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Opinion

Employee Stock Ownership Plan

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OPINION

Employee Stock Ownership Program (ESOP) An employee stock ownership plan (ESOP) is a type of employee benefit plan that gives employees a stake in the company in the form of stock shares. ESOPs are qualified plans because they provide various tax benefits to both the sponsoring company—the selling shareholder—and the members. Employers frequently use ESOPs as a corporate finance technique to match their employees' interests with their shareholders'. Employee ownership can be achieved in a number of different ways. Employees can purchase stock outright, receive stock as a bonus, earn stock options, or participate in a profit-sharing arrangement. Employee cooperatives, in which everyone has an equal vote, allow certain employees to become owners. The ESOP, or employee stock ownership plan, is by far the most frequent type of employee ownership in the United States. ESOPs, which were virtually non-existent until 1974, are now commonplace; according to the most recent data, there are 6,460 plans representing 14.2 million workers.

ESOPs can be used for a variety of objectives by businesses. ESOPs are nearly never utilised to save struggling companies, contrary to popular belief, and only a few of such plans are established each year. ESOPs are most typically utilised to offer a market for the shares of leaving owners of successful closely held businesses, to inspire and reward employees, or to take advantage of incentives to borrow money for the acquisition of new assets with pre-tax monies. ESOPs are nearly always a gift to the employee rather than a purchase by the employee.

An ESOP is a type of employee benefit plan that is comparable to a profit-sharing plan in some aspects. An ESOP is a trust fund into which a corporation invests new shares of its own stock or cash to purchase existing shares. Alternatively, the ESOP can borrow money to buy new or existing shares, and the company can return the loan by making cash payments to the plan. Company donations to the trust are tax-deductible, subject to certain limitations, regardless of how the plan obtains stock. For the next four years, the 2017 tax bill limits net interest deductions for firms to 30% of EBITDA (earnings before interest, taxes, depreciation, and amortisation), after which the cap drops to 20%. New leveraged ESOPs, in which the firm loans a considerable amount compared to its EBITDA, may find that their deductible expenses are smaller and, as a result, their taxable income is higher as a result of this shift. Because S businesses with 100% ESOP ownership do not pay taxes, this change will not affect them.

Individual employee accounts are given shares in the trust. Although there are certain exclusions, the plan is normally available to all full-time employees over the age of 21. Allocations are determined based on relative salary or some other more equitable formula. Employees have greater rights to the shares in their account as they gain seniority with the company, a process called as vesting. Employees must be fully vested in three to six years, depending on whether vesting is done all at once (cliff vesting) or over time (gradual vesting). Employees receive their stock when they leave the company, which the company must buy back at fair market value (unless there is a public market for the shares). To decide the price of their shares, private enterprises must have a yearly outside valuation. Employees must be able to vote their assigned shares on critical matters, such as closing or relocating, in private enterprises, but the company can choose whether to pass through voting rights on other topics (such as the board of directors). Employees in public firms must be able to vote on all matters.

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