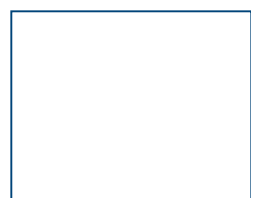


ESOPs

Michael S. Miller, CEBS



ESOP Administration

Leveraged ESOPs

Share Release Calculations

Example – New ESOP:

Loan amount:	\$1,000,000
Term of loan:	10 years
Interest rate (fixed):	6%
Variable rate (this year's rate):	6%
Number of shares purchased:	10,000

ESOP Administration

Leveraged ESOPs

Share Release Calculations – Example

Loan Amortization Schedule

Year	Principal Balance at Beg of Year	Interest Payment	Principal Payment	Principal Balance at End of Year
1	1,000,000	60,000	75,868	924,132
2	924,132	55,448	80,420	843,712
3	843,712	50,623	85,245	758,467
4	758,467	45,508	90,360	668,107
5	668,107	40,086	95,782	572,325
6	572,325	34,340	101,528	470,797
7	470,797	28,248	107,620	363,176
8	363,176	21,791	114,077	249,099
9	249,099	14,946	120,922	128,177
10	128,177	7,691	128,177	0

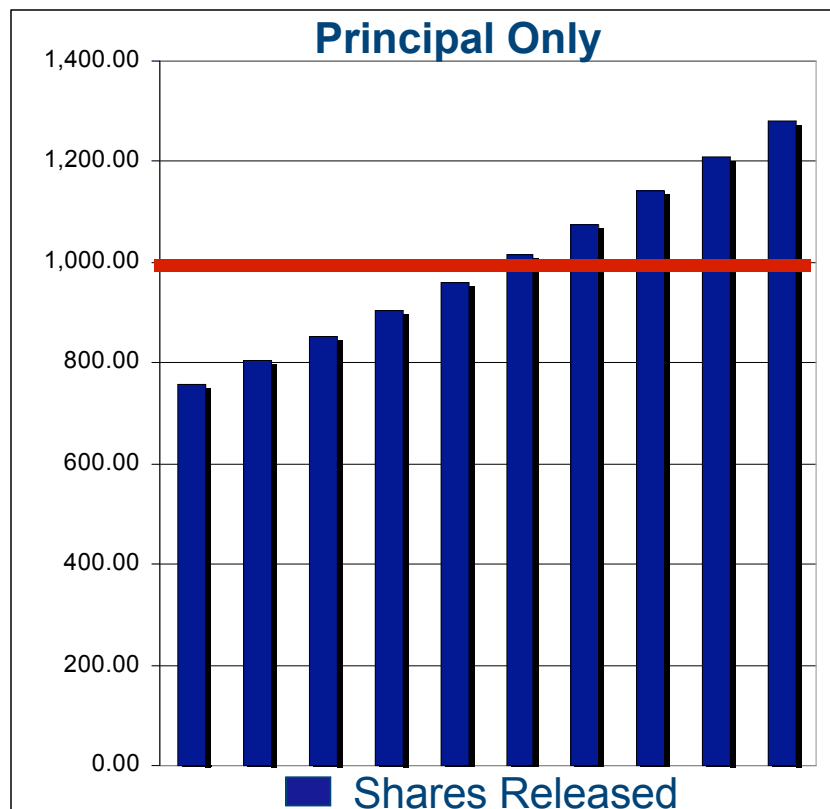
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Results of Share Release Calculations - Example

Principal & Interest Method		Principal Only Method	
Beg of Year Unallocated Shares	Shares Released Each Year	Beg of Year Unallocated Shares	Shares Released Each Year
10,000	1,000	10,000.00	758.68
9,000	1,000	9,241.31	804.20
8,000	1,000	8,437.12	852.45
7,000	1,000	7,584.67	903.60
6,000	1,000	6,681.07	957.83
5,000	1,000	5,723.25	1,015.28
4,000	1,000	4,707.97	1,076.20
3,000	1,000	3,631.76	1,140.77
2,000	1,000	2,490.99	1,209.22
1,000	1,000	1,281.77	1,281.77
	10,000		10,000.00

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Graph of Share Release Calculations - Example



ESOP Administration

- Restricted Eligibility
 - Certain participants who sell stock to the ESOP under the 1042 election are restricted from having such shares allocated to their account.
 - The seller's family and 25% owners are also restricted from allocation of these shares

ESOP Administration

Limits of Company Contributions – Example

What is deductible limit on employer contribution?

Assume 401(k) amounts are fixed; what contribution to ESOP is deductible?

§404 Limit

Eligible compensation	\$1,100,000
<u>Deductible limit</u>	<u>25%</u>
Maximum deduction	\$275,000

ESOP Administration

- Limits on Annual Additions
 - Individual Participant Limitations
 - “Annual Additions” are limited to the lesser of:
 - \$40,000, and
 - 100% of the participant’s compensation
 - Annual Additions include:
 - Employer contributions;
 - Employer before tax contributions [401(k) deferrals];
 - Employee after tax contributions; and
 - Forfeitures

Specific Provisions

Vesting

Years of Credited Service	Vested Percentage
Less Than 3	0%
3 Years	20%
4 Years	40%
5 Years	60%
6 Years	80%
7 Years or More	100%

ESOP Administration

- Diversification Rules
 - 3 ways to diversify
 - Pay out in shares or cash
 - Transfer to other investment option (at least three) within the ESOP, or
 - Transfer to other investment option (at least three) in another employer sponsored plan [such as a 401(k) plan]

Reasons for Installing the ESOP

- Long-range, organized Exit Strategy which is predictable and announceable
- Fit the Founders business philosophy of establishing mutually beneficial partnerships and win-win relationships
- Motivates and rewards committed employees whose efforts make the company successful
- Supports continuation of existing customer relationships
- Tax advantages

Establishing an Ownership Culture

- Cultural development by Employee Owners
 - More time than the minimum required
 - More effort than is routinely expected
 - Personal commitment to company success
 - Work ethic that supports partnering

Transforming Wage Earners into Employee-Owners

- Hiring the right people
- Education
 - ESOP Mechanics
 - Participation in ESOP Organizations
 - Company Values
 - Company Business Strategy
 - Company Economics
- Information Sharing
- Feedback and Reinforcement
- Celebrating Success