

## Client Alert

### ESOP Stock Valuations and COVID 19 Concerns

March 24, 2020

Companies that sponsor employee stock ownership plans (“ESOPs”) that expect to make material payments to ESOP participants in 2020 should consider an “interim valuation” of their stock if COVID 19 has materially affected their businesses.

Payouts from ESOPs to eligible participants must be based on the stock value on the most recent “valuation date” stated in the ESOP plan document. For example, under a calendar year ESOP, payments made in 2020 are ordinarily based on the December 31, 2019 stock valuation. When a company’s stock value declines, payouts based on a “stale” stock valuation can place an undue financial burden on the ESOP sponsor that is obliged to buy the stock back to fund employee distributions. This situation has led to litigation in the past (*see: Armstrong v. Amsted Indus. Inc., N.D. Ill. July 30, 2004*).

ESOP valuation firms are generally required to base their stock valuations on information that was “known or knowable” on the ESOP’s valuation date. As a result, a December 31, 2019 valuation cannot take into account a March 2020 downturn in business – it can only reflect what was known or knowable on December 31, 2019. Thus, unless ESOP sponsors take action now, 2020 payouts to ESOP participants may be based on a stock value that materially exceeds the stock value at the time of the payout.

One solution, if the ESOP plan document allows it, is to commission an interim stock valuation. For example, if a new stock valuation takes place on May 1, 2020, any payouts after May 1, 2020 can be based on the updated valuation.

For ESOP sponsors with material ESOP payouts scheduled for 2020, there are two steps to consider: (1) confirm whether your ESOP plan document permits interim valuations, or whether it would need to be amended to permit such valuations, and (2) compare the potential savings from reduced buyback costs with the cost of obtaining an interim valuation.

We are here to help. For further information, please feel free to get in touch with:

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Morrison Cohen LLP has created the COVID-19 Resource Taskforce, a multidisciplinary taskforce comprised of attorneys with deep expertise in a broad range of legal areas, to assist clients navigating the challenging and uncertain business and legal environment caused by the COVID-19 pandemic. We encourage clients to utilize our capabilities by reaching out to their primary Morrison Cohen attorney contact, who will put you in touch with the appropriate Taskforce person. You may also reach out directly to Joe Moldovan and Alec Nealon, the Taskforce co-chairs:

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