements are attached if available:

Sponsor statement:		Yes	// Also attached: Senate amendments, adopted 1-29-81 (with statement)
Committee statement:	Assembly	Yes	// (2 on 9-22-80)
	Senate	///	No
Fiscal Note:		///	No
Veto Message:		///	No
Message on Signing:		///	No

Following were printed:

Reports:	Yes	//
Hearings:	///	No

Sponsors' statement:
The purpose of this bill is expressed in its title.

(over)

Report referred to in s.6 of act:

974.90 L123 1982a — Employee stock ownership plans: a program for New Jersey. March 25, 1982. New Jersey. Department of Labor, 1982.

See also:

974.901 L20 — New Jersey. Department of Labor. Annual report to the Legislature on employee stock ownership plans in New Jersey... March 25, 1983. Trenton, 1983.

CHAPTER 82 LAWS OF N. J. 1981
APPROVED 3-25-81

[SECOND OFFICIAL COPY REPRINT]

ASSEMBLY, No. 1021

STATE OF NEW JERSEY

INTRODUCED FEBRUARY 21, 1980

By Assemblymen SCHWARTZ and PATERO

Referred to Committee on Labor

AN ACT directing the Department of Labor and Industry to conduct a study as to the best means of providing encouragement and assistance to the formulation, under certain circumstances, of employee stock ownership plans and to the organization under such plans of employee stock ownership trusts, and to develop a plan for providing such encouragement and assistance*, *and making an appropriation therefor**.

BE IT ENACTED *by the Senate and General Assembly of the State of New Jersey:*

1. The Legislature *[funds]* *finds*:

a. During the past decade, a number of industrial plants and other facilities located in this State have permanently terminated operations or *[removed]* *relocated* operations to sites in other states or abroad; and,

b. These terminations and *[removals]* *relocations* have had *a* serious and undesirable impact upon the economies of the communites in which they have occurred and upon the State as a whole, lowering the value of land and improvements which are abandoned or devoted to less intensive uses than formerly; reducing employment, business and personal income, and the resources of the State to the extent these depend thereon; and increasing claims upon those resources; and,

c. Even more important than the impact of these closings on the general State economy and the public sector are the social and personal costs to working persons and their families of confronting the forbidding alternatives of, on the one hand, permanent unemployment, and on the other, *either* extensive mid-career retraining*[,]* *or* forced relocation or both; and,

d. In a small number of cases across the nation, employees have met the threat of plant shutdown by collectively establishing a

EXPLANATION—Matter enclosed in bold-faced brackets [thus] in the above bill is not enacted and is intended to be omitted in the law.

stock ownership trust to purchase the facility in question and to continue its operations under the direction of a trusteeship acting on behalf of the employee owners; and,

e. These trusts can serve to save jobs, continue economic development otherwise likely to be suspended and promote within the private enterprise system the goal of worker participation in the risks and rewards of equity ownership; and,

f. In view of the facts hereinabove cited, and further in view of the avowed public policy of the Executive and Legislative branches to preserve and expand manufacturing and other economic activity in the State, the Legislature finds that a high priority must be given by relevant State agencies to the provision of technical and administrative assistance to workers seeking to save jobs by forming employee stock ownership trusts.

2. This act shall be known and may be cited as the "Worker Owned Corporation Study Act".

3. The Department of Labor and Industry is directed to undertake a study as to the best means of *[providng]* **providing** encouragement and assistance to the formulation of employee stock ownership plans providing for the partial or total acquisition, through purchase, distribution in lieu of compensation or a combination of these or any other lawful means, of shares of stock or other instruments of equity in facilities by persons employed at these facilities in cases in which operations at these facilities would, absent employee equity ownership, be terminated, relocated outside of the State, or so reduced in volume as to entail the permanent layoff of a substantial number of the employees.

4. In conducting its study, the department shall: a. consider Federal and State law relating directly or indirectly to these plans, and to the organization and operation of any trusts established pursuant thereto, including but not limited, to the Federal Internal Revenue Code and any regulations promulgated thereunder, the Federal Securities Act of 1933 and other Federal statutes providing for regulation of the issuance of securities, the Federal Employee Retirement Income *[and]* Security Act of 1974, the Chrysler loan guarantee legislation enacted by the United States Congress in 1979, and other Federal and *[any]* State laws relating to employment, compensation, taxation and retirement; b. consult with relevant persons in the public sector, including but not limited to, officers and employees of the New Jersey Economic Development Authority and of the Division of Economic Development in the Department of Labor and Industry, with relevant persons in the private sector, including trustees of any existing

employee stock ownership trust and employees of any firm operating under such a trust, and with members of the academic community and of relevant branches of the legal profession; c. examine the experience of trusts organized pursuant to an employee stock ownership plan in this State or in any other state; and, d. make other investigations as it may deem necessary in carrying out the purposes of this act.

5. Pursuant to the findings and conclusions of the study conducted as provided in sections 3. and 4. of this act, the Department of Labor and Industry shall develop a plan to encourage and assist the formulation of employee stock ownership plans providing for the acquisition by employees thereof of facilities in this State which are subject to closure or drastically curtailed operation and shall determine the amount of any costs of implementing the plan.

6. The Commissioner of the Department of Labor and Industry shall within 1 year of the effective date of this act report the findings and conclusion of the study, together with details of the plan developed pursuant thereto, to the Legislature, and shall include in his report any recommendations for legislation which he deems appropriate. Thereafter the commissioner shall annually submit to the Legislature a report concerning the formation of new employee stock ownership trusts and the operation of existing employee stock ownership trusts in this State, and shall include in the report an account of State activity, during the previous year, in connection with these trusts.

[*7. *There is appropriated to the Department of Labor and Industry, for the study directed herein, the sum of $91,000.00.]**

[7.] **[*8.*]** **7.** This act shall take effect immediately.

SENATE AMENDMENTS TO

ASSEMBLY, No. 1021

[OFFICIAL COPY REPRINT]

STATE OF NEW JERSEY

ADOPTED JANUARY 29, 1981

Amend page 3, section 7, lines 1-2, omit in their entirety.

Amend page 3, section 8, line 1, omit "8.", insert "7.".

STATEMENT

This amendment deletes the appropriation.

ASSEMBLY LABOR COMMITTEE

MINORITY STATEMENT TO

ASSEMBLY, No. 1021

with Assembly committee amendments

STATE OF NEW JERSEY

DATED: SEPTEMBER 22, 1980

Two committee members did not support the bill because they believed that the creation of four additional positions was unnecessary and that the Department of Labor and Industry had sufficient resources to conduct initial studies without the $91,000.00 appropriation.

ASSEMBLY LABOR COMMITTEE

STATEMENT TO

ASSEMBLY, No. 1021

with Assembly committee amendments

STATE OF NEW JERSEY

DATED: SEPTEMBER 22, 1980

The Assembly Labor Committee favorably reports this bill, with committee amendments, which directs the Department of Labor and Industry to study and plan for means of encouraging and assisting employees in the formulation of employee stock ownership plans (E.S.O.P.) and trusts when their companies are near closure, relocation or drastically curtailed operation. The bill also provides for annual submission by the Commissioner of the Department of a report on the formation of new employee stockownership trusts, the operation of existing trusts and an account of State activity in connection with such trusts.

The intent of State assistance would be to prevent the complicated process of partial or total acquisition from those owners willing to sell from becoming overburdened in bureaucratic detail. Testimony before the United States Senate Labor Subcommittee at a hearing in New Jersey last year indicated that obstacles standing in the way of E.S.O.P. establishment are not inconsiderable for failing firms—especially where high risk and complicated loan or grant agreements are entailed. Hopefully, plans drawn up by the department will enhance the effectiveness of government assistance in conjunction with private lenders. However, the Assembly Labor Committee recognizes the validity of a comment from one successful E.S.O.P. administrator who stated, "if management has been marked by neglect or indifference over the years, or there has been a lack of realism between management and unions, then any therapy or outside financial rehabilitation may be too late."

The committee amendments, aside from the inclusion of a $91,000.00 appropriation—which includes four new positions requested by the department—were technical. The committee believes that the cost of the study will be more than repaid if it results in the continued operation of a single manufacturing plant.

ANNUAL REPORT TO THE LEGISLATURE ON

EMPLOYEE STOCK OWNERSHIP PLANS IN NEW JERSEY

Submitted pursuant to P.L.1981, c.82.

New Jersey Department of Labor
Roger A. Bodman, Commissioner

March 25, 1983

ANNUAL REPORT TO THE LEGISLATURE ON
EMPLOYEE STOCK OWNERSHIP PLANS IN NEW JERSEY

The Worker Owned Corporation Study Act (P.L. 1981, c.82) called upon the New Jersey Department of Labor to study and develop a plan for the encouragement of and assistance to the formation of Employee Stock Ownership Plans (ESOPs) as a means of avoiding plant shutdowns and thereby saving jobs. It also called for annual reports on the formation of new ESOPs, the operation of existing ESOPs and any state activity with regard to such plans. In response to this mandate, a report entitled Employee Stock Ownership Plans: A Program for New Jersey was submitted to the Legislature on March 25, 1982.

Employee stock ownership plans are a form of deferred employee compensation plan. In addition to being a means of raising capital and offering workers equity in the corporation, ESOPs enjoy beneficial federal tax treatment that has encouraged their development.

There are several types of ESOPs, but the type that is pertinent here is the "leveraged" ESOP which is designed to borrow money that can be used to purchase all or part of a company's stock on behalf of the employees. It is clear from the language of P.L. 1981, c.82., that the Legislature's primary interest is in the use of the leveraged ESOP as an employee takeover device, such as the plans currently in operation in New Jersey at the Okonite Company and at Hyatt Clark Industries. These 100% worker-owned companies constitute only a small proportion of the nation's several thousand corporations with ESOPs of all types.[1/]

The formation of 100% worker-owned ESOPs is described and analyzed in some detail in this Department's March 25, 1982 report to the Legislature. In brief, it involves the creation of an Employee Stock Ownership Trust (ESOT). The trust borrows from lending institutions and uses the proceeds to purchase the stock from the former stockholders. The loans are secured by liens against the stock (initially held in a suspense account by the ESOT), but the liens are released as the debt is repaid, with shares of the trust gradually allocated to each participating employee's account under a predetermined formula.

In the case of a leveraged ESOP, all debt repayment--both interest and principal--is deductible for federal corporate income tax purposes. For companies earning profits, the unique deductibility of principal repayment can significantly cut federal tax liabilities.

THE DEPARTMENT OF LABOR'S 1982 RECOMMENDATIONS

As the Department's March 1982, report to the Legislature concluded, the ESOP technique for employee takeover of a company is an option worthy of consideration to save jobs that might otherwise have been lost because of a company's decision to close a facility viewed as inadequately profitable. It makes sense, however, only if there are reasonable prospects for the firm's survival. There must be a market for its output and it must be possible to operate at competitive costs. Since facilities facing shutdown are usually considered marginal by the current owners, this can entail considerable risks and may necessitate actions to cut production costs.

If an ESOP-type takeover offers a reasonable prospect for success, it would seem to be in the public interest to provide assistance. Avoidance of a plant shutdown not only saves the jobs of workers directly involved; it also prevents indirect economic impacts on a community and a loss to the state and local tax base. With this in mind, last year's report recommended the following:

1. The state should assist parties interested in forming ESOPs by making threshold determinations as to the applicability of this technique to their particular business situation. If it is determined that there is a potential application, assistance should be provided to help them select consultants to perform the necessary in-depth feasibility studies, the cost of which would be borne by the parties interested in forming an ESOP. It was recommended that this technical assistance be provided by the N. J. Economic Development Authority (NJEDA) in conjunction with the Division of Economic Development, both of the Department of Commerce and Economic Development.

2. The state should provide information to employee groups and employers regarding the advantages and disadvantages of ESOPs.

3. The state should encourage the cooperation of the banking community in ESOP financing. This could be facilitated by making interest on loans to ESOPs involving 100% employee ownership (100% ESOPs) exempt for state tax purposes. Less-than-100% ESOPs should qualify only if a substantial social impact can be demonstrated.

4. The state should also consider direct subsidies to 100% ESOPs for the payment of interest, either in the form of grants or long-term loans.

LEGISLATIVE ACTION

Prior to release of last year's Department of Labor report, two pieces of legislation pertaining to ESOPs had already been introduced in the Assembly. A.767 would amend the New Jersey Economic Authority Act (P.L.1970, c.80) to provide that applications to the Economic Development Authority for financial assistance submitted by ESOPs be given consideration without regard to location, i.e., even if they are not located in geographical areas targeted by

NJEDA for assistance. A.769 would appropriate \$25,000 from the Unemployment Compensation Auxiliary Fund to the Department of Commerce and Economic Development for the purpose of establishing a program of information, technical assistance and advocacy regarding the formation of employee-owned corporations through the use of ESOPs. Both of these bills were introduced on February 22, 1982 and referred to the Labor Committee where no further action has been taken.

On May 17, 1982, another bill (A.1470) was introduced that responded to the first two Department of Labor recommendations, but went beyond them with regard to the State's staff and financial commitment to feasibility and impact studies. It called upon the Department of Commerce and Economic Development to establish an ESOP information program and provide technical assistance to parties considering the creation of an ESOP. Technical assistance available to employees of a facility faced with closure or relocation outside of New Jersey would include: (1) determining economic feasibility; (2) arriving at a cost-benefit analysis of the effects of the facility closure on the local economy; and (3) helping the parties secure financing and apply for grants under existing governmental programs. The third type of assistance would be provided only if an ESOP take-over has been determined to be economically feasible and beneficial to the community. The bill included no specific appropriation nor did it provide for any unique financial inducements to ESOPs, e.g., exemption of interest from state taxation or subsidies on interest payments.

A.1470 passed the Assembly on June 21 and, with minor amendments, passed the Senate on January 1, 1983. The amended version passed the Assembly on January 27, but was vetoed by the Governor on March 14, 1983.

In his veto message, the Governor expressed his support for the establishment of "an economically feasible and reasonable ESOP program." He noted, however, that A.1470 departed from the Department of Labor's recommendations by mandating a substantial personnel and financial commitment, including grants, for the purpose of obtaining technical information regarding the establishment of an ESOP.

The Governor pointed out that, given the current fiscal constraints, resources are not available for the degree of financial commitment required by A.1470. He cited the Department of Labor's approach to this as a less burdensome way for the State to accomplish the legislation's purpose. The Department of Labor's recommendation had been to limit the state's participation in ESOP feasibility studies to that of helping parties make threshold determinations, or the initial informal decisions as to whether or not those parties should pursue the necessary in-depth feasibility studies on their own and at their own expense.

Another ESOP bill (S.3174) was introduced in the Senate on March 7, 1983. This bill, and a companion bill introduced in the Assembly on March 14 (A.3325), calls for information and technical assistance that is closer to the more limited Department of Labor recommendation and also would make interest received by lenders on loans to 100% ESOPs exempt from state corporate and personal income taxes. These bills have been referred to the Senate Committee on Labor, Industry and Professions and the Assembly Committee on Housing and Urban Policy.

ESOPS IN NEW JERSEY

It is not known how many ESOPs currently exist in the State of New Jersey. Though all ESOPs must file reports with the Internal Revenue Service and with the U. S. Department of Labor under the provisions of the Employee Retirement Income Security Act of 1974 (ERISA), up-to-date listings that would separately identify ESOPs are not available. The latest state-by-state listing available from the U. S. Department of Labor was prepared in 1978 and included--without distinction--all types of ESOPs, not just those formed to enable employees to acquire controlling ownership of a company. The vast majority can be presumed to be stock bonus or money purchase pension plans involving only fractional employee ownership of the corporation's stock.

The U. S. Department of Labor list for 1978 included 61 ESOPs of all types in New Jersey, a number that has undoubtedly grown since then considering the rising trend of ESOP formation across the nation. Of the New Jersey ESOPs identified at that time, 14 involved 100 or more employees. These included plans at such major companies as Exxon Research and Engineering, Becton Dickinson, Squibb, Gulton Industries, Federal Paperboard, Cooper Laboratories, Schering Corporation, Okonite and New Jersey National Bank.

As noted earlier, ESOPs formed for the purpose of enabling employees to gain full ownership--the primary interest of the Legislature--are still a rarity. There are two significant examples of these in New Jersey, however, both created since the mid-1970s and both involving a large number of workers. These are the Okonite Company and Hyatt Clark Industries.

Okonite Company [2/]

The employees of the Okonite Company utilized a leveraged ESOP to acquire 100% ownership of that company in 1976. Immediately prior to creation of the ESOP, Okonite was a subsidiary of Omega-Alpha, Inc., which had filed for bankruptcy in late 1974 and was under the jurisdiction of a federal judge and court-appointed trustees in Dallas, Texas. Prior to that it had undergone a series of ownership changes, having been divested from Kennecott Copper Corporation in 1965 and from the LTV Corporation of Dallas, Texas, in 1970 in accordance with anti-trust consent decrees.

Though Okonite, the only profitable portion of Omega-Alpha, had earned net profits of $7.2 million in the fiscal year ending June 30, 1975, its future was clouded by the bankruptcy proceedings and uncertainties regarding its future ownership. The company's management and employees decided, therefore, to seek ownership themselves to ensure continuity of employment and company growth.

Financing of the Okonite ESOP was achieved through $21 million of loans from a consortium of private lenders led by the Bank of America; $4 million of N. J. Economic Development Authority tax-exempt bonds; and $13 million of direct NJEDA loans supported by funds from the U. S. Economic Development Administration specifically granted for this initial purpose. (As this direct loan is repaid, the funds go into a revolving loan fund which NJEDA can use to support other projects.) As of December 31, 1982, Okonite's direct NJEDA loan balance was $10,739,200.

Okonite, a manufacturer of wire and cable in New Jersey since 1878, employed about 1,000 employees at the time of the take-over at facilities located in Passaic, Paterson, Ramsey and North Brunswick. It also had three plants outside of New Jersey. Its employment in the state was still at about the same level at the end of 1982, with all New Jersey facilities still in operation.

Hyatt Clark Industries [3/]

Hyatt Clark Industries, Inc., a New Jersey manufacturer of roller bearings since 1892, was formed as an ESOP on October 23, 1981, as a means of avoiding a plant shutdown scheduled by its former owners, General Motors. The initiative for forming an ESOP was originated by the local union (Local 736 of the United Auto Workers) and supported by salaried employees. The successful implementation of that initiative saved more than 1,000 jobs and prevented a significant economic loss to the community.

Financing for creation of the company's Employee Stock Ownership Trust (ESOT) was provided by loans from the Prudential Insurance Company of America, Chemical Bank, N.A., and General Motors. Hyatt Clark also has an application pending with the N. J. Economic Development Authority for a $4 million direct NJEDA loan that would replace part of its existing debt. This loan is dependent upon approval by the U. S. Economic Development Administration of a grant similar to the one used to support the direct loan made to Okonite back in 1976. In addition, the company was recently granted a loan through Urban Development Action Grant (UDAG) program to raise capital for modernization of machinery and production processes.

Employment at this facility peaked in 1968-69 at about 3,200 and then declined during the 1970s. Immediately prior to General Motors' phase-out of the plant, it employed about 1,800 hourly and salaried workers. When Hyatt Clark Industries was created, there were still about 830 employees on board. Despite the recession, employment has increased since then to the 1,100 to 1,200 range.

Hyatt Clark's major customer is still General Motors, with which it negotiated a three-year contract for supplying roller bearings. About 10% of the company's sales are to other buyers and it is seeking to penetrate the market more broadly through negotiations with both auto producers and other users of industrial roller bearings and related products.

Though the company has suffered along with the rest of the economy because of the current recession, both management and labor spokesmen feel it has the capability of more fully penetrating the market currently dominated by Timken, the biggest producer of roller bearings. Unit costs have been reduced as a result of sizeable wage cuts implemented at the time of the new company's inception and substantial productivity improvements since that time. Nonessential jobs have been eliminated and participative management has resulted in worker-originated ideas for more efficient operations. The company had a net loss of $5.6 million in the ten-month period ending August 31, 1982, but expects to break even in fiscal year 1983 and generate profits after that, with the work force remaining stable or increasing slightly.

The N. J. Department of Labor, through its Office of Customized Training, has been heavily involved in providing technical assistance to Hyatt Clark almost since its inception. The Office of Customized Training has helped the company develop a formalized on-the-job training program and improved procedures for evaluating employee proficiency and orienting new employees. These and other services of that office have all been designed to help the company achieve improved productivity.

CONCLUSION AND RECOMMENDATION REGARDING FUTURE REPORTS

Aside from monitoring legislative activity regarding ESOPs, providing customized training services to Hyatt Clark, and preparing this update report, the Department of Labor has not been involved in ESOP-related activities over the past year. Requests for specific ESOP-related technical assistance have not been received, nor is there a program in place to provide such assistance. Therefore, there are no new developments to report.

The responsibility for reporting to the Legislature on developments related to ESOPs was assigned to the Department of Labor and Industry prior to its split into a Department of Labor and separate Department of Commerce and Economic Development in January 1982. Because of the financial expertise residing in the Department of Commerce and Economic Development, the Department of Labor's March 1982 report to the Legislature recommended that department as the appropriate agency for providing information and technical assistance on the formation of ESOPs. Subsequent legislative proposals have similarly assigned the assistance responsibilities to that Department. For consistency, it is recommended that any such bills also shift the annual ESOP reporting responsibility currently mandated by P.L. 1981, c.82, from the Department of Labor to the Department of Commerce and Economic Development.

FOOTNOTES

1/ A survey conducted by Marsh and McAllister in 1980 revealed that ESOP trusts held 100% of the company's stock in only eight of 211 responding companies that had three or more years of experience with ESOPs. Marsh, Thomas R. and McAllister, Dale E., "ESOPS Tables: A Survey of Companies with Employee Stock Ownership Plans," Journal of Corporation Law, Spring 1981, pp. 551-623.

2/ This section is based on information provided by the New Jersey Economic Development Authority.

3/ This section is based on interviews with James May, President, Local 736, United Auto Workers and Patrick Mazzeo, Personnel Director, Hyatt Clark Industries, Inc., supplemented by Hyatt Clark's 1982 Annual Report and information from the New Jersey Economic Development Authority.