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I. Fair Exchange Model Legislation¹

The government invests taxpayer money in private businesses regularly. Most often, these investments occur at times of great stress and an urgency to act. Urgency tends to decrease deliberation in crafting bailouts. For these reasons, it is important for the federal government to have policies and procedures in place when faced with such exigencies, rather than having to invent them under the stress of the moment. The following is a proposal of general principles, and a design for specific legislation to ensure the public interest is protected in these difficult situations.

Key policy principles are these. 1) Government investment should come with enough equity rights that only companies who really need the help will want to sacrifice equity or similar valuable assets for the investment. 2) The government investor should act like a savvy investor and get upside benefit. 3) Government should favor employee owned or community based businesses over global businesses, because the former are much more likely to provide on-going, long-term local benefits. 4) A government investor should acknowledge the important role of all stakeholders in creating and sustaining the businesses, and not be overly focused on stockholders, as stockholders are often less fully committed to a particular company than are employees and other local stakeholders.

The following are models for two forms of federal Fair Exchange legislation: 1) for use when the federal government makes the investment; and 2) a means to raise the floor on negotiations between businesses and governments at the state and local level. They are frameworks developed in response to requests from interested legislators.

A. Model for investment of federal funds in businesses: the Fair Exchange Investment and Taxpayer Protection Act (Fair Exchange Act) of 2009 Draft, (“Fair Exchange Act”)

In summary, the sample Fair Exchange Act language below provides the following.

¹ The following is adapted from “Fair Exchange: Providing Citizens with Equity Managed by a Community Trust, in Return for Government Subsidies or Tax Breaks to Businesses”, by Deborah Groban Olson, 2009 *Cornell Journal of Law and Public Policy* 236 at 337-344 (the “FE Article”).

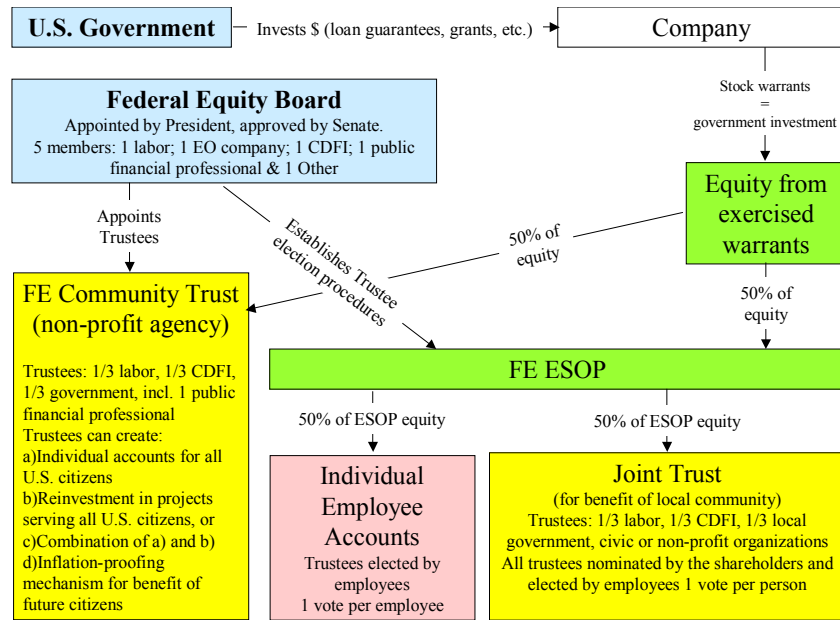
- 1) It creates a government board to negotiate and obtain equity in exchange for government subsidies to business, with a 5-member Federal Equity Exchange Board (“Equity Board”) appointed by the President and approved by the Senate.
- 2) The Board must include at least one representative from organized labor, one from a community development financial institution, one from a majority employee owned company; and one with substantial experience investing assets for public benefit or a broad based pension plan.
- 3) The fund equity is allocated equally between and managed by two bodies, the Fair Exchange ESOP (Fair Exchange ESOP), and the Fair Exchange Community Trust (Community Trust).
 - a. One half of the Fair Exchange ESOP assets are allocated to individual accounts for the Company’s employees the ability for individuals to withdraw and use the funds (available to them for limited purposes such as for home mortgages, tuition, licensed childcare for children of working or studying parents, retirement, etc.); and they elect the Fair Exchange ESOP Trustee.
 - b. The other half of the Fair Exchange ESOP’s stock goes to the Fair Exchange ESOP Joint Trust. The Fair Exchange ESOP Joint Trust holds its stock in a single account to be used for the benefit of current and future employees and the community. It is patient capital that sustains the enterprise and community but does not belong to any individual. Its trustees are elected 1/3 each by shareholders, employees and community representatives. The community representatives are nominated by shareholders and elected by company employees.

The Fair Exchange Community Trust (Community Trust) is a non-profit entity whose board is appointed by the Equity Board. It decides how to allocate its half of the stock between individual and community needs and future security within certain parameters. It is the body charged with being the Quebec Solidarity Fund² type board or Alaska Permanent Fund³ - type trustees.) Figure 1 (below) is a diagram of the trusts created under the Fair Exchange Act, the trustee appointments and uses of funds.

Figure 1: Fair Exchange Taxpayer Investment Protection Act of 2009

² Id at p. 313, See more broadly Canadian Labor Sponsored Investment Funds pp.313-320.

³ Id at pp. 291 -301.



Fair Exchange Act Article I – Preamble

Whereas, this Government has made loans, loan guarantees and provided other investments to private businesses since early in our history, including most railroad companies, most airlines, many large banks, AIG, Chrysler, Lockheed, the savings and loan industry; and others, and

Whereas, there is no reason to believe such investments will not be sought again and again from Congress; and

Whereas, due to the increase in foreign competition in many sectors of the U.S. economy, it is reasonable to anticipate that many more businesses will seek investment from the US government in the form of grants, loans and loan guarantees, to handle the damages and risks of this new situation; and

Whereas many of the firms seeking assistance own or operate assets both within and outside the United States; and

Whereas there has been a trend of U.S. companies outsourcing much of their work outside the U.S., and

Whereas, many individual taxpayers are also harmed by loss of employment due to the circumstances that cause companies to seek government grants, loans and/or loan guarantees, tax abatements, favorable licenses, etc. (hereinafter referred to as “Government Investment”), and

Whereas, corporations, unlike individuals, may be legal persons, but do not hold citizenship in any country; and

Whereas, the primary purpose of the government is to protect had defend the rights of its citizens to life, liberty, property and the pursuit of happiness.

Fair Exchange Act Article II – Creating the Federal Equity Exchange Board

(NOTE: Much of the following language is based on the Air Transportation Safety and Stabilization Act⁴.)

IT IS HEREBY RESOLVED that the Congress of the United States shall require in exchange for any grants, loans or loan guarantees made for or on behalf of any for-profit business entity (hereinafter “ the Business”) by the United States Government or any of its agencies (hereinafter “the Government”), the Federal Equity Exchange Board (hereinafter “Equity Board”) shall obtain contracts under which the Government, the Business’ employees and all current U.S. taxpayers shall participate in gain of the participating Business and/or its security holders through use of common or preferred stock and instruments such as warrants and stock options or other appropriate equity instruments.

- A) The Equity Board’s purpose is to utilize the lending capacity of the federal government to accomplish and balance four goals:
- 1) Broadly distribute “meaningful ownership” among U.S. citizens in the same way that the Homestead Act of the 1862 made many citizens landowners and that ESOPs make employees owners;
 - 2) While lending and making loan guarantees to stabilize US businesses and the U.S. economy;
 - 3) Create a non-wage stream of income or savings for all U.S. citizens available for individuals to withdraw and use the funds (for limited purposes such as for home mortgages, tuition, licensed childcare for children of working or studying parents, retirement, etc.); and
 - 4) Make investment decisions and exercise any securities voting rights on behalf of the greatest good of the greatest number of U.S. citizens considering their need for strong sustainable communities, jobs, income, health, safety, education, a clean environment, and retirement security.
- B) The Equity Board shall include five members appointed by the President with the advice and consent of the Senate. However, there must be at least one each from a community development financial institution, one from a national labor federation, one from a majority employee owned business and one with substantial experience investing assets for public benefit or a broad based pension plan.

⁴ Id at pp. 286 -290.

In carrying out the goals stated in Section 1 (above), the Equity Board may create revolving loan funds to further enable employee or community ownership programs with repaid loan funds.

C) “Meaningful ownership” shall be interpreted by the Equity Board, but shall include both voting and property rights.

Fair Exchange Act Article III - Powers and Functions of the Equity Board, FESSOP and Fair Exchange Community Trust

A) The Equity Board shall obtain contracts under which the Government, the Business’ employees and all current U.S. taxpayers shall participate in gain of the participating Business and/or its security holders through use of common or preferred stock and instruments such as warrants and stock options or other appropriate equity instruments as follows:

- 1) In exchange for any direct grant of funds to the Business, the Business shall provide stock (or its equivalent in a non-stock business) meeting all the requirements of IRC Sec.409 (a) (with the exceptions noted in paragraph 2 below) and shall contribute qualifying employer securities, as defined in IRC Sec.4975 (e)(7) and (8), with fair market value, as defined in ERISA 29 USC Sec. 1108(e) equivalent to the value of the grant made, which shall be divided equally between:
 - a) a Fair Exchange ESOP, defined in Section A (2) below (hereinafter “Fair Exchange Fair Exchange ESOP”) and
 - b) a Fair Exchange Community Trust (hereinafter “Community Trust”), defined in Section A (4) below.
- 2) The Business shall create a qualified Fair Exchange ESOP that shall be:
 - a) An employee stock ownership plan meeting the all the requirements of IRC Sec.409 (a) (with the exceptions noted in paragraph 2(b) below) and shall contribute qualifying employer securities, as defined in IRC Sec.4975 (e)(7) and (8), with fair market value, as defined in ERISA 29 USC Sec. 1108(e) equivalent to 50% of the value of the grant made.
 - b) A qualified Fair Exchange ESOP shall include the following features in addition to the requirements noted in paragraph 2(a) above, and (where these conflict with IRC Sec. 409(a), the requirements of this paragraph shall take precedence). These requirements include:
 - i. The majority of the Trustees of the Fair Exchange ESOP shall be elected on a one vote per person basis by the Fair Exchange ESOP participants, pursuant to procedures and regulations established by the Equity Board.

- ii. Allocations to the individual accounts of individual participants in a Fair Exchange ESOP shall be made from one half of the contributed stock;
 - iii. The other half of the stock contributed to the Fair Exchange ESOP shall be allocated to the “Fair Exchange ESOP Joint Trust”. The Fair Exchange ESOP Joint Trust shall hold its interest in the Fair Exchange ESOP stock for the benefit of current and future employees and the local community. Its Trustees shall be elected as follows: 1/3 by shareholders; 1/3 by the employees on a one vote per person basis; and 1/3 shall be comprised of representatives of local governmental, civic or non-profit organizations (located in communities where the Business has facilities) nominated by the shareholders and approved by vote of the employees on a one vote per person basis.
- 3) The Equity Board shall create a qualified Fair Exchange Community Trust (Community Trust) to which the Business will give the remaining 50% of the stock or equivalent required in Section a (1)(b) above.
- 4) A Community Trust shall be a non-profit agency with a board appointed by the Equity Board. Its board shall include an equal number of representatives from labor, community development financial institutions and government and at least one member with substantial experience investing assets for public benefit or a broad based pension plan.

The Community Trust is empowered to:

- a. Create individual accounts to annually allocate the equity or its income equally to each person who that year qualifies as a citizen of the U.S.; or
- b. Create a community reinvestment plan to use the equity or its income for projects that serve all the citizens of the U.S.; or
- c. Create some combination of the individual accounts and community reinvestment plan described above;
- d. Use its best efforts to create an inflation-proofing mechanism to provide a stream of income for future citizens as well as current citizens.

B. Federal legislation to level the playing field between states and communities

Federal legislation designed to level the playing field between communities and raise the floor in negotiations with businesses would require that any community desiring federal transportation fund *(or anything else Congress could agree upon that every local government needs)* payments comply with the following:

Section 1. Enact and enforce legislation requiring that in exchange for any government investment in a private business, the citizens shall receive equity in exchange or obtain a community benefit contract backed by securities (in the form of stock, warrants or property liens) equivalent to the value of the government investment. A portion of the interest or dividends from these securities shall be used to supply the residents of the taxing entity with a stream of income or other direct benefit(s); a portion of the income shall be used to inflation proof the fund; and a portion may be used for any public purpose approved by the community trust which may include contribution to the local government. The principal shall be held or reinvested by a community trust to provide for the “long-term benefit of the community and all its citizens” as defined in the community trust agreement. (NOTE: This language should be broad enough to allow experiments with a variety of positive examples described in Sections II and III of the FE Article.)

C. Federal “safe harbor” model for local laws

The following could be a safe harbor model for communities to use if Section 1 above were enacted:

“Whenever a Government invests in a private Benefited Business Entity (Company) by providing it with special benefits not given to all taxpayers in the ordinary course (hereinafter “Government Investment”), the business shall provide a quid pro quo at fair market value to the Commonwealth.

“*Benefited Business Entity*” means a for-profit enterprise in whatever form it is organized (hereinafter referred to as “Company” but not limited to enterprises organized in the corporate form).

“*Government Investment*” means any tax deduction, abatement, grant, government subsidized or guaranteed loan, license (e.g. banking and broadcasting), lease, concession, or contract, preparing and/or providing parcels of land, government contracts, and favorable utility rates, use of non-renewable resources, etc. or any other thing of value for which less than a market price is paid to the Community;

“*Quid pro quo*” means an amount equivalent to the Government Investment in corporate common stock or preferred stock or stock warrants convertible into such common stock if the Company is a stock company, or its equivalent in cash), or similar ownership rights in any other business form (hereinafter collectively referred to generally as “Company Stock”) in the Company. Said Company Stock shall have the greatest voting and dividend rights of any other class of Company Stock owned by the Company. For liability reasons, a community trust may prefer to refrain from becoming partners or LLC members with a company, and instead obtain escrow or bonds.

“Commonweal” means: (NOTE: Defining and structuring the “Commonweal” or “Community Trust” is the most challenging aspect of developing a Fair Exchange law.) Here the community must decide upon a private, public or quasi-public entity that meets specific tests of bona fide interest in protecting the long-term economic, social, ecological and/or cultural interests of the local citizens. This might be the government giving the tax break. Or the community may wish to use as a model such statements of principals or objectives as the Canadian Alliance Labor Sponsored Investment Funds’ (LSIF) Statement of Alliance Principles, the language defining the Alaska Permanent Fund, the Alberta Heritage Fund or the Tennessee Valley Authority (TVA) (all described in the FE Article) or some combination or variation of these.

This is also the place where the community must designate its “well-informed-citizen-surrogate” whether that be a set of trustees appointed by one or more elected leaders as in Alaska; a labor state or provincial labor federation, as in the Alliance LSIFs; a major cooperative federation, or a multi-party body such as the Conrail United States Railroad Act structure or leave that function to the local government as they did in Alberta.

The Commonweal or Community Trust shall provide benefits to the community generally, and (if the community so chooses) to all citizens individually as follows. (Note: Here choices must be made regarding what kinds of individual and community benefits will be provided, for example:

- a) on individual benefits (if they are to be provided): 1) dividends, savings or equity accounts for individual citizens with 2) the ability for individuals to withdraw and use the funds (for limited purposes such as for home mortgages, tuition, licensed childcare for children of working or studying parents, retirement, etc.); and 3) the ability (or not) to vote for some of the trust’s leadership; and
- b) on community benefits whether to follow: 1) the social investment model of the LSIFs; 2) the endowment fund model of the Alaska fund; 3) a mixed model – such as that used in Alberta; or 4) to try something based on the TVA model.)

Community Benefit Agreement language such as that used in the State Statutory Model below might be appropriate as a safe harbor as well.

D. Fair Exchange and International Trade Rules

The following federal legislation would also make sense as a requirement in international agreements, or at least as an exemption from rules that prevent communities from giving preference to local businesses. This paper was funded by a source focused solely on the United States. However, Kenneth Thomas, an expert on international trade agreements, reviewed the Fair Exchange proposals herein and concluded that they would not violate the World Trade Organization’s Agreement on Subsidies and Countervailing Measures. Furthermore, Fair

Exchanges would likely pass the European Union rules for government subsidies to businesses under the Treaty of Rome because they are structured like market transactions.⁵

⁵ Kenneth Thomas. "Fair Exchange at the National and International Level" (October 14, 2005).