EMPLOYEE-OWNED CONTRACTORS ROUNDTABLE

Who We Are

The Employee-Owned Contractor Roundtable (ECR) is a coalition of federal government contractors that are organized as private subchapter S corporations wholly-owned through an employee stock ownership plan (ESOP). ECR member companies provide products and services for the U.S. Government, ranging from manufacturing engines and timing belts to developing some of the most advanced combat simulators and sonar detection technologies. ECR members can be located across the entire United States, playing critical roles in several sectors of the American economy.

Since employee-owned companies provide significant benefits to the U.S. economy and unique advantages to rank and- file workers, the federal government has supported and promoted ESOPs for decades, through a variety of growth mechanisms, specifically through tax policy. ECR members believe it is time to modernize federal contracting regulations to align with existing federal pro-ESOP objectives by advancing policies to support and expand employee ownership within the federal contracting arena.

What is a Private, Subchapter S ESOP?

A Subchapter S corporation is a business entity that provides flow-through tax treatment to its shareholders. An ESOP is a qualified defined contribution plan that provides a company's workers with retirement savings through their investments in their employer's stock, *at no cost to the worker.* ESOPs are regulated by the Department of Labor under the Employee Retirement Income Security Act ("ERISA") just like pension funds, 401(k) plans, and other qualified retirement plans.

Congress authorized the S corporation ESOP ("S ESOP") structure over two decades ago to encourage and expand retirement savings by giving hundreds of thousands of American workers in all 50 states the opportunity to have equity in the companies where they work.

Employee-Owner Income vs Non- Employee Owner Income (Ages 28 to 34)

MEDIAN WAGES FROM INCOME	EMPLOYEE-OWNERS	NON-EMPLOYEE-OWNERS
Overall	$40,000	$30,000
Single women	$31,000	$25,000
Single women of color	$28,000	$24,000
Workers of color	$35,000	$27,000
Child 0-8 in household	$40,000	$30,000
Families of color with young child	$35,000	$26,000
All parents	$39,000	$30,000
All single parents	$33,000	$23,000
Single mothers	$28,000	$21,000
Non-college graduates	$35,000	$25,000
Under 50k income from wages	$30,000	$25,000
Under 30k income from wages	$22,000	$18,000
Under 25k income from wages	$17,160	$14,000

Source: National Center for Employee Ownership

Why America Benefits from Supporting ESOP-Owned Companies

As employee ownership in America has grown employee-owned businesses have consistently provided the economy, their workers, and their customers with unique and tangible benefits. When a company is owned by its employees, important socioeconomic dynamics arise that benefit workers, the company, the community, and the national economy. Because ESOPs are regulated by a strict legal code that requires ownership to be broadly held across employees, from the mailroom to the boardroom, companies that are ESOP-owned – and particularly those that are majority or wholly ESOP- owned – consistently report better job growth, fewer job reductions during economic downturns, boosted employee savings, and strong protections against foreign acquisitions. Among the data points that underscore the specific value of ESOPs:

- Despite the financial stresses caused by the 2008/09 economic downturn and resulting great recession**, ESOP-**

owned companies kept far more jobs than other private companies. According to a 2012 study by Alex Brill, **employment among employee-owned firms increased more than 60% from 2001-2011, while the private sector had flat or negative growth in the same period**.

- **ESOPs reduce wealth inequality in the American workforce.** A 2016 study by Jared Bernstein shows that by increasing wage-earning employees' share of their business capital, **ESOPs reduced the wealth concentration among the top 10 percent of employees by 2.5%.**
- Due to the work culture and structure of an ESOP business, contract officers (CO) and procurement managers (PM) prefer doing business with ESOP contractors because ESOPs can meet contracting deadlines in a more agile manner and reinvest in their company's technical abilities to meet the most challenging federal projects

National Defense Authorization Act (NDAA) FY22 Clears the Way for Contracting Officers to Work with 100% ESOPs

In the FY22 NDAA, Congress passed a provision to establish a five-year Department of Defense (DOD) pilot program to allow contracting officers (CO) the ability to sole-source the follow-on contracts of similar substance to 100% ESOPs. To qualify, ESOPs must possess the initial contract and completed the project at a "satisfactory" or above rating. These innovative first steps provide COs with greater choice in how to procure services from the contracting sector. Additionally, this program allows DOD more time to work with a 100% ESOP contractor that has a time-tested track record of fulfilling the needs of DOD.

Congress must now ensure that DOD implements this program and establishes the necessary data collection strategy, rules, and regulations to take advantage of this unique procurement strategy.

Modernizing Procurement Practices to Promote Subchapter S ESOP Contractors

While this follow-on provision is a strong first step, ECR members believe Congress can create more 100% ESOPs by incentivizing federal agencies to partner more regularly with ESOP companies with strong histories of completing projects in a timely and cost-effective manner. Procurement practices should leverage the unique benefits of the ESOP model to create a pathway for small businesses to grow by allowing small businesses the ability to become wholly owned through an ESOP and still compete for certain small business set-aside contracts. ECR is collaborating with Members of Congress to educate and engage on the following policy options:

- ***100% ESOP size-adjustment to provide growth opportunities for wholly-employed owned businesses***
    - ***Barring competition for specific preference programs (i.e., women/veteran-owned, 8a, etc.)***
    - ***Guardrails to protect very small businesses – no competition on receipt-based contracts under $16.5 million***
    - ***Graduation threshold for the wholly-owned ESOP business at 3 times the top NAICs code in both the headcount and receipts categories***
    - ***Limit such benefits only to USA headquartered Subchapter S businesses that are wholly-owned through an ESOP***
- ***Amend SBA affiliation rules to allow companies to establish standalone businesses wholly-owned through an ESOP and enter into mentor-protegee protégé agreements with the new entity***
- ***Define businesses wholly-owned ESOPs as non-traditional for Other Transaction Authority (OTA) contracts***
- ***Eliminate recertification on certain task orders for businesses wholly-owned through an ESOP***

To that end, legislation will soon be introduced to achieve these goals. **Should you wish to learn more about ECR activities, please do not hesitate to contact Matthew Pearce at MPearce@vennstrategies.com, or Matt Scott at Mscott@vennstrategies.com**