EMPLOYEE STOCK OWNERSHIP PLAN FREQUENTLY ASKED QUESTIONS

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WHAT IS AN ESOP?

An ESOP, formally known as an Employee Stock Ownership Plan, is a tax-qualified retirement plan that invests primarily in the employer's stock. The company sets aside stock in the ESOP to help employees prepare for retirement.

WHAT DOES AN ESOP MEAN TO ME?

It means the employee will be a beneficial owner of the company at no cost and will have equity in the company and retirement benefits. However, the employee will not participate in management, day-to-day decision-making, hiring and firing decisions, or have access to confidential information. The ESOP does not guarantee employment at the company.

WHAT IS THE PURPOSE OF AN ESOP?

Owners have many options when selling a company. An ESOP is an effective tool for ownership succession planning and enables employees to share in a company's success.

HOW IS AN ESOP DIFFERENT FROM A COMPANY'S 401(K) PLAN?

There are two key differences between ESOP and 401(k) plans. First, an ESOP invests primarily in an employer's stock, while a 401(k) plan generally offers various mutual funds in which employees may invest. Second, 401(k) plans permit employees to contribute their own money, while ESOP contributions come solely from the company—making them completely free to employees.

HOW IS THE PRICE OF ESOP STOCK DETERMINED? HOW OFTEN IS IT VALUED?

The price of the stock in an ESOP is typically determined annually by a qualified valuation company working in conjunction with the plan's trustee. These entities specialize in determining the value of ESOP-owned businesses based on factors such as the company's performance, industry trends, geography, and overall economic outlook.

HOW OFTEN WILL MY ESOP ACCOUNT BALANCE CHANGE?

An ESOP account balance changes once per year. Employees will receive an annual statement detailing the financial activity for the year, including the updated stock value.

HOW CAN THE VALUE OF AN ESOP ACCOUNT INCREASE?

Since an ESOP account's value is largely based on the company's stock, anything an employee does to help the company succeed—such as improving efficiency, cutting costs, or increasing sales—can contribute to account growth. Employee-owners play a role in building a better company and increasing its value.

WHERE IS AN EMPLOYEE'S PORTION OF THE ESOP KEPT?

The assets of the ESOP are held in the ESOP trust, a special entity established for the plan. Each employee's portion of the assets is recorded in an ESOP account under their name.

WHAT IS THE ROLE OF AN ESOP TRUSTEE?

The trustee controls the ESOP trust, represents the plan participants, and ensures that the plan operates in their best interests. The trustee also sets the annual stock price with the assistance of an independent valuation firm.

WHAT ARE THE MAIN TAX ADVANTAGES OF AN ESOP?

ESOP contributions are tax-deductible.

WHERE ARE ESOPS FOUND?

ESOPs exist across the U.S. in both private and public companies and across a variety of industries.

HOW MANY ESOPS ARE THERE IN THE U.S.?

There are roughly 6,500 ESOPs in the U.S., with a little over 6,300 companies having an ESOP, as some companies have multiple plans.

WHAT ARE THE TAX INCENTIVES FOR EMPLOYEES IN AN ESOP?

Employees pay no tax on ESOP shares until they receive distributions. Even then, they can roll distributions over into an IRA or another qualified retirement plan to defer taxes.

ARE ESOPS THE SAME AS STOCK OPTIONS?

No, they are completely different. An ESOP is a tax-favored retirement plan that holds stock for employees, includes most full-time workers with a year of service, and primarily pays out when employees leave the company. A stock option, however, is the right to buy stock at a set price and can be granted to select individuals. Outside the U.S., ESOPs may refer to stock options, such as in India.

HOW DO ESOP COMPANIES PERFORM?

ESOP companies tend to grow faster and lay off employees at significantly lower rates than comparable companies.

ARE ESOPS ONLY FOR EMPLOYEES?

Yes, except for former employees who have not yet been fully paid out. They remain participants in the plan until their distribution is complete.

HOW ARE ESOP DISTRIBUTIONS (PAYOUTS) TAXED?

Participants are taxed only when they receive distributions, following typical tax-qualified retirement plan rules. If you're younger than 59½ (or 55 if terminating employment), you'll pay income tax plus a 10% excise tax unless the funds are rolled over into an IRA.

WHY CAN'T I SELL MY ESOP SHARES ANYTIME I WANT?

The ESOP trust is the legal owner of the shares, not individual participants. Employees receive their shares only when they receive a distribution from the plan. Distributions are structured so that not all employees receive payouts at the same time, reinforcing the ESOP as a retirement plan rather than a short-term bonus.

WHEN IS ESOP MONTH (EMPLOYEE OWNERSHIP MONTH)?

Employee Ownership Month is celebrated in October.

WHO CAN I CONTACT ABOUT RECEIVING MY ESOP DISTRIBUTION?

For any ESOP-related questions not covered in these FAQs, please email questions@thompsonconesop.com and allow 3-5 business days for a response.

DO I LOSE MY ESOP ACCOUNT SHARES IF I QUIT? WHAT HAPPENS TO THEM?

If you are vested, you keep your shares, but they will be cashed out by the company within three years.

WHAT ARE THE REQUIREMENTS FOR BEING VESTED IN THE ESOP?

You must be a full-time employee and work at least 1,000 hours during the year. Vesting occurs over a six-year period.

WHAT HAPPENS IF AN ESOP EMPLOYEE PASSES AWAY?

The stock share value will be paid out to the employee’s designated beneficiary.

IF I QUIT AND GET REHIRED, HOW DOES THAT AFFECT MY ESOP?

If you were vested when you quit, your shares will be bought out. If you are rehired, you will start accumulating new shares under the six-year vesting schedule.