



D.C. Cooperative Business Ownership and Development Act¹

¹ The model act for this legislation was drafted by Christopher Michael and modified for use in D.C. by Kevin Gustafson. Both would like to thank all those who provided feedback on this draft.

SECTION 1. FINDINGS AND INTENT.

Cooperative, employee owned and operated business is a mainstream aspect of the U.S. economy with approximately 13.5 million workers participating in some form of employee ownership program at over 7,000 companies. The vast majority of such programs were the result of a transfer from traditional business owners to employees and in accordance with federal law² that seeks to facilitate such transfers. Cooperative ownership transfers are in the interest of business owners who seek to liquidate their ownership interest and/or retire. These transfers are also in the interest of the employees, who gain the opportunity to ensure the survival of the firm and their jobs, while gaining genuine ownership stake in their business and community.

In 2010, the DC City Council enacted a sweeping business association law, titled “District of Columbia Official Code Title 29 (Business Organizations) Enactment Act of 2010.” In it, the council defined a number of different types of business organizations, namely corporations, partnerships, non-profits, but also cooperative associations. Codified as DC Code § 29–900-939 (General Cooperative Associations) and §§ 29-1001-1015 (Limited Cooperative Associations) the law provides the definitions and necessary features of cooperatives recognized under DC law. The Council knew then that adding such provisions would allow District citizens to organize these important enterprises.

This Act aims to continue and build upon the council’s efforts, especially in under-served and underprivileged areas, by amplifying federal programs in support of employee ownership at the district level, proposing policies, addressing significant policy gaps, and creating programs to assist cooperative development and facilitation of transfers from privately held to cooperative business throughout the District through:

- (a) Tax incentives that promote a variety of broad-based employee ownership structures and encourage perpetual employee ownership.
- (b) Specific funding streams to facilitate cooperative development, and community control and ownership over essential services.
- (c) Loans and loan guarantees that provide financing for the conversion of existing businesses to employee ownership.

² Such as IRC § 4975(e)(7) and IRC § 409.

- (d) Procurement preferences that leverage public spending to benefit employee-owned businesses.
- (e) Establishes an education and advocacy center educate the public about the advantages of being a worker cooperative, learn how to start and run cooperative associations, and advocate for increased governmental support for cooperatives.

SECTION 2. DEFINITIONS.

In this Act:

- (a) "Office" means the District of Columbia Office of Tax and Revenue.
- (b) "Contracting agency" means the District of Columbia, or any department, board, commission, committee, authority, or agency of the District.
- (c) "Department" means the District of Columbia Department of Small and Local Business Development.
- (d) "Direct share ownership plan" means an arrangement in which a portion of the highest class of voting stock of a corporation or voting membership interest of a limited liability company is held directly by all tenured employees. Such stock or membership interest may be nontransferable and callable upon termination or retirement of the employee.
- (e) "Eligible transaction" means the qualified transfer of some or all of the stock of a corporation or membership interest of a limited liability company to an employee stock ownership plan, employee ownership trust, or direct share ownership plan. An eligible transaction includes an acquisition of stock or membership interest by an employee ownership association, as an intermediary, for the purpose of a qualified transfer to an employee stock ownership plan, employee ownership trust, or direct share ownership plan.
- (f) "Employee ownership association" means a business enterprise organized under DC Code § 29-900-939 (General Cooperative Associations) and §§ 29-1001-1015 (Limited Cooperative Associations).
- (g) "Employee ownership loan" means any of the following:
 - (1) Any loan to a corporation, limited liability company, employee stock ownership plan, employee ownership trust, or employee ownership association, to the extent that the proceeds are used to acquire employer stock or membership interest of an employer for a qualified transfer.
 - (2) Any loan to a corporation or limited liability company to the extent that, within 30 days, stock or membership interest of an employer are transferred to an employee stock ownership plan, employee ownership trust, or direct share ownership plan in an amount equal to the loan and in accordance with the terms of a qualified transfer.

- (h) "Employee ownership trust" means a trust, including a foreign trust, that holds the highest class of voting stock of a corporation or voting membership interest of a limited liability company and that meets the requirements under section 2A, and may be a noncharitable trust, perpetual trust, or both.
- (i) "Employee stock ownership plan" means an employee stock ownership plan as defined in section 4975(e)(7) of the Internal Revenue Code.
- (j) "Employer" includes 2 or more persons who are treated as a single employer under sections 414(b), (c), (m), or (o) of the Internal Revenue Code.
- (k) "Qualified transfer" means the transfer of any amount of stock of a corporation or membership interest of a limited liability company to an employee ownership association, employee stock ownership plan, or employee ownership trust if all of the following apply:
 - (1) The stock or membership interest has voting power equal to or in excess of the class of stock or membership interest of the employer having the greatest voting power.
 - (2) The stock or membership interest has dividend rights equal to or in excess of the class of stock or membership interest of the employer having the greatest dividend rights.
 - (3) If the transfer is to a direct share ownership plan, the largest amount of stock or membership interest transferred to any employee does not exceed a multiple of 10 times the smallest amount of stock or membership interest transferred to any tenured employee.
- (l) "Procurement" means the entire process of purchasing goods that includes the purchasing decision, the selection of the goods, and the payment made by the buyer to purchase the goods. It involves (1) planning the purchase, (2) determining purchasing standards, (3) developing purchasing specifications, (4) researching and selecting suppliers, (5) analyzing the value of potential purchases, (6) financing purchases, (7) negotiating the price of purchases, (8) purchasing logistics, (9) administration of purchasing contracts, (10) controlling the inventory of purchases and (11) disposing of residual supplies.
- (m) "Salary" means financial compensation an employee receives for performing the job, which is part of an employee compensation package. Salary can be provided on an hourly, daily, weekly, monthly, or yearly,

basis. Salary may also include overtime pay, bonuses, and commissions.

- (n) "Seniority" means a precedence of position, especially precedence over others of the same rank by reason of a longer span of service.
- (o) "Tax incentive" means a feature of the taxation system that encourages or discourages certain economic activities. It can be an inducement offered in the form of abatement of taxes.
- (p) "Tenured employee" means any employee or independent contractor who has provided at least 1,000 hours (approximately 6 months of full-time employment) of services to the employer within the immediately preceding 12-month period unless, with respect to an employee ownership trust or an employee ownership association, the by-laws have established a lower number of hours.
- (q) "Total cost" means all reasonable and necessary costs to be incurred in the course of an eligible transaction, including the fair market value of the business interest to be acquired, as well as costs for any additional construction, land acquisition, improvements, equipment, pertinent rights and easements, and associated technical, engineering, legal, and financial services.
- (r) "Trustee" means a person appointed, or required by law, to execute a trust; one in whom an estate, interest, or power is vested, under an express or implied agreement to administer or exercise it for the benefit or to the use of another.

SECTION 3. TAX INCENTIVES FOR EMPLOYEE OWNERSHIP

To encourage the use of employee ownership associations as the vehicle for economic development and growth, the City Council of the District of Columbia seeks to incentivize the transfer of enterprises already existing in the city from sole proprietorships, partnerships, limited liability companies and other ownerships structures, to employee ownership associations through the following acts:

- (a) Establishment of the D.C. Cooperative Development Program.
 - (1) The department shall establish and administer an economic development program under this section to incentivize the creation of employee ownership associations or facilitate the sale of business enterprises to employee ownership associations through various tax incentives to eligible applicants.

- (b) Capital Gains Exclusion.
 - (1) Gross income of a business transferring ownership to a certified employee ownership association shall not include any of the gain or income from a qualified transfer, except;
 - (2) That the gain or income from a qualified transfer to an employee ownership association which exceeds the smallest amount of stock or membership interest transferred to a tenured employee multiplied by the number of all tenured employees.

- (c) Interest Income Exclusion.
 - (1) Gross income of a bank or other commercial lender shall not include any of the interest income derived from an employee ownership loan.

- (d) Corporate Income Exclusion.
 - (1) Contributions to an employment ownership association, including contributions applied to repayment of the principal and interest on an employee ownership loan, are excluded from the gross income of the contributing party.
 - (2) The exclusion under subsection (d)(1) is subject to the limits under section 404(a)(3)(A) of the Internal Revenue Code. The amount of the exclusion under subsection (d)(1) for contributions to an employment ownership association may not exceed the value in the taxable year of the smallest amount of stock or membership interest distributed to a

tenured employee multiplied by the number of all tenured employees.

- (3) Contributions under this subsection (d) may be in cash, stock, or membership interest. For purposes of this subsection (d), the taxpayer shall submit with the taxpayer's return a copy of the findings of an independent appraiser regarding the fair market value of stock or membership interest.

(e) Trust Income Exclusion.

- (1) Any assets and/or income from an employee ownership trust shall be exempt from taxation.

(f) Individual Income Exclusion.

- (1) Gross income of an individual member of an employment ownership association shall not include stock or membership interest distributed through a direct share ownership plan, except;
- (2) that the amount of the income that may be excluded under subsection (f) may not exceed the amount of income derived in the taxable year from the smallest amount of stock or membership interest distributed to a tenured employee.

(g) Gift Tax Exclusion.

- (1) Any gift to an employment ownership association in accordance with the terms of a qualified transfer shall be exempt from gift tax.

(h) Optional Preapproval of Sale Price.

- (1) Application for preapproval of a qualified transfer for benefits under subsections (a) and (b) may be made at the time and in the manner as the District of Columbia Office of Tax and Revenue may prescribe. An application shall include the findings of an independent appraiser with respect to the fair market value of any stock or membership interest.
- (2) The Office shall make a preapproval decision, and inform the applicant of the Office's decision, no later than 30 days after the Office receives the applicant's application for preapproval of the sale price under subsection (g)(1). If the Office requests that an applicant supplement its application by submitting additional information, it shall have an additional 15 days after receiving the additional information by which it must make a preapproval decision and inform the applicant of the Office's decision.

SECTION 4. EMPLOYEE OWNERSHIP LOANS AND LOAN GUARANTEES.

(a) Establishment of Program.

- (1) The Department shall as part of the D.C. Cooperative Development Program establish and administer an economic development scheme under this section to make employee ownership loans and employee ownership loan guarantees to eligible applicants.

(b) Application.

- (1) Any employee ownership association may apply to the department for an employee ownership loan or employee ownership loan guarantee or both to finance an eligible transaction.

(c) Loans and Loan Guarantees.

The Department may contract with an applicant under subsection (b) to do any of the following:

- (1) Make an employee ownership loan to the applicant equal to up to 40 percent of the total start up or purchase cost.
- (2) Guarantee up to 100 percent of employee ownership loans made to the applicant by qualified lenders other than the department. All loan guarantees made to an applicant under subsection (c)(2) may not exceed 80 percent of the total cost.
- (3) Provide loans at below market-average and/or fixed interest rates as determined by the Department.

(d) Timeliness.

- (1) The Department shall make a loan decision or a loan guarantee decision under subsection (c), and inform the applicant of the Department's decision, no later than 30 days after the Department receives the applicant's application for an employee ownership loan or employee ownership loan guarantee under subsection (b). If the Department requests that an applicant supplement its application by submitting additional information, it shall have an additional 15 days after receiving the additional information, after which the Department must make a loan decision or loan guarantee decision under subsection (c) and inform the applicant of its decision.

SECTION 5. PUBLIC PROCUREMENT FOR EMPLOYEE OWNERSHIP ASSOCIATIONS.

(a) Cooperative Enterprise Certified Business Enterprise Categorization

- (1) A business enterprise that adopts an employee stock ownership plan, employee ownership trust, or direct share ownership plan and is incorporated under DC Code § 29–900-939 (General Cooperative Associations) and §§ 29-1001-1015 (Limited Cooperative Associations), will be eligible to be certified as a Local Business Enterprise system pursuant to D.C. Code § 2–218.31.
- (2) An additional subcategory of Local Business Enterprise system shall be added to the D.C. Code that incorporates the procurement and tax advantages therein enumerated.
- (3) Revocation - If any cooperative enterprise amends its bylaws to allow for share distributions that would not qualify it for cooperative status under DC Code § 29–900-939 (General Cooperative Associations) and §§ 29-1001-1015 (Limited Cooperative Associations), the department shall revoke the certification of said cooperative.

(b) Addition of Cooperative Associations to Minority and Women-Owned Business Assessment Program.

- (1) The Department program to support Minority and Women-Owned Business Assessment Program shall henceforth include Cooperative Associations incorporated under DC Code § 29–900-939 (General Cooperative Associations) and §§ 29-1001-1015 (Limited Cooperative Associations).
- (2) The program will:
 - i. Analyze the current state of Cooperative Associations qualifying as Certified Business Enterprises (“CBE”) as that term is defined in subchapter IX-A of chapter § 2-218.01 et seq., including counting the number of cooperative associations that have applied for CBE certification and the number that have been certified as CBEs since the inception of the CBE program;
 - ii. Record and track the number of cooperative associations that have been awarded government contracts under the procurement process utilized by the District; and
 - iii. Assess the findings, investigate, and recommend ways to encourage cooperative associations to compete in the procurement process

- utilized by the District.
- iv. The Department shall submit the findings and recommendations of the Program to the Chairman of the Council's Committee on Economic Development in the form of a report or reports. Specific steps for implementing the recommendations shall accompany the report or reports.

SECTION 6. COMMUNITY-BASED EMPLOYEE OWNERSHIP AND DEVELOPMENT CENTER.

(a) Establishment of Center.

- (1) Not later than 180 days after the date of enactment of this section, the department shall open bidding for organizations to be determined by the department as the D.C. Center for Employee Ownership.
- (2) The department shall announce the organization chosen to establish the Center within 30 days of the closing of the bidding process.
- (3) The council shall provide initial funding at an amount decided in the 2019 city budget to assist the organization in establishing the Center.

(b) Duties of the Center.

The Center shall:

- (1) Provide education and outreach to inform business owners about the benefits of employee ownership successions and the provisions of this Act.
- (2) Organize workshops and conferences on employee ownership successions.
- (3) Prepare and distribute materials concerning employee ownership successions.
- (4) Provide initial consultations to business owners exploring the possibility of transferring full or partial ownership to employees.
- (5) Provide a referral service to help business owners find legal, financial, and technical advice in connection with employee ownership successions.
- (6) Partner with key organizations, such as professional and trade associations, financial institutions, unions, economic development organizations, and other nonprofit entities, to promote employee ownership successions.
- (7) Support the growth of associations of employee-owned businesses.

(c) Government Relations.

The center shall:

- (1) Provide access to information regarding government rules and regulations that relate to employee ownership.
- (2) Develop, in partnership with appropriate government agencies, proposals for changes in policies to promote employee ownership.
- (3) Conduct investigations, research, studies, and analyses on the subject of employee ownership.
- (4) Elect a board member of the District's Workforce Investment Council (WIC) to assist it directing additional assistance to cooperative enterprises.