

111TH CONGRESS  
1ST SESSION

# S. 1612

To amend the Internal Revenue Code of 1986 to improve the operation of employee stock ownership plans, and for other purposes.

---

IN THE SENATE OF THE UNITED STATES

AUGUST 6, 2009

Mrs. LINCOLN (for herself and Ms. LANDRIEU) introduced the following bill;  
which was read twice and referred to the Committee on Finance

---

## A BILL

To amend the Internal Revenue Code of 1986 to improve the operation of employee stock ownership plans, and for other purposes.

1       *Be it enacted by the Senate and House of Representa-*  
2       *tives of the United States of America in Congress assembled,*

3       **SECTION 1. SHORT TITLE.**

4       This Act may be cited as the “Employee Stock Own-  
5       ership Plan Promotion and Improvement Act of 2009”.

1 **SEC. 2. 10 PERCENT PENALTY TAX NOT TO APPLY TO CER-**  
 2 **TAIN S CORPORATION DISTRIBUTIONS MADE**  
 3 **ON STOCK HELD BY EMPLOYEE STOCK OWN-**  
 4 **ERSHIP PLAN.**

5 (a) IN GENERAL.—Clause (vi) of section 72(t)(2)(A)  
 6 of the Internal Revenue Code of 1986 (relating to general  
 7 rule that subsection not to apply to certain distributions)  
 8 is amended by inserting before the comma at the end the  
 9 following: “or any distribution (as described in section  
 10 1368(a)) with respect to S corporation stock that con-  
 11 stitutes qualifying employer securities (as defined by sec-  
 12 tion 409(l)) to the extent that such distributions are paid  
 13 to a participant in the manner described in clause (i) or  
 14 (ii) of section 404(k)(2)(A)”.

15 (b) EFFECTIVE DATE.—The amendments made by  
 16 this section shall apply to distributions made after the  
 17 date of the enactment of this Act.

18 **SEC. 3. ESOP DIVIDEND EXCEPTION TO ADJUSTMENTS**  
 19 **BASED ON ADJUSTED CURRENT EARNINGS.**

20 (a) IN GENERAL.—Section 56(g)(4)(C) of the Inter-  
 21 nal Revenue Code of 1986 (relating to disallowance of  
 22 items not deductible in computing earnings and profits)  
 23 is amended by adding at the end the following new clause:

24 “(vii) TREATMENT OF ESOP DIVI-  
 25 DENDS.—Clause (i) shall not apply to any  
 26 deduction allowable under section 404(k) if

1           the deduction is allowed for dividends paid  
 2           on employer securities held by an employee  
 3           stock ownership plan established or author-  
 4           ized to be established before March 15,  
 5           1991.”.

6           (b) EFFECTIVE DATE.—The amendment made by  
 7 this section shall apply to taxable years beginning after  
 8 December 31, 1989.

9           (c) WAIVER OF LIMITATIONS.—If refund or credit of  
 10 any overpayment of tax resulting from the application of  
 11 the amendment made by this section is prevented at any  
 12 time before the close of the 1-year period beginning on  
 13 the date of the enactment of this Act by the operation  
 14 of any law or rule of law (including res judicata), such  
 15 refund or credit may nevertheless be made or allowed if  
 16 claim therefor is filed before the close of such period.

17 **SEC. 4. AMENDMENTS RELATED TO SECTION 1042.**

18           (a) DEFERRAL OF TAX FOR CERTAIN SALES TO EM-  
 19 PLOYEE STOCK OWNERSHIP PLAN SPONSORED BY S COR-  
 20 PORATION.—

21           (1) IN GENERAL.—Section 1042(c)(1)(A) of the  
 22 Internal Revenue Code of 1986 (defining qualified  
 23 securities) is amended by striking “C”.

1           (2) EFFECTIVE DATE.—The amendment made  
 2       by paragraph (1) shall apply to sales after the date  
 3       of the enactment of this Act.

4       (b) REINVESTMENT IN CERTAIN MUTUAL FUNDS  
 5 PERMITTED.—

6           (1) IN GENERAL.—Clause (ii) of section  
 7       1042(c)(4)(B) of the Internal Revenue Code of 1986  
 8       (defining operating corporation) is amended to read  
 9       as follows:

10                   “(ii) FINANCIAL INSTITUTIONS, IN-  
 11                   SURANCE COMPANIES, AND MUTUAL  
 12                   FUNDS.—The term ‘operating corporation’  
 13                   shall include—

14                           “(I) any financial institution de-  
 15                           scribed in section 581,

16                           “(II) any insurance company  
 17                           subject to tax under subchapter L,  
 18                           and

19                           “(III) any regulated investment  
 20                           company if substantially all of the se-  
 21                           curities held by such company are se-  
 22                           curities issued by operating corpora-  
 23                           tions (determined without regard to  
 24                           this subclause).”.

1           (2) EFFECTIVE DATE.—The amendment made  
 2           by paragraph (1) shall apply to sales of qualified se-  
 3           curities after the date of the enactment of this Act.

4           (c) MODIFICATION TO 25-PERCENT SHAREHOLDER  
 5 RULE.—

6           (1) IN GENERAL.—Subparagraph (B) of section  
 7           409(n)(1) of the Internal Revenue Code of 1986 (re-  
 8           lating to securities received in certain transactions)  
 9           is amended to read as follows:

10                   “(B) for the benefit of any other person  
 11                   who owns (after the application of section  
 12                   318(a)) more than 25 percent of—

13                           “(i) the total combined voting power  
 14                           of all classes of stock of the corporation  
 15                           which issued such employer securities or of  
 16                           any corporation which is a member of the  
 17                           same controlled group of corporations  
 18                           (within the meaning of subsection (l)(4))  
 19                           as such corporation, or

20                           “(ii) the total value of all classes of  
 21                           stock of any such corporation.”.

22           (2) EFFECTIVE DATE.—The amendment made  
 23           by paragraph (1) shall take effect on the date of the  
 24           enactment of this Act.

1 **SEC. 5. SMALL BUSINESS AND EMPLOYEE STOCK OWNER-**  
2 **SHIP.**

3 (a) FINDINGS.—Congress finds that—

4 (1) since 1974, the ownership of many small  
5 business concerns (as defined under section 3 of the  
6 Small Business Act (15 U.S.C. 632)) in the United  
7 States has transitioned from the original owner, or  
8 owners, to an employee stock ownership plan (re-  
9 ferred to in this section as an “ESOP”), as defined  
10 in section 4975(e)(7) of the Internal Revenue Code  
11 of 1986;

12 (2) data collected on the performance of these  
13 small business concerns owned 50 percent or more  
14 by an ESOP evidences that more often than not  
15 these ESOP-owned small business concerns provide  
16 significant benefit to the employees of the small  
17 business concerns and the communities in which the  
18 small business concerns are located;

19 (3) under the Small Business Act (15 U.S.C.  
20 631 et seq.) and the regulations promulgated by the  
21 Administrator of the Small Business Administration,  
22 a business concern that qualifies as a small business  
23 concern for the numerous preferences of the Act, is  
24 denied treatment as a small business concern once  
25 50 percent or more of the business is acquired on  
26 behalf of the employees by an ESOP; and

1           (4) a small business concern that was eligible  
 2           under the Small Business Act before being so ac-  
 3           quired on behalf of the employees by an ESOP, will  
 4           no longer be treated as eligible, even if the number  
 5           of employees, the revenue of the small business con-  
 6           cern, and the racial, gender, or other criteria used  
 7           under the Act to determine whether the small busi-  
 8           ness concern is eligible for benefits under the Act re-  
 9           main the same, solely because of the acquisition by  
 10          the ESOP.

11          (b) EMPLOYEE STOCK OWNERSHIP PLANS.—The  
 12          Small Business Act (15 U.S.C. 631 et seq.) is amended—

13               (1) by redesignating section 44 as section 45;  
 14          and

15               (2) by inserting after section 43 the following:

16          **“SEC. 44. EMPLOYEE STOCK OWNERSHIP PLANS.**

17               “(a) DEFINITIONS.—In this section—

18                       “(1) the term ‘ESOP’ means an employee stock  
 19                       ownership plan, as defined in section 4975(e)(7) of  
 20                       the Internal Revenue Code of 1986; and

21                       “(2) the term ‘ESOP business concern’ means  
 22                       a business concern that was a small business con-  
 23                       cern eligible for a loan or to participate in a con-  
 24                       tracting assistance or business development program  
 25                       under this Act before the date on which 50 percent

1 or more of the business concern was acquired by an  
 2 ESOP.

3 “(b) CONTINUED ELIGIBILITY.—An ESOP business  
 4 concern shall be deemed a small business concern for pur-  
 5 poses of a loan, preference, or other program under this  
 6 Act if—

7 “(1) on a continuing basis a majority of the  
 8 shares of and control of the ESOP that owns the  
 9 business concern are held by individuals who would  
 10 otherwise meet criteria necessary to be eligible for  
 11 the loan, preference, or other program (as the case  
 12 may be);

13 “(2) control of the ESOP business concern is  
 14 vested in the shareholders of the ESOP; and

15 “(3) the ESOP that owns the business concern  
 16 complies with all requirements of a tax qualified de-  
 17 ferred compensation arrangement under the Internal  
 18 Revenue Code of 1986.”.

19 (c) EFFECTIVE DATE.—The amendments made by  
 20 this section shall take effect on January 1 of the first cal-  
 21 endar year beginning after the date of enactment of this  
 22 Act.

○