**Statement for the Record**
**House Committee on Ways and Means**
**Hearing on "Reaching America's Potential: Delivering Growth and Opportunity for All Americans"**
**February 2, 2016**

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On behalf of the Employee-Owned S Corporations of America (ESCA), thank you for the opportunity to submit comments to the House Committee on Ways and Means. We commend the Committee for its continued focus on policies to drive economic growth, which are essential in addressing the difficulties that continue to vex the U.S. economy, working Americans, and their families.

ESCA represents private employee-owned companies operating in every state across the nation, in industries ranging from heavy manufacturing to construction to school photography to grocery stores. The expansion of S corporation ESOPs (employee stock ownership plans) in recent years is testimony to the fact that these companies are a dynamic and growing part of our economy. Currently, about 3,000 companies are S corporation ESOPs, and they employ 470,000 workers across the country and support nearly a million jobs in all. We would respectfully suggest to the Committee that a vital means of promoting economic opportunity for working Americans is to expand the availability of S corporation ESOPs for more companies and their workers.

On January 26th, economist Jared Bernstein, former chief economist for Vice President Biden, who testified at this hearing, released new research that reflects the benefits of expanding private employee ownership of U.S. businesses. In remarks during the hearing, Congressman Kind requested that Bernstein's report be entered into the hearing record. By increasing ownership of business capital, the study shows, ESOPs reduce wealth and wage inequality among workers. The fact that they only do this on a small scale, Bernstein asserts, is due to the fact that there are limited numbers of ESOPs in the United States. More ESOP companies would, he made clear, have an even greater and more beneficial impact on closing the growing wage and inequality gap in the American workforce.

Other key findings from Bernstein's new study include:

- That ESOPs help to address growing wage gaps between top management and other workers because they generally pay their workers better (and that the ESOP benefits companies offer aren't generally a substitute for other compensation);
- That ESOP-owned companies provide more stable employment than other businesses, and private, employee-owned companies are better able to weather economic downturns (like the Great Recession);
- That there isn't much behind assertions that employees who are part of ESOPs are in danger of being 'over exposed' to company stock. Bernstein notes that the great majority of ESOP-owned companies provide employees with an additional 401(k) or other similar plan, making their ownership stake in the company additive and highly beneficial.

Bernstein's report expands on what we already know: S corporation ESOPs are doing exactly what Congress intended when it created them in the late 1990s - generating economic activity, creating jobs, and promoting retirement savings. By any measure, these companies have been a remarkable success story, and a bright spot in an economy characterized over the course of the last decade or more by sluggish growth, anemic job creation, worker insecurity and wealth inequality.

It stands to reason that companies with ESOPs have displayed a dynamism and vitality lacking in other sectors of our economy. An ownership stake in one's place of work is not only a reason to help drive to greater productivity, but it also inspires greater loyalty as workers consider themselves aligned with the fortunes of the business, and avoid adversarial dynamics that can emerge when employees are convinced that the interests of stockholders and corporate board members are at odds with their own. For workers in S corporation ESOP firms, what is good for ownership is good for them by definition.

The evidence is compelling that expanding the availability of S corporation ESOPs for more companies and their workers would not only boost the retirement savings of countless Americans, but would also create more jobs, generate more economic activity, and encourage the formation of businesses that are more stable and successful because they provide their employees with the kind of built-in incentives conducive to loyalty and productivity.

As the Ways and Means Committee contemplates pro-growth measures, ***we urge members to support tax policies that expand the availability of S corporation ESOPs, allowing more workers to own their businesses and benefit from the advantages that employee-ownership holds***.

Toward that end, H.R. 2096 --introduced by Committee members Dave Reichert and Ron Kind along with Reps. Pat Tiberi, Richard Neal, Erik Paulsen, Earl Blumenauer, Charles Boustany and Bill Pascrell -- would help to grow the number of private ESOP businesses in the United States, giving more workers the opportunity to build savings, reduce wealth and wage inequality, and retire with dignity. The measure includes provisions to extend the gain-deferral provisions of Code section 1042 to sales of employer stock to SESOPs, encourage the flow of bank capital to ESOP-owned S corporations, provide resources to small businesses contemplating making the transition to an ESOP, and ensure that SBA-certified small businesses do not lose their status by becoming employee owned. H.R. 2096 currently has 63 bipartisan cosponsors (including 21 members of the Ways and Means Committee)

We look forward to working with Committee members to advance H.R. 2096 toward this year. We thank the Committee for its continued championship of employee ownership through the S ESOP model, and more broadly for its work on pro-growth policies for working Americans.

**Additional Background on S Corporation ESOPs**
A Subchapter S corporation is a business entity that provides flow-through tax treatment to its shareholders. An employee stock ownership plan ("ESOP") is a qualified defined contribution plan that provides a company's workers with retirement savings through their investments in their employer's stock, ***at no cost to the worker.*** ESOPs are regulated by the Employee Retirement Income Security Act ("ERISA") just like pension funds, 401(k) plans, and other qualified retirement plans.

In 1996, in the Small Business Jobs Protection Act, Congress authorized the S corporation ESOP structure, effective January 1, 1998, with the goal of encouraging and expanding retirement savings by giving American workers a greater opportunity to have equity in the companies where they work.

In the Taxpayer Relief Act of 1997, Congress repealed the unrelated business income tax (UBIT) originally imposed on the ESOP for its share of S corporation income, enabling S corporation ESOPs to become a viable new business structure to benefit American workers. Seventeen years later, there are more than 2,600 S ESOP companies operating in every state of the nation, in industries ranging from heavy manufacturing to retail grocery stores, from construction to consulting. Because of the structure of S ESOP tax policy, S ESOPs are achieving exactly what Congress intended: generating unparalleled retirement savings for workers, providing good and resilient jobs in high-performing businesses, and creating important macroeconomic benefits in their communities.

Over the years, ESCA has worked closely with federal policymakers to ensure that S ESOPs hold true to their original purpose of encouraging broad employee ownership. We collaborated with members of your committee in 2000-2001 to craft anti-abuse rules that became section 409(p) of the Internal Revenue Code. These rules, enacted in the Economic Growth and Tax Relief Reconciliation Act (EGTRRA), now mandate that S ESOPs provide for broad-based employee ownership and establish strict repercussions for violations.

> As the report language for EGGTRA (H.R. Rep. No. 107-51, part 1, at 100 (2001) states: *The Committee continues to believe that S corporations should be able to encourage employee ownership through an ESOP. The Committee does not believe, however, that ESOPs should be used by S corporation owners to obtain inappropriate tax deferral or avoidance.*
>
> *Specifically, the Committee believes that the tax deferral opportunities provided by an S corporation ESOP should be limited to those situations in which there is broad-based employee coverage under the ESOP and the ESOP benefits rank-and-file employees as well as highly compensated employees and historical owners.*

Since enactment, Section 409(p) has been highly effective in ensuring that S ESOPs serve their purpose. As a result, S ESOPs have become perhaps the most effective retirement savings plan under federal law, and today the average S ESOP plan participant has significantly more money saved in their ESOP account than they do in their 401(k) account.

**The Unparalleled Performance of S ESOPs**
Many studies over the years have documented why and how S ESOPs have proven to be so powerful for both workers as a retirement savings and economic security tool, and how they have contributed substantially to communities and the broader national economy.

Last year, Ernst and Young's Quantitative Economics and Statistics (QUEST) practice issued a study showing that **S corporation ESOPs outperformed the S&P Total Returns Index in terms of total return**

**per participant by an impressively large margin (62%)**, net assets of S ESOP accounts in the aggregate increased over three-fold, and retirement distributions to workers in S ESOPs totaled nearly $30 billion from 2002 to 2012.

In a study released in 2014, data compiled by the National Center for Employee Ownership (NCEO) shows that private employee-owned businesses have strikingly fewer loan defaults than other businesses. **NCEO finds that the default rate on bank loans to ESOP companies during the period 2009-2013 was, on average, an unusually low 0.2 percent annually**. By contrast, mid-market companies in the U.S. typically default on comparable loans at an annual rate of 2 to 3.75 percent. The tenfold difference between the economic strength of employee-owned companies and other businesses highlights the fact that **private businesses which are owned by their employees have the incentives and vision that makes them more stable, more successful, and better for employees as well as the larger economy.**

A 2012 study by Alex Brill, a former chief economist and policy director to the Ways and Means Committee and tax advisor to the Simpson-Bowles deficit reduction commission, found that:

- Employment among surveyed S ESOP firms increased more than 60% from 2001-2011, while the private sector as a whole had flat or negative growth in the same period.
- In the struggling manufacturing industry in particular, the S ESOP structure has buffered against economic adversity and job loss.
- S ESOPs have significantly expanded the pool of US workers who are saving for retirement, while also boosting company productivity – something that has greatly benefited their employee-owners.

In his study, Brill notes that "in the context of the current tax reform debate that seeks to curtail existing tax expenditures in favor of lower statutory rates, policymakers should recognize the evidence in support of S ESOPs and their positive economic contribution."

In 2013, Brill produced a follow-on study entitled "Macroeconomic Impact of S ESOPs on the U.S. Economy." Key findings of that broader assessment revealed that:

- **the number of S ESOPs and the level of active participation (number of employee-owners) have more than doubled since 2002.**
- **total output from S ESOPs and the industries they support is nearly 2 percent of GDP.**
- **S ESOPs directly employ 470,000 workers and support nearly a million jobs in all.**
- **S ESOPs paid $29 billion in labor income to their employees, with $48 billion in additional income for supported jobs.**

Brill's study on the macroeconomic impact of S ESOPs built upon findings issued in 2008, in a 2008 University of Pennsylvania report, whose authors found that S ESOPs contribute ***$14 billion in new savings for their workers each year beyond the income those workers otherwise would have earned,*** and that S corporation ESOPs offer workers greater job stability and increased job satisfaction. The study also found that S corporation ESOPs' higher productivity, profitability, job stability and job growth generate a collective ***$19 billion in economic value that otherwise would not exist.***

The Brill and University of Pennsylvania studies reinforce other important evidence about S ESOPs that show how powerful they can be.

In a 2010 Georgetown University/McDonough School of Business study, two leading tax economists, former Treasury Department officials Phillip Swagel and Robert Carroll, reviewed the performance of a cross-section of S corporation ESOP companies during the early part of the prior recession and found that these companies performed better than other equivalent companies in terms of job creation, revenue growth, and worker retirement security. Specifically, Swagel and Carroll found that:

- **Companies that are S corporation ESOPs are proven job-creators, even during tough times.** While overall U.S. private employment in 2008 fell by 2.8%, employment in surveyed S corporation ESOP companies rose by 2%. Meanwhile, 2008 wages per worker in surveyed S corporation ESOP companies rose by 6%, while overall U.S. earnings per worker grew only half that much.

- **S corporation ESOP companies provided substantial and diversified retirement savings for their employee-owners at a time when most comparable companies did not**. Despite the difficult economic climate, surveyed S corporation ESOP companies increased contributions to retirement benefits for employees by 19%, while other U.S. companies increased their contributions to employee retirement accounts by less than 3%.

As the Ways and Means Committee continues to work on comprehensive tax reform, ESCA would be pleased to serve as a resource and we look forward to continuing this important dialogue about a corporate structure and retirement savings plan that is enabling hundreds of thousands of Americans to achieve the American dream at work.

*The Employee-Owned S Corporations of America ("ESCA") is the Washington, DC voice for employee-owned S corporations. ESCA's exclusive mission is to advance and protect S corporation ESOPs and the benefits they provide to the employees who own them. These companies have an important story to tell policymakers about the tremendous success of the S ESOP structure in generating long-term retirement savings for working Americans and their families. ESCA provides the vehicle and the voice for these efforts. ESCA represents employee-owners in every state in the nation.*

Statement for the Record for

**Full Committee Hearing**

**"Reaching America's Potential: Delivering Growth and Opportunity for All Americans"**

**February 2, 2016**

The following statement is submitted by The ESOP Association, located at 1200 $18^{th}$ Street, NW, #1125, Washington, D.C. 20036, phone 202-293-2971. The person who drafted the following statement is J. Michael Keeling, President, email michael@esopassociation.org

"Before setting forth the evidence why employee stock ownership plans, referred to as ESOPs, should be promoted and encouraged as a means of expanding our nation's growth for providing more opportunity for all citizens to share in our free enterprise system, it is appropriate to set forth what an ESOP is, and its history, for the past 41 years of laws promoting the creation and operation of employee stock ownership via the ESOP model.

## What Is an ESOP?

Unique among ERISA plans, an ESOP, by law, <u>must</u> <u>be</u> primarily invested in the highest class of stock of the plan sponsor and the stock may be acquired with borrowed funds. In practical terms, the plan sponsor may take on 'debt' to acquire shares of the sponsor, and not be engaged in a prohibited transaction if the shares are acquired by the ESOP trust at a price no greater than the fair market value.

## Brief History of ESOPs

The ESOP model of employee ownership actually has its roots in a compensation practice from the $19^{th}$ Century. (A recent book, **<u>The Citizen's Share</u>**, Blasi, Freeman, and Kruse, Yale Press, wrote a very convincing case, pages 1 – 56, that our founding fathers, such as Washington, Jefferson, Adams, Hamilton, et al, believed in broad ownership of productive assets as being essential to the survival of a democracy. President Lincoln's views, as evidenced by the Homestead Act, were also in sync with our founding fathers' views.)

As the U.S. economy moved into the industrial age, corporations with nationwide reach, and large numbers of employees emerged — Procter & Gamble, Montgomery Ward, and others. Leaders of these companies realized that some employees would work for many years, reach an age requiring retirement, and retire with no income. There was no $19^{th}$ Century safety net for retirees, and leaders of a number of national firms decided to set aside company stock for the employees to have when they retired, and to "cash in."

After World War I, and the ratification of the $16^{th}$ Amendment to the Constitution authorizing a national income tax, Congress recognized that taxing income was not so simple, and that many issues had arisen because the basic definition that income is anything of value received by an individual, and the general rule that an income tax should tax anything of value.

In response to questions of what income should be taxed, Congress developed the very first true income tax code, the Code of 1921.

In developing the Code, those firms that were setting aside stock for their retiring employees came to the House Committee on Ways and Means and asked — "Is the stock set aside for an employee's retirement taxable when set aside, and is the value of the stock an employer's compensation cost?"

The Ways and Means Committee decided no, it was not current income to the employee, but would be taxed when the employee realized the previously deferred income; and yes, the set aside was compensation, and thus a cost of business for the employer and thus deductible for income tax purposes.

Thus, the first deferred compensation plan recognized by Congress was the "stock bonus plan," the forerunner of today's ESOP.

Fast forward to post War World II and owners of privately-held businesses began to consider how to "exit" their businesses and "cash" in their non-tradable stock in the company they started and which had become successful because of the hard work of the company employees. While somewhat lost in history due to the fact that until the mid-1970s private letter rulings were not public documents, an owner in Alaska, followed by others, obtained permission from the IRS, in a non-public letter ruling, that the company could "buy" his stock with borrowed money, have the stock placed in the company's stock bonus plan, and have the stock allocated to the employees as the debt was paid off.

A true visionary in San Francisco, California, Dr. Louis O. Kelso, developed a comprehensive economic philosophy in using such a method for funding stock bonus plans to expand ownership in a capitalistic society and to facilitate capitalization of for-profit businesses. He and his law firm colleagues led the way in expanding the use of this method blessed by the letter rulings, and many correctly note that the first "ESOP" was the sale by exiting shareholders of the *Monterrey Press* north of San Francisco in 1957 to an ESOP.

By the mid-1950s, many, both conservative and liberals, were seeing abuses in the area of pensions, or tax qualified deferred compensation plans, which the tax laws sanctioned and encouraged. Evidence was overwhelming that some pension funds were investing in organized crime activities. Then there was the collapse of major U.S. employers, leaving employees with no retirement income as promised. As a result, a drive in Congress to "reform" the tax and labor laws governing tax qualified deferred compensation plans, or "retirement savings plans," led to the enactment of ERISA in 1974.

During Congressional work on these "tax qualified deferred compensation plans," a major influence on tax policy of that era, Senator Russell B. Long, long time chair of the Senate Committee on Finance, became a champion of the economic philosophy of Dr. Kelso, and made sure the new ERISA law sanctioned ESOPs.

His support for the ESOP model grew stronger with each passing year, and his leadership led to major enactment of tax laws promoting the creation and operation of ESOPs. The bulk of these laws passed in 1984, in legislation referred to as DEFRA, and the perfection of those laws were in the Tax Reform Act of 1986.

In 1984 and 1986, Ways and Means members on the Conference Committee with members of the Senate Finance Committee, accepted nearly all provisions in the Senate bill promoting ESOPs.

In 1997, it was the Ways and Means Committee, by unanimous vote, accepted an amendment to the 1997 tax bill permitting S corporations to sponsor ESOPs. Former Congresswoman Nancy Johnson authorized the amendment.

Many of these laws of the 1980s, and the "Johnson" amendment remain in the Code.

While casual observes mistakenly think only the Senate Finance Committee reviewed the impact of ESOPs on employees, their companies, and our economy, the Ways and Means Committee had four oversight hearings on ESOPs in the period of 1987-1990. And in 2014-2015, the Committee's work on laying a foundation for comprehensive tax reform, led to former Chair Camp's tax reform proposal <u>maintaining</u> all current tax laws that encourage the creation and operation of ESOPs.

To be noted, a major partner with Senator Long promoting ESOPs in the 80s through 1988, was former President Ronald Reagan, who often spoke of his view that widespread ownership of productive assets was the core of maintaining equitable wealth ratios in a capitalistic society.

In sum, the Ways and Means Committee has a long, and a recent history, of supporting more employee stock ownership via the ESOP model.

**ESOPs, Ways and Means, and the 114th Congress**

It is important to note support for employee stock ownership by members of Ways and Means.

While the national media and, men and women running to be their parties' nominees for President in 2016, love, and the word love is used on purpose, to refer to members of Congress – which of course includes all members of Ways and Means, as "stupid", corrupt, lackeys of special interest groups, who do not "get along" for the good, the fact is ESOPs enjoys support from both Democrats and Republicans, liberal, moderate, and conservative members of Ways and Means.

For example, on April 29, 2015, eight members of Ways and Means, four Republicans and four Democrats, introduced H.R. 2096 – Representatives Reichert, Kind, Tiberi, Neal, Paulsen, Blumenauer, Boustany, and Pascrell. (Summary of H.R. 2096, Attachment 1) Since then, eleven more members of H.R. 2096 have joined their colleagues. Five other Ways and Means Committee members co-sponsored the same bill (H.R. 4837) in the 113th Congress.

The question is **WHY?** Why has a bi-partisan group of women and men serving in the House renewed evidence of a mainstream view set forth by the Congress since 1975 that the expansion of employee stock ownership via the ESOP model would be good public policy?

Just to include in this statement for the record some of the evidence why employees, their companies, and our economy all benefit from being owners through an ESOP, below are quick summaries of respected findings over the past two decades.

1. Since the 2002 prestigious General Social Survey up to the recently released 2014 GSS, evidences clearly that companies with employee stock ownership are much more likely to have layoff rates that are significantly less than conventionally owned companies—3% in 2002 for companies with employee ownership, 9.2% conventionally owned; 2006, 2.3% versus 8.5%; 2010, 2.6% versus 12.3%; and 2014, 1.3% versus 9.5%. Most impressive are the 2010 numbers, reflecting layoffs during the Great Recession. (Note that further data crunching by the National Center for Employee Ownership indicated that the fact these companies with employee stock ownership had fewer layoffs generated $14 billion dollars due to employees paying income, Social Security, and Medicare taxes, and not taking Unemployment Compensation or Food Stamps, seven times more than the general revenue estimates for the "tax expenditures" of special ESOP tax rules.)

2. A study of 1100 ESOP companies in the late 90's, compared to counterparts in the same industry, by Rutgers Professors Dr. Blasi, and Kruse, evidenced the ESOP companies had better sales, more employment, and were by a rate of 16% greater than their competitors over an 11-year period to remain independent.

3. Highly valued as a one source of history and data about employee stock ownership, and the ESOP model in particular, is the book "*The Citizen's Share",* by Dr.'s Blasi, Kruse of Rutgers, and Dr. Freeman of Harvard. The easy to read volume contains reference to nearly all of the research over the past 30 years with regard to the performance of ESOPs, both as a wealth creation, retirement savings, and as a jobs policy.

Attachment 2 is a fuller summary of research and its data of the track record of ESOP companies, and their reward of average pay employees.

In sum, Chair Brady and members of the Committee on Ways and Means, there is ample data, and real world experience to continue the push by the Committee to increase employee stock ownership. Bottom line, ESOPs are more productive, more sustainable, with jobs controlled by U.S. interests."

# Attachment 1

## Summary of H.R. 2096
## "Promotion and Expansion of Private Employee Ownership Act of 2015"
## (Same as Last Congress H.R. 4837)

H.R. 2096 will:

1. Permit owners of S stock to sell the stock to an ESOP and defer the capital gains tax on his/her gain if the proceeds are reinvested in the equities of U.S. operating corporations as owners of C corporations stock have done under IRC 1042 since 1984;

2. Permit lenders to S corporations with 50% or more ownership through an ESOP to exclude 50% of the interest from the loan, if used to acquire stock for the ESOP;

3. Establish an office in the Department of Treasury to provide technical assistance to S corporations with ESOPs;

4. Provide that a small business, S or C, eligible for one of the many programs provided by the Small Business Administration to remain eligible for SBA programs if the company becomes owned 50% or more by and ESOP, and the workforce remains the same or nearly the same as before the establishment of the 50% ownership by employees through the ESOP.

General Explanation

1. As evidenced in [name of your company] employee stock ownership plans are benefiting [name of company], our employees, and [name of your city or town.]

2. There is ample macro-data evidencing that the benefits our ESOP provides to [name of company] is also the case in the vast majority of privately-held ESOP companies in America.

3. H.R.2096 is a modest proposal that will not cost any significant tax revenues, and will build even larger account balances for retired employee owners, who will pay more taxes on their ESOP distributions than the targeted tax expenditure for ESOPs in H.R. 2096. For example, more ESOPs will be created, certain existing ESOP small businesses will qualify for SBA loans, and all S ESOP private companies can access Treasury experts on the complex rules governing S ESOPs.

4. In short H.R. 2096 will address the growing concerns of individual access to ownership, equitable distribution of our nation's capitalism, in companies that are more productive, more profitable, and more sustainable providing locally controlled jobs.

# Attachment 2

## Employee Owner Impact Corporate Performance Positively Overwhelming Evidence ESOP Companies More Productive, More Profitable, and More Sustainable, Providing Locally Controlled Jobs

- During the Great Recession, employee stock owned companies laid off employees at a rate of less than 3%, whereas conventionally owned companies laid off at a rate greater than 12%. (Data source: 2010 General Social Survey.)

- Because employees of ESOP companies were four times more likely to retain jobs during the Great Recession, Federal government recognized savings of over $14 billion in 2010 compared to tax payments foregone by laid off employees of conventionally owned companies; in other words for every $1 in tax expenditures to promote employee stock ownership, the Federal government collected $13 in taxes. (Data Source: 2010 General Social Survey analyzed by National Center for Employee Ownership.)

- A survey of 1,400 ESOP companies in 2010 evidenced the average age of the companies' ESOPs were 15 years, and the average account balances for employees were nearly $200,000, much higher than data reported for average 401(k) account balances. (The ESOP Company Survey, 2010, of The ESOP Association's Corporate members.)

- According to 2012 General Social Survey, 13% of employees of employee stock-owned companies were thinking of seeking employment elsewhere, whereas 24% of the employees of conventionally-owned companies were considering leaving their current job.

- In the summer of 2014, the Employee Ownership Foundation released results from the 23rd Annual Economic Performance Survey (EPS) of ESOP companies. Since the Employee Ownership Foundation's annual economic survey began 23 years ago, a very high percentage, 93% of survey respondents, have consistently agreed that creating employee ownership through an ESOP was "a good business decision that has helped the company." It should be noted that this figure has been over 85% for the last 14 years the survey has been conducted. In addition, 76% of respondents indicated the ESOP positively affected the overall productivity of the employee owners. In terms of revenue and profitability --- 70% of respondents noted that revenue increased and 64% of respondents reported that profitability increased. In terms of stock value, the majority of respondents, 80%, stated the company's stock value increased as determined by outside independent valuations; 18% of the respondents reported a decline in share value; 2% reported no change. The survey also asked respondents what year the ESOP was established. Among those responding to this survey, the average age of the ESOP was 16 years with the average year for establishment being 1998.

- More than half of the ESOP companies have two retirement savings plan (primarily a 401(k)), whereas more than half of all companies have <u>no</u> retirement income savings plan. (Analysis of forms 5500, and Bureau of Labor Statistics by the National Center for Employee Ownership, funded by the Employee Ownership Foundation.)

- The average ESOP company (less than 200 employees) has sales $9 million more per year than its non-employee owned comparable competition. (June 2008 Dissertation, Dr. Brent Kramer, CUNY.)

- A study of 1100 ESOP companies over eleven years compared to 1100 comparable conventional owned companies evidenced the 1100 ESOP companies had better sales, more employment, and were more likely over the period to remain independent businesses by 16%. (Most detailed study of ESOP companies by Dr. Joseph Blasi, and Dr. Douglas Kruse, tenured professors, Rutgers University School of Labor and Management, 1999.)

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**Reforming America's Taxes Equitably (RATE) Coalition**
Statement for the Record
Ways & Means Committee Hearing on
**Reaching America's Potential: Delivering Growth and**
Opportunity for All Americans

February 2, 2016

If Members of Congress wish to take true and meaningful action on policies to promote job creation and economic growth, they should act on bipartisan momentum for comprehensive tax reform. That means setting the corporate rate at 25 percent or less and closing the loopholes. American job creators face an uncompetitive tax code. That's why America desperately needs an overhaul of that code. Without reform to our uncompetitive code, we can expect continued corporate inversions and the loss of jobs and investment to other countries with fairer tax codes. Our foreign competitors are continuing to lower their rates leaving the U.S. at an increasing competitive disadvantage. And so the notorious phenomenon of "corporate tax inversions," for example, continues.

The answer to the question posed by the committee in today's hearing is clear if we look back to the Tax Reform Act of 1986. By lowering the rates and broadening the base, that piece of bipartisan legislation brought about two full decades of steady economic growth.

It really happened, not only in the 80s, but also in the 60s, and with the enthusiastic support of both parties. Indeed, we can look back at that era, from roughly 1962 to 1986, and see a time when both parties were on board. If we are willing to learn the lessons of that era, including the way that each party chose to view tax-rate reductions, then there's hope, even in this era of rancorous partisanship for achieving something great for the American people.

Yet if we really do want to return to those good old days, we need first to remember the ideas that brought the two parties into agreement. It wasn't that they saw eye-to-eye—not at all. Then as now, they had divergent visions, and yet back then, they were nevertheless able to align their differences into a single legislative package. That was the art, one might say, of that era.

So what were these two visions? In a nutshell, Republicans saw tax-rate reductions as a boon to the private economy. That is, workers, savers, and investors would see more money; they would enjoy, in the parlance, a higher after-tax return.

By contrast, Democrats saw tax-rate reductions as a boon to the public economy. To be sure, Democrats agreed that tax cuts could stimulate the private economy, but that wasn't their main goal. Their main goal was for the government to have more money to spend.

The champion of this sort of thinking was John F. Kennedy. In 1960, Kennedy had campaigned for the White House on a pledge to "Get the country moving again." And by that he meant that Uncle Sam should do more—more to fight communism abroad, more to fight poverty at home.

In other words, JFK's vision was primarily a pubic vision: He wanted the government to have more money to do more things. So on December 14, 1962, when he said, in a speech to the New York Economic Club, "It is a paradoxical truth that tax rates are too high today and tax revenues are too low," he meant exactly what he said—rates too high, revenues too low. Yet Kennedy was shrewd enough to see that lobbying for a simple tax increase would be counter-productive, and probably not politically feasible. He took a more complex route to his goals; he embraced the "paradox," as he called it, that lowering tax rates would yield higher tax revenue.

Yes, in Kennedy's mind, the government needed more money. As he spoke at the Waldorf Hotel in Manhattan in 1962, the 35th President wasn't worried that savvy New York City investors would fail to see the advantage to them in lower tax rates. Instead, his message was bigger and broader, aimed at the larger national audience that might not have been as alert to the variables of marginal taxation and after-tax return.

Indeed, to get a better sense of Kennedy's argument in that era, we might consider what is probably his best-known quote about the economy: "A rising tide lifts all boats." We can note that those words were said in a speech delivered in late 1963, as he lobbied once more for the tax-rate reduction. (Those tax cuts would not, in fact, occur in Kennedy's lifetime; they were not enacted until 1964—then, as now, Congress moved slowly.) Yet because JFK's words about a "rising tide" were uttered during his tax-cut campaign, it is often assumed that this rising tide had something to do with tax cuts. And in a way, they did—but only in a paradoxical way, only indirectly. As we shall see, Kennedy was referring, specifically, not to the positive impact of tax cuts, but to the positive impact of spending increases—yet gained, to be sure, by those very same cuts.

On October 3, 1963, JFK traveled to Heber Springs, Arkansas, to dedicate the Greers Ferry Dam. In his remarks that day, he was at pains to delineate the public benefits of public-works projects: "A rising tide lifts all the boats, and as Arkansas becomes more prosperous so does the United States."

That is, Americans didn't have to calculate their after-tax return, nor did they need to trust, in any way, the "magic of the marketplace" to see the benefit of his policies. Instead, thanks to greater prosperity and greater revenues, all they had to do was look out their window and enjoy the many benefits of their new dam.

And that was Kennedy's bold idea. He himself was fully aware of the stimulatory effect of tax cuts, but what he wanted to sell, especially to his fellow Democrats, was the benefit of that stimulus—higher tax revenues that could be spent on public works, such as the Greers Ferry dam.

One Republican who agreed with Kennedy was another JFK: Jack F. Kemp. Kemp, born in 1935, was very much a member of Kennedy's New Frontier generation. And so, in the 70s and 80s, it was easy for Kemp, a "supply side" Republican, to say that the purpose of tax-rate reductions was to give more to workers, savers, and investors. That was the Republican message. And yet at the same time, Kemp could say, echoing JFK, that the goal was also to generate more tax revenue for social programs. That was a message that spoke to Democrats and made Kemp such an important "crossover figure" and bipartisan bridge-builder. And so such staunch Republicans as Ronald Reagan, and such staunch Democrats as Lloyd Bentsen, both became persuaded by Kemp's way of thinking, which, as we have seen, was tried-and-true, even as it was fresh.

Many Republicans came to regard Kemp as a "big government" conservative, and in the minds of some, that jibe was justified. However, he was the intellectual champion of the two great tax-rate reductions of the 80s, in 1981 and 1986.

Thus we can see, at the risk of overusing the word, a further "paradox": Tax-rate reductions, as Kennedy and Kemp foresaw in their different eras, would so stimulate the economy that revenues would increase as well. And that was good news for Democrats, even those who mistrusted the private sector. Meanwhile, Republicans, who mistrusted the public sector—and thus wouldn't want the government to have more money—would have to make a calculation: Did their affection for private economic growth exceed their hostility toward an enlarged public sector?

During the Reagan years, everything came together—for both parties. Federal revenues soared, from $617 billion in fiscal 1982 to $991 billion in fiscal 1989, and yes, this revenue-surge happened even as the top personal tax rate was cut from 70 percent to 28 percent and the corporate tax rate from 46 percent to 34 percent. So was this a victory, or a defeat, for Republicans? To Reagan and Kemp, it was undeniably a victory, because real GDP rose by more than a third in that era. But many Democrats had voted for the '81 and '86 tax reforms as well, and for them, too, it was a victory: After all, federal spending rose by more than half during the Reagan years.

As we have seen, in that golden quarter-century, 1962 to 1986, both parties preferred to go with their hopes, not their fears. They voted, together, for growth.

We hope that this Congress agrees that we need that same spirit of bipartisan problem-solving today.