



SUPPORT: DPC ESOP EXPANSION

S.5261(Kennedy) /A.1891A(Lupardo)

Background:

In 2012, New York State passed legislation allowing the creation of a new corporate form called the Design Professional Corporation (DPC). In a DPC, engineers, architects, land surveyors, landscape architects and geologists may join together to form a company to practice these professional disciplines. This legislation also states that if a firm's Employee Stock Ownership Plan qualifies under certain criteria (75% of the ESOP's plan committee spots are held by licensed design professionals), it can be the largest shareholder and own up to 24.9% of the firm.

Proposed Update:

S.5261 (Kennedy) / A.1891A (Lupardo) would allow a Design Professional Corporation's qualifying ESOP to own greater than 24.9% of the firm. A qualifying ESOP is one where at least 75% of the ESOP's board and plan committee are licensed design professionals. This bill will align New York's policy with that of the majority of states in allowing ESOP ownership, while also ensuring the protection of employee stakeholders through following ERISA and US DOL best practices.

Control: Key to this proposal is that the firm will still be *controlled* by licensed professionals. There would be no change to the existing law requiring that the firm's President, CEO and Chairperson of the Board, as well as at least 75% of the firm's officers and directors, must be licensed professionals (engineers, architects, land surveyors, landscape architects or geologists). All professional decision making of the firm would remain in the hands of licensed professionals. The ESOP trust operates in a fiduciary capacity to protect the interest of the participants, and by design, it is not involved in the day-to-day operation of the firm and is removed from any management or professional decision. The ESOP trust exercises decision-making authority only in major corporate events, such as the sale of the firm.

Ownership: This bill **maintains** the 24.9% cap on direct ownership of firm shares by unlicensed individuals. Employees participating in the qualifying ESOP do not directly own shares in the firm but rather own beneficial interests in the ESOP trust. The qualifying, design professional-controlled ESOP is the legal owner of the firm's shares. If a firm's ESOP does not have at least 75% of its board and plan committee slots held by licensed design professionals, it is not a qualifying ESOP and would not be eligible under this amendment.

Ultimately, this bill would maintain current law's restrictions on unlicensed individuals' ownership and preserve the requirements that the firm's controlling management positions be filled predominantly by licensed design professionals. Engineers and other licensed design professionals ultimately remain in charge of and fully responsible for their professional work.

Benefits:

Research conducted by the National Center on Employee ownership, Harvard University, Northwestern University and other institutions shows a clear pattern that ESOP-owned firms have **lower employee turnover, higher profitability, faster growth and greater employee satisfaction** compared to firms not offering ESOPs. Studies conducted in the 1980s and 1990s found productivity increases of up to 4-5%, on average, in the year an ESOP is adopted. ESOP firms show considerably greater stability and resiliency during times of economic downturn. A study tracking the entire population of ESOP companies over ten years (1998-1999) found that privately held ESOPs were only half as likely as non-ESOP firms to go bankrupt or close and only three-fifths as likely to disappear for any reason. A 2018 survey of S corporation ESOPs conducted by the NCEO with support from the Employee-Owned S Corporations of America (ESCA), reports that ESOP participants represented in this survey have more than twice the average total retirement balance of Americans nationally, and those making less than \$26,000 a year also have on average more than double the retirement savings compared to similar workers nationally. Other research shows that ESOP participants to have 2.2 times as much in retirement plans and 20% more financial assets overall compared to the comparison group at non-ESOP companies.

This legislation also assists New York State-licensed design professional firms, which risk losing talented employees to employers in bordering states where ESOP ownership of engineering firms is commonplace. Nationally, engineering firms are prominent among the largest ESOP-owned companies. ACEC National and New York members Parsons, Black & Veatch, HDR, Burns & McDonnell, Terracon Consultants-NY, CDM Smith, HNTB New York Engineering and Architecture, P.C., JMT of New York, Inc., and Brown and Caldwell Associates are all in the national top 100 largest ESOP-owned firms. These firms are joined by smaller ESOP owned firms such as Jacobs, Greenman Pedersen Inc., McFarland-Johnson Inc., and Michael Baker International, Inc. in providing engineering and professional design services in New York State.

There are numerous (approximately 86) firms operating in New York State under Education Law §7209(6) – the so-called “Grandfather” firms. Because of the flexibility with which these firms can operate, numerous Grandfather firms are already operating in the state with majority or 100% ESOP ownership.

Some of the ESOP-owned engineering firms listed above are Grandfather firms and have safely and professionally provided engineering and design services in New York for decades. Others on the same list, indistinguishable in the quality and professionalism of service they provide, are unable to obtain one of the remaining 86 Grandfather charters, despite being 100% ESOP owned in other jurisdictions. Accordingly, these firms must create complicated alternative legal structures to do business in New York. Passage of this legislation would bring parity to and allow the stability, compensation, and growth benefits of ESOP ownership to more of New York State's workers.

This bill helps locally-owned firms stay locally owned and managed by providing a desirable succession planning and transition option. Expanded ESOP ownership allows the employees of the firm to purchase the shares of the current owners. This allows the owners to receive fair market valuation for their stakes without having to resort to selling to larger or out-of-state firms, which can often lead to the loss of jobs as main office operations are eliminated. Facilitating greater ESOP ownership assists with succession planning and keeps firms locally owned and employee operated.

This bill is a common-sense measure that maintains the public safety concerns of the state while providing additional flexibility to the operation of the business, and ACEC New York urges its passage.