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ARTICLE: UNION EXPERIENCES WITH WORKER OWNERSHIP: LEGAL AND PRACTICAL ISSUES RAISED BY ESOPS, TRASOPS, STOCK PURCHASES AND CO-OPERATIVES.

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LEXISNEXIS SUMMARY:
... In addition, special pension problems must also be considered when a union is asked to provide investment capital by changing or ending a diversified pension plan. ... Employees were also told that the ESOP would replace their pension plan. ... Because ESOPs were relatively new, especially in unionized situations, the local union was unable to find any information about ESOPs to counter the assertion that the pension plan had to end. In fact, in many ESOPs, such as the Rath Packing ESOP, the pension plan was continued. ... Since SBL continued Amsted's business, the union's position was that the employer violated the pension section of the collective bargaining agreement by offering SBL employees a new contract that unilaterally excluded the pension plan, added the ESOP, and changed vacation and some pay rates. ... Amsted amended the pension plan to remove nonvested SBL employees from pension plan coverage instead of terminating the plan. ... In most cases, the wiser choice is to accept deferrals of other benefits and leave the pension plan intact. ... In a number of situations, employees were told that the only way to save their jobs was to give up their pension plan. ... Employees need not necessarily give up a pension plan in order to provide necessary capital for the buyout. ... A tax-qualified pension plan can be converted into an ESOP in some cases. ...

TEXT:
[*732] I. INTRODUCTION: CHANGES IN THE BARGAINING CLIMATE REQUIRE NEW

RESPONSES

Employee ownership of businesses through Employee Stock Ownership Plans (ESOPs n1 or TRASOPs n2) and co-operatives n3 is increasingly attracting the interest of workers and unions, as current

[*733] economic conditions decrease their ability to bargain for more material benefits and they seek new methods of ensuring job security. Although these mechanisms have existed for a number of years,

[*734] ESOPs and TRASOPs have been of primary interest to employers because of their tax and capital formation advantages. n4 More recently,

[*735] however, unions have sought or have been offered company stock either in exchange for bargaining concessions or to save jobs in plants scheduled for closing.

Preventing plant closings was not Congress' specific objective in creating ESOPs and TRASOPs. n5 Rather, ESOPs and TRASOPs were created as a method of strengthening the free enterprise system. They provide the means both to stimulate necessary capital formation and to expand stock ownership possibilities for a broader base of the population -- employees. n6 Because these ownership mechanisms were created primarily as financial vehicles, their structures are extremely flexible and the degree of democracy in their structures varies widely. A range of stock transfer options is thus open to present and future labor negotiation.

For the employer, there are considerable tax and financial advantages to giving or selling stock to employees through an ESOP or TRASOP. n7 For employees and employers, stock transfers may be an attractive employee benefit when the employer is otherwise unable to provide any wage or deferred benefit increases. Otherwise, most unionists prefer clearly defined wages and benefits to payments of stock, which by its nature has a fluctuating value. Employees may

[*736] also be interested in stock transfers, however, as a means for obtaining greater control over their working conditions and future job security. Additionally, an ESOP or TRASOP is another form of deferred retirement income for employees. n8

This article discusses a number of union experiences with worker ownership and the lessons derived from them. Union members have obtained more control over employee-owned companies as labor's understanding of these flexible mechanisms has increased. In most of the cases discussed here, jobs and the enterprise have, to date, been saved. n9 It is important to emphasize, however, that the potential benefits of employee ownership for workers and unions are not confined to concessions or plant closing situations. n10 Nor is such a plan always a wise choice. There will be some employee-owned companies that fail. n11 Of the wide variety of reasons for plant closure, n12 only some present reasonable prospects for viable employee buyouts. n13

This article explores a range of legal issues posed by the uses of employee ownership by unionized employees. Several preliminary issues confront a union that is considering negotiation of an ESOP for its members. Those emanating from the National Labor Relations Act of 1935, as amended, include: the "employee" status of employee-stockholders; the employer's duty to bargain with the union; the possibility of employer domination of the union; and the possibility of union interference with employer selection of a bargaining representative.

The union's role as negotiator of voting rights for its union members who are employee-stockholders is also discussed. Stock voting arrangements are a critical factor in determining the value of

[*737] a plan. n14 Employees may be offered straight stock purchase plans: TRASOPs, which must pass through voting rights; or ESOPs, in which voting rights may be passed through. n15 Most ESOP and TRASOP plans do not give employees an ownership majority. However, where employees have voting stock held in a trust, which they can control democratically by majority rule bloc voting, over time they can have a significant or controlling interest in the company without holding a majority of stock. n16 Once the stock transfer is completed, voting trusts or voting blocs of employee-stockholders can become a powerful tool in developing worker control, facilitating changes in both managers and management policies. Employee-stockholders have the right to raise any issue of concern at a stockholders meeting, provided proper notice is given. n17

Unions in the United States generally have avoided involvement in corporate decisionmaking. n18 Many unionists are skeptical about union involvement in employee ownership programs because of a number of potential conflicts of interest arising under the Landrum-Griffin Act and the antitrust laws. Labor organizations also fear becoming involved in business decisionmaking because of their

[*738] duty of fair representation. n19 Some unionists view minority representation on corporate boards as a waste of time n20 or see it as a ploy to mislead workers into thinking they are capitalists. n21 There are a few instances, however, in which union officers sit on the boards of directors of corporations with which they negotiate. n22 This article discusses the mechanisms that are available to resolve some of the potential conflict of interest and duty of fair representation problems posed by union representation of employee-stockholders, and the antitrust issues raised by the appointment of union representatives to the corporate boards of directors. Whether the securities laws require registration and disclosure of information to employees who will receive stock in the stock-ownership plan is also discussed. In addition, special pension problems must also be considered

[*739] when a union is asked to provide investment capital by changing or ending a diversified pension plan.

The reader should note the distinctions between ESOPs, TRASOPs, stock-bonus or stock-purchase plans, n23 producer co-operatives, n24 Taft-Hartley trusts n25 and co-operative ESOPs, n26 all of which are discussed in this article. Stock-ownership plans range from a small percentage of employee ownership to full buyouts. However, since possible uses of ownership rights and liabilities develop on a continuum, the lessons from a buyout may be relevant even to a small percentage TRASOP.

II. UNION EXPERIENCES WITH STOCK PLANS, CO-OPERATIVES AND BOARD MEMBERSHIP

A. Direct Stock Purchase -- Chicago and North Western Railway (CNWRW)

Prior to the 1972 sale of the railroad to its employees, the old Chicago and North Western Railway Company was a wholly owned

[*740] subsidiary of Northwest Industries, Inc. n27 Beginning in 1956, Ben Heineman became the controlling stockholder of CNWRW. He worked to increase the value of the corporation by merging it with other railroads. The last railroad mergers for CNWRW came in the late 1960's. Thereafter, the corporation had a business downturn and began to defer maintenance of the railroad. The average speed on their track went from sixty or seventy miles per hour down to ten. The corporation also sold off railroad real estate n28 and began to acquire other companies, including Fruit of the Loom, Cutty Sark and Terra Chemicals. n29

In 1972, CNWRW completed the sale of the railroad to its employees in the following manner. n30 A new corporation was created, North Western Employees Transportation Company, now called Chicago and North Western Transportation Company (CNWTC). The new company assumed the transportation obligations and acquired the transportation assets of the old company without any payment of cash. This bargain arrangement was made in part because the parent corporation wanted to be rid of its less profitable railroad operation and the regulatory structure associated with it. n31

The new corporation, CNWTC, obtained operating cash by making a stock offering of 300,000 shares to all employees of the old company. No financing was needed for the actual purchase of the assets and liabilities, although stock purchases totaling at least $ 1,000,000 were required as a condition of the asset purchase. Class A common stock was offered at fifty dollars per share for only nineteen days. There were no payroll financing arrangements. The minimum stock purchase allowed was ten shares. The maximum stock purchase allowed was graduated on the basis of income. An employee earning less than $ 10,000 was limited to 100 shares, while an employee earning $ 30,000 or more could purchase as much as 2000 shares. n32

[*741] Only a small number of employees purchased stock in this first offering. Most of them were management or higher paid employees. From this offering, employees purchased a total of approximately $ 3,600,000 of stock. Within the first two years of operation under the new corporation, the stock value increased greatly and then split sixty to one. Therefore, there was another stock offering in which employees were not limited as to the number of shares they could buy, and employee-stockholders could tender their own stock for sale at the fixed price. A payroll deduction for employee stock purchase finally was established. n33 At that time, approximately ninety-seven percent of the company's stock was employee owned. In 1980 or 1981, CNWTC stock became listed on the New York Stock Exchange. Since the sale of the stock was not limited to employees, the percentage of employee ownership declined as the value of the stock increased and a public market became available. n34

Approximately ninety percent of CNWTC and CNWRW employees are, and were, unionized. n35 Yet, the unions were not involved in any of the buyout negotiations. n36 Although some union members bought stock and made large profits -- the original fifty dollar shares split sixty to one and then rose from a value of eleven dollars each to ninety dollars each -- most union members were skeptical about whether the old management, which had allowed the railroad to deteriorate, would do any better in the new company. n37 Furthermore, unionized employees may not have been intended to be the major beneficiaries of this "employee ownership" plan since there was no payroll deduction plan for the first significant stock offering, lower paid employees were limited in the amount of stock they could buy, and the offering was only good for nineteen days. Rather, this plan was apparently aimed at selling the company to its management.

The employee-ownership plan was not negotiated with the unions, and the unions have made no attempts to organize their shareholder-members' votes into a bloc. n38 Many of the hourly employees who owned stock sold that stock to management or outsiders because it became so valuable. n39 No ESOP was involved here. Yet, the Class A common stock was essentially held in trust. n40 There are only

[*742] three shares of Class T common stock; two owned by employees, the third owned by an outside trustee. n41 All the other employees own Class A common stock. Until May 1982, only the holders of the Class T stock had the power to vote for directors and to vote on most matters submitted to stockholders. n42 Therefore, until May 1982, the unions could have had no voting power, even if they had organized their shareholder-members as a bloc. Hourly employees, thus, had no more voice in management than they did before the buyout. n43

CNWTC is an example of a profitable employee-owned company, purchased from the former owners when it was unprofitable. However, it is not an example of an employee-owned company designed to be owned or controlled by all employees. Nor did the union influence the buyout in any way.

B. Unionized Worker Buyouts of Whole Companies or Divisions

In the following three cases, Vermont Asbestos Group (VAG), South Bend Lathe (SBL), and Rath Packing Company (Rath), employee ownership saved the workers' jobs. At VAG and SBL, where local union leaders and many employees were displeased with a number of factors in the plans, the local union leaders expressed much faith in the concept of worker ownership. Both current local presidents, Monte Mason, n44 United Cement Lime, Gypsum and Allied Workers International Union Local 338 (VAG) and John Deal, n45 United Steelworkers of America, AFL-CIO, CLC, Local 1722 (SBL), and former VAG local president, Lawrence Despault, n46 stated that they believed worker ownership could work if the local union people were better informed when developing or negotiating with the developers of the buyout plans. Apparently, Local 46 United Food and Commercial Workers International Union at Rath Packing in Waterloo, Iowa, learned a great deal from the experiences

[*743] of others.

1. VERMONT ASBESTOS GROUP

Prior to the March 1975 purchase by its employees, GAF Corporation owned the asbestos mine located near Eden Mills, Vermont in the foothills of the Lowell Mountains. n47 The asbestos mine was only a small division of GAF, acquired as part of a merger ten years earlier. n48 In GAF's view, the mine became economically unfeasible in 1975 when the Environmental Protection Agency (EPA) ordered the company to install approximately $ 1,000,000 of pollution control equipment. n49 It was also apparent to both the company and the union that further dust control devices might become necessary because of developingl occupational safety and health standards. n50

The mine, however, was the major economic resource for the local community. With over 175 employees, it was the major employer in the area. n51 After several unsuccessful attempts to save the mine by political means, the workers and community members decided to try to buy the mine. n52 GAF agreed to sell them the mine, which produced $ 7,000,000 in sales in 1977, at a salvage price of $ 450,000. n53 However, the miners encountered difficulties in putting together a financing package.

In order to raise the needed capital, the miners began to sell stock in their new company, Vermont Asbestos Group (VAG). They agreed to keep at least fifty-one percent of the stock in the hands of fellow workers. n54 One hundred percent of the employees bought stock. n55 Shares were sold at fifty dollars per share, and no one was allowed to buy more than $ 5000 of stock. Stock not sold to mine employees was sold to people in the local community, raising $ 78,000. After this success, the Vermont Agency for Development and Community Affairs agreed to guarantee eighty percent of any bank loan to VAG. Thereafter, a consortium of seven banks finally agreed to lend the workers $ 1,500,000 toward the purchase of the

[*744] mine and pollution control equipment. n56

VAG honored the union contract that had been negotiated with GAF, and the collective bargaining relationship continued. Several hourly workers became members of the new VAG board of directors, although they did not constitute a majority. n57 VAG employees did not lose any pension rights or credits due to the change in employers. n58 Some senior employees received pensions from both GAF and VAG. n59 GAF pension credits were transferred to VAG employees. n60

According to current Local 338 President Monte Mason, the first year of business for VAG was much better than expected due to the closing of asbestos mines in Canada and increases in the price of asbestos. In the first year, the company paid off the entire mortgage and a $ 3,000,000 loan for pollution control equipment. n61 In the 1976-78 union contract, there were substantial increases in wages and insurance and retirement benefits. n62 Union members were much more concerned with the company, they worked harder, their safety record improved dramatically n63 and they became more involved with the union. n64

Today, the majority of VAG stock is not owned by VAG employees. In August 1981 the mine was still in operation and employed most of its complement of 1975 employees. n65 Yet, the union members' involvement in the company has decreased. n66 The employees

[*745] lost control of the company because many of them sold their stock. A local businessman named Howard Manosh bought a significant number of their shares. Manosh now controls VAG through the shares he owns and the support of a few other significant shareholders. n67

Employees sold their stock for two reasons. The company was profitable. During most of 1978, the shares, originally purchased for fifty dollars, were worth $ 1800 to $ 2000. The price peaked at $ 2200 per share. n68 For workers with an annual income of $ 9000 to $ 10,000, the prospect of making such a profit was quite tempting. Yet, both current Local 338 President Monte Mason and former Local 338 President Lawrence Despault said that most of the employees probably would have kept their stock had they not felt betrayed as stockholders by their board of directors, who ignored the stockholder's vote against a major investment in August 1977. n69 To date, the company has lost approximately $ 5,000,000 on this project, n70 a 100% internally financed plant for processing asbestos waste into wallboard.

Many of the stockholders were outraged at the board's action. They believed that, as stockholders, they had no means to protect their investment if they could not control the board. n71 The August 1977 stockholders meeting illustrated a growing problem. n72 The workers felt they were not adequately represented in the decisionmaking

[*746] of the company they owned. n73 Hourly workers were on the board of directors, but according to former Local 338 President Lawrence Despault, some of these worker directors became "brainwashed" after becoming directors. n74

The union took an active role in picking some of its most active and capable members to run for the board of directors in the first two elections. n75 Yet, Despault believed that once on the board, other board members prevailed upon them not to discuss certain matters with the union. The hourly-employee board members complied. Thus, the board knew what took place in the union meetings -- for example, the union's bottom line in bargaining -- but the union did not have similar information about the company's position, despite having members on the board. n76 One union negotiating team member who was elected to the board of directors was convinced by others on the board that he should give up either his negotiating team position or his board position. He resigned from the board. n77

In reflecting on their experiences at VAG, both the present and former local union presidents feel that both the initial spirit of the buyout and the hourly workers' influence over the company could have been retained had the union known how to retain such control. The union has had no program or training for its members who become board members. It had no clear answers to the conflict of interest arguments that management directors made to the worker directors. n78

At the time of the buyout, there was some discussion of creating an ESOP. However, then Local President Despault had been warned by a representative from another union that, "you may not get out of it what you put in." As a result, the VAG employees voted

[*747] against the ESOP. n79 Ironically, it appears that if the hourly workers had pooled their stock in an ESOP, voting it as a bloc instead of relying on a few untrained individual members, they may have had more control over the company. n80 This would not necessarily be true of all ESOPs, but it would probably be true of ESOPs designed on the Rath Packing model. n81

As in the case of the Chicago and North Western Railway, the VAG worker buyout saved the workers' jobs, but was not an ideal example of worker control. At VAG, hourly workers were more involved in making the buyout happen. There were, and still are, hourly worker union members on the board of directors whom the stockholders elect. However, individual stock ownership, as shown by CNWTC and VAG, is not conducive to joint action. Each individual is concerned primarily with his own investment and has no institutional method of acting as a bloc with fellow workers. Unions should be aware of the various trust and co-operative arrangements which present solutions to this problem. n82

2. SOUTH BEND LATHE

a. Background

South Bend Lathe (SBL) is a manufacturer of metal cutting lathes and other machine tools which has been 100% employee-owned through an ESOP since it was purchased from its former conglomerate parent, Amsted Industries, Inc., on July 3, 1975. n83 In 1975, SBL had approximately 500 employees; n84 approximately 300 were hourly employees represented by the Union Steelworkers of America (USWA), AFL-CIO, CLC, Local 1722. There were 240

[*748] hoursly employees in 1981. n85

In January 1975, it became public knowledge, n86 through Amsted advertisements, that Amsted intended to sell its South Bend Lathe Division because it had been losing money steadily since 1970. n87 Some of the potential buyers were liquidators. n88 Under threat of plant closing and liquidation, J.R. "Dick" Boulis n89 sought financing to buy out the plant, and elicited support from the employees and the local union in efforts to create an ESOP and find financing to buy out the plant. SBL received a $ 5,000,000 loan through the United States Economic Development Administration (EDA). The loan was from EDA to the City of South Bend, which made a loan to SBL at three percent per annum for twenty-five years. n90 Additional private financing also was arranged. Some employees were told by Boulis that as a condition of a federal grant, an ESOP would be established. n91 The details of the ESOP plan were developed by Boulis and his attorneys. The plan was not negotiated with the union, but rather was presented as a take-it-or-leave-it proposal. n92 SBL employees were sell acquainted with the horrendous effects of plant closings, since many of them were former employees of Studebaker n93 or had lived in South Bend at the time Studebaker closed all of its South Bend facilities in 1964. n94

[*749] b. Pension problems

Employees were also told that the ESOP would replace their pension plan. n95 From the beginning of the ESOP proposals, the local leadership and the employees were told:

In order to stay alive (meaning to keep the plant open), we had to have an ESOP, but the ESOP had no provisions for a Pension Plan. . . . [We] had no choice to make . . . whether we could keep our pension or not . . . because we would have no Plan. . . . We had no choice to say whether we wanted to go with or without a pension. n96

Because ESOPs were relatively new, especially in unionized situations, n97 the local union was unable to find any information about ESOPs to counter the assertion that the pension plan had to end. n98 In fact, in many ESOPs, such as the Rath Packing ESOP, the pension plan was continued.

The SBL sale occurred shortly after parts of the Employee Retirement Income Security Act of 1974 (ERISA) n99 had become effective. n100 Because of the complexity of the new Act, the local union could not obtain a precise answer regarding Amsted's pension obligations upon the sale of the company to the ESOP company, SBL, and only later learned that ERISA did not cover Amsted's plan at SBL at the time of the sale. n101 Without even informing the union, Amsted unilaterally amended the pension plan so that benefits were payable only to those who were retired or eligible for immediate retirement as of July 3, 1975. n102 A number of SBL employees who were

[*750] only a year or two away from retirement thus were ineligible for any collectively bargained pension plan benefits. n103

The sale to SBL occurred between July 1-3, 1975, but the collective bargaining agreement in force at the time, which contained a successorship clause, did not expire until October 1977. n104 Since SBL continued Amsted's business, the union's position was that the employer violated the pension section of the collective bargaining agreement by offering SBL employees a new contract that unilaterally excluded the pension plan, added the ESOP, and changed vacation and some pay rates. n105 In January 1976, the union grieved SBL's refusal to pay any pension benefits to employees who became eligible for them after July 3, 1975. Boulis refused to accept any appeal of the grievance to the international representative level and also refused to agree to mandatory arbitration. n106 Therefore, the union is now seeking a court order to require SBL to arbitrate the pension grievance. n107

Amsted amended the pension plan to remove nonvested SBL employees from pension plan coverage instead of terminating the plan. The pension plan beneficiaries did not have the ERISA protections afforded to those whose plans have been terminated pursuant to ERISA n108 and *section 411(d)(3) of the Internal Revenue Code*. n109 SBL illustrates the importance of a thorough exploration of the ERISA consequences for the employee-beneficiaries before they make the decision to convert n110 or terminate a pension plan. In most cases, the wiser choice is to accept deferrals of other benefits and leave the pension plan intact. n111

[*751] c. Voting rights

The voting rights of the employee-stockholders at SBL are quite limited. When SBL was created, the board of directors unilaterally adopted the ESOP and installed a committee to manage the Employee Stock Ownership Trust (ESOT) which holds all the company's stock. n112 The employees do not receive title to their shares except upon retirement, death or after a break in service of more than one year, provided the employee has any vested shares. n113 Under sections six and seven of the SBL ESOP Plan, stock is allocated to each employee each year of his employment. n114 However, the employee's right to vote this stock or to obtain it upon termination of employment does not occur until it has vested. Until an employee has completed three years of company service, he has no vested accumulation. After three years of service, the employee is thirty percent vested and can vote thirty percent of the shares allocated to his account. After four years, he is forty percent vested and can vote forty percent of the shares allocated to his account. Finally, after ten years of service, the employee can vote one hundred percent of the shares allocated to his account.

The committee sends out proxy statements soliciting votes from ESOP participants based on the number of vested shares held by each. The trustee is then required to vote those vested shares as instructed by the participants and to vote the rest of the ESOP shares, including shares already allocated to but not yet vested in employees, as the ESOT committee thinks best. n115 According to a proxy statement sent to employee-stockholders on September 24, 1980, only 3,755.69 of the 16,884 shares of common stock in the ESOP were vested and eligible for participant voting. n116 Thus, the

[*752] ESOP committee, which is itself appointed by the board of directors, elects the board of directors. n117

d. Attempted union busting

The wedge that Boulis may have attempted to create between the local and international unions concerning the pension question n118 appeared to be part of a larger strategy. Form July 1975 when SBL bought the plant until 1977 when the USWA sought and won a new NLRB election, Boulis refused to deal with the international union, which had been the bargaining representative of the workers in that plant for the prior thirty years. n119 Boulis dealt only with the

[*753] local union and tried to convince the employees that since they had an ESOP, they did not need the union. n120

For some unions, the term "ESOP" has become synonymous with union busting due to experiences like that at SBL, where an entrepreneur creates employee ownership without employee control under imminent threat of a plant closing, or experiences where ESOP promoters claim that employee ownership and profit sharing are good ways to keep unions out. However, the degree of worker control is not determined by the mechanism itself, which is quite flexible, but rather by the way it is employed.

The SBL ESOP Plan is drafted in incomprehensible language, and reads like the most baffling of insurance policies or tax laws. n121 The plan participants, therefore, neither understood the meaninglessness of their voting rights when the plan was proposed, nor knew that the law permitted greater voting rights. n122 According to Local 1722 President John Deak, if the union had known to push for more direct voting rights under the plan at the time it was presented, they would have had the leverage to change the plan. n123 At the time, however, the union did not know enough about ESOPs to exert their power to secure better voting rights or a more favorable pension arrangement. n124

3. RATH PACKING COMPANY

a. Background

Rath Packing Company, a nationally known meatpacker specializing in pork products, is the second largest employer in Waterloo, Iowa and the surrounding Black Hawk County. Rath employs 2200 local people with an annual payroll of $ 35,000,000, and provides a significant local livestock market. During the 1970's, it lost over $ 20,000,000. n125

To remain competitive, Rath needed $ 4,500,000 in capital investments

[*754] for modernization. Community officials proposed that the United States Department of Housing and Urban Development (HUD) grant the city money under its Urban Development Action Grant (UDAG) program to be lent, in turn, to Rath. n126 HUD conditioned the loan on new equity investment.

In March 1979, UFCW Local 46 officials presented their own plan for the employees to purchase the company, which was accepted by the company, HUD and the EDA. n127 The union's objectives in presenting its own plan were to save jobs, limit concessions, gain control of the company and management decisionmaking, protect the pension plan, and prevent a proposed buyout that would have included drastic wage and benefit cuts without giving the union or employees any control over the company. n128

The local leadership acted on its knowledge that for the last ten years, 1,800,000 shares of common stock, equaling a sixty percent interest in the company, were available in authorized but unissued treasury stock. n129 The employees raised matching funds for the HUD loan by taking temporary pay and benefit deferrals. n130 They contributed their foregone wages, by weekly payroll deductions, to purchase the authorized but unissued treasury stock through an ESOP. n131 Each employee in the plan was credited with ten shares in lieu of twenty dollars pay each week, until the shares were all purchased. The deferred vacation, sick pay and pension increases

[*755] were kept in a company escrow account. The union retained veto power over expenditures from the account to ensure that it was used for the needed modernization. n132 The escrow fund was discontinued when the stock purchase agreement closed. It was replaced by a profit-sharing plan which ultimately will return these deferrals n133 to employees through profit sharing on future pre-tax profits allocated on the basis of accumulated deferred benefits.

Local 46 was well situated to initiate and carry out this buyout plan because it represents almost all the employees of the Rath Company. n134 The local leaders also timed the announcement of their plan to follow, rather than to precede, national negotiations to prevent use of their "deferrals" by employers in national negotiations. They consciously sought to make their "deferrals" so costly to the employer in terms of worker control that their union brethren would have strong arguments against giving any similar "deferrals" without gaining majority control over the company. n135

b. Rath response to the control dilution problem

The local leadership at Rath wanted to avoid the pitfalls of an individual stock ownership plan like VAG, which had caused the employees to lose control of the company. They considered creation of a co-operative but found that, at that time, they would have had to gain control of 100% of the Rath stock to change the corporation into a co-operative. n136 They also tried to create a non-ESOP perpetual stock trust but the Department of Labor denied the necessary

[*756] ERISA exemptions. n137 As a result, the union leadership developed the ESOP under which they now operate.

One of the features of the plan is that distribution of benefits "normally will not be made earlier than five years after the date the employee commenced participation in the ESOP, regardless of when termination of his employment occurs. . . ." n138 The purpose of this language was to create a five-year grace period during which the drafters hoped the ESOP rules would be changed to allow a majority employee-owned ESOP to pay its termination distributions in cash rather than in stock. A cash distribution would prevent dilution of control of the company out of the hands of active employees. n139

[*757] The Economic Recovery Tax Act of 1981 made just that change. n140

c. Mechanics of the Rath plan and trust

All bargaining unit employees participate in the ESOP, and nonbargaining unit employees may participate. Each participant purchases ten shares of Rath stock per week, in lieu of twenty dollars in pay, which are placed in the ESOT. The market value of the stock as of July 15, 1981 was $ 4.50 per share. n141 The stock is actually held in the ESOT and attributed to separate accounts for each employee. The participant does not hold title to the shares until they are distributed upon her termination of employment, at which time the participant may opt to take her distribution in stock or cash. n142

The ESOT board of trustees is empowered to vote all stock and other voting securities held in the ESOT. The board of trustees is elected democratically by all participants on a one vote per person, not a one vote per share, basis. Before each stockholders meeting, the members of the ESOP meet to vote on all issues that will be

[*758] voted on by the shareholders. The trustees are bound to vote all the ESOT shares as instructed by the majority of those voting at the membership meeting. n143 All plan trustees must be plan participants, but they may not be "officer[s], employee[s], agent[s] or representative[s] of the union [UFCW Local 46], or of any other labor organization." n144

d. Rath relationship between the ESOP and the union

Although the ESOT trustees may not be officers or agents of the union, Local 46 explicitly has retained veto power over any possible changes in power, any plan modification or termination of its agreements that created the plan with Rath. n145 Furthermore, since the Rath Packing Company has direct voting by shares for all director seats, the majority voting bloc can elect the entire board of directors. n146 The board of directors was expanded from six to sixteen members during the transition period to majority employee ownership at Rath Packing. The additional ten directors are called "provisional" directors and became permanent only when the 1,800,000 shares of stock were sold to the ESOP. Until then, the nominees for the board of directors had to be mutually acceptable to the company and Local 46. n147

Along with the employee-ownership plan, the company and the local union at Rath have put a lot of effort into developing a working system of management that involves all employees. n148 However, the UFCW International Union does not officially encourage employee

[*759] ownership. n149 John Mancuso, Assistant to the Director of the Packinghouse Division, reasoned that "we find it hard to be bosses and workers at the same time." n150

Despite Local 46's efforts to maintain the structure of the national pattern agreement between the UFCW International Union and the big four meatpackers, n151 Mancuso points out that its pension plan n152 is only funded at eleven and one-half dollars per month per year of service, while the industry pattern is fifteen dollars per month per year of service. In addition, the Rath employees are only paid half-time for their ten holidays instead of the full pay involved in the pattern. At Rath, employees also are paid only half of the straight time rate for vacations, although they are allowed the same number of weeks off as the national pattern provides. The master agreement provides for full pay for vacation days. n153

In the United States, there are very few examples of worker ownership and worker control in the same company. n154 Rath Packing is one of the first such experiments in an industrial plant. n155 Because of the control extracted at Rath in exchange for the "deferrals," other companies do not use Rath as an example in seeking concessions. n156 Community leaders in other communities have used Rath as an example in encouraging workers to buy failing plants spun off by larger companies. However, such a purchase is much less advantageous than the purchase of an entire company as at Rath.

e. Later economic difficulties

Rath illustrates an innovative ESOP trust structure, and financing mechanisms developed with the clear intention of preserving trade union principles as well as jobs. Rath faces grave financial

[*760] problems due to an unfavorable hog market, very old facilities and excess capacity in the industry. n157 The structural innovations should not be discarded or blamed if Rath ultimately fails due to economic circumstances. The Rath experiment has already succeeded in preserving several thousand jobs since 1980.

Because of bad economic circumstances, all three Rath Packing Company pension plans were terminated in September 1982. By a sixty percent vote, the union approved the company's request to the Pension Benefit Guarantee Corporation (PBGC) to terminate the union pension plan, along with two other plans, in order to save the company and jobs. Upon termination of any pension plan, PBGC has the authority to place a lien on the company in an amount equal to the lesser of the plan asset deficit or thirty percent of the employer's net worth, n158 and thus can force a company to close. However, Rath, which has a negative net worth, has entered into a ten-year agreement with the PBGC under which Rath is required to pay its pension liabilities to PBGC, and cannot create any new pension plans for at least ten years. UFCW Local 46 President Lyle Taylor said the termination was essential to keep the company alive. n159

The PBGC will pay benefits to retirees and employees with vested benefits. Retirees and employees with at least ten years of service will receive almost all their pension benefits. The benefit level of current employees with over ten years of service will be frozen at thirteen dollars per month per year of past service, and they will accrue no further pension credits. Approximately 390 bargaining unit employees and a total of approximately 600 employees from all three plans who have less than ten years of service will lose all their pension rights.

C. Unionized Worker Buyouts of a Single Plant vs. Full Company Buyouts

1. HYATT-CLARK INDUSTRIES

In the fall of 1981, General Motors (GM) sold its New Departure Hyatt Roller Bearing Plant in Clark, New Jersey to a group of its former employees, consisting primarily of UAW members and former management employees. n160 GM's primary reasons for closing

[*761] the plant were: 1) its new front-wheel drive cars did not need the taper bearings produced at that plant; 2) the bearings it needed could be supplied more cheaply by outside sources; n161 and 3) labor costs were too high due to both the UAW national agreement with GM and the local agreement with Local 736. n162

In order to save jobs in the plant, the employees organized a committee to fund a feasibility study concerning purchase of the plant. Upon receipt of a favorable study, the committee organized purchase of the plant by means of an ESOP. n163 The employees took a twenty-five percent cut in pay and benefits to make their costs feasible, although they retained health and retirement benefits at the former UAW levels. n164 Employees hope to be repaid these "deferrals" under a profit-sharing plan. GM agreed to a contract to purchase bearings from the plant for three years. n165

The union also obtained a one vote per person distribution of voting rights within the ESOP. n166 The employees have a greater voice in management of the plant, n167 and in nine years shall elect half of the company's board of directors. n168 The workforce has been reduced to about one-half its former size. n169 None of the former employees who desired a job at Hyatt-Clark has been refused one. Many of the former GM employees sought special early retirement under plant closing language negotiated in the former GM contract and maintained by the union as an essential part of the sale agreement. n170 However, the new company must pay GM $ 15,000,000 over twenty years to retain $ 60,000,000 in plant closing pension benefits. n171

The local leadership has stated frequently that the international

[*762] union was of no help in the employees' efforts to purchase the plant, and has alluded to a history of animosity between the local and international union which long predated the buyout. n172 The international union faced several problems in aiding this local. First, the local sought $ 5,000,000 from the international union as part of the Hyatt-Clark ESOP loan package. n173 The international was told that the New Jersey Economic Development Authority would guarantee only fifty percent of the $ 5,000,000, although the UAW originally was told a ninety percent guarantee was available. n174 The local did not know of this disparity. n175

A greater problem for the international union was the fact that it did not have an established policy for dealing with such a situation. If it loaned $ 5,000,000 to this local ESOP committee, on what criteria could it then deny or grant such a loan to another local? n176 Furthermore, the local agreed to give the new company wage and benefit cuts before the international union had agreed to reopen the national agreements. Although the local agreement did not directly violate the national agreement, the new company's employees were working at wage and benefit rates that undercut the international union's national agreements with GM. n177

Members of UAW Local 736 who were employees when the

[*763] plant was owned by GM and who opposed the buyout filed a duty of fair representation case against the local and international unions and GM, contesting the union's involvement in developing the ESOP and granting employment preference in the new company to those who contributed to the feasibility study. n178 The NLRB has dismissed the charge. The lawsuit filed against the local was dismissed with prejudice and without costs, by mutual agreement of the parties. n179

2. FORD-SHEFFIELD

In July 1981, a joint union-management task force was created at Ford Motor Company's aluminum die-cast plant in Sheffield, Alabama in an attempt to reduce operating losses. Through the efforts of this committee and 100 suggestions provided by workers, the company saved $ 1,500,000 at their plant in August and September 1981. n180 Yet, on October 21, 1981, Ford announced that it would close the plant unless the employees agreed to accept a fifty percent cut in pay and benefits by November 15, 1981. If they had accepted the cuts, they would have had until January 1, 1982 to decide whether to adopt a profit-sharing plan or to buy the plant themselves. n181

UAW Local 255 President L.C. "Sonny" McCanless sought guidance from UAW International President Douglas Fraser regarding whether the local could enter into negotiations with Ford over the proposed cuts. President Fraser said, "Constitutionally (under the UAW International Constitution) this is not possible. The entire UAW-Ford membership ratified the National Agreement." n182 Fraser also stated that the UAW Ford Council had adopted a resolution on March 19, 1981 opposing reopening the national agreement. n183

[*764] Therefore, the local refused to discuss Ford's initial offer.

After the local rejected the cuts, which had been a prerequisite to any discussion of the ESOP, Ford again offered to sell the plant to the employees. Ford stated that the previously required cuts "were not a prerequisite for buying the plant," n184 although Ford still believed such cuts were essential to running the plant successfully. n185 According to Ford spokesman Davis, when Ford offered to discuss the ESOP without a wage cut prerequisite the local union demanded, as a precondition to negotiation of the ESOP, that Ford guarantee to give its employees "special early retirement" benefits it had provided in other plant closing situations. n186 Local 255 President McCanless said the union did not consider special early retirement a precondition to further negotiation. Rather, the union was concerned with protecting the contractual rights of its members, such as special early retirement, should the workers collectively decide to buy the plant. Based on International UAW President Fraser's decision, the local union determined that they could not negotiate the ESOP without breaching the national UAW-Ford contract. Only the workers as buyers, not as union members, could pursue the ESOP. n187 Ford refused to guarantee these benefits as a precondition to further negotiations, and the ESOP talks ended. n188

According to its president, Sonny McCanless, the majority of UAW Local 255 members were skeptical of Ford's ESOP proposal for several reasons. The initial proposal of a fifty percent wage and benefit cut was so drastic it caused the employees to see Ford's ESOP proposal as insincere and an attempt to break the national

[*765] agreement. n189 Further, less than one month was provided for the cut decision, which gave the local inadequate time to evaluate the feasibility of such a purchase. n190 Moreover, management told the union that it had set the plant's price for the specialized transmission casting for ATX transmission cases at fifty-one dollars, although it cost ninety-seven dollars to produce. n191 Such internal pricing procedures could account for much of the alleged $ 3,000,000 monthly loss. n192

Ford said it had decided to lower its labor costs drastically or close the plant because it was losing $ 3,000,000 per month. n193 Ford had tried to sell the plant to other parties, but the labor costs deterred buyers. n194 According to Ford spokesperson Michael Davis,

[*766] the Ford Casting Division management believed the plant could have been profitable if the employees had bought it, had lowered their costs, and had increased the plant's use by contracting with other automobile and agricultural implementmakers for die-cast. n195 Ford viewed the Sheffield workforce as one of its best, most loyal and well-educated workforces. n196 In February 1982, the plant was operating at thirty-five percent capacity. n197

One possible view of Ford's strategy is that it is trying to organize itself like a Japanese company, giving lifetime job security to its employees in its central production operations, but buying its parts from independent supplier companies who compete with each other and are not covered by the UAW-Ford contract. If Ford had planned to use the Sheffield plant for only a few more years until it found a more convenient place to produce the parts made there, it certainly would have saved money by selling to an ESOP if it could have sold the plant, along with its pension and plant closing benefit obligations. Ford also could have obtained the tax advantages accorded ESOP contributions if it had helped finance the ESOP purchase. Yet, Ford denied any tax motives and asserted it would not have encouraged the purchase if it had believed the plant would not succeed because Ford would not want to be involved with a bankrupt supplier. n198

In the Ford-UAW national agreement reached on February 13, 1982, the union agreed to benefit concessions and limited wage increases in return for Ford's agreement not to close any more plants due to outsourcing. This agreement applies only to plants where a closing announcement had not already been made; therefore, it excluded Sheffield from protection. n199 The union also won a Guaranteed Income Stream (GIS) plan, which provides high-seniority employees

[*767] with payments until retirement if they are laid off due to plant closings, as well as increased Supplemental Unemployment Benefits (SUB) payments for lower-seniority Ford workers who are laid off. n200 UAW Local 255 approved the new Ford national agreement and voted overwhelmingly to allow the local to reopen negotiations on its local agreement with Ford management, thus opening the door to possible local concessions. Ford reviewed the planned closing, n201 and decided to close the plant. n202 Although the new benefits did not protect the Sheffield workers from the planned closing, they made it more attractive for the employees to let the plant close instead of taking the ESOP offer. n203 To many it seemed foolish to risk losing early retirement benefits, GIS, SUB and other plant closing benefit guarantees to take on a risky ESOP, especially where the long-established UAW principle of national agreements was being challenged.

When asked what lessons other unionists should learn from the Ford-Sheffield experience, Sonny McCanless replied, "the value of an international union and its national agreements as the source of ultimate protection for workers." n204 James Zarello, shop chairman of UAW Local 736 at Hyatt-Clark, distinguished the situation in Sheffield from that in New Jersey, where GM did not require a cut in wages and benefits as a prerequisite to selling its plant to the workers. n205 Another clear difference is that GM gave its employees time to obtain a feasibility study before they were required to make a final decision to buy. GM also agreed to purchase bearings from the Hyatt plant for three years and lent the new company $ 20,000,000. n206

The Hyatt-Clark and Ford-Sheffield single plant buyouts must

[*768] be viewed differently by unions than cases of whole company buyouts such as Rath, VAG or CNWTC. A single plant buyout separates that plant from a master contract, creating wage competition between those who were formerly unified in their wage and benefit demands to the company. Yet, the question for the workers involved is, how else can we save our jobs? Is a worker ultimately better protected by keeping the union's national contract strong or by gaining some control over his own plant?

A similar question arose concerning Rath Packing. The UFCW has a pattern master agreement with all the unionized meatpackers. n207 Even though Rath Packing is a separate company, and thus does not present the immediate problem of wage and benefit competition between union brethren under contract with the same employer, the International UFCW found that community leaders use Rath as an example to encourage the union members to buy single, failing plants of multiplant employers. n208 Where there is a national agreement, however, single plant buyouts always present the issues exemplified by the Hyatt-Clark and Ford-Sheffield cases.

Rath Packing is distinguishable because it represents a different type of buyout. There, the unionized employees obtained majority control of the entire corporation: its brand name, its sales force, its supply and distribution network. The Rath ESOP company is not a captive supplier to its parent; it is the parent. Even at Rath, however, the "deferrals" taken from the national agreement affect the strength of the master agreements. Yet the Rath example shows that use of timing and a conscious effort to protect the national agreement can blunt the ability of employers to take advantage of such "deferrals." n209

The fragmenting aspect of small ESOP companies in unionized corporate industries presents a basic problem for unions. Yet, without ownership rights or other union controls over management pre-rogatives, unions have no effective means of preventing outsourcing, capital flight and job loss. One possible solution is to seek ownership rights across the board in national agreements as a means of obtaining some control over management decisions on divesting, out-sourcing

[*769] and foreign and domestic investment. Some of the potential drawbacks to such a plan are dealt with elsewhere in this article. n210

D. Industrial Co-operatives

Industrial or producer co-operatives form a small portion of the existing co-operatives in the United States. Some of the oldest industrial co-operatives in the United States are the plywood co-operatives, formed in the 1920's and 1930's. Of the approximately thirty plywood co-operatives formed during that period, sixteen are still in operation. n211 Many of these co-operatives are run quite democratically, with workers serving on the boards of directors and either electing a manager from among themselves or hiring a manager from the outside. n212 The manager usually has a limit for spending without board approval, but a membership vote is often required for expenditures in excess of $ 25,000 or some similar figure. n213 Members frequently have the right to appeal any disciplinary action to the board of directors and then to the membership. n214 Since the directors work on the shop floor, rank and file members have constant contact with the board and are able to exert a considerable degree of informal control. n215 Elected managers may often believe that they do not always act in the best long-range interest of the firm because of their short-range political needs to remain popular. Thus, they may defer major purchases to provide more cash in pay or in dividends to the members. n216 Not all the plywood co-operatives, however, are run democratically. Often the nonmmeber manager hired from the outside has all the management powers of a conventional firm executive. n217

A number of studies have compared the performance of worker-owned plywood firms to that of conventional plywood firms. A United States tax court settlement and other studies show the plywood co-operatives to be twenty-five to sixty percent more productive than conventional mills. n218 However, the International

[*770] Woodworkers of America (IWA) disputes the methods used to measure productivity, claiming that the mills compared in the studies engaged in very different types of work. n219

The plywood co-operatives generally were formed as new companies or successors to short-lived private companies. n220 This distinguishes them from the previous examples in which unionized employee groups purchased their former employers' companies which had been in existence for many years. In these cases the unions either have taken a leading role in organizing the employee-ownership attempt, or have at least retained a positive and necessary role in the eyes of the workers after the change in ownership. In contrast, most of the plywood co-operatives began as groups of unemployed lumberworkers who needed work rather than as unionized groups. n221 One of the exceptions is Everett Plywood, where the union has survived since the days the mill was privately owned. n222 Others, such as Hoquaim Plywood and North Pacific Plywood in the State of Washington, were purchased from former owners and then turned into co-operatives. n223

The ownership of the plywood co-operatives generally has been on the basis of one share per member. As the value of the companies has increased, shares which were originally worth $ 1500 to $ 2000 have risen in value to $ 25,000 to $ 50,000. Thus, younger workers often cannot afford to purchase a share in the company, and retiring workers often are forced to sell their shares to nonemployees in order to liquidate their share value. This has led some of the co-operatives to sell out to conglomerates, n224 while others have a substantial number of nonshareholder employees. n225 In many instances, the nonshareholder employees earn less money, are assigned the less desirable jobs and have fewer protections against improper discipline than shareholders have. n226

The IWA and the Lumber and Sawmill Workers affiliated with the United Brotherhood of Carpenters and Joiners of America,

[*771] AFL-CIO (Carpenters) were both involved in a number of reported cases involving attempts to organize nonshareholder employees of these plywood co-operatives. n227 These cases illustrate the unwillingness of many of these co-operatives to become unionized. One of the main issues raised by the co-operative managements in these cases is the right of the shareholder employees to be included in bargaining units of nonshareholder employees. The National Labor Relations Board (NLRB) found that employee shareholders could be "employees" within the meaning of the National Labor Relations Act (NLRA), but that nonshareholder employees and shareholder employees could not be in the same bargaining unit if their interests conflicted. n228 Differences in decisionmaking power, disciplinary procedures, pay and job status were all considered indicia of such conflict. n229 Thus, at least the IWA has developed a rather negative impression of the plywood co-operatives as examples of continuing institutions of worker democracy. n230

Researchers refer to the ownership structures that make it difficult for new members to buy into these co-operatives as "examples of collective selfishness." n231 The IWA cites the case of NLRB v. Fort Vancouver Plywood Co. n232 to illustrate this phenomenon. n233 "In this case, the shareholder board of directors met in an emergency when learning of a union organizing drive among the nonshareholder workers and subsequently fired every one of the nonshareholders." n234 The NLRB and the Ninth Circuit found these actions to be blatant violations of the NLRA. n235

[*772] The Industrial Co-operative Association (ICA) n236 has studied the plywood co-operatives, as well as a number of other models, n237 and has attempted to devise workable models for overcoming the "collective selfishness" aspects of retaining all voting rights and equity within one share. n238 The ICA's basic formula is to separate voting rights from equity or economic profit rights in the company, whether the company is formed within the shell of a stock corporation or as a statutory co-operative. Each worker has one vote, based on membership in the co-operative, but each receives her dividend-type distributions to her internal capital account. Thus, when internal capital accounts are paid out, usually at least every five years and upon termination of employment, long-term employees will receive more than short-term employees because long-term employees have more equity. Under this system, new employees may become members without purchasing the entire equity of retiring members or diluting the equity of the older members. The newly createc co-operative ESOPs n239 have adopted some elements of this structure.

E. Nonmajority Stock Plans

Nonmajority stock plans in publicly traded companies are probably the most important types of plans to consider and study because most collective bargaining agreements are negotiated with large companies in which the employees cannot hope or expect to obtain majority control over the corporate board, at least in the foreseeable future. Approximately 5000 employee-ownership plans exist in the United States today. At least 250 companies of ten employees of more are majority employee-owned. n240 What, if any, is the value of such stock to employees or unions? The answer depends on the types of plans negotiated. Over time, a plan providing a small percentage of employee ownership in a closed trust controlled only

[*773] by active employees possibly could develop into a significant voting bloc.

1. GENERAL MOTORS AND FORD TRASOPS

Nonmajority plans come in a variety of forms. The automobile company plans are typical examples. n241 In their 1979-82 collective bargaining agreements, the International Union United Automobile, Aerospace and Agricultural Implement Workers of America, AFL-CIO, CLC (UAW) negotiated TRASOP n242 -type employee stock ownership plans with Ford and General Motors (GM). The UAW negotiated a letter agreeing to establish a similar plan with Chrysler Corporation in their 1979-82 contract, which becomes effective when Chrysler reaches taxpaying status and the relevant tax credits become available. n243

Some of the TRASOP rules that were operative when these plans were negotiated include the following: 1) employee participation in a TRASOP must not be a condition of employment, n244 and 2) employer stock must be allocated to the employee-participant's account in amounts equal to the employee's contributions. n245 A TRASOP, unlike other ESOPs, requires a pass through of voting rights n246 and the use of voting stock; it cannot be used for leveraged borrowing; and it is limited to an amount of stock equal to 1.5% of the employer's investment tax credit each year in which the employer elects to take an investment tax credit, provided that the last one-half percent is matched by employee TRASOP contributions. n247 The accumulation of stock in the fund thus remains insignificant for a long period of time.

[*774] In the Ford n248 and GM n249 TRASOP plans, the company is defined as the administrator of the plan. The stock is common stock. Stock voting, dividend rights and investment credit language follow the requirements of the Internal Revenue Code. n250 The named fiduciary is the finance committee of the corporate board of directors. The employees' contributions to the plan, for the years in which they seek investment tax credits, will be contributions to all company ESOPs based on the compensation of each employee. There are separate plans for salaried and hourly employees, without an equal allocation to each employee's account.

Each employee has the right to direct the trustee to vote all of the employee's shares and fractional shares. Where the employee gives no direction to the trustee, the shares in the employee's account will not be voted. Participant shares are neither assignable nor transferrable except by death, mental incompetency, or upon a vested employee's termination of employment.

Thus, participants in these plans vote their stock through the trustee, but have no structurally established means of voting their stock as a bloc. n251 Under the Ford and GM TRASOPs, many members simply may not vote. Consequently their ownership rights will not benefit their fellow union members. In addition, there is no requirement to hold meetings at which issues before the stockholders might be explained and a union position decided. Thus, the hourly employees may unknowingly split their ESOT vote instructions to the trustee.

Voting rights in the Ford and GM plans are structured this way because the union decided, upon advice of counsel, that the TRASOP pass through voting requirements would make it quite difficult to arrange for bloc voting by the union. n252 Furthermore, the union believes it can adequately inform its members to vote the stock in their own interests when such a vote is meaningful and needed. n253 That belief is probably well founded over the short run, especially since there is usually an insignificant amount of total stock in the TRASOPs.

[*775] These TRASOPs are deliberately designed as individual employee benefits, without group accumulation and bloc-voting features. Since these plans require distribution of shares upon termination of the participant's employment, the trusts cannot accumulate a significant number of shares over time to create meaningful voting blocs. However, the 1981 amendment to *section 409A(h)(2) of the Internal Revenue Code* n254 allows for distributions of cash instead of stock where the employer's charter or bylaws restrict the ownership of substantially all outstanding employer securities to employees or to a trust (or an ESOP) plan. Thus, a TRASOP could be designed or later amended to hold substantially all of the employer's outstanding securities. n255

Even in their present form, TRASOPs provide benefits to both employers and employees. As the tax laws change and as the companies' needs for investment capital increase, the companies may find it necessary to consider broader ESOP plans. The unions also may demand stock in exchange for concessions. Already Congress has modified the TRASOP concept to benefit employers by changing the basis upon which investment tax credit ESOPs (TRASOPs) qualify. Beginning in 1983, the additional tax credits will be based on payroll n256 instead of capital investment. These may be called PAYSOPs.

2. CHRYSLER ESOP

The Chrysler ESOP plan illustrates how a company's need for financial assistance n257 can force the company to give its employees as ESOP plan that will give them, collectively, a substantial amount of stock over a relatively short period of time. In June 1981,

[*776] Chrysler employees received over $ 40,000,000 of Chrysler stock under the ESOP mandated by Congress. Each of the 94,000 employees (67,000 UAW members) received sixty-six shares, valued at $ 441, which are held in the ESOP trust. n258 The employer pays all expenses, except taxes, of plan and trust fund administration, including trustee fees permitted by *section 409A of the Internal Revenue Code*.

Every person who was a Chrysler employee with nine months of continuous service on the effective date, working in an employee group whose compensation and benefits were modified pursuant to the Chrysler Corporation Loan Guarantee Act of 1979, is a plan participant. The Chrysler ESOP n259 is administered by a trustee appointed by the Retirement Fund Review Committee of the Chrysler Corporation Board of Directors. Each plan participant can direct the trustee to vote the shares of stock allocated to the participant. Any shares for which the trustee is given no direction are to be voted in proportion to the shares for which directions are given. Thus, the full weight of employee voting strength is exercised, although the ESOP participants do not have a majority-rule bloc vote.

The Chrysler ESOP has a Plan Board consisting of two UAW representatives and two corporation representations. They establish rules of plan administration with respect to eligibility, participation and benefit amounts, construe plan language, determine plan policy with respect to such items, and receive financial reports covering plan operations. There is also an ESOP Plan Committee established by the corporate board of directors, which has complete authority to control and manage the operation of the plan except regarding the matters reserved to the Plan Board. The Plan Committee is to adopt any Plan Board policies established within the Plan Board's jurisdiction.

Each year the Plan Committee allocates equally among the participants the corporation's contribution, if any, to the trust fund plan. Thus, the employees draw equally, not proportionally, based on rates of pay. The plan provides that the employer shall contribute not less than $ 162,500,000 before the end of 1984 in installments of not less than $ 40,625,000 per year. After 1984, the Chrysler Board of Directors may terminate the plan. The board of directors may amend the plan at any time with written notice to the Plan Committee

[*777] and the trustee, but only if the purpose is to benefit the participants and beneficiaries. n260 Also, the corporation may not suspend, modify or change the plan prior to September 15, 1982 without first obtaining UAW concurrence. n261

Chrysler and the UAW further agreed in a letter of understanding attached to the plan n262 that: 1) where the members of the ESOP board are unable to resolve a matter within their power, the matter shall be referred to the Chrysler Vice President -- Employee and Industrial Relations Staff and the Director-Chrysler Department UAW, who shall agree upon a method of resolution; 2) a plan participant employee-stockholder shall not be prevented from attending an annual shareholder meeting of the corporation as an observer, but any absences from work for attending such meetings shall be treated as any other excused absence, requiring prior approvals based on operating efficiency needs and the employee's absence record; and 3) employee claims pursuant to the plan are to be processed pursuant to a special claim review procedure set forth in the Summary Plan Description and are not subject to the grievance procedure under any collective bargaining agreement between the parties.

Provided that Chrysler is still in existence in 1984, this plan could provide Chrysler employees with a significant voice in corporate decisionmaking, beyond whatever influence the appointment of UAW International President Douglas Fraser to the Chrysler Board may have. The ESOP will not have a majority interest in the corporation's stock in 1984, but will hold the largest bloc of corporate shares. The UAW estimates that at the end of the four-year period, the ESOP participants will own approximately fifteen percent of Chrysler's stock -- a rough calculation that will fluctuate based on stock prices and other Chrysler stock offerings. n263 That will make the ESOP participants collectively the single largest stockholder, since no other Chrysler stockholder holds five percent or more of Chrysler stock. n264 The next largest stockholder is the trustee of the Thrift Stock Ownership Program. n265

[*778] Thus, despite the fact that Chrysler does not have cumulative voting for board seats, n266 the UAW should be able to control more seats on the Chrysler board. Most Chrysler stockholders are individuals, not institutions. n267 Thus, in a proxy solicitation battle, the UAW might have as great an influence on the other stockholders as Chrysler management, although it should be noted that some ESOP participants and stock thrift plan stockholders are management employees.

3. PAN AMERICAN AIRLINES ESOPS AND BOARD SEATS

At Pan American World Airways (Pan Am), four of the five unions n268 that represent most of the company's hourly employees have agreed to a ten percent wage cut and a wage freeze through 1982 n269 in exchange for an agreement to create an ESOP. According to the agreement, the ESOP will give those employees between twelve to sixteen percent of Pan Am's stock during the first year of the agreement as well as the right to name one member of the board of directors. n270 Over a period of five to seven years, the ESOP participants may collectively acquire between twenty and thirty-five percent of the company's stock. n271 The unions believe this will lead to union control over four or five director positions n272 on a board of seventeen. The Pan Am union leaders interviewed did not believe the unions needed to control a majority of the board seats in order to achieve their goals of regaining the concessions made in the last collective bargaining agreement, increasing job security, and increasing their members' income by holding shares in a profitable company. The unions felt the company was being mismanaged financially

[*779] and sought to have a union watchdog on the board to ensure that economically unsound decisions would not be made. The unions believe that even one director, trusted and chosen by them for his competence, can serve the necessary function. n273

In a going concern, employee interests may be served well enough by having one or two representatives on the corporate board to serve as watchdogs over the other directors and ensure that the union always knows the company's financial actions. If the union feels the company has been mismanaged, it may be valuable to the membership to exchange some of its fixed financial benefits for a watchdog and the attendant job security, as was done at Pan Am. In a company that needs a more drastic overhaul in management because of a great risk of total business failure, however, it might be unwise for union members to settle for less than a majority interest in the company.

Regardless of the union's share of interest in the company, union representation on a corporate board through nonmajority stock ownership may add to job security. Unions are hardest hit by plant closings when they have short notice because they have little time to defend the rights of their members or to convince management to change its mind. First, board representation will, in most cases, ensure substantially more union notice of plant closing plans, potentially at a stage of the discussions when the employer might be open to alternative proposals. n274 Second, the union would know of critical investment decisions, such as the decision to close a marginally profitable plant or to disinvest in United States plants in order to invest in, or contract from, foreign plants. Employee stockholders might consider a stockholder derivative suit, n275 or the union might consider other types of action to bring pressure on the company to attain greater job security.

While it is too early to conclude that nonmajority worker or union representation on corporate boards definitely will provide more job security, reinvestment in the United States or humane introduction

[*780] of technology, it seems to be one of the few conceivable practical options for obtaining local control over corporations. In the Pan Am case, the unions are hopeful that their agreement will provide more job security. n276

III. LEGAL AND PRACTICAL ISSUES RAISED BY THESE EXPERIENCES

The involvement of unionized employees in the ownership, management or direction of corporations poses numerous legal questions. The legal issues raised fall into three categories: 1) potential conflicts of interest between the union's roles in representing employees as employees and in representing employees as owners on boards of directors; 2) union and employee concerns about protecting employee benefits on the one hand and obtaining more control over the employer on the other; and 3) government antitrust concerns.

These conflict of interest issues arise in many contexts. Nevertheless, a common theme connects and resolves most of these problems: employee-stockholders have employee rights when they act as employees and stockholder rights when they act as stockholders. A union may organize its stockholder members to aid them in acting collectively, but the union risks conflicts of interest when it becomes an institutional owner of a company for which it represents employees in collective bargaining. n277 Union representation on a corporate board of directors may occur by stockholder election, by corporate decision or through collective bargaining. Although the method of appointment may affect antitrust considerations, union representatives who sit on corporate boards must be aware of their legal obligations to the union, the government and the corporation regardless of their method of appointment.

A. Potential or Perceived Conflicts Of Interest Under the NLRA

1. "EMPLOYEE" STATUS UNDER LABOR LAW FOR EMPLOYEE-STOCKHOLDERS

The NLRB has considered, in a number of cases, whether employee-stockholders are "employees" under the National Labor Relations Act. n278 The Board determinations have depended on the procedural

[*781] status of the case, n279 the degree of control employee-stockholders have over the board of directors and corporate decisionmaking, n280 and whether there is preferential treatment of employee-stockholders conflicting with the interests of nonstockholding

[*782] employees. n281 The Board's basic rule is that an employee-stockholder is protected by the Act unless the employee-stockholder's interest gives him an "effective voice" in the formulation and determination of corporate policy. n282

There have been cases in which the Board has included employee-stockholders in bargaining units with nonstockholders, n283 has included employee-stockholders in units where all employees were stockholders, n284 has excluded from the bargaining unit employee-stockholders who were on the corporate board of directors, n285 has held that all employee-stockholders were nonemployees, n286 and has even included employee-stockholders serving on the board of directors in the bargaining unit. n287

Thus the Board has not automatically found employee-stockholders to be nonemployees under the Act in all situations in which there were both stockholder and nonstockholder employees. n288 However, when preferential treatment is accorded to stockholder employees, they must, at least, be in a separate bargaining unit from nonstockholder employees or they must be excluded totally from

[*783] the bargaining unit. n289 The Board's exclusion of stockholders from units including nonstockholders, especially where the stockholders received preferential treatment, logically follows the basic principle of bargaining units: they must represent a "community of interest." Significantly, none of these cases exclude employee-stockholders from protection of the Act in situations in which no conflict of interest would arise within the unit, i.e., where all employees are stockholders.

In Everett Plywood and Door Corp., n290 where all the employees were stockholders, the Board found employee-stockholders n291 to be employees within the meaning of the Act, despite the fact that each had "all the rights and privileges of a stockholder." n292 It is not clear what type of voting rights the employee-stockholders had, but since their structure was referred to as a "co-operative set-up" one could assume they had one vote per person. They also had a guaranteed wage and special rights to a hearing before the board of directors in the event of a discharge by the manager. The board of directors, not management, had ultimate discharge authority. Thus, Everett Plywood stands for the proposition that the Board's "effective voice in management" rule does not apply to 100% employee-owned firms. As the Board stated:

The mere fact that an employee also has the rights and privileges of a stockholder is not sufficient to debar him from availing himself, in his capacity as an employee, of the rights of employees to engage in concerted activities for the purposes of collective bargaining or other mutual aid or protection. . . . [S]tockholder employees not only have a proprietary interest in the employer-corporation, but also have an interest, at least as great, in their status as paid workers. n293

2. THE DUTY TO BARGAIN OVER EMPLOYEE RIGHTS IN STOCK PLANS

Although employees must receive voting stock in TRASOP

[*784] plans, n294 ESOP plans may give nonvoting stock. n295 It would be unreasonable for all unions, especially in potential buyout situations, to insist on TRASOPs instead of ESOPs since the quantity of stock that may be transferred through a TRASOP is much more limited than through an ESOP. n296 Regardless of the specific stock transfer arrangement, the voting structure will determine whether the employee stock will be maintained as a bloc, whether it will be individually owned, whether the democratic principle of one vote per person will prevail, and what role, if any, the union will play in organizing or directing the use of the vote.

The unions' experiences at South Bend Lathe, Vermont Asbestos Group and Rath Packing illustrate the importance of obtaining favorable voting arrangements in a stock plan at the tim the plan is initially created. n297 At South Bend Lathe n298 the employees did not obtain any significant voting rights during at least the first five years of the ESOP despite their ownership of 100% of the company's stock. At Chicago and North Western Transportation Company n299 and Vermont Asbestos Group, n300 the employees received stock as individuals, thus making it possible for the stock to be sold to a few major investors, and for employee control to be diluted. Rath Packing n301 provides the best example to date of a unionized ESOP in which the power of a bloc vote and democratic principles have been combined to maximize the use of employee stock ownership for the interests of present and future employees. Recent changes in the law n302 make further improvements in the Rath model possible. n303

In the case of South Bend Lathe, the employees' lack of voting rights led to a strike over a number of issues related to the employees' lack of voice in company decisions. Although the parties may

[*785] avoid direct joinder of this issue in their upcoming negotiations as well as in possible NLRB litigation, the South Bend Lathe situation poses the question of whether the subject of employee voting rights is a mandatory subject of bargaining.

What portions of employee stock plans are mandatory subjects of bargaining? In Richfield Oil Corp., n304 the Board held, and the District of Columbia Court of Appeals affirmed, that a voluntary employee stock purchase plan unilaterally announced by the employer "represent[ed] a mandatory subject of collective bargaining" n305 with regard to all the plan items that the union sought to negotiate. n306 The employer had maintained that the purpose of the plan was "to foster a closer and continuing association" between the employer and its employees n307 and to create an incentive for employees to invest in the company. n308 The employer then argued that such a program could not be subject to mandatory bargaining because to do so would be tantamount to requiring bargaining about ownership and control of the company, and could "result in the union's obtaining a seat on both sides of the bargaining table. . . ." n309 The Board and the court of appeals rejected this argument, finding that the employer's duty to bargain over the stock purchase plan arose from the plan's status as both deferred "wages" and as a "condition of employment." n310

Richfield Oil and similar cases n311 establish that all items in an ESOP or other employee stock plan concerning compensation or the accumulation of credits are mandatory subjects of bargaining.

[*786] Voting rights were not an issue in Richfield Oil. n312 However, dicta in Richfield Oil regarding other types of stockholder rights needs to be analyzed in light of today's bargaining situations. Although the union in Richfield Oil made no bargaining demands over these issues, the Board stated:

On the occasion of stockholder meetings, corporate elections, or any other matter in which only stockholders have the right to be heard, the union has no voice whatever as a statutory representative.

It by no means follows that the effect of our decision here is to require the Respondent to bargain with respect to its dividend, debt, and financial policies, simply because, as the dissenting opinion would have it, such matters are "relevant" to the establishment of a stock purchase plan. Indeed, these factors are no less relevant where a union seeks to bargain about higher wages, pension plans, or profit sharing plans, all of which have been held by this Board and by the courts to be subjects of mandatory collective bargaining. Yet, no one can seriously contend that those decisions have forced employers to bargain as to their dividend, debt, or financial policies. n313

The Board made these statements in response to claims by the respondent and the dissent that to allow union bargaining about the stock plan would permit the union "to interfere with matters solely within the province of management" n314 and to have "an inconsistent dual role" disallowed by the Board in Bausch & Lomb Optical Company. n315 The Board majority in Richfield Oil specifically distinguished the stock purchase plan therein from the union ownership arrangement in Bausch & Lomb, n316 stating "the Union would not, as a consequence of employees acquiring stock in the Respondent occupy a dual capacity as alleged by the Respondent." n317

The Richfield Oil stock plan was created for a much different purpose than many of the current stock plans discussed above which were created to save failing employers. n318 Since the Richfield

[*787] Oil stock plan was imposed unilaterally, the union clearly was not asked to take wage, benefit or other concessions in order to obtain the benefits of the stock plan. This is the crucial fact that distinguishes it from stock plans inaugurated to help capitalize and save a troubled company, such as Chrysler, or to effect a total purchase of the company by its employees to save their jobs, as in the cases of South Bend Lathe, Hyatt-Clark and Rath Packing. In each of these more recent plans, the quid pro quo for creation of the stock plan was an agreement to give up some already negotiated benefit. n319 In each of these cases, the stock plan concerned more than mere wages, and had a significant effect on the lives of the employees involved. Adoption of the plan usually meant agreeing to give up some of the financial security won through long union struggles and taking on some of the employer's entrepreneurial risk in order to save the company and their jobs. In each of these cases, the creation of the plan and its terms "vitally affected" the working conditions, indeed the continued existence, of the employees' employment.

In such cases, the union involved in negotiating the stock plan should not be limited to negotiation of only the financial and benefit computation aspects of the plan. At least in situations where the employees are forced by external economic circumstances to leap into entrepreneurial risk by agreeing to a stock plan in exchange for some previously negotiated pay or benefits, all aspects of the plan, including voting rights, must be mandatory subjects of bargaining. Otherwise, employees faced with the terrifying prospect of losing jobs in a failing economy are forced to be sitting ducks and easy prey for ESOP promoters. n320 Because of fear, disorganization and the need for speed in closing the deal when financing becomes available

[*788] in a plant buyout situation, it is not always possible for the parties to develop the best stock-ownership arrangements at the time a worker buyout or stock plan is created. However, such contingencies should not forever doom the employees to existence under an unfair plan, which they made possible by giving up some negotiated benefits.

The purposes of labor law are not served by preventing unions from demanding voting rights in stock plans to the point of impasse. The concept of management rights, protected by labor law, protects the interests of the equityholders or stockholders from undue interference from labor. However, the balance of legal equities shifts when the majority of stockholders are employees represented by the union. Employees, as majority stockholders, should be able to enjoy the rights and privileges of majority stockholders. If their trusted collective voice is their union, it should be treated no differently than any other proxyholder. Otherwise, as in the case of South Bend Lathe, a minority stockholder or stockholder's group, usually made up of management employees, can obtain exclusive control over the company. If they devise an ESOP that allows them to control the appointment of ESOT trustees they can control the votes of the union member employee-stockholders' shares and are not accountable to the majority of the stockholders.

Furthermore, in such a situation, the concept of management rights is not truly a protection of ownership or property rights. It is, in fact, a counterfeit argument aimed at giving managers rights in their capacity as managers that do not derive from property rights and thus are not legitimate for consideration in the balance struck by labor law between the rights of property and the rights to organize and bargain.

Finally, union negotiation for employees in obtaining rights to vote the stock they have acquired as compensation is not the same as a union seeking representation in its capacity as a union on both sides of the bargaining table. Bargaining to obtain the right for employees to vote their stock is not the same thing as voting it for them. n321

3. THE UNION'S DUAL ROLE AS BARGAINING AGENT AND COMPETITOR

The NLRB and the courts have considered cases in which employers

[*789] have refused to bargain with unions because of union ownership of stock in a competitor or loans made by a union-controlled pension fund to a competitor. Stock ownership by union members in their own employer, however, is legally distinguishable from stock ownership by the union or union pension fund in the employer or one of its competitors because their potential conflicts of interest differ.

In Bausch & Lomb Optical Co. and United Optical & Instrument Workers of America, Local 678, n322 the Board held that the employer did not violate section 8(a)(5) n323 of the NLRA by refusing to bargain with the union, with which it had an ongoing bargaining relationship, after the union set up an optical business in direct competition with it. Union memebership was a prerequisite to stock ownership in the new company, and the union admitted that it controlled the new company. The Board reasoned that the union might bargain in bad faith to improve its own company's position at the expense of Bausch & Lomb. Through excessive bargaining demands, strikes, hard bargaining and control over the relevant labor market, the union could increase Bausch & Lomb's labor costs or put it out of business. n324

In NLRB v. David Buttrick Co., n325 the First Circuit initially refused to enforce a section 8(a)(5) bargaining order against Buttrick on the basis of Buttrick's claim that the international union's pension fund had made a substantial loan to one of Buttrick's competitors, Whiting Milk Company, which gave the pension fund trustees control of Whiting Milk as collateral. The court remanded the case to the Board for further investigation of the possibility of intervention and asked the Board to promulgate guidelines. The Board originally had ordered bargaining because it found the connection between the fund and the local was not "definite and substantial" and thus the nature of the potential conflict was too speculative to disqualify the local. n326 Upon remand, the Board found no evidence that

[*790] Whiting Milk's financial condition was likely to cause any pressure to secure the loan, and that the international had limited powers over the local. Thus, the Board maintained its position, but declined to issue guidelines. The First Circuit endorsed the NLRB's second bargaining order emphasizing the "strong public policy favoring the free choice of a bargaining agent by employees." n327

The principles of Bausch & Lomb and Buttrick, n328 however, do not apply to a situation in which the employees own stock in their employer. Unlike unions that own a competing business or have union-controlled pension funds invested in a competing employer, individual union members who own stock in their own employer are in no sense competing with their employer. Accordingly, the conflicts of interest suggested in the above cited cases do not exist. They have even more reason to keep their employer afloat and competitive in the market than they may have had as mere employees. As employee-stockholders, they may depend on their employer's success not only for their jobs, but often to protect their lifesavings and, in some cases, their pensions. In those circumstances, the union is no more sitting on both sides of the bargaining table than the employer is sitting in the union meetings. Although the adversary lines may blur as employer and employee interests in the company's survival merge, nothing in labor law policy frowns upon such an arrangement so long as the conflicts of interest that could exist within a bargaining unit of stockholder and nonstockholder employees n329 are not present, and so long as the union's fiduciary and representational duties are not compromised. n330

Since employee-owned firms are not necessarily managed in a democratic fashion, unionized workers may still need a union even though they have obtained some ownership interest in a firm. Ownership is not necessarily control. Whoever runs the company, individual employees still need a union's protection from unfair action. Everett Plywood confirms that an employee's status as a stockholder does not per se bar her from exercising rights as an employee

[*791] under the NLRA. n331

4. EMPLOYER DOMINATION OF THE UNION

Employer domination of the union in violation of section 8(a)(2) of the NLRA, n332 and union interference with the employer's right to select its representation for collective bargaining or adjustment of grievances prohibited by NLRA section 8(b)(1)(B) n333 are two similar potential problems arising from union representation on corporate boards. n334 There are a number of cases that address the issue of employer domination of a union in violation of NLRA section 8(a)(2), where union representatives sit on an institution's board of trustees or directors and the union also represents the institution's employees. These cases have arisen primarily at health care institutions connected to, or serving, a substantial number of patients under union health and welfare plans. n335

The NLRB has declined to provide precise guidelines n336 for determining when such a conflict of interest exists. On a case-by-case basis, it has developed review criteria. There is still debate over whether there must be some evidence that union-employer-trustees have actually abused their influence over the union, interfering with the union's ability to single-mindedly represent the employees, or whether the mere potential for such abuse, if great enough, violates section 8(a)(2).

In cases where the majority of an institution's board of trustees or directors were officers, agents, members or retired members of a union that also represented the institution's employees, n337 the Board has held that there was a conflict of interest in violation of NLRA section 8(a)(2). In most of these cases, n338 the institution also received the majority of its revenue from a union health care plan or

[*792] union members. n339 The Board found that the union's domination of the institution's board and the union's substantial interest in the clinic's prosperity created dual roles in collective bargaining. n340 The interrelationship of powers, interests and temptations constituted conflicts of interest creating a "proximate danger of infection of the bargaining process." n341 In determining whether there is such a "proximate danger," the Board and the courts consider the amount of influence the union representatives have on the corporate board, the amount of control the union has over the people who actually bargain for the employees and the amount of temptation the situation gives the union to exert such control. n342

[*793] Thus, the Board has found an actual conflict of interest in violation of section 8(a)(2) where a high-ranking union official was the employer's collective bargaining representative who actually sat on the opposite side of the table from a union staff person representing the employees. n343 In one such case, the hearing officer suggested that the conflict could be remedied by a change in employer negotiators, n344 but the Board did not agree. n345

In Anchorage Community Hospital, n346 however, the NLRB found the Teamsters should not be disqualified as the hospital employees' exclusive bargaining agent even though Teamster officials and representatives comprised seven of the fifteen member hospital board of trustees. Two additional board members were also affiliated with the Teamsters, as the administrator and the officer of a Teamsters employer health and welfare trust fund. Thus, the Teamsters were one seat short of a majority, or actually comprised a majority if the latter two individuals from the trust fund were counted. Four of the Teamsters-affiliated people sat on the hospital's five member executive committee. The Teamsters also had made a ten million dollar construction loan to the hospital. Ten percent of the hospital's gross revenue came from medical services purchased by the Teamsters-Employees Trust Fund. n347 In this case, the NLRB established the principle that minority representation on an employer's board of trustees and executive committee does not establish a conflict of interest absent evidence to indicate "abuse [of] that role." n348 Thus, minority union representation on a corporate board is likely to be held to a standard of actual abuse, rather than potential abuse.

Union representatives elected to a corporate board by employee stockholders, whether they constitute a majority or minority of the board are distinguishable from clinic and hospital trustees, who are usually appointed. n349 Whereas clinic and hospital trustees may be appointed by an international union, which can have great power over a local, a corporate board member, elected by the stockholder constituency over which he presides, is more directly accountable

[*794] to that stockholder constituency, whether local or national, than is an international appointee. Therefore, the "control" aspect of the above-stated test is not as great a problem. Further, an employee-stockholder representative may have more factors balancing against the "temptation" to consider the employer's benefit over the employees' than an international appointee. Usually he is an employee who must live with the conditions he helps create. Secondly, since he is elected to the board position, he has a constituency to please or he can be unseated. However, an elected employee-stockholder may be less sophisticated about potential conflicts of interest than a union-appointee.

In UMWA Welfare and Retirement Fund, n350 the NLRB indicated that an NLRB election might resolve a conflict evidenced by employer financial assistance to the local union, which the employer had voluntarily recognized as its employees' collective bargaining representative based on a union-run vote. Although a union-appointed representative sat on the employer's board, the NLRB found no section 8(a)(2) violation on that basis because the union did not have majority control of the board.

Finally, in addition to the question of union representation on employer boards, it is possible that the company may cooperate more with the union as it establishes a voice in the company, perhaps providing meeting facilities or allowing meetings on company time. There are a series of section 8(a)(2) cases in which the courts of appeals and the NLRB have found that labor-management cooperation does not constitute illegal section 8(a)(2) domination, although the Board and the courts have not agreed in all cases. n351

[*795] 5. UNION COERCION OF THE EMPLOYER'S CHOICE OF BARGAINING REPRESENTATIVE

Mere cooperation between the parties is also unlikely to create a violation of NLRB section 8(b)(1)(B), which prohibits union interference with an employer in selecting its bargaining representative. Conceivably, a stockholder or a board of directors fight over the employer's choice of bargaining representatives led by either union stockholders or board members could result in such a charge. However, a section 8(b)(1)(B) violation usually requires some sort of threat or coercive act.

Although not directly on point, NLRB v. Amax Coal n352 is a recent illustrative case including section 8(b)(1)(B) charges. In Amax Coal, a union struck to induce an employer to join a multiemployer national trust fund for employee pension and welfare benefits. Amax filed section 8(b)(1)(B) charges claiming that the management-appointed trustee of the national trust fund was a "collective bargaining representative" whose appointment the union had no right to try to influence. The United States Supreme Court held that the management-appointed trustee was not a collective bargaining representative because the trust fund was an employee benefit plan. The trustee's function was to hold the plan assets for the sole benefit of the employee beneficiaries and the trustee was not to serve in the adversary role of a collective bargaining representative. Thus, the union did not violate section 8(b)(1)(B).

Just as the Court in Amax Coal looked to the underlying purpose of the trust fund and the proper role of a trustee, a court should distinguish between a union qua union, using its typical weapons such as strikes or job actions to obtain a change in employer bargaining representatives, and a group of stockholders or directors using their corporate powers to seek a change in management personnel or policy. The use of corporate powers to change management direction is well within the proper authority of board or stockholder

[*796] action. n353

B. Potential Fair Representation Problems for Unions with Employee-Stockholder Members

The duty of fair representation is a judicially created doctrine emanating from the principle that a union, which has been given exclusive bargaining recognition by law, must treat all unit employees in a manner that is not arbitrary, capricious, discriminatory or in bad faith. n354 The cases provide a union more latitude in negotiating contract language than in administering contracts, however, because in contract negotiations the union necessarily must trade off the interests of some members to obtain the greatest good for the greatest number. n355 Few recorded duty of fair representation cases concern employee stock plans, although there are numerous ways a union might be exposed to such liability. This article is limited to some of the concerns that have already been raised.

In Bodecker v. Local Union No. P-46, n356 Rath Packing employees, brought suit against the union and the employer pursuant to section 301 of the NLRA, as amended, n357 and the Iowa Wage and Hour Law. The employees claimed that by amending the collective bargaining agreement to establish stock acquisition and profit sharing plans founded by payroll deferrals, the union acquiesced in allowing the employer to withhold or defer wages owed to the employees under the collective bargaining agreement. The Eighth Circuit Court of Appeals upheld the district court's denial of plaintiffs' motions for preliminary and permanent injunctions and its findings that: 1) the district court was without jurisdiction to issue an injunction under the Norris-LaGuardia Act n358 because the plaintiffs' claim involved a labor dispute; 2) the union and its president had not breached any duty of fair representation owed the plaintiffs since all changes in negotiated benefits had been bargained collectively by the union and ratified by the union membership following the procedures provided in the union constitution and bylaws; 3) compliance with the Iowa statute was not required because wage or benefit deferrals were made pursuant to a valid collective bargaining agreement; and 4) even if the Iowa statute applied, it was preempted

[*797] by federal law. n359

The Hyatt-Clark ESOP n360 has produced several duty of fair representation concerns. First, the local union's request to the international union for a five million dollar loan raised fairness and fiduciary questions concerning the international union's allocation of its resources. n361 If it provided one local union a capital loan to aid them in a plant buyout, would it then be liable to provide such loans to any local union that made such a request? One such loan could become the basis for fair representation claims by other local unions that were denied such loans. However, if an international union developed a policy that set objective criteria for providing such loans to its locals, or if it devised a limited revolving loan fund available on a first-come, first-serve basis to local unions fitting designated criteria, it could meet its fiduciary obligations to the membership at large while providing a useful service to those local unions where both the circumstances and initiative exist for making a realistic attempt at employee ownership.

Second, in order to obtain funds for a feasibility study, the Local 736 leadership at Hyatt-Clark originally asked the membership to tax themselves as union members an assessment of thirty-five dollars each to pay for the study. n362 This proposal was defeated. A committee of UAW members and management employees then was formed to raise funds for the feasibility study. They sought a $ 100 contribution per member. Union members were induced to join this committee and pay the $ 100 by a promise of preferential hiring status and, implicitly, higher seniority in the ESOP company than those who did not contribute. n363

A group of UAW Local 736 members filed a duty of fair representation suit, claiming that the local leadership's effort to create the ESOP after the local officially had decided not to tax members to pay for the study, was a breach of their obligation to carry out the will of the members. n364 This case seems unlikely to succeed because: 1) no grievance was filed; 2) no internal union redress was sought; 3) apparently no union funds were diverted to the ESOP company; and 4) under successorship principles, the new company may negotiate

[*798] a new collective bargaining agreement, and thus new seniority provisions, with a union with which it has a duty to bargain. This case, however, raises questions about the propriety of a union allowing its members to alter their seniority by paying money. The strength of the successorship clause with the original employer and the timing of negotiations on altered seniority could be key factors in a plaintiff's case under similar circumstances. n365

In Baker v. Amsted Industries, Inc., n366 several South Bend Lathe employees sued Amsted for breach of contract and the union for violating its duty of fair representation when the union did not bring suit against Amsted to recover pension payments due after Amsted's July 3, 1975 sale of its South Bend Lathe Division to SBL, Inc. The Amsted collective bargaining agreement ran from October 1974 through October 1977. SBL hired all union-represented employees, including the four plaintiffs, and adopted most of the Amsted collective bargaining agreement provisions except for the pension provisions, which it unilaterally replaced with the ESOP. The union negotiated with both employers to no avail and then sued both to compel tripartite arbitration of the pension matter. The district court denied the request to compel tripartite arbitration, but granted the union leave to reinstate proceedings against Amsted Industries, Inc., in the event that Amsted failed to arbitrate bilaterally. n367 Thereafter, the union sued only SBL, Inc., choosing to wait until the outcome of that litigation before suing Amsted again, on the theory that if it won all pension benefits due since the date of sale from SBL, Amsted would have no liability. Amsted had previously agreed to pay any benefits due to pension eligible employees and retirees as of the date of sale. Thus, the plaintiffs' suit was a challenge to the union's litigation strategy.

The Seventh Circuit Court of Appeals in Baker found the union's litigation strategy reasonable and affirmed the lower court's decision that the union had not breached its duty of fair representation. The court stated:

Even if the union's litigation strategy were subsequently determined to be misconceived, it would be excessively intrusive into Union decision-making for the courts to decide, in the absence of bad faith or egregious conduct, whether the Union has pursued the tactics most appropriate to

[*799] the aggrieved employees' needs. n368

Finally, in a recent duty of fair representation case, a union was held liable for an employer pension default because an international union representative sat on the pension plan board of trustees. n369 A union has also been held liable in a wrongful death suit where the collective bargaining agreement stated that the union was fully responsible for the enforcement of certain occupational safety provisions. n370 In both cases, the court's rationale was that the union had assumed an oversight or enforcement role that made it responsible for injury to employees. Although to date no case has arisen in an employee stock plan situation, union counsel have expressed concern that a union might be liable for the total investment lost by members who have invested their savings, pensions, wage or benefit concessions in a stock plan or other purchase scheme on the advice of the union staff. n371

Employees faced with a closing plant are generally desperately trying to save their jobs, and are often willing to try almost anything to do so. They seek advice, technical assistance and often money from the union. n372 Care must be exercised in any stock plan situation, especially in a buyout, so that a union does not become a guarantor of the business proposition involved. A union may give its members the information and assistance they seek, but needs to protect itself from making any guarantees about the feasibility of a project. Employees who may invest their savings in their failing employer must know the risks involved and take responsibility for those risks themselves. Without becoming an insurer of the plan, perhaps by means of specific disclaimers, union research and legal

[*800] staff may be the best resources available to a local union in finding qualified professionals to provide a feasibility study and other assistance.

C. Potential Conflicts of Interest under the Landrum-Griffin Act and the Antitrust Laws for Union Officers or Agents on Corporate Boards of Directors

Unlike the above-mentioned NLRA and duty of fair representation issues, which do not present major obstacles to employee-ownership schemes, the Landrum-Griffin Act and the antitrust laws contain some specific requirements that must be met to ensure the legality of a plan. At any unionized company where the parties are considering employee ownership, they must consider the following potential conflicts of interest and design the employee-ownership plan accordingly.

1. LANDRUM-GRIFFIN ACT

a. Payments to union officers

Sections 302(a) and (b) of the Taft-Hartley Act, n373 as amended by section 505 of the Labor-Management Reporting and Disclosure Act of 1959 (L.M.R.D.A., also known as the Landrum-Griffin Act), n374 make it unlawful for an employer to pay an money or other thing of value to any labor organization or officer that represents any of that employer's employees, and for any person to receive any such payment. Thus, a union officer or agent who might be appointed or elected to serve on a corporate board should not accept any payment of fees normally paid to corporate directors.

In its letter of opinion to the United Auto Workers (UAW) concerning the possible appointment of a union member or representative to the American Motors Corporation (AMC) Board of Directors, the Department of Labor stated that: 1) section 302 did not apply to any director fees, since the UAW and AMC had agreed that neither the union director nor the union would receive the normal fees paid to directors; n375 and 2) it would not be improper "for AMC to pay necessary expenses, such as hotel accommodations, incurred by the UAW member in his or her capacity as a member of the board

[*801] of directors." n376

b. Investing union money in employer stock

Section 501(a) of L.M.R.D.A. n377 provides that officers, agents and representatives of a labor organization hold positions of trust as fiduciaries in relation to the union and its members. This duty requires that such officers and agents hold, manage, invest and expend the money and property of the union solely for its benefit in accordance with its constitution, bylaws and resolutions. Such officers and agents must neither hold nor acquire any pecuniary or personal interest that conflicts with the interests of the union. They also must provide an accounting for any profits they receive in any capacity connected with transactions conducted by them or under their direction on the union's behalf. n378

Section 501 may present a problem for a union that seeks to invest union funds in an employer's stock. n379 This problem might be overcome by a carefully worded union resolution n380 and an arm's-length union-employer transaction that is commercially sound. In general, it is probably best for the employees to invest their own funds instead of using union funds, even if the stock purchase is through a payroll checkoff.

c. Holding of employer stock by union officers and agents

L.M.R.D.A. section 501 fiduciary obligations may also present problems for union officers and agents who wish to hold employer stock. In addition, some union constitutions prohibit or place limits on the holding of stock by union officers or staff. n381 Such limitations

[*802] must be considered, and/or the union constitutions must be amended before a stock--ownership plan is adopted. n382

At Rath Packing Company, the union circumvented the section 501 fiduciary problem with the following provision: "All members of the Board of Trustees are required to be participants in the ESOP. However, no officer, employee, agent or representative of any union is eligible to serve as a member of the Board of Trustees." n383 The trustees of the ESOT hold the actual title and voting rights to all the employees' stock held in the plan. The fact that no union officers actually hold this financial interest in the company avoids any section 501 problems. Furthermore, union officers at Rath may and do serve on the corporate board of directors n384 since their personal stock ownership is only part of their regular compensation under the terms of the collective bargaining agreement that established the ESOP. n385

d. Reporting requirements

L.M.R.D.A. section 202(a)(1) n386 requires every officer and employee of a union to report annually any stock held or any income derived from any employer whose employees his labor organization represents beyond normal compensation for his work as an employee of the employer. n387 Section 203(a) requires every employee of a labor organization. n388 Depending on the profitability of the company and the plan arrangements, stock dividends may be considered only remuneration for work and thus outside the reporting requirement. However, it is worthwhile to check with the Department of Labor to determine what reports will be required for a particular plan.

L.M.R.D.A. section 202(a)(5) requires every union officer and employee to report each fiscal year "any direct or indirect business

[*803] transaction or arrangement between him . . . and any employer whose employees his organization represents." n389 In the UAW-AMC case, the Department of Labor determined that "it is possible that the arrangement by which a UAW member is elected to and serves on the Board of Directors could be construed as a 'business arrangement' under this section. Therefore, as a precautionary measure, the union officer should file such a report." n390

2. ANTITRUST IMPLICATIONS

Union representation on boards of competing firms in the same industry raises antitrust issues. The concern is that union representives on boards of competing firms would have both the motivation and the opportunity to engage in price fixing, n391 contrary to the purposes of the Sherman n392 and Clayton n393 Antitrust Acts. n394 However, one commentator who raises this concern notes that "illegality would only attach to a labor union interlock if an actual conspiracy in restraint of trade could be proven under the Sherman Act or Federal Trade Commission Act." n395 He further concludes that section 8 n396 of the Clayton Act does not prohibit many kinds of "indirect interlocks" between corporations so long as one individual is

[*804] not a director of two competing corporations. n397

Section 6 of the Clayton Act n398 might exempt union representatives on corporate boards from antitrust law coverage. Section 6 provides, in part: "Nothing contained in the antitrust laws shall be construed to forbid the existence and operation of labor, agricultural, and horticultural organizations . . . or to forbid or restrain individual members of such organizations from lawfully carrying out the legitimate objects thereof. . . ." In the context of union representation on corporate boards, however, no court has yet decided whether interlocking directorates are "legitimate objects" of labor organizations, n399 thus exempting them from antitrust coverage.

The Federal Trade Commission and the United States Department of Justice-Antitrust Division recently considered these issues in advisory opinions rendered to the UAW concerning an agreement with AMC. During their 1980 contract negotiations, the UAW and AMC agreed that AMC would nominate a UAW member, other than

[*805] UAW President Douglas Fraser, who has served on Chrysler's board, to serve on its board contingent upon determinations of "legal acceptability" to the Federal Trade Commission, the Department of Justice and the Department of Labor.

In its opinion letter, the Federal Trade Commission (FTC) n400 stated the issues presented to it as follows:

It appears that Chrysler and AMC are competitors, that they satisfy the size requirement contained in section 8, and they engage in interstate commerce. Thus, some elements of a violation are present, and the law would be violated if the same person were a director of both companies and if no exemption from the antitrust laws were applicable. This letter, therefore, focuses on the issue of whether the UAW is a "person" within the meaning of section 8 and, if so, whether it would be a "director" of AMC and Chrysler in the circumstances described . . . and . . . whether the labor feature of the arrangement renders section 8 inapplicable. n401

The FTC concluded that the proposed UAW representative on the AMC board would not give rise to a violation of section 8:

[W]e do not believe section 8 was intended to reach interlocking directorates formed through "representatives" of a common labor union. Such a construction of section 8 would extend its reach beyond the situations, which Congress intended to be per se unlawful and might preclude particular labor-management relationships which may not present the risk of competitive harm at which section 8 was aimed. Consequently, we do not believe that section 8 should be construed to make unlawful the type of labor-management experiment at issue here.

Further, the UAW has made clear . . . that it intends that the director on the AMC board will function independently and will refrain from sharing confidential commercial information with other union officials, including the UAW director of the Chrysler board. The proposed arrangement arises in the novel context of worker involvement in the affairs of corporate management with expressed aims that do not raise section 8 concerns. On these facts . . . we do not believe a "representative" relationship for the purpose of section 8 is present. n402

The Department of Justice-Antitrust Division, however, refused to issue a "no action" letter. n403 Adhering to the government's position that a "corporation or association" can be a "person" within the meaning of section 8, the Antitrust Division determined

[*806] that a union might also be such a person. In considering "the question of whether a 'corporation or association' is on the board of two companies," the Antitrust Division stated:

[This question] is normally a factual issue, in part turning upon the existence and strength of any interest the third party corporation or association might have in the operation of either or both of the competing companies, and the nature of the relationship between the individual directors and the third party corporation or association. It may be . . . in a given case . . . shown that the directors in question are acting purely as individuals. On the other hand, it may be that the third party has such an interest in the activities of the competing companies, and has such control over the individual directors, that they should be considered to be serving not merely as individuals, but as representatives of that third party. The legality of the UAW's proposal thus depends on the resolution of a factual question: will it be in fact the UAW that sits on the boards of both AMC and Chrysler? n404

Although the Antitrust Division refused to determine whether the UAW member would be sitting on the AMC board in a basically representative as opposed to individual capacity, the Antitrust Division analyzed the facts of the case at length. The Antitrust Division emphasized two facts as raising potential problems: 1) that the union demanded and gained the agreement to nominate a UAW member to the AMC board in collective bargaining negotiations; and 2) that the UAW may have an interest in influencing the commercial and financial affairs of the major automakers, although this

[*807] interest was seen as "only indirect." n405 The Antitrust Division ultimately refused to issue the "no action" letter stating:

We are unable to conclude on the present record that the antitrust questions raised by your proposal have been resolved -- the uncertainties inherent in this case are too numerous and too important, particularly in view of the origin, indefinite duration and possibly changing nature of the proposed relationship. n406

The Antitrust Division's reasoning focused heavily on the fact that the UAW had sought its position on the AMC board through collective bargaining. One resolution of this issue would be to obtain employee or union representation on a corporate board through voting of employee stock rather than through collective bargaining. A union member employee-stockholder, elected to a corporate board would be in a much better position to claim her board status as an individual stockholder than would a board member who obtained her seat purely as a result of a bargaining demand. A union member appointed to a board without negotiation also cannot be labelled as one who attained the position as a result of bargaining. Furthermore, an ESOP elected board representative would most likely fall outside the category of union "director," thereby avoiding the problem of "direct interlock" and serving as a union "representative" in the opinion of the FTC and the Antitrust Division.

An ESOP in a unionized shop can provide a useful means of creating a de facto union voting bloc of employee-stockholders without running afoul of antitrust laws. For example, although the employee-stockholders at Rath Packing Company vote their ESOP shares in a bloc, n407 any union representative who serves on the board

[*808] is actually elected by the stockholders. This independent, nonrepresentative status of a board member, who is also a union member employee-stockholder, could create control questions for a union involved in creation of the plan. These are not easily solved. At Rath, the union, when it negotiated the ESOP, retained a number of veto powers over changes in the plan n408 and over new nominees to the Rath Board of Directors. n409

No legal challenge to this arrangement has been made. Since it is the local rather than the international union that is consulted, there is no direct link with any other corporation board over which the international union might have influcence. Furthermore, the United Food and Commercial Workers International Union has no officer on the board of directors of any competing company with which it negotiates. n410 Also, the local union's veto power over nominees to the board is apparently temporary, existing only until the employees have a stock majority. n411 The essence of the agreement is that the union, which negotiated the employee buyout of the corporation, is acting as a guardian of members' interests as employee-stockholders until they can exercise full majority powers. The employee-stockholders' financial commitment and the union's posture distinguish this case from that of a union acting solely as a collective bargaining agent.

Although the previously mentioned antitrust problems are speculative since there is no judicial precedent and the potential conflict of interest is only indirect, union members who serve on corporate boards of competing firms should not be individuals who have an opportunity and reason to meet on a regular basis within the union. If such representatives live in different cities or occupy union positions at different organizational levels, the government does not have as strong an argument that an opportunity to collude illegally exists.

Finally, if a union were charged with antitrust violations after

[*809] obtaining board seats or a worker buyout at a failing company, it may have a defense. The "failing business doctrine" is a judicially created doctrine n412 which has been used primarily as a defense to antitrust charges in merger cases under section 7 of the Clayton Act. Under this doctrine, acquisition of a company by another does not substantially lessen competition within the meaning of section 7 of the Clayton Act n413 if the following conditions are met: 1) the company's resources are depleted with such little prospect of rehabilitation that the company faces a probable business failure; and 2) there are no other prospective purchasers. n414 The failing business doctrine only applies where the party claiming the defense establishes that the company acquiring the failing company is "the only available purchaser." n415

Although apparently no cases have applied this doctrine to a Clayton Act section 8 case concerning interlocking directorates, the doctrine could be utilized by a union as a defense to a section 8 claim where it obtained one or more directors on the board of a failing corporation. The United States Supreme Court has noted the harmful effects of plant closure on the community in accepting the failing business doctrine defense to other alleged violations of the Clayton Act. n416

D. Protecting Existing Employee Benefits

1. SECURITIES REGULATIONS PROVIDE USEFUL INFORMATION AND SAFEGUARDS

There are a number of phases in the establishment and operation of an ESOP that are likely to have substantial securities laws n417

[*810] implications. These include: 1) the sale and purchase of the employer's stock by the ESOT trustee; 2) the accrual of employees' interests in the securities held in the trust; 3) the distribution of the securities to employees and beneficiaries under the terms of the plan and trust; 4) use of the plan by the employer to "go private" or to defeat a tender offer to maintain control of the firm; and 5) resale of the securities after distribution. n418 The intricacies and ramifications of each type of transaction are beyond the scope of this article. n419 A few issues are highlighted here as they relate to collectively bargained plans.

It is well established that contribution of stock to an ESOT is exempt from the registration requirement of the 1933 Securities Act on the basis that it is not a "sale," but rather is a "bonus" where: 1) the plan is qualified under *I.R.C. section 401*; 2) no employee will be required or permitted to contribute any cash consideration for his stock; and 3) no participant in the plan will have the choice of receiving cash in lieu of stock. n420 In these circumstances, the SEC has issued "no action" letters on the theory that such contributions did not involve a "sale" or "offer to sell" within the meaning of section 2(3) of the Act. These shares are not considered to have been bargained for or given to employees "for value" specifically received. When a plan is installed as a result of collective bargaining, however, it is arguable that the shares are being acquired "for value"

[*811] and that an offering has been made. n421 Similarly, if the plan permits or requires employee contributions to purchase company stock, the plan has some element of investment discretion on the part of employees and acquisition of stock by the plan will involve a "sale" or offer to sell within the meaning of section 2(3). n422

Where an employer issues or sells stock to its own employees or their own ESOT, the employer might seek an exemption from registration on the basis that the sale is a "private placement" and not an "offer of sale." This was the position taken by the company in SEC v. Ralston Purina n423 when it offered to sell unregistered treasury stock to certain of its key employees, including an artist, bake shop foreman, clerical assistant, electrician, stock clerk, product trainee, stenographer and veterinarian. n424 The United States Supreme Court found that these employees did not have access to the kind of information that registration would disclose, n425 and thus held that the transaction was not exempt because the employees needed the Act's protection.

There are a variety of circumstances and types of exemptions under which a company might seek to avoid registration requirements upon offering stock to employees through an ESOP. Avoidance of the expense of registration may look quite reasonable when the purpose of adopting the plan is to strengthen a faltering company. However, for the long-range protection of the workers and the union, the disclosure required by registration and the issuance of a prospectus to the employees asked to participate in the ESOP may prove quite valuable. Furthermore, the union may avoid future duty of fair representation liability by securing for union members the type of information outsiders receive before making such investment decisions, and by ensuring that each union member receives a systematic explanation of the risks involved in the plan. Since the company registering the stock will prepare the registration forms and the prospectus, the union involved in negotiating a plan that will be registered may wish to retain some right of review over the prospectus language to ensure that it will be understandable to the members.

[*812] 2. PROTECTING THE PENSION PLAN

ESOPs have been used to eliminate pension plans, n426 but they need not be designed that way. In some cases, employees lost benefits that could have become vested had the pension plan changes been fully understood and negotiated. n427 In a number of situations, employees were told that the only way to save their jobs was to give up their pension plan. n428

Employees need not necessarily give up a pension plan in order to provide necessary capital for the buyout. Where there is an existing pension plan, an ESOP can be created in addition to the pension plan, or the existing pension plan can be converted into an ESOP. A leveraged ESOP may be used to borrow money. Also, the employees can regularly buy stock by payroll deduction, as they do at Rath Packing. n429

A tax-qualified pension plan can be converted into an ESOP in some cases. The possible consequences of a conversion are: 1) the pension plan assets can be invested in an employer's securities with substantially higher returns than the general ERISA limit of ten percent; n430 and 2) the employer can avoid the vesting of employee rights not yet vested under the prior plan. n431 If the prior tax-qualified pension plan is terminated, as defined by *I.R.C. section 411(d)(3)*, the rights of all affected employees to covered, funded benefits accrued become vested. n432 Any qualified defined-benefit pension plan that is amended or converted to become a defined-contribution plan, such as an ESOP, is treated as terminated under ERISA. n433

Upon termination of a covered plan, the Pension Benefit Guarantee Corporation (PBGC) becomes involved. If the plan is not fully funded, PBGC may place a lien on up to thirty percent of the company's assets to meet the plan's obligations to beneficiaries. n434

[*813] Furthermore, an ESOP is an investment in the stock of one employer. Because the return is never certain, it is an unsuitable replacement for diversified pension investments or defined benefits. Thus, any contemplation n435 of termination or conversion of a pension plan to enable creation of an ESOP requires extremely careful consideration of these far-reaching consequences. It is best to avoid such termination or conversion if at all possible. n436

[*814] IV. CONCLUSIONS: SOME STRATEGIES, MECHANISMS AND LESSONS

The case histories and legal questions discussed above, while not exhaustive of the potential issues raised by employee ownership, illustrate many of the concerns that have manifested to date. Employee ownership of businesses through the mechanisms available in the United States, is certainly not the final answer to plant closings caused by capital flight, foreign competition and increased energy prices. Much broader legislative solutions are needed to increase employment and stabilize industrial working conditions.

This article does not attempt to present or analyze such legislation. Furthermore, political conditions in recent times have not been conducive to obtaining such legislation. In an increasing number of situations, therefore, unions and workers may have to consider immediately available, imperfect and perhaps temporary employee-ownership mechanisms. Some positive uses of existing employee-ownership options are summarized below.

A. Partial Ownership: Stock as an Employee Benefit

In collective bargaining, either the company or the union might consider stock transfer as part of the employee benefit package. n437 If the stock transfer is arranged through an ESOP or TRASOP, there are considerable tax and financial advantages for the employer. n438 The ESOP or TRASOP may be designed as a profit sharing plan, or

[*815] in addition to one. n439 ESOPs and TRASOPs also may create another form of deferred retirement income for the workers. Employer contributions to an ESOP or TRASOP are not taxable to the employee until they are distributed, either when the employee terminates employment or when the plan terminates. Upon distribution, the employee can keep the stock, sell it or "roll over" the distribution into a retirement annuity. n440 Furthermore, dividends may be passed

[*816] through to employee-stockholders, although any stock dividends are usually reinvested in the ESOP or TRASOP.

B. New Bargaining Options and Legal Responsibilities

A union acting as a collective bargaining representative is legally limited regarding the subjects about which it can require an employer to bargain n441 under the National Labor Relations Act. Employee-stockholders, however, have the right to raise any issue of concern at a stockholders meeting, provided proper notice is given and securities regulations are obeyed. n442

Union organization of voting trusts of voting blocs of employee-stockholders can become a powerful tool in developing worker control,

[*817] and in changing management policies and managers. A separate sister organization to the union, such as an ESOP trust controlled by the participant employees, can be extremely useful. It can be the employees' voice on management issues without directly involving the union in bargaining nonmandatory subjects. n443 Regardless of where the NLRB and the courts finally place the line of demarcation between mandatory and nonmandatory bargaining subjects in ESOPs, the employee trust is not bound, in its stockholder status, by those limitations.

A stock trust that does not allow union officers or agents to serve as trustees, such as the Rath ESOT, avoids problems arising under section 302 of the Taft-Hartley Act and sections 505 and 501 of the Landrum-Griffin Act. These provisions concern the control union officers have over the stock and finances of a firm with which they bargain. An employee-controlled ESOT could also avoid antitrust problems. n444

Finally, if a union needs to amend its constitution and bylaws to allow its members, officers or agents to serve on corporate boards, it should consider adding language to its code of ethical practices to provide that union representatives on corporate boards will not engage in any anticompetitive practices prohibited by the antitrust laws, and will keep corporate pricing, marketing, financing and design matters confidential. The ethical code also could define some of the union representatives' obligations as corporate board members.

Once on the board, an employee-stockholder may entirely lose her roots and become overwhelmed by management thinking. These accusations were made at Vermont Asbestos Group. n445 However, unions could go a long way in preventing that type of problem by educating union members who sit on corporate boards regarding the skills needed to be an active board member and the expectation that union representatives will maintain union principles. A number of European trade unions provide such training programs for workers who are board representatives. n446

[*818] C. Timing is Key to Obtaining Voting Rights and Democratic Structures

Unlike collective bargaining agreements, which usually expire in a one to three year period, an employee stock plan may form the financial basis of a new perpetual corporation. The voting structures and classes of stock created by the new corporation may affect the existence or lack of democracy within that corporation for the foreseeable future. Once the corporate voting structure is in place, it is very difficult to change it if some but not all stockholders are unhappy with it.

The best time to implement a structure that maximizes employee voting rights or any union control is in the beginning. Initially, an employer is probably attracted to an ESOP for the tax advantages it offers. Employee voting rights will probably have the least impact in the early stages of the plan when there is little employee or ESOT equity. The employer may need to install the ESOP to obtain leveraged financing or to assemble a financial package within a tight time frame. When the employer needs the union's agreement to install the ESOP, the union has the greatest economic leverage over the format of the plan. The union at South Bend Lathe agreed to an ESOP requiring it to give up its pension plan because of time pressures involved in obtaining necessary financing. However, the SBL management promoting the plan faced the same financing time pressure. At that point, the union had the leverage to threaten to kill the project if the plan did not reflect their proposed changes. Although at that time they had no alternate structure to propose, since then union knowledge of such plans has become more advanced. At Rath Packing, UFCW Local 46 was able to obtain a democratic structure by proposing a plan to management and by creating a public relations situation that required a fast response. The union's plan was adopted. n447

D. The Co-operative ESOP: A Flexible, Democratic Combination

A co-operative ESOP is a newly emerging, hybrid method of employee ownership that merges the democratic structure of a co-operative with the financing advantages and flexibility of an ESOP. A co-operative ESOP can be created in a regular stock company. The employee stock is held in an ESOT trust that is organized on co-operative principles. Equity may accrue to each employee

[*819] equally or according to his work, pay or seniority. Each employee has one vote in the ESOT, and the trustees vote the ESOT stock as a majority-determined bloc in corporate shareholder meetings.

During the 1970's and 1980's, co-operative and worker ESOP companies have struggled with the limitations of both co-operatives and ESOPs. The co-operative form has the advantage of being democratic; its primary principle is "one vote per person." However, the plywood co-operatives n448 illustrate the problem created when each co-operative member owns only one share of stock. If the company is successful, the stock appreciates in value to a price at which it is impossible for most young employees to purchase a share from a retiring employee. Thus, young employees are hired as nonshareholders, and retirees may be forced to sell their stock to nonemployees to recover their equity upon retirement.

This problem can be resolved by separating voting rights and equity accumulation. The Industrial Co-operative Association n449 model, based upon the Mondragon Co-operative System in Spain, n450 provides for separate equity accounts for each member. Over the years, members obtain dividends based upon the amount in their internal accounts. New members buy their interest in the co-operative over a period of years, and retiring members are paid their equity over a number of years. Thus, the new member need not have the capital to purchase the full share of the retiree, the co-operative need not come up with the cash to purchase the retiring employee's full share all at once, and new and old members have equal votes.

Finding financing for a co-operative is not easy. n451 Until recently, it has been extremely difficult to own a portion of a company cooperatively. Generally, a company must be set up as an individual proprietorship, a partnership, a stock company or a co-operative. n452

Often when a group of employees might like to buy out their employer, the employer is a stock company. The employees may not have the capital, or may be otherwise unable to obtain 100% of the stock. Yet, they may have the funds to purchase a controlling interest,

[*820] collectively, immediately or over time. Creation of an ESOP trust (ESOT) enables employees to do just that. They can purchase stock in a company and hold it collectively. They need not purchase the entire company immediately, but can create a plan whereby, over time, the ESOT will hold a controlling interest.

The chief problems with ESOPs for the creation of democratically controlled companies have been: 1) the law does not require that ESOP stock rights be passed through; n453 2) ESOP stock need not be allocated equally to all employees and is often distributed on the basis of pay; n454 3) even when stock is allocated equally to all employees monthly, if voting rights go with each share, new employees have less voting power than older employees; and 4) until recently, the law required the ESOP to begin distribution n455 of an employee's shares to her within five years of termination of employment. An employee also had the option of taking cash instead of stock. n456 As a result, ESOPs had to retain huge cash reserves to purchase total distributions from terminating employees in order to prevent dilution of active employees' voting strength.

[*821] The first three problems create inequality which can be divisive. n457 They can, however, be resolved by proper draftsmanship of the plan. The fourth problem, the distribution requirement, made it potentially impossible for a majority employee-owned ESOP to retain its voting majority in trust or in the hands of active employees. However, a recent change in *I.R.C. section 409A(h)* has eliminated that problem for predominantly employee-owned ESOP companies, allowing them to maintain their employee-owned status by giving departing employees cash instead of stock. n458 Such an ESOP need not wait for the employee to exercise a put option, but can instead expect to purchase the stock of all departing employees. Thus, the ESOT of a co-operative ESOP can plan distributions over a period of time and use democratic structures modeled on Mondragon or other such co-operatives. There are a few existing examples of co-operative ESOPs. n459

Although co-operatives have some tax advantages, n460 ESOPs are generally considered to be more flexible financing mechanisms, because they enable an employer to borrow capital without paying tax on either interest or principal.

ESOP financing requires no cash outlay by the employees. The corporation and the trust insulate the workers against personal risk in case the loan cannot be repaid. Unlike a co-operative, the ESOP protects the worker from being taxed on the shares received through the ESOP, at least until the employee leaves the company; the tax laws treat the stock held for a worker by an ESOP trust as non-taxable deferred compensation, a major saving to the worker. n461

[*822] A co-operative ESOP can be designed with the financing flexibility of an ESOP and the democratic features of a co-operative. n462

E. Practical Considerations for Potential Employee Owners

Employee ownership can be used to save jobs at a particular plant or company. Sometimes the ownership scheme is designed to or has the effect of undercutting a master collective bargaining agreement with the company or in the industry. n463 In some industries, a small or single plant company can be economically viable, in others it may not.

Unions should consider the following factors in evaluating a buyout proposal, especially regarding multiplant, multinational corporations:

1) Does this proposal undercut or maintain industry agreements? If it modifies some standards in exchange for more worker or union control over management and investment decisions, are these new controls positive models that can be used to enhance worker or union control at other locations, or to further other union goals?

2) Who made the proposal and why? Is the company trying to unload a totally unsalvageable division or to create a captive supplier outside of the master agreement? Is there useful life in the plant to produce for an existing or realistic potential market and to provide a livelihood for the workers without undercutting union brothers and sisters? Does the proposal provide for retention of existing equipment, marketing, sales and other professional staff, suppliers and customers, or is the seller planning to remove these?

If the company has proposed ESOPing several of its plants, the union might propose ESOPing the whole profitable multinational company. The ensuing negotiations would likely shed light on the

[*823] market conditions and reasons behind the initial proposal and could lead to a new mechanism to control capital flight.

3) Can a plan be created with local government cooperation to provide more industrial production jobs in the area while increasing employee and community control or influence over the employer's decisions about location, relocation and use of other local business as sources of supply? A coordinated local plan may help overcome the inexperience and lack of marketing, financial and management skills that might otherwise plague a new employee-owned company. Such planning might also provide a depressed area with more marketable product lines and a greater chance of success. n464

In larger corporations where buying out the company is unrealistic, unions and union members may benefit from obtaining some voting stock. Stockholder meetings or possibly lawsuits may provide an interim forum in the fight against capital flight until legislative solutions are obtained.

No claim is made here that ESOPs provide a panacea, nor that they are the primary answer to plant closings. They are flexible mechanisms which unions and workers should understand and be able to analyze, use or fight with sophistication.

Legal Topics:

For related research and practice materials, see the following legal topics:
Business & Corporate LawCorporationsFinanceInitial Capitalization & Stock SubscriptionsClasses of StockPensions & Benefits LawEmployee Benefit PlansEmployee Stock Ownership PlansPensions & Benefits LawEmployee Retirement Income Security Act (ERISA)Prohibited TransactionsEmployer Securities

FOOTNOTES:

n1 An Employee Stock Ownership Plan (ESOP) is defined in *I.R.C. § 4975(e)(7)* (1976 & Supp. IV 1980). It is an Internal Revenue Service (IRS) -qualified stock bonus or stock purchase plan, pursuant to *I.R.C. § 401(a)* (1976 & Supp. IV 1980), designed to encourage employers to give or sell stock to their employees through a trust (called an ESOT) in exchange for tax advantages. ESOP qualifications and limitations on contributions are defined in the Internal Revenue Code (IRC) regulations (Regs.) and in the Employee Retirement Income Security Act of 1974 (ERISA), *29 U.S.C. § 1001* (1976). Employer contributions to the ESOP are completely tax deductible if the contribution does not exceed 15% of the compensation paid to participants in a stock bonus plan each year, or 25% of such compensation where there is both a stock bonus plan and a money purchase plan or a separate pension plan. *I.R.C. § 404(a)(3)(A)*, (a)(7) (1976). The employer pays no social security or FICA tax on stock contributed to a qualified ESOP on a payroll deduction plan. *I.R.C. §§ 501(a)*, *3401(a)(12)* (1976 & Supp. IV 1980). For other employer tax advantages, see infra note 4. Many plans that are called ESOPs are really only stock bonus plans pursuant to *I.R.C. § 401(a)* (Supp. IV 1980), fashioned as ESOPs. Statutory ESOPs, which must meet the additional requirements of *I.R.C. § 4975(e)(7)* (1976 & Supp. IV 1980), usually are established only by parties who wish to take advantage of the leveraging features discussed infra note 4, the right to use a money purchase pension plan along with a stock bonus plan, or the higher tax-free contribution limits

available pursuant to *I.R.C. § 415(c)(6)* (1976 & Supp. IV 1980). R. Ludwig, Speech to the ESOP Association of America Conference entitled New Legislative and Regulatory Developments Affecting ESOPs (Oct. 14, 1982).

The employees, or their beneficiaries, actually receive their vested stock from the ESOT upon termination of employment. Through an ESOP, an employee may acquire stock without payment or at a lower than market price. The employee pays income tax only on employee contributions for the stock, not necessarily on its market value. If she pays nothing for the stock there is no tax on it until it is distribute. *I.R.C. §§ 401(a)*, *402(e)*, *501(a)* (1976 & Supp. IV 1980). Upon distribution there are tax advantages available to the employee as well. See infra note 440 for more details.

ESOPs are exempt from several important ERISA protections: 1) ESOP funds are invested "primarily" in employer securities, and thus are exempt from the 10% limitation rule on investment of pension funds in employer securities, E.R.I.S.A. § 407(a), (b)(1), (d)(3)(A), *29 U.S.C. § 1107*(a), (b)(1), (d)(3)(A) (1976); 2) an ESOP is not subject to the funding requirements of a pension plan, *I.R.C. § 412(h)* (1976); and 3) an ESOP, as a defined contribution plan, is not covered by Pension Benefit Guarantee Corporation (PBGC) insurance, E.R.I.S.A. §§ 4021(a), (b)(1), 4022, *29 U.S.C. §§ 1321*(a), (b)(1), 1322 (1976 & Supp. IV 1980). See Ludwig, Conversion of Existing Plans to Employee Stock Ownership Plans, *26 AM. U.L. REV. 632, 643 nn.62, 63 (1977).*

An employer can use an ESOP to obtain investment capital, create a market for his stock, cash out and pass on the company to his employees or hand-picked successor, limit pension obligations or convert a pension plan to an ESOP. See R. FRISCH, ESOP FOR THE 80's (1982) [hereinafter cited as R. FRISCH, ESOP]; R. FRISCH, THE MAGIC OF ESOT: THE FABULOUS NEW INSTRUMENT OF CORPORATE FINANCE (1975) [hereinafter cited as R. FRISCH, THE MAGIC OF ESOT]; R. FRISCH, THE TRIUMPH OF ESOP (1977) [hereinafter cited as R. FRISCH, TRIUMPH]; J. MENKE, HOW TO ANALYZE, DESIGN AND INSTALL AN ESOP (1981). See infra note 4 for other employer uses of ESOPs.

A union can use an ESOP to set up a worker-owned and worker-controlled company, see infra text accompanying notes 125-60, or to obtain more information and greater control over a company in which its members do not own a majority of stock. See infra text accompanying notes 240-76, 437-40.

n2 A TRASOP is a type of ESOP created by the Tax Reduction Act of 1975, Pub. L. No. 94-12, § 301(d), 89 Stat. 26 (1975), *26 U.S.C. §§ 46,* 48, and the Tax Reform Act of 1976, Pub. L. No. 94-455, 90 Stat. 1525 (1976). Thus is is called a "TRA"SOP. It is also known as a "tax credit employee stock-ownership plan," defined in *I.R.C. §§ 401(a)*, *409A(a)* (1976 & Supp. IV 1980). An ESOP must meet additional qualifications to be a TRASOP. *I.R.C. § 409A(a)(3)* (Supp. IV 1980). A single company may have either an ESOP or a TRASOP, or both.

Congress designed TRASOPs to induce employers to try ESOPs as a type of employee benefit plan. Initially, the incentive was the right for the employer to claim up to an additional 1.5% investment tax credit by making contributions to a qualified TRASOP. Employer contributions to a qualified TRASOP automatically allow an employer to increase her invest-

ment tax credit from 10% to 11%. The other .5% is allowed if it is matched by employee voluntary contributions to the TRASOP. *I.R.C. § 48(n)* (Supp. IV 1980). Starting in 1983, TRASOPs will be based on payroll instead of investment tax credits. The tax credit allowed to an employer based on its contribution to the tax credit employee stock ownership plan will then be no more than .5% of covered payroll. For 1985, 1986 and 1987, it will be .75% of covered payroll. Economic Recovery Tax Act of 1981 (ERTA) § 331, *26 U.S.C. § 44G,* 95 Stat. 290 (1981). These may be called PAYSOPs. See infra note 256.

One of the most significant additional requirements for a TRASOP is that, unlike a regular ESOP, it must provide for pass through of voting rights to employee participants. This means that may employee participant may instruct the plan on how to vote the securities allocated to his account. *I.R.C. § 409A(e)*, (1) (Supp. IV 1980). See infra note 15. A TRASOP may not be used for leverage financing, although an ESOP may be used in this manner. See infra note 4.

n3 A producer co-operative is a company that is wholly owned, except for any mortgage rights that lenders own, by the people who work in it. A membership share in a co-operative represents the same type of rights as a share of stock with the following variations: 1) a co-operative share cannot be sold except by a departing member to a new member or back to the co-operative; and 2) each member holds only one voting share, although equity interests of members may differ based on accumulation is individual capital accounts. In contrast, in a stock corporation voting is based on one vote per share of voting stock on whatever matters that class of stock has power to vote.

A co-operative may be set up within the shell of a for-profit stock corporation or as a non-profit, nonstock corporation. However, one must obtain 100% ownership or agreement with 100% of the owners to restructure an existing for-profit stock corporation into a co-operative. D. Ellerman, What is a Worker's Cooperative? (1979) (available from Industrial Cooperative Association, Cambridge, Mass.).

There are at least several thousand worker co-operatives in the United States, although most have fewer than 10 employees. These small co-operatives usually are involved in labor intensive retail areas. However, there are many "industrial" co-operatives with several hundred employees. The best known are the plywood co-operatives in the northwestern United States. See infra text accompanying notes 211-39.

The two predominant models of worker co-operatives in the United States are the "Rochdale" model and the "Mondragon" model. The "Mondragon" model is the only one that separates membership rights from equity rights by means of separate internal accounts. See infra text accompanying notes 211-39 for more details. See also C. ROSEN, EMPLOYEE OWNERSHIP: ISSUES, RESOURCES & LEGISLATION, A HANDBOOK FOR EMPLOYEES AND PUBLIC OFFICIALS 14-15 (1981).

n4 There are many advantages to an employer, in addition to those described in supra note 1. First, an employer can use an ESOP to borrow money and then can repay the loan with untaxed (called pretax) dollars. For example, the ESOT borrows the money from the bank, and the employer guarantees the loan, using stock issued to the ESOT as collateral. The ESOT uses the loan money to buy the employer's stock (the collateral). The employer than repays

the loan by annually contributing to the ESOT the payments owed to the bank. Those contributions to the ESOT are tax free. As the loan is repaid, the stock is released by the bank and is allocated to the accounts of the employees in the ESOP plan. This is called a leveraged ESOP. See R. FRISCH, ESOP, supra note 1, at 13, 14, 37-42, 213, for more detail. Diagram of a leveraged ESOP:

[See Illustration in Original]

Furthermore, if the employer uses the original tax savings to buy depreciable capital equipment, she can obtain a second tax write-off from the use of that loan money. Under a TRASOP, additional investment tax credits are available. See supra note 2 for more details. J. MENKE, supra note 1, at 2001, provides a tax-planning checklist that details uses of ESOTs with the following entries:

Provide an in-house market for the purchase of stock from a controlling stockholder. Repurchase stock owned by minority shareholders, inactive shareholders and outside shareholders. Obtain new financing so that both interest and principal will be paid with tax deductible dollars. Refinance existing debt so that the repayment is made with pre-tax dollars. Reduce corporate taxes and increase cash flow and working capital. Achieve some liquidity at capital gains rates for major stockholders of a public company. Facilitate financing of the acquisition of another company. Create liquidity for the owners of a closely held corporation as an alternative to a merger with a public company. Facilitate divestiture of a private company which had been acquired by a public company. Make a tender offer either to buy company stock selling at an abnormally low price or to reduce the chance of a takeover attempt. Enable a public company to "go private." Provide an employee incentive plan. Coordinate a company's goals with the estate planning objectives of the principal stockholders. Obtain a refund of corporate income taxes by creating a tax loss carryback.

Increased productivity may be another benefit to an employer who uses an ESOP. C. ROSEN, supra note 3, at 12, states:

Employee Ownership has grown rapidly in the past several years. Almost unknown in the early 1970s, there are now perhaps 5,000 employee ownership plans, with two to three million participants. In addition, at least 250 companies of 10 employees or more are majority employee owned. In part, this growth has been in response to a series of federal tax laws giving special incentives to employee ownership; in part it has also been a response to the success employee ownership has demonstrated. In one major study, . . . firms with employee ownership plans were found to be 1.5 times as profitable as comparable conventional firms. Moreover, the more equity employees owned the greater the profitability ratio became.

A. TANNENBAUM & M. CONTE, EMPLOYEE OWNERSHIP: REPORT TO THE ECONOMIC DEVELOPMENT ADMINISTRATION (1977) is a study of 98 employee-owned firms, 30 of which supplied the researchers with data about profit. Of the 98, 68 were firms in which employees owned at least 50% of the equity. In 20 firms, nonmanagerial employees owned at least 50% of the equity, either directly or through an employee stock ownership trust. They found the following:

The thirty firms in our sample for which data about profit are available do show a higher level of profit than do similar conventional firms in their industry, although it is not possible

to assert on the basis of this comparison that employee owned firms in general are more profitable than conventional firms, since the firms in our sample may be select with respect to profit.

Id. at 2. In other words, those who provided profit data may have been the more profitable ones. Of these 30 companies, the single most important correlate of profitability among the aspects of ownership measured was the percentage of the company's equity owned by nonmanagerial employees. The greater this percentage, the greater the profitability of the firm. Id. at 3.

Others contend, however, that it is the amount of employee control, not employee ownership, that stimulates greater productivity and distinguishes the successful from the unsuccessful employee-owned firms. O'Toole, The Uneven Record of Employee Ownership, HARV. BUS. REV. Nov.-Dec. 1979, at 185. Furthermore, THE UNITED STATES COMPTROLLER GENERAL, REPORT TO THE COMMITTEE ON FINANCE U.S. SENATE, EMPLOYEE STOCI OWNERSHIP PLANS: WHO BENEFITS MOST IN CLOSELY HELD COMPANIES? 39-42 (1980) [hereinafter cited as GAO STUDY] found that available independent studies on motivation and productivity were inconclusive as to whether the plans improved employee morale or increased productivity.

n5 However, Congress explicitly required creation of an ESOP as a condition of the Chrysler loan guarantee. Chrysler Corporation Loan Guarantee Act of 1979, *15 U.S.C. §§ 1861*-1875 (Supp. IV 1980).

n6 GAO STUDY, supra note 4, at 3.

n7 See supra notes 1, 4.

n8 See infra notes 439-40 and accompanying text.

n9 Some cases discussed in this article did not involve failing companies, as in the Ford and General Motors TRASOP plans. Others, such as Ford-Sheffield, have not adopted such plans at all.

n10 A union-economist and a city policy analyst suggested employee ownership as a cornerstone for the reindustrialization of Detroit. Their plan emphasized the social value of job security and employee control of working conditions, while looking to local government to organize and direct multiparty planning functions. D. LURIA & J. RUSSELL, RATIONAL REINDUSTRIALIZATION: AN ECONOMIC DEVELOPMENT AGENDA FOR DETROIT (1981).

n11 Employee-owned companies are certainly not immune to the economic forces that cause business failures. In fact, their unconventionality itself often causes problems in obtaining financing and in devising satisfactory management organization. Such firms, how-

ever, may have the added advantage of increased employee concern and productivity where the employees have a substantial voice in running the company. O'Toole, supra note 4, at 185.

n12 B. BLUESTONE, B. HARRISON & L. BAKER, CORPORATE FLIGHT, THE CAUSES AND CONSEQUENCES OF ECONOMIC DISLOCATION (1981).

n13 Id. at 57-61.

n14 See infra text accompanying notes 437-64, 112-17, 141-60.

n15 In a TRASOP the stock must be voting stock and the voting rights in trust securities must pass through to the participants. *I.R.C. § 409A(e)*, (1) (Supp. IV 1980). The stock contributed to an ESOP in a publicly traded company must be common stock that is readily tradeable on an established securities market. *I.R.C. §§ 4975(e)(7)*, (8), 409A(1) (Supp. IV 1980). This is usually voting stock. ESOPs in publicly traded companies must pass through any voting rights in all contributed employer securities. *I.R.C. § 409A(e)* (Supp. IV 1980). An ESOP in a closely held firm, where more than 10% of the plan's total assets are invested in employer securities, must pass through voting rights to ESOP participants on major corporate issues upon which the corporate charter or state law requires approval by a majority of shareholders. *I.R.C. § 409A(e)(3)* (Supp. IV 1980). Thus some state laws might not prohibit the use of nonvoting stock or disproportionate voting rights in closely held ESOP firms. J. MENKE, supra note 1, at 4335-36.

Most publicly traded firms pass through full voting rights in ESOP stock, while many privately or closely held ESOPs do not. R. FRISCH, ESOP, supra note 1, at 196-97. Moreover, many so called "ESOPs" are not statutory ESOPs, but are only stock bonus plans organized similarly to ESOPs, but without following the voting rights strictures of *I.R.C. §§ 4975(e)(7)*, (8), 409A (Supp. IV 1980). R. Ludgwig speech, supra note 1.

n16 See infra text accompanying notes 141-60, 437-64. Even 100% employee ownership may not guarantee employee control. See infra text accompanying notes 112-17.

n17 In contrast, a union acting as a collective bargining representative is legally limited as to the subjects about which it can require an employer to bargain under the National Labor Relations Act. See infra text accompanying notes 240-76, 27-43, 161-210, 448-62.

n18 See J. RIFKIN & R. BARBER, THE NORTH WILL RISE AGAIN: PENSION, POLITICS AND POWER IN THE 1980s (1978). That attitude is changing in the pension area as unions are demanding more information about and involvement in decisions about pension investment. See INDUSTRIAL UNION DEPARTMENT, AFL-CIO, PENSIONS: A STUDY OF BENEFIT FUND POLICIES (1980).

n19 Letter from International UAW Associate General Counsel Leonard R. Page to Deborah Groban Olson (Sept. 21, 1981) [hereinafter cited as Page letter].

n20 D. ZWERDLING, WORKPLACE DEMOCRACY 173 (1980) states:

Many union leaders fear that workers and their union could be weakened if they owned their own enterprise.

"Ownership?" [International Association of Machinists, IAM, AFL-CIO President William] Winpisinger asks. "I view that as a catastrophe." For one thing, Winpisinger and other labor leaders say, owning a company puts workers and unions in the same bind as serving on a corporate board. They'll lose their identity. "Pretty soon you'll get workers managing workers, and then you'll have management managing the workers all over again," as Winpisinger envisions it.

Furthermore, some labor leaders argue, by giving workers ownership of an enterprise, they'll develop a competitive ownership mentality: instead of joining together in union brotherhood (and sisterhood) they'll start squabbling over the profits.
Zwerdling also states that union leaders are concerned that if a company cannot make a plant profitable, neither can a union. He says experience generally has not borne out that concern. Id. at 173-74.

In a speech at the University of Michigan, Ann Arbor, Aug. 1, 1981, James Smith, Assistant to the President and Research Director, United Steelworkers of America, AFL-CIO, CLC, expressed a concern that workers may know how to run a factory, but not an enterprise. But see D. LURIA & J. RUSSELL supra note 10 (entrepreneurial help may be available if local management joins in the buyout or if local government develops an industrial planning and technical assistance structure).

n21 Telephone interviews with John Mancuso, Assistant to the Director of Packing-house Division, United Food and Commercial Workers International Union, AFL-CIO (UFCW) (Feb. 18, 1982; April 6, 1982) [hereinafter cited as Mancuso interview]; letter from John Mancuso to Deborah Groban Olson (May 7, 1982).

n22 United Auto Workers (UAW) President Fraser sits on the Board of Directors of Chrysler Corporation. However, when the Canadian UAW member Chrysler workers struck in November 1982, UAW President Fraser temporarily suspended his attendance at Chrysler board meetings and involvement in board deliberations until the collective bargaining disputes between the UAW and Chrysler in both the United States and Canada are resolved to avoid any appearance of conflict of interest. N.Y. Times, Nov. 8, 1982, at 1, col. 5. Pan American World Airways has agreed to allow four of the unions with which it bargains collectively to name one board member. Vermont Asbestos Group and Rath Packing have union members on their corporate boards. See infra text accompanying notes 211-39, 47-83, 125-61.

n23 An employer may give or sell stock to employees under other stock-bonus or stock-

-purchase plans but if they are not ESOP or TRASOP plans qualified under *I.R.C. §§ 4975(e)(7)* or *409A* (1976 & Supp. IV 1980), they will not receive all the favorable tax treatment mentioned in supra notes 1, 2, 4. Such plans may be qualified for other tax purposes under *I.R.C. § 401* (1976 & Supp. IV 1980).

n24 See supra note 3.

n25 A trust set up under Taft-Hartley § 302 and L.M.R.D.A. § 505, *29 U.S.C. § 186* (1976) can also hold stock perpetually for employees and pay out retirement benefits. Under this type of trust, the employer and employees administering the fund must be represented equally, and a neutral person must resolve conflicts. If the trust is established to provide pass through of stock voting rights to participants, the influence of the employer representatives' presence on the board could be minimized.

n26 A co-operative ESOP is an ESOP in which the employee stock-ownership trust (ESOT) is organized as a co-operative, and accordingly the voting rights are separated from the equity value of stock accumulating in members' accounts. The stock remains within the trust. Departing members receive cash, not stock, upon leaving. New members buy one low cost share of voting stock upon hire or after a probationary period. They then accumulate nonvoting stock credits over their worklives with the company. All employees are members of the trust and have only one vote.

There are still few co-operative ESOPs because an ESOP was required to give all members the option of taking their distribution in stock instead of cash union terminating employment until the Economic Recovery Tax Act (ERTA) of 1981, Pub. L. No. 97-34, 95 Stat. 172, *26 U.S.C. § 1* made changes in *I.R.C. § 409A(h)* (made applicable to ESOPs by *I.R.C. § 4975(e)(7)* (Supp. IV 1980)), quoted infra at note 139. Now a predominantly employee-owned ESOP can retain its employee-owned status by giving departing employees cash instead of stock. *I.R.C. § 409A(h)(2)*, as amended by ERTA. For more details, see infra notes 448-62 and accompanying text.

n27 Telephone interviews with Associate General Counsel of Chicago and North Western Transportation Company, George Hollander (May 21, 1981; June 29, 1982) [hereinafter cited as Hollander interviews].

n28 Interview with Gerald Rupert, Vice-Chairman of Chicago and North Western Transportation Company General Committee, Brotherhood of Locomotive Engineers (July 15, 1981) [hereinafter cited as Rupert interview].

n29 Id.

n30 Chicago and North Western Transportation Company, Offering Circular of Security by Transportation Company (May 5, 1972) [hereinafter cited as CNWTC Offering Circular].

n31 Hollander interviews, supra note 27. The parent company, Northwest Industries, was subject to regulation because of the railroad operation, whereas its competitors in the nonrailroad industries were unregulated.

n32 CNWTC Offering Circular, supra note 30, at 1.

n33 Hollander interviews, supra note 27.

n34 Id.

n35 Id.

n36 Id.; Rupert interview, supra note 28.

n37 Rupert interview, supra note 28.

n38 Id.

n39 Id.

n40 Hollander interviews, supra note 27; CNWTC Offering Circular, supra note 30, at 35-36.

n41 Hollander interviews, supra note 27; CNWTC Offering Circular, supra note 30, at 35-36.

n42 Id.

n43 Rupert interview, supra note 28.

n44 Interview with Monte Mason, President, Local 338, Cement, Lime, Gypsum and Allied Workers International Union, AFL-CIO (Aug. 23, 1981) [hereinafter cited as Mason interview]; letter from Monte Mason to Deborah Groban Olson (April 17, 1982); telephone interview with Monte Mason (Nov. 22, 1982).

n45 Interview with John Deak, President, Local 1722, United Steelworkers of America, AFL-CIO, CLC (July 14, 1981) [hereinafter cited as Deak interview].

n46 Interview with Lawrence Despault, former President, Local 338, Cement, Lime, Gypsum and Allied Workers International Union, AFL-CIO (Aug. 24, 1981) [hereinafter cited as Despault interview].

n47 D. ZWERDLING, supra note 20, at 53-55.

n48 Id.

n49 Id.

n50 Masson interview, supra note 44.

n51 D. ZWERDLING, supra note 20, at 53-55.

n52 Id. at 56-57.

n53 Id. at 56.

n54 Id.; Mason interview, supra note 44.

n55 Mason interview, supra note 44.

n56 D. ZWERDLING, supra note 20, at 56-57.

n57 Originally, the VAG Board of Directors had six out of 15 directors who were union members. Later the board membership decreased to only nine members. Mason interview, supra note 44. As of February 21, 1982, there were two hourly employees, i.e., union members, on the nine member board. Telephone interview with Maurice Eldred, VAG board member, who has been an hourly employee at the mine for 33 years and who was formerly a union committeeman for five years (Feb. 21, 1982) [hereinafter cited as Eldred interview]; letter from Maurice Eldred to Deborah Groban Olson (April 19, 1982).

n58 Mason interview, supra note 44.

n59 Id.

n60 Id.

n61 Id.

n62 The wage increase in the 1976-78 union contract was 75 per hour in the first year and 50 per hour in the second year. Mason interview, supra note 44. D. ZWERDLING, supra note 20, at 57, states that the wage and benefit increases in the first year were 19.4%.

n63 For 15 months after the sale from GAF to VAG, no lost-time accidents occurred in the mine. In 1979, there was a lost-time accident and there have been many since then. Mason interview, supra note 44. "Under VAG the men worked harder and safer." Despault interview, supra note 46.

n64 Mason interview, supra note 44.

n65 Id. However, there was a layoff of all but 11 or 12 employees from January 1 to June 1, 1982, then a reopening of the mine with 175 employees until November 12, 1982 when a new indefinite layoff began due to lack of sales. The employees expect to be recalled in the spring of 1983.

n66 Id.

n67 Howard Manosh holds approximately 429 out of the 1362 outstanding shares of VAG stock and has sufficient support among a group of stockholders to control the corporation. Eldred interview, supra note 57.

n68 Despault interview, supra note 46. However, former VAG board member, John Lupien, states that VAG stock was once appraised at $ 3500 per share. Telephone interview with John Lupien, former GAF maintenance supervisor and first Chairman of the VAG Board of Directors (Feb. 22, 1982) [hereinafter cited as Lupien interview].

n69 In the summer of 1977, some board members proposed using company profits to build a subsidiary wallboard company using asbestos waste produced by the mine. D. ZWERDLING, supra note 20, at 59-60; Despault interview, supra note 46; Mason interview, supra note 44. Many of the stockholders felt that corporate reserves would be needed for major expenses in the mine. Others felt that some of the reserves should be used to pay higher wages to the miners. D. ZWERDLING, supra note 20, at 60. The August 1977 stockholders meeting voted down the proposed investment, unless at least 50% of the financing could be obtained from outside sources. Id.; Despault interview, supra note 46. The board ignored this directive from the stockholders and built the plant, Vermont Industrial Products (VIP), with 100% financing from VAG. D. ZWERDLING, supra note 20, at 61. One of the board members, John Lupien, contends that the board did not defy the stockholders because VIP received 80% financing from Vermont Industrial Development Authority and thus was not 100% financed by VAG profits. Lupien interview, supra note 68.

n70 D. ZWERDLING, supra note 20, at 59-62; Despault interview, supra note 46.

n71 Despault interview, supra note 46; Mason interview, supra note 44.

n72 Monte Mason called the stockholders meeting the "straw that broke the camel's back." Mason interview supra note 44.

n73 VAG was organized to save jobs, not because of a philosophical desire for workers' control. The lenders were particularly concerned that management decisions not be made by the stockholders on the shop floor. The former management remained and today still controls management decisions and withholds from employee-stockholders most of the managerial and financial information usually kept from employees, such as salaries of officers and expense account uses. D. ZWERDLING, supra note 20, at 58-59.

n74 Despault interview, supra note 46.

n75 Id.

n76 Id. However, union member and board member, Maurice Eldred, stated that the board never asked him what the union's bottom line was, and that he has been able to state the union's case to the board on grievance matters, causing them to be settled in the union's favor. Eldred interview, supra note 57.

n77 Despault interview, supra note 46. Maurice Eldred said that when he was elected to the board of directors, the union asked him to resign from the union grievance and bargaining committee. The company asked him to get out of his union bargaining duties. Eldred interview, supra note 57.

n78 Despault interview, supra note 46; Mason interview, supra note 44.

n79 Despault interview, supra note 46.

n80 John Lupien supported the idea of creating an ESOP at VAG to maintain employee control of the company. Lupien interview, supra note 68.

n81 See infra text accompanying notes 125-60.

n82 See supra text accompanying notes 1-81; see infra text accompanying notes 83-276, 437-64.

n83 Brief in Support of Plaintiff Union's Motion for Summary Judgment Against Defendant South Bend Lathe, Inc. at 1-4, United Steelworkers of America v. South Bend Lathe, Inc., No. H-76-115 (N.D. Ind. filed Apr. 30, 1976) [hereinafter cited as Brief of USWA]. Amsted Industries, Inc. is referred to as Amsted throughout this article.

n84 Hearings to Learn About Employee Stock Ownership Plans at Employee Owned Companies Which Would Otherwise Have Closed: Hearings on H.R. 2203, Before the Subcommittee on Economic Stabilization of Committee on Banking, Finance and Urban Affairs, U.S. House of Representatives, 96th Cong., 1st Sess. (1979) (statement of Richard Boulis, Chairman and President of South Bend Lathe, Inc.).

n85 SBL has been importing some of its product from Korea. Deak interview, supra note 45.

n86 Brief of USWA, supra note 83, at 3-4; deposition of John S. Deak taken on Sept. 29, 1976 in United Steelworkers of American v. South Bend Lathe, Inc. at 16-23, No. H-76-115 (N.D. Ind. filed April 30, 1976) [hereinafter cited as Deak deposition]; Deak interview, supra note 45.

n87 South Bend Lathe lost "$ 427,000 in 1970, $ 977,000 in 1971, $ 479,000 in 1972, $ 302,000 in 1973, $ 514,000 in 1974, and finally $ 3.68 million (which includes Amsted's losses in the sale to SBL) in 1975." Workers at Employee-Owned Firm find the Going Rough, Washington Post, Sept. 30, 1980, at A4, col. 1 [hereinafter cited as Washington Post].

n88 Brief of USWA, supra note 83, at 3-4.

n89 J.R. "Dick" Boulis, president, chief executive officer and the prime mover in the creation of SBL, was the president and principal management representative of Amsted's South Bend Lathe Division since 1969. Brief of USWA, supra note 83, at 2-7; Washington Post, supra note 87.

n90 Washington Post, supra note 87; Brief of USWA, supra note 83, at 2.

n91 Brief of USWA, supra note 83, at 5.

n92 Deak interview, supra note 45.

n93 SBL production and office facilities are located in the former engine plant and engineering building of Studebaker Corporation which closed all its South Bend facilities in 1964. Saving Jobs, How and Why U.S. Helped 500 Workers Take Over a Machine-Tool Manufacturer, Wall St. J., Aug. 16, 1976, at 28, col. 1.

n94 Id.; Deak deposition, supra note 86, at 36-37.

n95 Id.; telephone interview with SBL President J. R. Boulis (Oct. 15, 1982) [hereinafter cited as Boulis interview].

n96 Deak deposition, supra note 86, at 43-44. See also id. at 73, 75, 79.

n97 SBL was the first, or one of the first, ESOP experiences for the USWA. Id. at 81.

n98 The international union was not involved in the ESCOP project initially because Boulis asked the local union not to spread the information he gave them concerning the EDA and the ESOP for fear it would hurt negotiations with other possible purchasers. Interviews with United Steelworkers of America Attorney William Schmelling (July 15, 1981; April 20, 1982; Nov. 24, 1982) [hereinafter cited as Schmelling interviews]. Although some of the local union officers were aware of the pension problems posed by the ESOP in January 1975, the USWA district office and international pension experts were not aware of these problems until perhaps as late as June 1975, weeks before the sale. Id.

n99 ERISA of 1974, *29 U.S.C. § 1001* (1976).

n100 Id.; Deak interview, supra note 45.

n101 Deak deposition, supra note 86, at 37-41; Deak interview, supra note 45.

n102 Deak interview, supra note 45; Schmelling interviews, supra note 98. ERISA's funding and vesting provisions did not cover the Amsted plan until 1976. Boulis interview, supra note 95; telephone interview with Amsted's attorney, William McKittrick (Nov. 24, 1982) [hereinafter cited as McKittrick interview]. McKittrick stated that after Amsted and the USWA reached impasse on the pension issue, Amsted decided to amend its pension plan to cease funding and accumulation of service credits for all participants not retired or immediately eligible for retirement. It unilaterally sought and received approval of this action from the IRS and the Pension Benefit Guarantee Corporation (PBGC). In retrospect, McKittrick does not believ PBGC approval was required as this was an amendment and not a termination.

n103 Deak interview, supra note 45; Schmelling interviews, supra note 98; Brief of USWA, supra note 83, at 20-21.

n104 Brief of USWA, supra note 83, at 13.

n105 Id. at 15-16 (quoting letter from Boulis to South Bend Lathe employees dated June

24, 1975).

n106 Id. at 21-22.

n107 United Steelworkers of America v. South Bend Lathe, Inc., No H-76-115 (N.D. Ind. filed April 30, 1976). Amsted was originally a defendant, but the court later dismissed it from the lawsuit. See infra notes 366-68 and accompanying text.

n108 *29 U.S.C. §§ 1341,* 1341a (1976 & Supp. IV 1980).

n109 See infra note 436.

n110 Id.

n111 This idea is explored further infra text accompanying notes 426-36.

n112 Deak interview, supra note 45.

n113 South Bend Lathe, Inc. Employee Stock Ownership Plan [hereinafter cited as SBL Plan] § 14. Since the employees do not, in fact, own the stock (rather the ESOT owns it), during the SBL strike in 1980, the county court issued an injunction prohibiting the employee-stockholders from trespassing on company property. South Bend Lathe, Inc. v. United Steelworkers of America and Local Union 1722, No. 1539 (St. Joseph County, Ind. Cir. Ct., filed Sept. 30, 1980) (Special Findings of Fact and Conclusions of Law Upon Issuance of Temporary Restraining Order).

n114 SBL Plan, supra note 113, at §§ 6-7.

n115 Id. §§ 9, 13; Deak interview, supra note 45; Proxy Statement and Request for Voting Direction and Annual Shareholder Meeting to be Held on Oct. 16, 1980 of South Bend Lathe, Inc. [hereinafter cited as SBL Proxy Statement]; letter to John Deak from the South Bend Lathe, Inc. Employee Stock Ownership Committee (Sept. 24, 1980) [hereinafter cited as letter to Deak].

n116 SBL Proxy Statement, supra note 115.

The proxy statement also informed the employee-stockholders that the only way to direct the trustee's vote was to use the attached "Voting Direction Form." Otherwise, "[i]f your Voting Direction Form is not returned by that date or in the event that the intent of your Voting Direction Form cannot be determined or followed as a legal matter, the shares . . . will be voted by the ESOP committee in such manner as it decides."

On this statement, no time or place was given for the annual shareholders meeting. Nor was any employee-shareholder informed on the manner of voting in person. Furthermore, the proxy statement stated that the purpose of the annual meeting was to elect three members to the board of directors and that that was "normally the only issue voted on by shareholders." Attached to the proxy statement was a list of three proposed directors. The attached "Voting Direction Form" gave the voter the right to vote "for" or "against" all three nominees at once. Based on the form, it was not possible to vote for one and against another. Nor was there any way to write in a nominee without taking the chance of invalidating the Voting Direction Form. Id.; letter to Deak, supra note 115.

n117 SBL Plan, supra note 113, §§ 2, 18.

n118 See supra notes 98-107 and accompanying text.

n119 Deak interview, supra note 45. See J. Smith, Assistant to the President, United Steelworkers of America, Speech to the Yale School of Organization and Management entitled The Labor Movement and Worker Ownership, at 7, 9 (Feb. 25, 1981). Mr. Smith states:

During the 1970's a new weapon was added to the armory of anti-union managements -- the ESOP, or Employee Stock Ownership Plan. While there are as many kinds of ESOP's as can be imagined, the predominant form of ESOP as an anti-union scam has been the type used at South Bend Lathe Company. . . .

The clash between these legalized swindles and the trade union movement is inevitable. It arises out of one or a combination of three elements. These are:

First: Trade unions in the United States have long since accepted the opinions uniformly expressed by all professional pension advisers, that pension funds should be invested broadly, rather than being concentrated in one business.

Second: As mentioned above, ESOP's are frequently advanced to serve the purposes of managers who are philosophically anti-union.

Third: Even if the managers aren't anti-union at the outset, their self-perpetuation virtually requires elimination of any agency through which the fraud can be exposed to the workers. A union is such an agency.

In the case of South Bend Lathe, a USWA local union had existed for some 30 years at the plant. Management and the ESOP promoters did all they could to destroy it. After two years without a labor-management contract, however, the workers voted overwhelmingly that they did want to be represented by our Union.

A contract was thereafter negotiated, but the bitterly anti-union management refused to agree to a contract of more than one year. At the end of that year management forced the workers to conduct a lengthy strike (last year) to preserve their wage and fringe benefits other than pensions.

n120 Deak interview, supra note 45; Washington Post, supra note 87.

n121 In contrast, the Rath Packing Company Employee Stock Ownership Plan and Summary Plan Description were written for the layperson and present no comprehension problems.

n122 See supra notes 1, 2, 15.

n123 The City of South Bend had control over the EDA money, and city officials were listening to the union. Thus, the union probably had the clout to kill the ESOP unless the plan was changed to its liking.

n124 Deak interview, supra note 45.

n125 Gunn, The Fruits of Rath: A New Model of Self-Management, WORKING PAPERS FOR A NEW SOCIETY, Mar.-Apr. 1981, at 117.

n126 HUD granted the city $ 4,600,000. The city lent $ 4,500,000 of the grant to Rath for capital investment. Id.; interviews with Lyle Taylor, President, Local 46 United Food and Commercial Workers International Union (UFCW), AFL-CIO (July 15, 1981; June 4, 1982; June 22, 1982; Sept. 21, 1982) [hereinafter cited as Taylor interviews]; letter from Lyle Taylor to Deborah Groban Olson (April 23, 1982); Rath Packing Company Employee Stock Ownership Plan Prospectus 15 (Dec. 10, 1982).

n127 This plan was the local's response to considerable pressure from the employer and community leaders to take concessions in order to save the company from closing. A different investor also had made a proposal to take over the company. That proposal would have required the workers to accept enormous pay and benefit cuts, contrary to the national agreement negotiated by their union, without providing them with any assurances that additional future cuts would not be required to keep their employer afloat. Gunn, supra note 125; Taylor interviews, supra note 126.

n128 Taylor interviews, supra note 126.

n129 Rath Packing Company Prospectus 8-9 (Dec. 30, 1980) (on file with the author). The prospectus describes the specific structure and provisions of the Rath escrow account, the deferrals, the financial package, the repayment provisions and the labor agreement that created the foundation for the ESOP.

n130 Telephone interview with Lyle Taylor (June 4, 1982). The union provided the impetus for the organization of the Black Hawk County Economic Development Committee, which received a $ 3,000,000 loan from the United States Economic Development Administration (EDA) to capitalize Rath. The EDA money and the wage and fringe benefit deferrals

negotiated by the union were considered matching funds for the HUD loan. Id.

n131 Gunn, supra note 125.

n132 Taylor interviews, supra note 126.

n133 According to the Rath Packing Company Prospectus, supra note 129, at 8, in June 1979, Local 46 UFCW (with the exception of some very small units) agreed to defer into an escrow account 25 per hour of the COLA increase due on July 1, 1979; 15 per hour of the general wage increase due on September 1, 1979; and 5 per hour of the general wage increase due on September 1, 1980. The increases had been negotiated in the master labor agreement between the International Union and Armour Company. Increased benefits under the pension plans for bargaining unit employees were not to be touched.

For the term of the Local Agreement, which expires 8/31/82, Rath's pre-tax profits are to be allocated first, to restore proper funding to the Rath Pension Plan for any year which is not funded fully, and to meet all contract requirements for all years to and including 1979 . . . and second to a pro rata rebate to the employees and former employees of all benefit payments accruing during that same year, but deferred and made contingent under the Local Agreement or the escrow fund arrangement.
Id. at 8.

n134 The company has several plants. By far the largest is the one in Waterloo where the majority of Local 46's membership is employed. Taylor interviews, supra note 126.

n135 Id.

n136 Id.

n137 This trust would have avoided many of the ESOP regulations, reporting requirements and the necessity to offer departing employees stock instead of cash. Under Local 46's proposal, the employees would have purchased the outstanding 1,800,000 shares of Rath stock through a wage plan, whereby the employees would purchase stock to be valued at two dollars per share over a 2 1/2 year period. The trust created by the plan was to be administered by six trustees, all Rath employees. Of the six trustees initially proposed, five were bargaining unit employees. (Lebowitz letter, cited below, said "six trustees . . . all of whom are employees represented by the Local" but Rath Employee's Trust (the Plan) Exemption Application No. D-1836 to U.S. Dep't of Labor, filed Mar. 15, 1980, Exhibit A to Application for Prohibited Transaction Exemption, at 6, states "of the initial Board of Trustees . . . to serve until the first annual election . . . five bargaining unit employees, and one supervisory non-bargaining unit employee.") Each employee would have incurred a wage reduction equal to the amount of stock and cash transferred to the trust on his behalf. Each employee would then have maintained an undivided beneficial interest in the total assets of the trust, with not

less than eight shares per week contributed on his behalf. The distribution of benefits to plan participants upon retirement was to be in cash at the fair market value of the stock, except that these benefits would have been held artificially below market value for a period of up to 13 years from the inception of the plan. Letter of Assistant Administrator for Fiduciary Standards, Pension and Welfare and Benefits Programs, U.S. Dep't of Labor Alan Lebowitz, to UFCW Attorney Russell Woody 3 (Aug. 5, 1980) [hereinafter cited as Lebowitz letter].

No part of this plan was intended to alter the existing pension plan at Rath, nor was the plan intended to be tax-qualified for ERISA purposes. Yet, the Department of Labor denied this plan an exemption under E.R.I.S.A. § 408(a), *29 U.S.C. § 1108* (1976) for a transaction prohibited under E.R.I.S.A. § 406, *29 U.S.C. § 1106* (1976). Therefore, the plan was not exempt from taxation under *I.R.C. § 4975(a)*, (b). The Department of Labor decided that this plan was a pension plan and, as such, did not meet the restrictions limiting investment in employer securities to 10%. E.R.I.S.A. § 407(a)(2), *29 U.S.C. § 1107*(a)(2) (1976). The Department further suggested that this 10% limitation applied to all plans except for eligible individual account plans under E.R.I.S.A. § 407(d)(3)(A), *29 U.S.C. § 1107*(d)(3)(A) (1976), including profit sharing, stock bonus, thrift, savings, employee stock ownership or money purchase plans. Lebowitz letter, supra this note, at 5-6.

n138 *Rath Employee Stock Ownership Plan Prospectus, supra* note 126, at 8. The Board of Trustees has the discretion to accelerate or defer commencing the distribution of a participant's ESOP benefit to a time prior to or after such five year period. However, the benefit must be paid within 60 days after the close of the plan year in which the latest of the following occurs: 1) the participant's termination of employment; 2) his or her 65th birthday; or 3) the 10th anniversary of his or her participation in the plan.

n139 Interview with Charles Mueller, UFCW Local 46 Chief Steward (July 15, 1981) [hereinafter cited as Mueller interview].

At the time the Rath plan was created, *I.R.C. § 409A(h)(1)*, (2) (Supp. IV 1980) (made applicable to ESOPs by *I.R.C. § 4975(e)(7)* (Supp. IV 1980)) provided that ESOP participants must be given the option to take their distribution in either stock or cash, as follows:

(1) In general

A plan meets the requirements of this subsection if a participant who is entitled to a distribution from the plan --

(A) has a right to demand that his benefits be distributed in the form of employer securities, and

(B) if the employer securities are not readily tradeable on an established market, has a right to require that the employer repurchase employer securities under a fair valuation formula.

(2) Plan May Distribute Cash In Certain Cases

A plan which otherwise meets the requirements of this section or of section 4975(e)(7) shall not be considered to have failed to meet the requirements of section 401(a) merely because under the plan the benefits may be distributed in cash or in the form of employer secur-

ities.

n140 The Economic Recovery Tax Act of 1981, *26 U.S.C. § 409A*(h)(2) (enacted Aug. 31, 1981) provides in part:

[A] plan which otherwise meets the requirements of this subsection or section 4975(e)(7) shall not be considered to have failed to meet the requirements of section 401(a) merely because it does not permit a participant to exercise the right described in paragraph (1)(A) if such plan provides that participants entitled to a distribution from the plan shall have a right to receive such distribution in cash.
(emphasis supplied.)

n141 Taylor interviews, supra note 126.

n142 *Rath Employee Stock Ownership Plan Prospectus, supra* note 126, at App. A.

n143 Id. at App. A, B.

n144 Id. at App. B-3.

n145 Rath Packing Company Prospectus, supra note 129, at 5, 6, 11, App. A; Letter of Understanding to Rath Packing Company from Local P-46 President Lyle Taylor, cosigned by Emmet McGuire for Rath (May 13, 1980).

n146 Taylor interviews, supra note 126. The negotiated ESOP plan provides that "[a] slate of nominees for director of the Company, consisting of persons agreed upon by the Company and the Union, shall have been submitted to and elected by the shareholders." Rath Packing Company Prospectus, supra note 129, at App. A-5. This agreement reached in May 1980 was ratified by the shareholders in June 1980. Id. at App. A-3.

Some companies have cumulative voting, which allows a substantial minority stockholder to gain a board seat.

n147 Taylor interviews, supra note 126. Lyle Taylor, President of Local 46, was recently elected to a seat as a regular, not a provisional, director. All the current provisional directors were recommended by Local 46. Id.

n148 Id. Much has been written about the quality of working life program at Rath Packing, but it is beyond the scope of this article. For more information, contact the Program on Participation in Labor Managed Systems, Cornell University, Ithaca, New York. See also Sklar, An Experiment in Worker Ownership, 29 DISSENT 61, 67-68 (1982).

n149 Mancuso interview, supra note 21.

n150 Id.; letter from John Mancuso to Deborah Groban Olson (May 7, 1982).

n151 In meatpacking, the union has pattern bargaining based on agreements reached with Armour, Swift, Morrell and Wilson. Mancuso interview, supra note 21.

n152 For several years, beginning in 1976, the Rath pension plans have been subject to the minimum funding requirements of the IRC and ERISA. Rath has received several IRS waivers. Rath Packing Company Prospectus, supra note 129, at 9-10 (which describes the status of the pension plans at the time the ESOP was created). "Since 1977 Rath has used three of five waivers allowed within a 15 year span and already has partial waivers for 1982 and 1983. It is $ 26 million behind in pension payments, and its $ 103 million in pension liabilities exceed assets in the plan by $ 75 million." An Acid Test for Worker-Owners, BUS. WK. Aug. 2, 1982, at 67, 70. See also PENSION & INVESTMENT AGE, Sept. 13, 1982, at 1; infra notes 157-60 and accompanying text.

n153 Mancuso interview, supra note 21.

n154 D. ZWERDLING, supra note 20, at 1-8.

n155 Gunn, supra note 125, at 17-18.

n156 Mancuso interview, supra note 21.

n157 An Acid Test for Worker-Owners, supra note 152, at 71.

n158 29 C.F.R. §§ 2622.3, 2622.9 (1981).

n159 Telephone interview with Lyle Taylor, UFCW Local 46 Pres. (Sept. 21, 1982). See also PENSION & INVESTMENT AGE, supra note 152, at 1.

n160 Revival at Dying GM Factory, New York Times, Oct. 26, 1981, at D1, col. 3.

Originally, the company was unreceiptive to the employees' interest in buying the plant. The company became more responsive when it was unable to find other prospective buyers. Speech by James May, UAW Local 736 President at Unions and Employee Ownership Conference, Washington, D.C. (Jan. 26, 1981) [hereinafter cited as May speech].

n161 Either at its other bearing plants, or by Timken. May speech, supra note 160.

n162 May speech, supra note 160.

n163 Id.

n164 Id.; Revival at Dying GM Factory, supra note 160.

n165 Revival at Dying GM Factory, supra note 160.

n166 May speech, supra note 160.

n167 Workers Buying Beleagured GM Plant, Florence (Alabama) Times Tri-Cities Daily, Nov. 4, 1981, at 1.

n168 Telephone interviews with union local attorney Craig Livingston (Jan. 25, 1982; Nov. 23, 1982) [hereinafter cited as Livingston interviews]; letter from Craig Livingston to Deborah Gorban Olson (May 14, 1982).

n169 May speech, supra note 160.

n170 Livingston interviews, supra note 168.

n171 Moberg, Should the Union Give Back or Buy In?, IN THESE TIMES, Dec. 30, 1981-Jan. 5, 1982, 3, at 6.

n172 Interview with James May, UAW Local 736 President and Chief Steward James Zarrello (July 1, 1981).

n173 Id.

n174 Telephone interview with George Schwartz, UAW Economist (July 10, 1981) [hereinafter cited as Schwartz interview]; letter from George Schwartz to Deborah Groban Olson (June 30, 1982).

n175 Livingston interviews, supra note 168.

n176 Schwartz interview, supra note 174.

n177 Moberg, supra note 171. The effect of the Hyatt ESOP agreement on GM contract negotiations is considered one of the reasons why GM was willing to help facilitate the Hyatt buyout. The local would respond, however, that they can find no alternative to save jobs. Id.

The following accounts were given of the Hyatt buyout.

Roger B. Smith, G.M.'s Chairman and chief executive, expressed delight about developments at Clark, which were begun by union officials after G.M. announced last March that it planned to close the factory. The episode fits neatly into his campaign to persuade the U.A.W. to accept wage reductions before the current contract expires next year. Revival at Dying GM Factory, supra note 160. Attorney Alan V. Lowenstein, who set up the [Hyatt] ESOP and is now chairman of the board says, "GM stopped their loss. They've got an assured second source of supply besides Timken. But there was another motive they had: they wanted to prove we could do this and put this on the bargaining table next year when they negotiate with the UAW." Moberg, supra note 171, at 3.

Rube Singer, former president of UAW Local 736, believes that the ESOP will not work because the automobile industry's need for tapered bearings is ending as front-wheel drive cars are replacing rear-wheel drive cars. He feels that GM is keeping this plant alive as an ESOP to use for its own purposes in upcoming negotiations with the UAW. He suggests that the ESOP's heavy indebtedness to GM and a consortium of banks places the real ownership of the company in the hands of the consortium and not in the hands of the workers. See Singer, Auto Design Changes Doom the Clark Plant, IN THESE TIMES, Feb. 17-23, 1982, at 12.

n178 Breen v. Local 736 UAW, No. 81-3301 (D.N.J., filed Oct. 26, 1981). For more details see infra notes 362-65 and accompanying text.

n179 Telephone interview with Attorney Craig Livingston (Nov. 23, 1982).

n180 Moberg, supra note 171; UAW, Ford Face Empty Expectations, Florence Times Tri-Cities Daily, Nov. 1, 1981, at 1; Interview with Lavoye C. "Sonny" McCanless, President of UAW Local 255 (Feb. 9, 1982) [hereinafter cited as McCanless interview]; telephone interview with Lavoye C. McCanless (June 1, 1982); letter from McCanless to Deborah Groban Olson (July 21, 1982) [hereinafter cited as McCanless letter].

n181 Workers Buying Beleagured GM Plant, supra note 167; Ford Motor Company Press Release (Oct. 21, 1981).

n182 UAW, Ford Face Empty Expectations, supra note 180; UAW Local 255 Press Release (Oct. 30, 1981).

n183 Telegram from UAW International President Douglas Fraser to Local 255 President L. C. McCanless (Oct. 29, 1981).

n184 Peter Pestillo, Ford Motor Company Vice President for Labor Relations, quoted in Ford V.P. Says Plant's Future Up To Workers, Florence Times Tri-Cities Daily, Nov. 7, 1981, at 1, col. 1.

n185 Id.; McCanless letter, supra note 180.

n186 Interview with Ford Motor Company Public Relations Service Manager Michael Davis (Feb. 9, 1982) [hereinafter cited as Davis interview].

n187 McCanless interview, supra note 180.

n188 Michael Davis of Ford said Ford was inspired by the Hyatt-Clark experience of GM. In the initial discussions between the UAW and Ford about a possible ESOP, "Ford indicated a willingness to do exactly the same thing as General Motors had done in New Jersey." Letter from Donald F. Ephlin, UAW Vice President and Director -- National Ford Department, to Deborah Groban Olson (May 11, 1982) [hereinafter cited as Ephlin letter]. In later discussions, however, when the union asked if Ford would give "special early retirement" plant closing benefits if an ESOP were adopted, Ford refused. GM ultimately agreed to provide such benefits but required that the new employer, Hyatt-Clark, pay part of the cost of these benefits. The Ford parties were unaware of this part of the Hyatt-Clark agreement during their initial discussions. McCanless interview, supra note 180.

n189 McCanless interview, supra note 180.

n190 Professor Joseph Blasi, Harvard University, and Professor William Whyte, Cornell University, Harvard University UAW/Ford Study Press Release (Nov. 23, 1981).

n191 McCanless interview, supra note 180.

n192 Moberg, supra note 171.

n193 Davis interview, supra note 186.

The castings made at Sheffield are sent primarily to engine plants in Windsor, Ontario, Cleveland and Lima, Ohio and to transmission plants in Michigan and Ohio. The Sheffield plant, which Ford opened in 1957, was originally located so far away from the plants it supplies because of a great energy cost advantage available in that Tennessee Valley Authority (TVA) supplied area. Because aluminum reduction is an energy intensive process, the energy cost differential was significant in 1957. Id. Since 1957, however, the TVA has increased its energy rates considerably. Thus, the previous energy cost differential between Sheffield and other areas in the United States and Canada has become inconsequential. Telephone interview with Alan Carmichael, Tennessee Valley Authority (TVA) News Desk, Knoxville, Tenn. (Feb. 9, 1982) (confirmed by letter to Deborah Groban Olson (April 15, 1982)) (Carmichael provided comparative figures of a monthly electrical bill for an industrial user with a 1000 kilowatt demand and 4000 kilowatt hours per month in nine United States cities for 1981 as follows: Portland, Ore., $ 13,540; TVA, $ 17,431; St. Louis, $ 18,851; Detroit, $ 23,667; Chicago, $ 23,304; Los Angeles, $ 21,746; Washington D.C., $ 27,721; Boston, $ 32,428 and

New York City, $ 45,814).

Furthermore, in July, 1980 the Reynolds Metals Aluminum Smelting Plant adjacent to the Ford Sheffield Plant, which provides molten metal for die-casting, shut down four of its primary aluminum production lines, laying off 450 workers, idling 70,000 tons of productive capacity, and reducing its output by 35% because of increased power costs and a decreased demand from the adjacent Ford Foundry. Reynolds Lays Off Workers, Florence Times Tri-Cities Daily, July 4, 1980. In October 1981, Reynolds decided to close down one of its two remaining aluminum production potlines citing "soaring utility rates" as a reason along with low aluminum prices and declining demand. Reynolds Unfair, Says TVA Official, Florence Times Tri-Cities Daily, Oct. 18, 1981. In August 1981, the TVA had announced that it would increase rates for electric power by approximately 20% in October.

Thus, the Ford plant was left with a rapidly declining source of increasingly expensive aluminum. Ford, however, said that labor cost, not aluminum or transportation costs, was the reason for the announced shutdown. Davis interview, supra note 186 (Davis said Ford is replacing primary with secondary aluminum to lower the aluminum cost.).

n194 Davis interview, supra note 186. However, Local 255 Pres. McCanless notes that Sheffield labor costs are no higher than those at GM's Central Foundry at Massena, N.Y., which is similar to the Sheffield plant. McCanless letter, supra note 180.

n195 Davis interview, supra note 186. Aluminum die-casting is predicted to be a growing industry because many vehicle maufacturers are turning from iron and steel casting to aluminum to lighten vehicle weight and increase fuel efficiency. Since die-casting is so closely related to the automobile industry, it is currently suffering from the plight of the United States economy and automobile industry. Telephone interviews with Marie Harris, U.S. Department of Commerce Aluminum Specialist (Feb. 11, 1982; April 21, 1982). Harris cited a speech by American Die-Casting Institute President Findley, speaking before a group of die-casting executives in Japan in 1981, as follows: "That aluminum die-casting production has grown 63% in the last five years, primarily for automotive weight reduction applications . . . projected usage is 1.25 million tons in 1985, a 186% increase over 10 years." MAGNESIUM, May-June 1981, at 5 (newsletter of the International Magnesium Association).

n196 Davis interview, supra note 186.

n197 Id.

n198 Id.

n199 Ford-UAW Make a Deal, The Detroit News, Feb. 14, 1982, at 1, col. 1; UAW, UAW-Ford Report (Feb. 1982).

n200 Id.

n201 Sheffield Workers Consent to New Talks, Detroit Free Press, Mar. 5, 1982, at 10-C, col. 4.

n202 UAW Press Release (June 18, 1982).

n203 The ESOP offer was not absolutely dead until the final decision was made to close the plant. Because the ESOP was pursued by neither the union nor its members, it is unclear whether the company would have withdrawn it at any certain date. Ephlin letter, supra note 188.

n204 McCanless interview, supra note 180.

ESOP never got off the ground because of the way they came in here. . . . New there's feeling of relief. We did what we had to do. We don't want to see the plant shut but we weren't going to give up our dignity. We'll go out with our heads up. There's no rah-rah thing, people flexing their muscles. The national master agreement is just something that's almost sacred. I would take a strong position against being involved in ESOPs if we're going to have national agreements, or you will have to take the United out of Auto Workers.
Id.

n205 Workers Buying Beleagured GM Plant, supra note 167.

n206 Id.

n207 Taylor interviews, supra note 126.

n208 See supra notes 154-56 and accompanying text. Many companies flee unionized higher-wage areas for lower-wage areas. B. BLUESTONE, B. HARRISON & L. BAKER, supra note 12, at 55. Community leaders who encourage employee purchases of single plants of multiplant employers may not be aware of the distinctions made in this article between single plant and full company buyouts. They may not see the marketing problems for the new plant and may be even less aware of, or concerned about, the internal union conflicts of interest created by wage competition with sister union plants.

n209 See supra text accompanying notes 125-40.

n210 See infra text accompanying notes 322-31; 373-416; 437-64.

n211 D. ZWERDLING, supra note 20, at 95-96.

n212 Id. at 96-97.

n213 Id. at 97.

n214 Id. at 96-97.

n215 Id. at 97-99.

n216 Id. at 98-99.

n217 Id. at 97.

n218 K. BERMAN, WORKER OWNED PLYWOOD COMPANIES: AN ECONOMIC ANALYSIS (1967); D. ZWERDLING, supra note 20, at 100. See also Bernstein, Run Your Own Business: Worker-Owned Plywood Firms, WORKING PAPERS FOR A NEW SOCIETY, Summer 1974; Bernstein, Worker-Owned Plywood Firms Steadily Outperform Industry, WORLD OF WORK REPORT, May 1977.

n219 Letter from R. Denny Scott, Research Economist, International Woodworkers of America, to Professor Paul Bernstein (June 17, 1977) (on file with the author).

n220 D. ZWERDLING, supra note 20, at 95-96.

n221 Some of the companies, such as Linton Plywood Association and Olympia Veneer near Portland, Oregon, started as co-operatives from scratch.

n222 D. ZWERDLING, supra note 20, at 103.

n223 Id. at 96.

n224 Id. at 103.

n225 Id. at 102-03.

n226 Id. See also infra notes 279-89 and accompanying text.

n227 See *Everett Plywood & Door Corp., 105 N.L.R.B. 17 (1953);* motion denied, *105 N.L.R.B. 957 (1953); Coastal Plywood & Timber Co., 102 N.L.R.B. 300 (1953); Brookings Plywood, 98 N.L.R.B. 794 (1952),* vacated, *100 N.L.R.B. 431 (1952); Alderwood Products*

Corp., 81 N.L.R.B. 136 (1949). For a similar fact situation, see *NLRB v. Fort Vancouver Plywood Co., 604 F.2d 596 (9th Cir. 1979).*

n228 See infra text accompanying notes 278-93.

n229 Id.

n230 Letter from R. Denny Scott, Research Economist, IWA, to Deborah Groban Olson (May 22, 1981) [hereinafter cited as Scott letter]. The letter shows, however, that the IWA has had some favorable experiences with government-owned mills in Canada and is not opposed, in principle, to government or community ownership.

n231 D. ZWERDLING, supra note 20, at 103.

n232 *604 F.2d 596 (9th Cir. 1979).*

n233 Scott letter, supra note 230; Scott letter to Deborah Groban Olson (April 19, 1982).

n234 Id.

n235 *Fort Vancouver Plywood, 604 F.2d 596 (9th Cir. 1979).*

n236 ICA is located at 249 Elm Street, Somerville, Mass. 02144 and is an organization that provides technical assistance in the creation and development of worker-owned co-operative businesses.

n237 In particular, the ICA likes the structural model of the Mondragon complex in the Basque region of Spain. D. Ellerman, supra note 3. The Mondragon model is described in more detail in Johnson & Whyte, The Mondragon System of Worker Production Co-operatives *31 INDUS. & LAB. REL. REV. 18 (1977).*

n238 D. Ellerman, Workers' Co-operatives: The Question of Legal Structure (rev. ed. 1981); Legal Aspects of a Workers' Co-operative: The Outer Shell and the Inner Structure (1981); The Employment Relation, Property Rights and Organizations Structure (1980).

n239 Co-operative ESOPs are discussed in more detail infra text accompanying notes 448-62; supra note 26.

n240 C. ROSEN, supra note 3, at 2.

n241 The Chrysler ESOP, which was created as a requirement of the United States Government Loan Guarantee to Chrysler, is atypical of large corporation ESOPs because it was mandated by the government, and because it gives the employees the largest bloc of voting stock in the company. See infra text accompanying notes 257-67, especially notes 263-64 and accompanying text. Otherwise its terms are typical of other ESOPs.

n242 See supra note 2.

n243 UAW Chrysler Department, Summary of the 1979-82 UAW Chrysler Contract Gains, CHRYSLER NEWSGRAM, Nov. 1979, at 14. See also supra note 2.

n244 *I.R.C. § 48(n)(1)(B)* (Supp. IV 1980).

n245 Id.

n246 Id. § 409A(e), (1) (Supp. IV 1980). See also supra note 15.

n247 See supra note 2.

n248 UAW and Ford Motor Co., Exhibit D, Supplemental Agreement (Employee Stock Ownership Plan) to UAW-Ford Motor Collective Bargaining Agreement of 1979-82.

n249 UAW and General Motors Corp., Exhibit D, Supplemental Agreement (Employee Stock Ownership Plan) to UAW-GM Collective Bargaining Agreement of 1979-82.

n250 *I.R.C. § 409A(b)*, (e) (Supp. IV 1980).

n251 This is unlike the Rath ESOT in which the participants hold a meeting before each stockholders meeting to instruct the trustees; and the majority at that meeting determines how all the ESOT stock will be voted. See supra notes 143-44 and accompanying text.

n252 Telephone interview with UAW Economist George Schwartz (Mar. 24, 1982).

n253 Id.

n254 See infra note 456.

n255 A Rath type of bloc voting might be subject to challenge since TRASOPs require pass through of voting rights. The trustees could safely be instructed to vote the shares purchased from retiring employees in proportion to the votes of active employees. However,

nothing in *I.R.C. § 409A(e)* (Supp. IV 1980) necessarily prevents a plan from instructing the trustees to vote all repurchased stock as a bloc according to the dictates of the majority of the active employee-stockholders. Majority bloc voting may well be found to be an adequate means of providing the participant's right to instruct the trustee on voting of her stock under *I.R.C. § 409A* (Supp. IV 1980).

n256 The Economic Recovery Tax Act of 1981 § 331, *I.R.C. § 44G* (1981) allows a corporate tax credit, beginning in 1983, in the amount of either the aggregate value of employer securities transferred by the corporation for the taxable year to a qualifying TRASOP or a statutorily specified percentage of the annual payroll for all employees participating in the TRASOP, whichever is less. There may be a further limitation under § 44G(6) (1981) depending on the amount of tax liability.

n257 In the Chrysler case, the financial assistance was provided pursuant to the Chrysler Corporation Loan Guarantee Act of 1979, *15 U.S.C. §§ 1861*-1875 (Supp. IV 1980).

n258 Press Release from UAW Vice President Marc Stepp (June 30, 1981); telephone interview with Chrysler Director of Investor Relations, Robert Johnson (Jan. 29, 1982) [hereinafter cited as Johnson interview]; telephone interview with Johnson's assistant, Wendy Markham (April 30, 1982). The press release says 63 shares; Markham said 66 shares.

n259 Chrysler Corporation, Chrysler Employee Stock Ownership Plan (Apr. 7, 1980).

n260 Id.

n261 Letter of Understanding from William O'Brien of Chrysler Corporation to Marc Stepp of the UAW (Mar. 31, 1980).

n262 Id.

n263 Telephone interview with Frank Musick, UAW Research Department (Jan. 29, 1982) [hereinafter cited as Musick interview].

n264 Id.

n265 Johnson interview, supra note 258. The Chrysler Thrift Stock Ownership program was created primarily for salaried employees at the time the union negotiated Supplemental Unemployment Benefits (SUB). Corporation contributions have since been suspended. The Thrift Plan trustee held 5,000,000 shares as of December 30, 1980; the ESOP trustee held 5,987,400 shares as of June 1981.

n266 Musick interview, supra note 263.

n267 Id.

n268 International Brotherhood of Teamsters (IBT), Airline Pilots Association, Flight Engineers International Association, Transport Workers Union of America. The fifth union, Independent Union of Flight Attendants, may join in the agreement early in 1982.

n269 Teamsters Union Asks Pan Am to Select New Director From Among 3 Candidates, Wall St. J., Oct. 20, 1982, at 8, col. 2.

n270 Interviews with William Genoese, Chairman of the International Brotherhood of Teamsters -- Pan Am bargaining committee, and Secretary-Treasurer of IBT Local 732, and Richard Phenneger, Vice President for Contracts Pan Am Chapter of the Flight Engineers International Association as of Oct. 7, 1981, now the Pan Am Joint Labor Council ESOP Communications Co-ordinator (Jan. 26, 1982) [hereinafter cited as Genoese and Phenneger interview]. The terms of the ESOP negotiated with the unions are described in Pan American Wage Reduction Agreement, Attachment B (Oct. 7, 1981) (on file with the author).

n271 Genoese and Phenneger interview, supra note 270.

n272 Id.

n273 Id.

n274 Swedish unions have found that minority board representation helps to prevent closings by providing notice. However, their representation is not based on individual employee stock ownership. Interview with Birgitta Olsson, Research Officer, Swedish Metalworkers Union (Sept. 3, 1981) [hereinafter cited as Olsson interview].

n275 Of course in a stockholder derivative action, the stockholders bringing suit must present their case as one in which the corporation's directors are not acting in the best interests of the firm. It is not enough that the minority employee stockholders will be hurt as employees. They must show that the value of their stock or the firm's overall interests will be harmed by the action they seek to change. See H. HENN, HANDBOOK OF LAW OF CORPORATIONS 749-87 (2d ed. 1970).

n276 Genoese and Phenneger interview, supra note 270.

n277 There are and have been non-ESOP companies with union members on their corporate boards. See infra note 285.

n278 *29 U.S.C. § 152*(3) (1976).

n279 Most of the cases that arose in the late 1940's and early 1950's, cited infra note 280, were based on union certification (RC) petitions seeking initial recognition in the newly organized plywood co-operatives. In those cases, the Board felt free to exercise its full discretion to determine the scope and composition of an appropriate unit. The Board used various factors, including a review of corporate bylaws and past practices, to determine whether the employee-stockholders had an "effective voice" in management, received preferential treatment compared with nonstockholder employees, or had a conflict of interest with nonstockholder employees.

However, in *S-B Printers Inc., 227 N.L.R.B. 1274 (1977),* the issue of employee-stockholder status arose upon a decertification (RD) petition, filed in a unionized shop that had recently been purchased by a group of 38 of the 45 employees. There were 13 bargaining unit employees, of whom 10 were stockholders. After the decertification petition was filed, the union sought to exclude the employee-stockholders from the unit. The Board held that, "Board precedent clearly establishes that, unless contrary to the statute or Board policy, the scope of the unit in a decertification election should be coextensive with the certified or recognized bargaining unit." *227 N.L.R.B. at 1274* (footnote omitted). In S-B Printers, the Board decided against the union's contention that employee-stockholders should be excluded from the unit because "they control a substantial portion of the outstanding stock and can effect management decisions." According to the Board, this was not a "statutory basis" for seeking exclusion. Id.

n280 In *Union Furniture Co., 67 N.L.R.B. 1307 (1946),* the NLRB excluded employees on the corporate board from the bargaining unit because labor relations policy was referred to the board. It also excluded stockholder-employees from the unit because they held a substantial share of the stock and because "matters of fundamental labor policy . . . would be referred to stockholders." *Id. at 1310.* (There were 26 stockholders, each holding not less than 80 shares; five of the 90 bargaining unit employees were stockholders; and four of the directors were employees.)

In Red and White Airway Cab Co., 123 N.L.R.B. 83 (1959), the sole owners of the company were stockholder-drivers. They elected the board of directors, including owner-drivers, which supervised the paid manager. The manager's power to hire, fire and discipline was limited to nonowner drivers. Owner-drivers had a separate grievance procedure, and preference in shift selection. Only the owners could force another owner to leave. Thirty-eight of the company's 48 cabs were owned by owner-drivers. Thus, they owned a controlling interest. Although both the petitioning union and intervenor sought the owner-driver's inclusion in the unit, the Board excluded them due to their "effective voice in formulation and determination of company policy," and their divergent interests from those of nonowner drivers. *123 N.L.R.B. 83, 85.*

In *Everett Plywood & Door Corp., 105 N.L.R.B. 17, 19 (1953),* all the employees were stockholders, and they all received equal pay. Supervisors assigned work, the board of direct-

ors had discharge powers, and employee-stockholders had the right to appeal such discharges to the corporate membership which could advise, but not overrule, the board. The NLRB decided the production and maintenance employee-stockholders were employees under the NLRA, despite their extraordinary appeal rights, but excluded supervisors and employees who were on the corporate board of directors. It reaffirmed this decision, despite *Brookings Plywood Corp., 98 N.L.R.B. 794 (1952),* in *Everett Plywood, 105 N.L.R.B. at 958.*

In *Brookings Plywood Corp., 98 N.L.R.B. 794, 798-99 (1952),* employee-stockholders were excluded from the unit both because they had preferential employee status over non-stockholder employees and because the collective voting strength of the employee-stockholders created a real possibility of influencing management policies (118 of the nonsupervisory employees were stockholders with 1/250th of the voting stock each). See infra notes 281, 289.

By contrast, in Mutual Rough Hat, 86 N.L.R.B. (1949), employee-directors were held to be employees because the corporate officers held all control, and none of the other stockholders "participate[d] in management conferences or determine[d] management policy." *86 N.L.R.B. at 444.* In *Coastal Plywood & Timber Co., 102 N.L.R.B. 300 (1953),* stockholders remained in the unit because they had no voting rights and no employment preferences. The employee-stockholders were found not to have an "effective voice" in management because they had neither employment preferences nor a substantial collective bloc of votes (50 out of 250 shares, or 20% of the stock was held by nonsupervisory employees). Thus, they were included in a production and maintenance bargaining unit. *Id. at 301-02.* In *Alderwood Products Corp., 81 N.L.R.B. 136 (1949)* only two of 51 bargaining unit employees held stock. The Board found no "conclusive evidence that the employee-stockholders . . . exercise as stockholders an effective control over corporate policy and therefore did not exclude them." *Id. at 138.* See also *Muskogee Dairy Products Inc., 85 N.L.R.B. 520 (1979).*

n281 In *Brookings Plywood Corp., 98 N.L.R.B. 794, 799 (1952),* employee-stockholders were excluded from the unit because they had a guaranteed wage, a separate grievance procedure and the right to bump nonstockholder-employees from desirable jobs. See also *Union Furniture Co., 67 N.L.R.B. 1307 (1946); Sida of Hawaii Inc., 191 N.L.R.B. 194 (1971).*

n282 See *Brookings Plywood Corp. 98 N.L.R.B. 795, 798 (1952);* see also *Muskogee Dairy Products Co., 85 N.L.R.B. 520, 521 (1949); Alderwood Products Corp., 81 N.L.R.B. 136, 138 (1949); S-B Printers Inc., 227 N.L.R.B. 1274, 1275 (1977); Mutual Rough Hat Co., 86 N.L.R.B. 440, 444 (1949).*

n283 See *Mutual Rough Hat Co., 86 N.L.R.B. 440 (1949); Muskogee Dairy Products Co., 85 N.L.R.B. 520 (1979); Alderwood Products Corp., 81 N.L.R.B. 136 (1949); Coastal Plywood, 102 N.L.R.B. 300 (1953).*

n284 See *Everett Plywood & Door Corp., 105 N.L.R.B. 957, 958 (1953).*

n285 See *Union Furniture Co., 67 N.L.R.B. 1307, 1309 (1946).*

n286 See *id. at 1310; Sida of Hawaii Inc., 191 N.L.R.B. 194, 195 (1971).*

n287 See *Mutual Rough Hat Co., 86 N.L.R.B. 440, 444 (1949).*

n288 See *S-B Printers Inc., 227 N.L.R.B. 1274 (1977); Coastal Plywood, 102 N.L.R.B. 300 (1953).*

n289 In *Brookings Plywood Corp., 98 N.L.R.B. 794, 798-99 (1952),* 188 of 242 stockholders were nonsupervisory employees. There were a total of 211 nonsupervisory employees. The Board noted that 113 of the 117 employees in the plywood plant were stockholders. All stockholders were excluded from the designated bargaining units because they had a "uniform (preferential) wage rate," could bump nonstockholders to get desirable jobs, and had a separate grievance procedure for stockholders. Later it was noted in *Everett Plywood & Door Corp., 105 N.L.R.B. 957 (1953),* that the Board in Brookings Plywood "held that stockholder employees could not be included in the same bargaining unit as nonstockholder employees."

n290 *105 N.L.R.B. 17 (1953).*

n291 See supra note 280.

n292 *Everett Plywood, 105 N.L.R.B. at 19.*

n293 Id. (citation omitted).

n294 See supra notes 2, 15 and text accompanying notes 240-76.

n295 See supra notes 1, 15.

n296 See supra note 2.

n297 In plant closing situations, time is often of the essence in negotiations concerning any possible sale or salvage of the plant. The time constraint is usually caused by availability of financing, maintenance of relationships with customers and suppliers, and alternate plans to sell or scrap the plant or its most valuable machinery. See supra text accompanying notes 27-210. Since worker buyouts such as South Bend Lathe and Vermont Asbestos Group were negotiated in haste, the unions and workers paid little attention to the details of the actual plan proposed. In both cases, the plan proponents and union supporters were preoccupied with saving jobs and obtaining financing. See supra text accompanying notes 47-124. See also infra text accompanying note 447.

n298 See supra text accompanying notes 83-124.

n299 See supra text accompanying notes 27-43.

n300 See supra text accompanying notes 47-82.

n301 See supra text accompanying notes 125-60.

n302 See id.; supra note 26; infra text accompanying notes 448-62.

n303 See supra note 26; infra notes 448-62 and accompanying text.

n304 *110 N.L.R.B. 356 (1954),* enforced, *231 F.2d 717* (D.C. Cir.), cert. denied, *351 U.S. 909 (1956).*

n305 *110 N.L.R.B. at 364; 231 F.2d at 719.*

n306 These items included the definition of "service" under the plan, how to determine "wages," upon which the percentage of possible contributions would be based, how to determine continuity of status and to preserve it in case of layoff, strike, lockout or leave of absence for union business, and whether such status would be defined solely by company policy. *231 F.2d at 723.*

n307 *Richfield Oil, 110 N.L.R.B. 356 at 358.*

n308 *Id. at 359.*

n309 *Id. at 362.*

n310 *Richfield Oil, 231 F.2d at 724* (citing *W.W. Cross & Co. v. NLRB, 174 F.2d 875, 878 (1st Cir. 1949)* and *Inland Steel Co. v. NLRB 170 F.2d 247, 253 (7th Cir. 1943)* cert. denied on this issue, *336 U.S. 960 (1949)); Richfield Oil, 110 N.L.R.B. at 359-61.*

n311 In *NLRB v. Black-Clawson Co., 210 F.2d 523 (6th Cir. 1954),* the Sixth Circuit affirmed the Board's finding that a profit sharing retirement plan was amandatory subject of bargaining. Similarly, in *Winn-Dixie Stories, Inc., 224 N.L.R.B. 1418 (1976),* rev'd in part on other grounds, *567 F.2d 1343 (5th Cir. 1978),* cert. denied, *439 U.S. 985 (1981),* the Board held that "whether the plan is designated a profit-sharing plan or a retirement plan plus a profit-sharing plan . . . the Respondent ha[s] the obligation to negotiate and bargain in good faith with the union as to all aspects of the plan." (emphasis supplied) *224 N.L.R.B. at 1419.*

In *Allied Chemical & Alkali Workers of America Local 1 v. Pittsburgh Plate Glass Co., 404 U.S. 157 (1971),* the Supreme Court determined that mandatory subjects of bargaining are those that "vitally affect" employees' terms and conditions of employment.

n312 Since voting rights were not an issue in Richfield Oil, neither the Board nor the court said anything about how the trusteed stock was voted during the time it was held in the plan. Apparently, the stock was not available for direct ownership, and members did not have voting rights until termination of their employment with the employer. The equities of the voting issue were not explored in that case.

n313 *Richfield Oil, 110 N.L.R.B. at 363* (citation omitted).

n314 *Id. at 368* (Beeson, M., dissenting) (citation omitted).

n315 *108 N.L.R.B. 1555 (1954).*

n316 Distinguished and discussed infra text accompanying notes 322-31.

n317 *Richfield Oil, 110 N.L.R.B. at 363 n.15.*

n318 In 1953, Richfield Oil offered its employees participation in a newly created employee stock purchase plan through which employees could purchase stock by payroll deduction. The stock was to be held in trust accounts until termination of employment, retirement or withdrawal from the plan. The employer made a contribution equal to 50% of the employees' monthly contributions plus an annual contribution that depended in amount upon the ratio of profits to invested capital. The stock was held in accounts credited to each employee, one for the employee's contribution, one for the employer's. The plan was offered unilaterally by the employer to employees. It was voluntary. The employer refused the union's request to negotiate about any terms of the plan, despite the fact that the company's contribution "may amount to as much as 75 percent of the members' contributions." *Richfield Oil, 110 N.L.R.B. at 358.* The case arose from the union's refusal to bargain charge filed against Richfield Oil.

n319 At South Bend Lathe, the quid pro quo was the pension plan; at Rath Packing, holiday, vacation and sick pay; at Chrysler, wage increases and paid personal days. See supra text accompanying notes 95-111, 132, 257-67.

n320 There are many books and law review articles for businessmen on "the magic of ESOT," testifying to the numerous methods available to an employer for cashing out her business, giving stock to her employees, and still giving control to her appointed heir. See, e.g., R. FRISCH, ESOP, supra note 1; R. FRISCH, THE MAGIC OF ESOT, supra note 1; R. FRISCH, TRIUMPH, supra note 1; J. MENKE, supra note 1.

n321 Provided securities regulations are followed, unions can solicit proxies from their stockholder members, as was done at Eastern Airlines. Charles Bryant, IAM Local President, Speech at University of Michigan Summer School for Extending Workplace Democracy (July 31, 1981).

n322 *108 N.L.R.B. 1555 (1954).*

n323 *29 U.S.C. § 158*(a)(5) (1976).

n324 In *Bausch & Lomb, 108 N.L.R.B. 1555 (1954),* the Board found no evidence that the union had committed any act that established a conflict of interest. The Board's holding was a condemnation of a potential conflict. The type of analysis of potential conflicts of interest involved in such cases is not part of the NLRB's labor law expertise, and would probably best be handled by some form of regulation other than contests over section 8(a)(5) duty to bargain. See Recent Cases, Investment by International's Pension Fund in *Competitor of Local Union's Employer Necessitates NLRB Assessment of Potential Conflict of Interest -- NLRB v. David Buttrick Co., 361 F.2d 300 (1st Cir. 1966), 80 HARV. L. REV. 1606 (1967).*

n325 *361 F.2d 300 (1st Cir. 1966).*

n326 *154 N.L.R.B. 1468 (1965),* enforcement denied and remanded, *361 F.2d 300 (1st Cir. 1966).*

n327 *NLRB v. David Buttrick Co., 167 N.L.R.B. 398,* enforced, *399 F.2d 505, 507 (1st Cir. 1968).* See also *H.P. Hood & Sons, Inc., 182 N.L.R.B. 194 (1970).*

n328 ERISA now limits some of the problems raised in Buttrick. For example, E.R.I.S.A. §§ 401-414, *29 U.S.C. §§ 1101*-1114 (1976 & Supp. IV 1980) establish fiduciary obligations of pension plan trustees that severely limit their ability to make speculative investments with pension money. E.R.I.S.A. § 407, *29 U.S.C. § 1107* (1976) particularly limits covered pension plans from investing more than 10% of the plan in employer securities.

n329 See supra text accompanying notes 278-328; infra text accompanying notes 330-53.

n330 See infra text accompanying notes 373-416.

n331 *Everett Plywood & Door Corp., 105 N.L.R.B. 17, 19 (1953)* ("[T]he mere fact that an employee . . . has the rights and privileges of a stockholder is not sufficient to debar him from availing himself, in his capacity as am employee, of the rights of employees.").

n332 *29 U.S.C. § 158*(a)(2) (1976).

n333 *29 U.S.C. § 158*(b)(1)(B) (1976).

n334 Union interference with the employer's right to select its bargaining representatives is discussed infra text accompanying notes 352-53.

n335 *St. Louis Labor Health Institute, 230 N.L.R.B. 180 (1977); Anchorage Community Hospital, Inc., 225 N.L.R.B. 575 (1976); Medical Foundation of Bellaire, 193 N.L.R.B. 62 (1971); United Mineworkers of America Welfare and Retirement Fund, 192 N.L.R.B. 1022 (1971); Centerville Clinics, Inc., 181 N.L.R.B. 135 (1970).*

n336 See *St. Louis Labor Health Institute, 230 N.L.R.B. 180 n.1 (1977).*

n337 *St. Louis Labor Health Institute, 230 N.L.R.B. 180 (1977); Medical Foundation of Bellaire, 193 N.L.R.B. 62 (1971); Centerville Clinics, Inc., 181 N.L.R.B. 135 (1970).*

n338 *Medical Foundation of Bellaire, 193 N.L.R.B. at 62* is an exception.

n339 *St. Louis Labor Health Institute, 230 N.L.R.B. at 181; Centerville Clinics, Inc., 181 N.L.R.B. at 139.*

n340 *St. Louis Labor Health Institute, 230 N.L.R.B. 180 (1977); Medical Foundation of Bellaire, 193 N.L.R.B. 62 (1971); UMWA Welfare and Retirement Fund, 192 N.L.R.B. 1022 (1971); Centerville Clinics, 181 N.L.R.B. 135 (1970).*

n341 *Centerville Clinics, 181 N.L.R.B. at 140* (citing *NLRB v. David Buttrick Co., 399 F.2d 505, 508 (1st Cir. 1968)).*

n342 The section 8(a)(2) cases involving substantial union representation on institution boards and a union financial stake in these institutions relied upon the reasoning in cases involving a union pension fund secured loan to an employer. Therein, the Board investigated the amount of control of the international over the local and the actual union temptation to consider the employer's benefit over that of the employees because of the employer's financial condition.

In *NLRB v. David Buttrick Co., 167 N.L.R.B. 398,* enforced, *399 F.2d 505 (1st Cir. 1968),* and *H.P. Hood & Sons, Inc., 182 N.L.R.B. 194 (1970),* employers alleged that the Teamsters were not qualified to represent their employees because of loans made to their competitor, Whiting Milk Co., by a Teamsters pension fund. The pension fund was controlled by trustees appointed by the international union. The NLRB, and the First Circuit in Buttrick, reviewed Whiting Milk's financial status and determined that its condition was not sufficiently bad to tempt the international to influence local bargaining for Whiting Milks benefit against the in-

terests of Buttrick, Hood and their employees. Although the competitor, Whiting Milk Co., was in financial difficulty, causing it to extend its repayment schedule to the pension fund, it was making all scheduled payments on time. In Hood, the Board found that any danger of the international taking over Whiting Milk or pressuring Local 380's bargaining with Hood to benefit Whiting Milk was not "clear and present." The fund was an ordinary secured debtholder, without an "equity-like" concern for the everyday fluctuations in Whiting Milk's business, *182 N.L.R.B. 194, 196.* In Buttrick the First Circuit Stated that the burden of showing a clear and present danger of a conflict of interest was on the nonconsenting employer. *399 F.2d at 507.*

In H.P. Hood, the NLRB described the review criteria as follows:

In our opinion, the court [in Buttrick] did not prescribe any such discrete classification and quantitative measurement of each of these two aspects of the conflict of interest issue [control and temptation]. That issue simply cannot be reduced to a formula of (1) and/or (2) equals "clear and present" danger. A minimal amount of power over local bargaining may suffice if the temptation is great; and complete bargaining control may be insufficient where the temptation is nonexistent or slight. . . . [O]ur task is to carefully scrutinize . . . elements of both power and temptation, and, from this overall appraisal, determine the proximity of the danger that a remote financial interest will infect the bargaining process.
182 N.L.R.B. at 194.

n343 *St. Louis Labor Health Institute, 230 N.L.R.B. 180 (1977); Centerville Clinics, Inc., 181 N.L.R.B. 135 (1970).*

n344 *St. Louis Labor Health Institute, 230 N.L.R.B. at 183.*

n345 *Id. at 180 n.1.*

n346 *225 N.L.R.B. 575 (1976).*

n347 *Anchorage Hospital, 225 N.L.R.B. at 575-76* (Walther, M., dissenting).

n348 *Id. at 575.*

n349 Elected union representatives on corporate boards likewise are distinguishable from union-appointed pension fund trustees. See supra note 342 for a discussion of conflict of interest cases involving union pension fund secured loans to employers.

n350 In *UMWA Welfare and Retirement Fund, 192 N.L.R.B. 1022 (1971),* the NLRB hearing examiner found that the local was incompetent to represent the fund's employees. Although the NLRB found specific sections 8(a)(1) and (2) violations based on financial assistance and ordered the employer to stop such assistance, it also determined that the local was not inherently disqualified from representing fund employees because only one of the fund's

three trustees was directly responsible to the UMWA. Thus, the local was only disqualified from representation (previously based on voluntary recognition) of these employees "unless and until Local 13410 shall have been certified as the collective-bargaining representative pursuant to a Board-conducted election among Respondent's employees." Id.

n351 *Hertzka v. Knowles, 503 F.2d 625 (9th Cir. 1974)* denied enforcement of an NLRB order and held that a section 8(a)(2) violation requires evidence that the employees' free choice was stifled by the employer's involvement or cooperation. *Id. at 630.* Employer participation in in-house committees formed for employee bargaining, which met at the firm on firm time, was not a prohibited interference. In *General Foods Corp., 231 N.L.R.B. 1232 (1977),* the Board considered whether the employer's implementation of an employee team system, under which all nonsupervisory employees were assigned to one of four work teams, violated section 8(a)(2). Because these teams did not deal with management on behalf of the employees regarding labor relations matters, the Board held that the teams were not "labor organizations" under the Act and that there was therefore no illegal domination. In *NLRB v. Northeastern University, 601 F.2d 1208 (1st Cir. 1979),* the court denied enforcement of the NLRB order and held that the standard is one of "actual domination." The court found that the employee association was not actually dominated, despite the fact that the employer allowed meetings on company property during company time and sent out the union election ballots with paychecks, that the labor association had no dues, no mass meetings and no written collective bargaining agreement and that the employer had authority to appoint certain members of the labor association's board. In *Chicago Rawhide Manufacturing Co. v. NLRB, 221 F.2d 165 (7th Cir. 1955),* the court denied enforcement of the NLRB order and held that "the test of whether an employee organization is employer controlled is not an objective one but rather subjective from the standpoint of the employees." *221 F.2d at 168.* See also *UMWA Welfare and Retirement Fund, 192 N.L.R.B. at 1028.*

n352 *453 U.S. 322 (1981).*

n353 H. HENN, LAW OF CORPORATIONS 361-62, 415-16 (1970).

n354 *Steele v. Louisville & Nashville R.R., 323 U.S. 192 (1944).*

n355 See *Ford Motor Co. v. Huffman, 345 U.S. 330 (1952).*

n356 *640 F.2d 182 (8th Cir. 1981).*

n357 *29 U.S.C. § 185* (1976).

n358 *29 U.S.C. §§ 101,* 104 (1976).

n359 *Bodecker, 640 F.2d at 185.*

n360 See supra text accompanying notes 161-79.

n361 See infra note 379.

n362 Answer, Counterclaim and Jury Demand of Defendants UAW Local 736, James May and James Zarrello, Breen v. Local 736 UAW, No. 81-3301 (D.N.J., filed Oct. 26, 1981), at 1-2.

n363 Defendant Local's Memorandum of Law at 7, Local 736, UAW and Glen Wormuth, No. 22-CB-4653 NLRB Region 26.

n364 Breen v. Local 736 UAW, No. 81-3301 (D.N.J., filed Oct. 26, 1981).

n365 See *Howard Johnson Co. v. Detroit Local Joint Executive Bd., 417 U.S. 249 (1974); NLRB v. Burns International Security Services, Inc., 406 U.S. 272 (1972); John Wiley & Sons, Inc. v. Livingston, 376 U.S. 543 (1964).*

n366 *656 F.2d 1245 (7th Cir. 1981),* cert. denied, *U.S. , 102 S.Ct. 2011 (1982).*

n367 *656 F.2d at 1248.*

n368 *656 F.2d at 1252.*

n369 See infra note 371.

n370 *Helton v. Hake, 564 S.W.2d 313* (Mo. Ct. App.), cert. denied, *439 U.S. 959 (1978).* The court in Helton explicitly refused to apply the fair representation standard because the union had chosen to assume a responsibility far beyond the usual advisory and representative function. *564 S.W.2d at 320-21.*

n371 In *Brown v. United Automobile Workers, 512 F. Supp. 1337 (W.D. Mich. 1981),* former employees of a bankrupt employer claimed that the international union breached its duty of fair representation because its international representative was one of three union representatives on the pension plan board of trustees, who failed to monitor properly the employer's pension contributions. The employer defaulted on its pension obligations. The union was held liable for breach of its duty to represent fairly the workers because of the international union's expertise in the pension area and its international representative's negligent failure to monitor that fund. However, the district court held that the union's breach did not damage the employees because any action the union might have taken against the employer, had it properly monitored the fund, would have been futile or contrary to the interests of the work-

ers because it would have driven the employer into bankruptcy and deprived the workers of their jobs sooner. Thus, no damages were assessed against the union.

n372 Page letter, supra note 19.

n373 *29 U.S.C. § 186*(a), (b) (1976).

n374 *29 U.S.C. § 186* (1976 & Supp. IV 1980).

n375 Letter from Solicitor of Labor Carin Clauss to UAW General Counsel John Fillion (Jan. 16, 1981) [hereinafter cited as Clauss letter].

n376 Id. at 2. Citing for comparison *United States v. Sink, 355 F. Supp. 1067, 1072* (E.D. Pa.), aff'd, *485 F.2d 683 (3d Cir. 1973).*

n377 *29 U.S.C. § 501*(a) (1976).

n378 Id.

n379 Some of these fiduciary concerns about the wisdom of and arm's-length nature of such an investment arose when the UAW International Union was asked to loan five million dollars to help finance Hyatt-Clark. See supra text accompanying notes 160-79.

n380 In the AMC case, the Department of Labor found "section 501 . . . does not appear to apply to this situation, since the union has explicitly authorized such participation on the Board of Directors." Clauss letter, supra note 375.

n381 For example, Constitution of the International Union UAW, Ethical Practices Code 97 (1980) provides:

No officer or representative shall have any substantial financial interest (even in the publicly traded, widely-held stock of a corporation except for stock-purchase plans, profit sharing or nominal amounts of such stock), in any business with which the UAW bargains. An officer or representative shall not have any substantial interest in a business with which the UAW bargains collectively.

n382 Note that in the UAW-AMC proposal referred to in this article there was no plan for the union member on the board to hold stock or to have any other financial benefit from his position. The UAW-AMC plan mentioned supra notes 375-76 and infra notes 400-06 should not be confused with AMC's proposals, made late in 1981, that UAW members forego negotiated pay increases to lend the company development money, which the company proposed to repay at 10% interest.

n383 *Rath Employee Stock Ownership Plan Prospectus, supra* note 126.

n384 See supra notes 144-46 and accompanying text.

n385 See supra text accompanying notes 141-56.

n386 *29 U.S.C. § 432*(a)(1) (1976).

n387 Id.

n388 Id. § 433(a).

n389 Id. § 432(a)(5).

n390 Clauss letter, supra note 375.

n391 Steuer, Employee Representation on the Board: Industrial Democracy or Interlocking Directorate?, *16 COLUM. J. TRANSNAT'L L. 255, 292-96 (1977)*. However, Steuer's references to "motivation" and "opportunity" do not come from cases interpreting the present section 8 of the Clayton Act, but rather come from cases arising under other antitrust laws (for instance, § 409(a) of the Federal Aviation Act) which, he argues, support proposed legislation to make "indirect interlocks" illegal under section 8 of the Clayton Act. *Id. at 288.*

n392 Sherman Antitrust Act, *15 U.S.C. § 1* (1976).

n393 Clayton Act, *15 U.S.C. § 12; 18 U.S.C. §§ 402,* 660, 2385, 3691; *29 U.S.C. §§ 53,* 55 (1976).

n394 Steuer, supra note 391, at 274-96.

n395 Id. at 279; *15 U.S.C. §§ 1,* 2, 45 (1976).

n396 Clayton Act § 8, *15 U.S.C. § 19* (1976) provides in relevant part:

No person at the same time shall be a director in any two or more corporations, any one of which has capital, surplus, and undivided profits aggregating more than $ 1,000,000, engaged in whole or in part in commerce, . . . if such corporations are or shall have been theretofore, by virtue of their business and location of operation, competitors, so that the elimination of competition by agreement between them would constitute a violation of any of the provisions

of any of the antitrust laws. The eligibility of a director under the foregoing provision shall be determined by the aggregate amount of the capital, surplus, and undivided profits, exclusive of dividends declared but not paid to stockholders, at the end of the fiscal year of said corporation next preceding the election of directors, and when a director has been elected in accordance with the provisions of this Act is shall be lawful for him to continue as such for one year thereafter.

n397 Steuer, supra note 391, at 277-79 states:

Interlocks between potential competitors are not prohibited. . . . Vertical interlocks between suppliers and customers are not forbidden among industrial and commercial corporations, although they are controlled by section 10, which applies to common carriers. . . .

Most importantly, the language of section 8 places no restriction on so-called "indirect interlocks." These include the situation in which two competing corporations which have no director in common each have a representative who sits on the board of a third company. Indirect interlocks can also exist where a non-competing organization has different representatives on the boards of each of two or more competing companies. Such an organization could . . . be a labor union, if unions succeed in gaining representation on the boards of American corporations. Indirect interlocks can be created not only by persons who hold multiple directorships but also by persons who hold only one directorship and are officers or members, rather than directors, of another organization. Of course, single-directorship interlocks can also be direct, when a corporation puts an officer but not a director on the board of a competitor.

Under section 8 of the Clayton Act, it would be illegal for the president of a union to assume seats on the boards of directors of two or more competing firms in any industry, provided [the one million dollar size and interstate commerce requirements are satisfied]. . . .

If individual members of a labor union were to assume seats on the boards of directors of competing corporations, with no member holding more than one seat . . . [t]he arrangement would, however, fit within two of the loopholes of section 8. The interlock would be indirect, since directors of competitors would be linked only by a third organization, the union. The interlock would also involve persons who hold only one directorship, and are officers or members, rather than directors, of the union. In order to reach employee representation of the character outlined above, section 8 would have to extend to directors of competitors who are not directors, but merely officers or members of a third organization. (citations omitted)

n398 *15 U.S.C. § 17* (1976).

n399 Steuer, supra note 391, at 279 n.152.

n400 Letter from Carol M. Thomas, Secretary Federal Trade Commission to UAW General Counsel John Fillion (May 1, 1981).

n401 Id. at 2.

n402 Id. at 2-3.

n403 Letter from Assistant Attorney General U.S. Dept. of Justice Antitrust Division Sanford M. Litvack, to UAW General Counsel John Fillion (Feb. 26, 1981) [hereinafter cited as Litvack letter].

n404 Id. at 2. The Antitrust Division referred to *United States v. Cleveland Trust Co., 392 F. Supp. 699 (N.D. Ohio 1974),* aff'd, *513 F.2d 633 (6th Cir. 1975)* and *United Mine Workers of America v. Coronado Coal Co., 259 U.S. 344 (1922)* to support its opinion, although neither is directly on point. In Cleveland Trust, the district court did not decide the question of whether a corporation could be a "director" within the meaning of section 8 of the Clayton Act, although the government's position was that it could. The court held that determination of such a question was not necessary to decide the government's motion for summary judgment. It went on to say that "the issue of deputization is a question of fact to be settled case by case." *392 F. Supp. at 712.* Thus, the government's citation of Cleveland Trust in its opinion letter to the UAW regarding the AMC board seat is only a reiteration of its position in Cleveland Trust on which the court never passed judgment.

In Coronado Coal, a union and its members were charged with conspiracy in restaint of trade for organizing and engaging in strikes and otherwise trying to prevent operation of nonunion mines. The United States Supreme Court found that the union was an "association" subject to the Sherman Act, but held that its actions did not violate the Act where the "motive" was "local." *259 U.S. at 409.* However, a finding in 1922 that a union was an "association" under antitrust law today because the Norris-LaGuardia Act of 1932, *29, U.S.C. §§ 101*-115, was created to curtail use of federal antitrust law in regulating labor disputes. Thus, the Coronado Coal construction of "association" under section 7 of the Sherman Act may not mean that section 8 should be construed to include unions as "associations" that could be deputized as "persons" prohibited from sitting on boards of directors of competing firms. The Antitrust Division's reliance on Coronado Coal, therefore, may have been misplaced.

n405 Litvack letter, supra note 403, at 2.

According to Phillip Areeda, a well-established antitrust authority, "The regulatory authorities have, as a matter of course, approved interlocks . . . (thus) unenthusiastic enforcement is perhaps the major reason why section 8 is virtually ignored today." P. AREEDA, ANTITRUST ANALYSIS, PROBLEMS, TEXT, CASES P669 (1967).

If that is so, why has the Department of Justice taken such a strict position regarding labor unions?

n406 Litvack letter, supra note 403, at 3. However, this refusal to issue an advisory opinion clearing the way for the UAW-AMC board member must not be viewed as a condemnation of that proposal as illegal. If Professor Areeda, supra note 405, is correct, the UAW and AMC, or similarly situated parties, might create union board seats without incurring Justice

Department litigation. If they did, they might prevail based on the theories suggested in supra text accompanying notes 398-402.

n407 Rath employees obtain full voting rights in the ESOT (Employee Stock Ownership Trust) as soon as they purchase shares under the plan. Their shares are held in the ESOT trust until they leave the company.

The Rath Plan provides for distribution, upon termination of employment, of either stock or cash at the option of the employee. See supra text accompanying notes 139, 140. However, under the present law, an ESOP plan that restricts ownership of substantially all the outstanding employer securities to employees may provide that an employee must take cash, rather than stock, upon termination. See *26 U.S.C. § 409A*(h)(2) (Supp. IV 1980); supra text accompanying note 140, as well as supra note 26. This amendment allows an ESOT perpetually to hold the stock majority it may obtain without the fear that it will be diluted by retirees selling their stock on the market or to other nonemployees upon retirement. See also infra notes 448-62.

n408 See supra notes 132, 143-47 and accompanying text.

n409 See supra text accompanying notes 145-56.

n410 Telephone interview with UFCW Staff Attorney Robert Funk (Feb. 25, 1982).

n411 May 13, 1980 UFCW Local P-46 and Rath Packing Co. Letter of Understanding, Appendix A to Rath Packing Co. Prospectus of Dec. 30, 1980 at A6.

n412 *Citizens Publishing Co. v. United States, 394 U.S. 131, 136-37 nn.2 & 3 (1969).*

n413 *15 U.S.C. § 18* (1976 & Supp. IV 1980).

n414 *394 U.S. at 137.*

n415 *Id. at 138.*

n416 *International Shoe Co. v. Federal Trade Comm'n, 280 U.S. 291 (1930):*

In light of the case thus disclosed of a corporation with resources so depleted and the prospect of rehabilitation so remote that it faced the grave probability of a business failure with resulting loss to its stockholders and injury to the communities where its plants were operated, we hold that the purchase of its capital stock by a competitor (there being no other prospective purchaser) not with a purchase to lessen competition, but to facilitate the accumulated business of the purchaser and with the effect of mitigating seriously injurious consequences otherwise probable, is not in contemplation of law prejudicial to the public and

does not substantially lessen competition or restrain commerce within the intent of the Clayton Act. (emphasis supplied)
Id. at 302-03.

n417 The fundamental purpose of the securities laws -- Securities Act of 1933, *15 U.S.C. § 77*(a) (1976); Securities Exchange Act of 1934, *15 U.S.C. § 78*(a) (1976); and state blue sky laws -- is to ensure that investors have access to sufficiently thorough and accurate information to make reasonable decisions regarding the purchase and sale of securities. *SEC v. Ralston Purina Co., 346 U.S. 119, 124 (1953)* (the ultimate test is whether the particular class of persons protected needs the protection of the Act). One of the chief concerns of these acts is to regulate purchases and sales by insiders who might use such information to the disadvantage of outside purchasers, especially where the securities are publicly traded. See Securities Exchange Act of 1934, *15 U.S.C. § 16*(d), *15 U.S.C. § 78*(a) (1976). Exemptions from these requirements are common, especially in situations involving private transactions in which the SEC or another securities agency believes that the intended purchaser has access to sufficient data on the status of the issuer to make an informed decision. See S.E.C. Rule 146, *17 C.F.R. § 230.146 (1976)*; Gresham, Employee Stock Ownership Plans: Obligations of the Sponsor and Protection of the Beneficiaries Under the Federal Securities Laws, *26 AM. U.L. REV. 569, 577 (1977).*

n418 Gresham, supra note 417, at 576-77.

n419 For further explanation of the different types of securities ramifications as regards various types of ESOPs, see J. MENKE, supra note 1, at 3191-99; Gresham, supra note 417, at 569-92. See also GAO STUDY, supra note 4, at 6-28, for a description of some of the problems of valuation and marketability of stock in ESOPs of closely held firms. Where there is no public market for the employer's stock in a closely held firm, it is probably wise for a union to have the stock independently appraised before agreeing to a negotiated plan that values the employer's stock at a specific amount.

n420 See J. MENKE, supra note 1, at 3191, 3199.

n421 Id. at 3191.

n422 Id.

n423 *SEC v. Ralston Purina, 346 U.S. 119 (1953).*

n424 *Id. at 121.*

n425 *Id. at 127.*

n426 See supra note 119; supra text accompanying notes 85-111.

n427 See supra text accompanying notes 83-103; Deak interview, supra note 45.

n428 Id.

n429 Rath, however, also sought and received IRS waivers that allowed for the underfunding of the Rath plan. See supra note 152 and accompanying text. Ultimately, the Rath pension plan was terminated. See supra notes 157-59 and accompanying text.

n430 *I.R.C. § 411(d)(3)(A)*, (B) (Supp. IV 1980); E.R.I.S.A. § 407(a), (b)(1), (d)(3)(A), *29 U.S.C. § 1107*(a), (b)(1), (d)(3)(A) (1976); see supra note 109.

n431 *I.R.C. § 411(d)(3)(A)*, (B) (Supp. IV 1980); E.R.I.S.A. § 407(a), (b)(1), (d)(3)(A), *29 U.S.C. § 1107*(a), (b)(1), (d)(3)(A) (1976).

n432 *I.R.C. § 411(d)(3)*; *Treas. Reg. § 1.402(a)-1(a)(1)* (1956).

n433 *29 U.S.C. § 1341*(f) provides that:

[A] plan [defined benefit plan covered by PBGC] with respect to which basic benefits are guaranteed shall be treated as terminated upon adoption of an amendment to such plan, if after giving effect to such amendment, the plan is a plan described in section 1321(b)1 of this title.

n434 E.R.I.S.A. *29 U.S.C. § 1341* (1976 & Supp. IV 1980); 29 C.F.R. §§ 2622.3 and 2622.9 (1981).

n435 See Ludwig, supra note 1, at 635.

n436 See supra notes 157-60 and accompanying text.

29 U.S.C. §§ 1341, 1341a (1976 & Supp. IV 1980) provide for termination of qualified pension plans. Upon formal "termination" of a plan certain ERISA protections and guarantees are activated for the beneficiaries, in particular, all allocated and funded covered pension benefits become vested as of the termination. These protections are not activated by a conversion of a pension plan to an ESOP. Moreover, upon termination the Pension Benefit Guarantee Corporation (PBGC) may place a lien on employer assets to pay plan benefits. *29 U.S.C. § 1368* (1976). A pension termination, therefore, may threaten the continued operation of an employer's business. See supra notes 430-34 and accompanying text.

Under *I.R.C. § 411(d)(3)* (1976), a qualified stock bonus, profit-sharing or pension plan must provide that:

(A) upon its termination or partial termination, or

(B) in the case of [stock bonus or profit-sharing plans] upon complete discontinuance of contributions under the plan, the rights of all affected employees to benefits accrued . . ., to the extent funded . . ., or the amounts credited to the employees' accounts, are nonforfeitable. With a conversion, the employer may be able to avoid the vesting of otherwise forfeitable employees rights in the prior plan. The vesting effects of conversion as compared with termination are explained in Ludwig, supra note 1, at 634-35 n.13 as follows:

A plan participant with less than five years employment whose employment is terminated will not normally be entitled to any benefit from the plan. [*I.R.C.] § 411(a)(2)*. If, however, the plan is terminated or discontinued before such an employee is terminated, the benefits accrued (or funded in the case of a pension plan) will become vested. Such vesting will not adversely affect the deferred-taxation status of the plan benefits, however, unless those benefits are, upon vesting, made available to the plan participants. See *Treas. Reg. § 1.402(a)-1(a)(1)* (1956).

Qualified plans are not considered "terminated" for purposes of § 411(d)(3)(A) if replaced with a "comparable" plan. *Treas. Reg. §§ 1.381(c)(11)-1(d)(4)*, *T.D. 6556, 1961-1 C.B. 129, 132-33;* 1.401-6(b)(1) (1963). Replacement of an existing plan by an ESOP is subject to this comparability requirement. Proposed Treas. Reg. § 54.4975-11(a)(3), *41 Fed. Reg. 31,836 (1976)*. Pension plans are generally comparable to other pension plans, and stock bonus and profit-sharing plans are comparable to each other. *Treas. Reg. §§ 1.381(c)(11)-1(d)(4)*, *T.D. 6556, 1961-1 C.B. 129, 132-33;* 1.401-6(b)(1) (1963) . . . .

Where, therefore, an existing stock bonus or profit-sharing plan is to be replaced with an ESOP, a necessary element of which is a stock bonus plan, it would appear that vesting would not occur whether the existing plan were terminated or converted. This is undoubtedly true where the prior plan contained the provision described in *I.R.C. § 411(d)(3)(A)* (relating to termination), which, by its terms, applies to all plans. Where, however, the existing plan contains the provision described in id. § 411(d)(3)(B) (relating to discontinuance of contributions under the plan), it would appear that vesting could be avoided only by converting the existing plan by amendment so that contributions to the plan will not be discontinued. This anomalous result is not clarified by the Treasury regulations which, in fact, imply that all plans must contain both provisions of § 411(d)(3). See temporary Treas. Reg. § 11.411(d)-2(a)(1), *T.D. 7387, 1975-2 C.B. 159, 179.*

n437 Some suggestions and cautions for unions negotiating ESOPs are provided in UAW Social Security Department, Employee Stock Ownership Plans, ESOPs, 15-21 (1977). These include: 1) cash held in a negotiated ESOP that is not invested in employer securities should only be invested in the safest form of short-term securities, such as United States Treasury notes or bonds; loose investment language should be avoided; 2) dividends should be paid to or accrue to the benefit of employees, and should not reduce company contributions; 3) unions should try to convince the company to pay for any "key man insurance" premiums in addition to its ESOP contributions instead of having them taken out of the employees' ESOP accounts; 4) stock need not be allocated on the basis of compensation; it can be allocated equally to all or on a point system considering seniority and excluding management bonuses; 5) investment losses should be allocated on the basis of compensation, especially if contribu-

tions are allocated on that basis, but gains should be allocated in proportion to the size of the employee's account; 6) the union should have at least equal representation with the company on the ESOP committee; and 7) the union should demand full disclosure of financial statements in order to make an intelligent decision on the ESOP proposal.

n438 See supra notes 2, 4.

n439 J. MENKE, supra note 1, at 3021.

n440 Id. at 3131-35 explains the federal income and estate tax consequences of ESOPs for employees pursuant to *I.R.C. §§ 401*, *402(a)*, (b), 402(e) (Supp. IV 1980) as follows:

Lump Sum Distributions

Under the Internal Revenue Code, as amended by ERISA, if an employee's entire interest is distributed to him or to his beneficiary in one taxable year because of the participant's retirement, attainment of age 59 1/2, total disability, death, or termination of employment, such distribution may be taxed under the favorable tax rules applicable to so-called "lump sum distributions. . . ."

If the distribution qualifies as a "lump sum distribution," the tax consequences to the participant or beneficiary upon distribution of the employer stock are as follows:

1. There is no tax to the extent the stock was purchased with the employee's own contributions.

2. There is no tax on the unrealized appreciation on the employer stock. . . .

3. Under Code § 402(e)(4)(D), the "total taxable amount" is defined as the amount of the distribution which exceeds the sum of amounts contributed by the employee and the net unrealized appreciation attributable to employer securities. . . .

4. The total taxable amount of the distribution is subject to a "minimum distribution allowance" which is tax free. If the total taxable amount of the distribution is less than $ 20,000, the minimum distribution allowance is 50% of such taxable amount. If the total taxable amount is greater than $ 20,000 but less than $ 70,000, the minimum distribution allowance is $ 10,000 less 20% of the amount of the taxable portion over $ 20,000.

5. The total taxable amount (as reduced by the minimum distribution allowance) attributable to participation in the plan after 1973 is taxed as ordinary income. . . .

6. The total taxable amount attributable to participation in the plan prior to 1973 is taxed at long-term capital gains rates. . . .

Installment Distributions

Unlike lump-sum distributions, installment distributions and other distributions that do not qualify as lump-sum distributions are taxed at ordinary income tax rates. . . .

Subsequent Sale of Stock

If the stock was received by the employee in a lump-sum distribution, the unrealized ap-

preciation is not taxed upon distribution but only upon subsequent sale. . . .

Death Subsequent to Distribution

If the employee dies after receiving his stock in a lump-sum distribution but before selling it, the stock will be includable in his estate at full market value but IRS has ruled that it will not receive a step-up in basis as is normally the case with property included in a decedent's estate. Rather, . . . such gain will be treated as "income in respect of a decedent" under Code § 691 and taxed as long-term capital gain upon subsequent sale. *Rev. Rul. 75-125, 1975-15 IRB 13.*

Death Prior to Distribution

If an employee dies prior to receiving full distribution from the trust, the undistributed portion is not included in his estate for federal estate tax purposes, provided the beneficiary is not the employee's estate but is a named beneficiary and provided the distribution is made in installments. . . .

Distribution at age 59 1/2

ERISA added a provision to the lump-sum distribution rules that permits an employee to receive a lump-sum distribution after attaining age 59 1/2 without termination of service. . . .

Final Distribution

. . . If the distribution [made as soon as the employee terminates] is of the entire amount, then in the employee's account, the distribution will qualify as a lump-sum distribution even though the plan makes a subsequent distribution of an amount equivalent to the employee's share of the last year's contribution. . . . [T]he last distribution will be taxable as ordinary income rather than as a part of a lump-sum distribution. . . .

Cash Distribution

. . . An employee who elects to receive cash instead of employer stock should be aware that he stands to lose a tax advantage by doing so. As noted above, when stock is distributed, there is no immediate tax on "unrealized appreciation" of the stock. Instead, upon a later sale of the stock, the difference between the "cost basis" of the stock (i.e., the ESOT's purchase price) and the fair market value of the stock on the date of distribution is taxed as a capital gain. When an employee elects to take cash, however, the general tax rules applying to distributions from a qualified plan will apply. The greatest tax advantage loss would occur where a participant would otherwise receive a distribution of employer stock with a low "cost basis" but a high fair market value at the time of distribution.
However, the cash received would still receive favorable capital gains tax treatment. *I.R.C. §§ 1201-1253* (1976 & Supp. IV 1980).

n441 See supra text accompanying notes 278-353; infra text accompanying note 447.

n442 See supra notes 417-25 and accompanying text.

n443 The ramifications of classifying a bargaining subject as permissive are explained in

C. MORRIS, THE DEVELOPING LABOR LAW ch. 16 (1971).

n444 See supra text accompanying notes 403-11.

n445 See supra note 74 and accompanying text.

n446 J. BANK, J. JONES & BRITISH STEEL CORPORATION EMPLOYEE DIRECTORS, WORKER DIRECTORS SPEAK (1977); Olsson interview, supra note 274.

n447 Taylor interviews, supra note 126.

n448 See supra notes 211-35 and accompanying text.

n449 D. Ellerman, Workers' Co-operatives: The Question of Legal Structure, supra note 238.

n450 *Johnson & Whyte, supra* note 237.

n451 The National Consumer Co-operative Bank was created because, among other reasons, co-operatives have traditionally had a hard time obtaining credit. NATIONAL CONSUMER CO-OPERATIVE BANK, 1981 ANNUAL REPORT 3 (1981). The Co-operative Bank primarily funds housing and consumer co-operatives, though as of March 31, 1982 its outstanding loans for producer co-operatives comprised 0.8% of its $ 91,147,528 in Title I loans and 5.68% of its $ 13,108,582 in Title II funds. Id. at 5.

n452 D. Ellerman, supra note 238.

n453 See supra text accompanying notes 44-160, 278-353, 447.

n454 ESOP stock must be distributed on a "nondiscriminatory" basis pursuant to *I.R.C. § 401(a)* 4, 5 (Supp. IV 1980), but "nondiscriminatory" is defined so that higher-paid employees may receive more stock, but only in proportion to their pay. Nothing in the Internal Revenue Code prohibits distribution of equal shares to all employees regardless of their pay rate.

n455 Unless the plan participant elects otherwise, the time at which the ESOP must begin to pay benefits is as follows:

. . . not later than the 60th day after the latest of the close of the plan year in which --

(A) the date on which the participant attains the earlier of age 65 or the normal retirement age specified under the plan,

(B) occurs the 10th anniversary of the year in which the participant commenced participation in the plan, or

(C) the participant terminates his service with the employer.
I.R.C. § 401(a)(14) (1976).

Under *I.R.C. § 409A(h)(2)*, as amended by ERTA, the plan may restrict ownership to current employees if the outstanding stock is or will become substantially employee owned. Under *I.R.C. § 409A(h)(4)*, as amended by ERTA, an ESOP participant has the right to exercise her put option within 60 days of the distribution date and has a new 60 day period to exercise the put option in the following plan year. A five-year installment note, payable in equal installments, may be given by the employer to the participant in lieu of a lump-sum payment to satisfy either option. No security is required to back the note. If the participant agrees, the note can be extended an additional five years, subject to adequate security on the extension. See *Treas. Reg. § 54.4975-7(b)(12)(iv)*, (v) (July 1982). See also R. FRISCH, ESOP, supra note 1, at 25; SENATE COMM. ON FINANCE, EMPLOYEE STOCK OWNERSHIP PLANS: AN EMPLOYER HANDBOOK 10-11 (1980).

n456 *I.R.C. § 409A(h)* (Supp. IV 1980) (made applicable to ESOPs by *I.R.C. § 4975(e)(7)* (Supp. IV 1980)) until changed by ERTA at *26 U.S.C. § 409A*(h)(2) (August 1981).

n457 Despault interview, supra note 46.

n458 See supra notes 26, 448-62 and accompanying text.

n459 Namar Foods in Washington, D.C. and San Francisco Solar Center. See Kurland, Combining an ESOP and a Co-operative, 1 EMPLOYEE OWNERSHIP 2 (1981).

n460 See ESOPs in 100% Employee-Owned Firms (1980). Co-operatives are not subject to corporate income taxes for any amount paid out as "patronage dividends." *I.R.C. § 1381* (1976). However, such patronage dividends are taxable income to the employees. See also D. Ellerman, supra note 3, at 9, who states:

A simpler tax break can be arranged for small workers' co-ops where the members' pay is relatively low. Then any annual net earnings, that the co-op is likely to see, could probably be declared as wage bonuses and deducted from taxable income on that basis. This probably would not raise any IRS eyebrows if it didn't raise the workers' income very far above the normal wages in that industry. . . . As always, the personal income tax must be paid on the total distribution of cash and IOU notes. When the IOU notes are issued, in either the patronage dividend or wage bonus tax breaks, then those notes would constitute a revolving loan fund that could be revolved on a seniority basis. This Revolving Loan Fund of IOU notes to members is, in effect, a part of the internal accounts, but it would be added to the co-operative balance sheet as the most subordinate form of external debt capital.

n461 Kurland, supra note 459, at 3.

n462 Namar Foods of Washington, D.C. is currently being purchased by its employees. According to Namar's attorney, Norman Kurland, they have established an ESOP within their co-operative. Namar is using the ESOP to obtain a tax-free loan to purchase the company. Employees accumulate stock credits in individual accounts that become vested over 10 years. When they leave their employment they can sell the vested value of their stock back to the company for cash. The company repurchases the stock and recycles it to new employees. Voting rights are not attached to this stock, but rather to another class of stock that has a fixed par value of $ 20 per share. Only Namar employees may purchase such stock after a 30 day probationary period. Each employee may buy only one voting share. Each worker must buy at least four shares of nonvoting stock at $ 20 each. The Solar Center, a solar insulation company established in 1977 in San Francisco, is also organized as a co-operative ESOP employing 22 people, 18 of whom are owners. Kurland, supra note 459, at 2.

n463 See supra text accompanying notes 160-211.

n464 D. LURIA & J. RUSSELL, supra note 10.