



Washington State Liquor and Cannabis Board

Topic: Petition for Adoption, Amendment, or Repeal of a State Administrative Rule – (WAC 314-55-035) Employee Stock Ownership Plans (ESOP)

Date: May 22, 2024

Presented by: Daniel Jacobs, Policy & Rules Coordinator

DISCLAIMER

This response to a petition for adoption, repeal or amendment of a state administrative rule is drafted pursuant to [RCW 34.05.330](#) and [chapter 82.05 WAC](#). This is for general information purposes only and should not be construed as legal advice or individual advice for specific problems.

Background

On March 26, 2024, Vicki Christopherson on behalf of the Washington Cannabusiness Association, submitted a petition for rulemaking to the Washington State Liquor and Cannabis Board (Board) requesting the Board initiate rulemaking to consider amending [WAC 314-55-035](#) to specifically contemplate an Employee Stock Ownership Plan (ESOP) business model for owning cannabis licensees and identify who and/or what in relation to an ESOP counts as a “true party of interest.”

Submitted with the Petition form was a letter included here:

This petition seeks to amend WAC 314-55-035 to (1) specifically contemplate cannabis businesses providing stock in their companies to their employees through Employee Stock Ownership Plans (ESOPs) and (2) establish who in a licensed business with an ESOP must be vetted as a “true party of interest.” Cannabis entrepreneurs should have the option of establishing an ESOP. Allowing Employee Stock Ownership Plans (ESOPs) as a viable option for cannabis businesses that brings new opportunities for both business owners and their valued employees.

Stock ownership is offered as a meaningful employee benefit in a variety of industries and could similarly be offered to cannabis employees. In addition to competitive salaries and comprehensive benefits, ESOP companies provide employees with unique wealth-building opportunities through stock ownership. This ensures that employees not only share in the success of the company but also have a pathway to financial security and prosperity. Stock ownership makes employees feel more a part of the success of the business and motivates performance.

ESOPs also benefit the companies that offer them. They serve as catalysts for enhanced employee engagement, paving the way for heightened productivity, innovation, and retention, all of which are vital for fostering superior business performance and sustainable growth. They also allow cannabis businesses to compete for talent in the workforce that may have a path to stock ownership in other industries.

Under the current rule, every employee with stock under an ESOP—no matter how small the percentage of ownership—would need to be vetted. This is simply impractical for the business, the employees, and the LCB. Therefore, who is a “true party of interest” must also be revised. The LCB can still ensure that the actual people that control the company—i.e., the larger shareholders and board/officers—are properly vetted and licensed.

The introduction of ESOPs for cannabis businesses represents a transformative opportunity to empower employees, foster job satisfaction, and promote long-term stability for cannabis businesses that choose to offer them. This can be accomplished with simple changes to the WAC while still preserving the integrity of true party of interest provisions and the LCB’s licensing mandate and processes.

Issue

Whether the Board should accept the petition to initiate the rulemaking process to consider amending WAC 314-55-035 to address the ESOP ownership model and who and/or what needs to be vetted as a “true party of interest.”

Statutes & Regulations

Legislation

Substitute Senate Bill 5096 ([chapter 392, Laws of 2023](#)) is known as the Expanding Employee Ownership Act and provided a statutory definition of “Employee Stock Ownership Plan” in Washington law.

Statutes

[26 USC § 280E](#) states that no deduction or credit shall be allowed for any amount paid or incurred during the taxable year in carrying on any trade or business if such trade or business (or the activities which comprise such trade or business) consists of trafficking in controlled substances (within the meaning of schedule I and II of the Controlled Substances Act) which is prohibited by Federal law or the law of any State in which such trade or business is conducted.

[26 USC § 4975\(e\)\(7\)](#) defines an “employee stock ownership plan” as a defined contribution plan which

- (A) which is a stock bonus plan which is qualified, or a stock bonus and a money purchase plan both of which are qualified under section 401(a), and which are designed to invest primarily in qualifying employer securities; and
- (B) which is otherwise defined in regulations prescribed by the Secretary.

A plan shall not be treated as an employee stock ownership plan unless it meets the requirements of section 409(h), section 409(o), and, if applicable, section 409(n) and

section 664(g) and, if the employer has a registration-type class of securities (as defined in section 409(e)(4)), it meets the requirements of section 409(e).

[RCW 69.50.342](#) identifies the rulemaking authority the Board has over matters related to cannabis.

[RCW 82.04.4488\(6\)\(c\)](#) states that "Employee stock ownership plan" has the same meaning as set forth in 26 U.S.C. Sec. 4975(e)(7), as of July 1, 2024.

Regulations

[WAC 314-07-035](#) is the true parties of interest rule for alcohol licensees.

[WAC 314-55-035](#) states that [a] cannabis license must be issued in the name(s) of the true party(ies) of interest. The board may conduct an investigation of any true party of interest who exercises control over the applicant's business operations. This may include financial and criminal background investigations.

[WAC 314-55-035\(1\)](#) states that [t]rue parties of interest must qualify to be listed on the license, and meet residency requirements consistent with this chapter. For purposes of this title, "true party of interest" means:

Entity	True party(ies) of interest
Sole proprietorship	Sole proprietor
General partnership	All partners
Limited partnership, limited liability partnership, or limited liability limited partnership	All general partners All limited partners
Limited liability company (LLC)	All LLC members All LLC managers
Privately held corporation	All corporate officers and directors (or persons with equivalent title) All stockholders
Multilevel ownership structures	All persons and entities that make up the ownership structure
Any entity(ies) or person(s) with a right to receive revenue, gross profit, or net profit, or exercising control over a licensed business	Any entity(ies) or person(s) with a right to receive some or all of the revenue, gross profit, or net profit from the licensed business during any full or partial calendar or fiscal year Any entity(ies) or person(s) who exercise(s) control over the licensed business
Nonprofit corporations	All individuals and entities having membership rights in accordance with the provisions of the articles of incorporation or bylaws

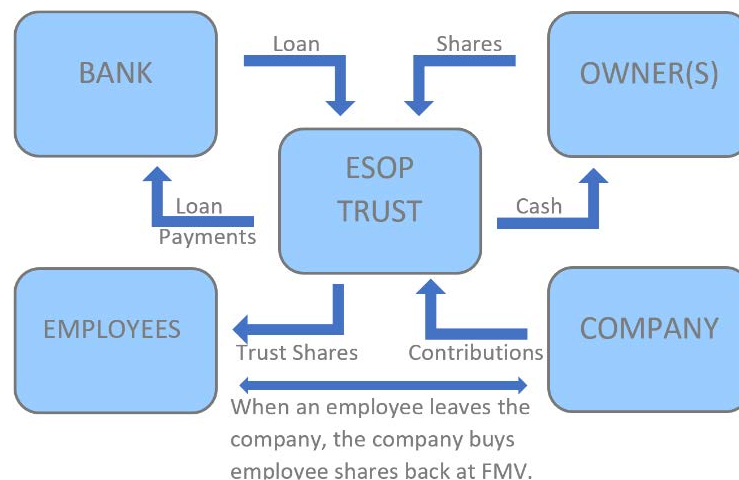
[WAC 314-55-035\(3\)\(b\)](#) defines a financial institution as any bank, mutual savings bank, consumer loan company, credit union, savings and loan association, trust company, or other lending institution under the jurisdiction of the department of financial institutions.

[WAC 314-55-035\(4\)\(g\)](#) states that, for purposes of this chapter, “true party of interest” does not include a financial institution.

Analysis

During the 2023 legislative session, the Washington state legislature passed [Substitute Senate Bill 5096](#) (known as the Expanding Employee Ownership Act) which defines an Employee Stock Ownership Plan (ESOP) by pointing to a federal statute, 26 USC § 4975(e)(7), which in turn defines it as a stock bonus contribution plan that meets a whole host of federal requirements.

The below is a diagram of how the basic structure of the financial arrangements that create an ESOP work:



In lay terms, an ESOP is a tax-qualified retirement plan that owns company stock.² A “sponsoring employer”, in this case, a cannabis licensee, will form an ESOP trust, and fund it, typically via loan. Those funds are used to buy the company’s shares, place them in the ESOP, along with annual financial contributions. Each year as the loan is paid down, the company adds shares pro rata to the employees’ ESOP accounts, based on how long they’ve been at the company. When an employee leaves, they get those shares held in the trust, which the company then buys from them at what is then fair market value

¹ Image copied from <https://www.wcl.american.edu/academics/experientialedu/clinical/theclinics/elc/tlcc/for-businesses-nonprofits/esops-info-sheet/#:~:text=An%20ESOP%20is%20an%20employee,flexibly%20out%20of%20the%20business>. (Last accessed 4/29/24)

² <https://www.cannabisbusinesstimes.com/news/esops-and-mewas-and-why-they-might-trend-in-cannabis/#:~:text=ESOPs%20are%20particularly%20hot%20in,from%20federal%20income%20tax%20and> (Last accessed 4/29/24).

(FMV). Thus, the longer the employee is at the company, the more shares they have in their ESOP trust account when they leave, and assuming each share is worth more by virtue of the company hopefully being worth more when they leave, this “retirement benefit” increases in value over time.³

Cannabis businesses, unlike all other businesses, are prohibited from deducting regular business expenses by 26 USC § 280E, which bars deductions for any business in the trade of “trafficking” in controlled substances as defined by the Controlled Substances Act, of which cannabis is still classified as Schedule I.

However, a company whose shares are entirely in an ESOP trust S-corporation (a closely-held entity that makes pass through elections on business incomes, deductions, credits etc., to its shareholders) is exempt from federal income tax. As such, an entity that is exempt from federal income tax does not need to worry about being barred from taking any federal income tax deductions, and thus can avoid the tax problems created by § 280E.

A quick online search of the terms “cannabis” and “ESOP” produces numerous results and recent news stories indicating that the avoidance of the § 280E tax burden is a primary motivating concern for cannabis businesses in their desire for ESOP formation.⁴ This topic is even the subject of a webinar scheduled to occur the day before this petition response is scheduled to be presented.⁵

While several cannabis licensees have approached Board agency staff in various settings about whether an ESOP structure would be approved by the Licensing division, no ESOP structure has been formally submitted to Licensing for approval. Preliminary discussions identified concerns with the true party of interest (TPI) analysis, and what type of entity an ESOP trust would qualify as under WAC 314-55-035. While some licensees have suggested that an ESOP trust would qualify as a financial institution under WAC 314-55-035(3)(b), and therefore not a true part of interest under WAC 314-55-035(4)(g), this theory has not been tested in practice.

The primary concern lies in the ESOP structure where the participating employees have a degree of control through trust management documents that is required by federal regulations for proper tax treatment and consideration as an ESOP. However, this same level of control may trigger TPI questions and thus the possibility that every participating employee would need to meet TPI requirements, such as Washington state residency.

³ Id.

⁴ <https://www.eisneramper.com/insights/cannabis/esops-cannabis-0324/> (Last accessed 4/29/24); <https://www.forbes.com/sites/dariosabaghi/2024/04/02/how-do-cannabis-employee-owned-companies-avoid-tax-burden/?sh=232e172c54e7> (last accessed 4/29/24); <https://www.greenmarketreport.com/theory-wellness-esop/> (last accessed 4/29/24).

⁵ <https://www.dentons.com/en/about-dentons/news-events-and-awards/events/2024/may/21/cannabis-esops-why-an-esop-is-an-industry-game-changer> (Last accessed 4/29/24).

The petitioner seeks to clarify this position by requesting rule language stating that participating employees in an ESOP do not need to be vetted per the TPI process solely by virtue of their participation in an ESOP.

Licensing staff having already flagged concerns, accepting the petition does not necessarily predetermine that changes to the rule language in WAC 314-55-035 would or should occur. However, due to the complexity of this topic, and the overlapping regulatory authorities of state and federal agencies, further exploration of this possible entity structure and how it could potentially comply with existing Washington state cannabis regulations would best be done through the formal rulemaking process.

Having reached out to multiple state agencies that regulate financial entities, Director's office staff have learned that the Department of Revenue is in the process of implementing [SSB 5096](#) and should the Board decide to approve this petition, such rulemaking would need to coordinate with the Department of Revenue, and likely other agencies involved in SSB 5096, such as the Department of Financial Institutions, Department of Commerce, and potentially the Secretary of State.

It should be noted SSB 5096 identifies the legislative intent is to encourage the growth of employee ownership structures through this expanding employee ownership act.

Divisional Coordination

Licensing – The Licensing division notes that changing the rule as requested would be a large policy shift and would require updates to licensing processes, forms, and letters. Licensing is unsure how the division would verify certain statutory requirements such as [RCW 69.50.325](#) which limits ownership or control to no more than five retailers, [RCW 69.50.328](#) which prohibits any cross-tier direct or indirect financial interest, and [RCW 69.50.339](#) requiring the licensee to submit to the board and obtain approval of any stock ownership change more than ten percent. Should this petition be accepted, the Licensing division would like to have further discussions to understand how this change might impact the social equity program.

Enforcement & Education – The Enforcement & Education division identified several potential concerns resulting if this rulemaking were to proceed and with potentially changing the rule language as requested by the Petitioner. It could create a significant impact with hidden ownership investigations if all “owners,” “TPI” or other “vested” parties are not properly vetted into licensing requirements. This may create additional barriers in investigating a member of an ESOP regarding hidden ownership or undue influence under this new petition. Out of state and unvetted partial owners are already a concern and this rule change would add challenges in investigating this if they are not considered a “larger shareholder.”

Additional issues may be seen including money laundering using employee contributions and payments as layering, and undue influence by use of ESOP or the benefit of.

If rule changes are to be made to the TPI rule, the Enforcement & Education division would recommend amending WAC 314-55-035 to align it as closely with [WAC 314-07-035](#) as possible. The language used in any potential revisions should define that people exercising control over the business have to be vetted. If a managers or supervisors have significant shares and are exercising control, then those people should be vetted. WAC 314-07-035 currently includes much more detailed language about LLC members, TPIs, and privately held corporations that should be added to WAC 314-55-035.

Finance – no impacts on the Finance division immediately identified.

IT – no IT impacts immediately identified.

Public Health – no public health impacts have been identified that would result from this rulemaking, should the petition be accepted.

Interagency Coordination

Department of Financial Institutions (DFI) – will need to consult regarding implementation of SSB 5096.

Department of Revenue (DOR) – will need to consult regarding implementation of SSB 5096.

Department of Commerce (Commerce) – will need to consult regarding implementation of SSB 5096.

Department of Labor & Industries – no immediate impact identified.

Department of Health - no immediate impact identified.

Department of Agriculture – no immediate impact identified.

Department of Ecology – no immediate impact identified.

Sovereign to Sovereign Consultations

There has not been an immediate impact identified that may impact Tribal governments any more so than any other cannabis licensees. The tax consequences and considerations that provide much of the benefit to the ESOP structure may not be present with Tribal businesses.

Recommendation

The Director's Office recommends the Board accept the rulemaking petition submitted by Vicki Christopherson on March 26, 2024. Given the complexity of the issues involved, it is likely rule language changes will be needed to allow for cannabis business to utilize

ESOP entity structure and still comply with existing Washington cannabis regulations. Accepting the petition for rulemaking does not necessarily mean the rule language will be changed as requested by the Petitioner. Further, it should be noted any rule development by LCB may be dependent upon other agency’s rule development, therefore the opening of a CR 101 may be delayed.

Board Action

After considering the recommendation of Director’s Office staff, the Board accepts/denies the petition for rulemaking submitted by Vicki Christopherson on March 26, 2024.

_____ Accept _____ Deny _____
David Postman, Chair Date

_____ Accept _____ Deny _____
Ollie Garrett, Board Member Date

_____ Accept _____ Deny _____
Jim Vollendroff, Board Member Date

Attachments:

- 1) Petition form and Letter from Petitioner



PETITION FOR ADOPTION, AMENDMENT, OR REPEAL OF A STATE ADMINISTRATIVE RULE

Print Form

In accordance with [RCW 34.05.330](#), the Office of Financial Management (OFM) created this form for individuals or groups who wish to petition a state agency or institution of higher education to adopt, amend, or repeal an administrative rule. You may use this form to submit your request. You also may contact agencies using other formats, such as a letter or email.

The agency or institution will give full consideration to your petition and will respond to you within 60 days of receiving your petition. For more information on the rule petition process, see Chapter 82-05 of the Washington Administrative Code (WAC) at <http://apps.leg.wa.gov/wac/default.aspx?cite=82-05>.

CONTACT INFORMATION *(please type or print)*

Petitioner's Name Vicki Christophersen
Name of Organization Washington CannaBusiness Association
Mailing Address PO Box 3329
City Kirkland State WA Zip Code 98033
Telephone 360.485.2026 Email vicki@christopherseninc.com

COMPLETING AND SENDING PETITION FORM

- Check all of the boxes that apply.
- Provide relevant examples.
- Include suggested language for a rule, if possible.
- Attach additional pages, if needed.
- Send your petition to the agency with authority to adopt or administer the rule. Here is a list of agencies and their rules coordinators: <http://www.leg.wa.gov/CodeReviser/Documents/RClist.htm>.

INFORMATION ON RULE PETITION

Agency responsible for adopting or administering the rule: _____

1. NEW RULE - I am requesting the agency to adopt a new rule.

The subject (or purpose) of this rule is: _____

The rule is needed because: _____

The new rule would affect the following people or groups: _____

2. AMEND RULE - I am requesting the agency to change an existing rule.

List rule number (WAC), if known: WAC 314-55-035 Qualifying for a cannabis license.

I am requesting the following change: See attached

This change is needed because: See attached

The effect of this rule change will be: See attached

The rule is not clearly or simply stated: _____

3. REPEAL RULE - I am requesting the agency to eliminate an existing rule.

List rule number (WAC), if known: _____

(Check one or more boxes)

It does not do what it was intended to do.

It is no longer needed because: _____

It imposes unreasonable costs: _____

The agency has no authority to make this rule: _____

It is applied differently to public and private parties: _____

It conflicts with another federal, state, or local law or rule. List conflicting law or rule, if known: _____

It duplicates another federal, state or local law or rule. List duplicate law or rule, if known: _____

Other (please explain): _____

Petitioner Name: Vicki Christophersen

Name of Organization: Washington CannaBusiness Association

Mailing address: PO Box 3329
Kirkland WA 98033

Email: vicki@christopherseninc.com

Phone: 360.485.2026

Petition to Washington State Liquor and Cannabis Board: Introducing Employee Stock Ownership Plans (ESOPs) for Cannabis Businesses

This petition seeks to amend WAC 314-55-035 to (1) specifically contemplate cannabis businesses providing stock in their companies to their employees through Employee Stock Ownership Plans (ESOPs) and (2) establish who in a licensed business with an ESOP must be vetted as a “true party of interest.” Cannabis entrepreneurs should have the option of establishing an ESOP. Allowing Employee Stock Ownership Plans (ESOPs) as a viable option for cannabis businesses that brings new opportunities for both business owners and their valued employees.

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The introduction of ESOPs for cannabis businesses represents a transformative opportunity to empower employees, foster job satisfaction, and promote long-term stability for cannabis businesses that choose to offer them. This can be accomplished with simple changes to the

WAC while still preserving the integrity of true party of interest provisions and the LCB's licensing mandate and processes.

CERTIFICATION OF ENROLLMENT

SUBSTITUTE SENATE BILL 5096

Chapter 392, Laws of 2023

68th Legislature
2023 Regular Session

EMPLOYEE OWNERSHIP PROGRAM

EFFECTIVE DATE: July 23, 2023—Except for sections 4 and 5, which
take effect July 1, 2024.

Passed by the Senate April 19, 2023
Yeas 48 Nays 0

DENNY HECK

President of the Senate

Passed by the House April 17, 2023
Yeas 96 Nays 0

LAURIE JINKINS

**Speaker of the House of
Representatives**

Approved May 9, 2023 2:25 PM

JAY INSLEE

Governor of the State of Washington

CERTIFICATE

I, Sarah Bannister, Secretary of
the Senate of the State of
Washington, do hereby certify that
the attached is **SUBSTITUTE SENATE
BILL 5096** as passed by the Senate
and the House of Representatives on
the dates hereon set forth.

SARAH BANNISTER

Secretary

FILED

May 10, 2023

**Secretary of State
State of Washington**

SUBSTITUTE SENATE BILL 5096

AS AMENDED BY THE HOUSE

Passed Legislature - 2023 Regular Session

State of Washington 68th Legislature 2023 Regular Session

By Senate Business, Financial Services, Gaming & Trade (originally sponsored by Senators Padden, Pedersen, Hasegawa, and Schoesler)

READ FIRST TIME 01/25/23.

1 AN ACT Relating to expanding employee ownership; adding new
2 sections to chapter 43.330 RCW; adding a new section to chapter 82.04
3 RCW; creating new sections; providing an effective date; and
4 providing an expiration date.

5 BE IT ENACTED BY THE LEGISLATURE OF THE STATE OF WASHINGTON:

6 NEW SECTION. **Sec. 1.** The legislature finds that:

7 Employee ownership in companies provides numerous benefits to
8 both businesses and workers across all industries. Research from the
9 national center for employee ownership found that one such structure,
10 employee stock ownership plans, had better workforce retention,
11 benefits and retirement security, and firm performance than
12 nonemployee stock ownership plans companies in the same industry. In
13 addition, the Rutgers school of management and labor relations found
14 that employee-owned companies outperformed nonemployee-owned
15 companies in job retention, pay, and workplace health safety
16 throughout the COVID-19 pandemic. At their core, employee ownership
17 structures allow employees to gain ownership stake in a business,
18 increasing their personal wealth without the risks related to
19 starting or purchasing their own company.

20 States throughout the nation have moved to provide support for
21 employee ownership structures. The Colorado employee ownership office

1 has operated since 2019 to create a network of technical support and
2 service providers considering employee ownership structures.
3 Recently, both California and Massachusetts passed legislation to
4 establish their own dedicated employee ownership support programs.
5 Other states, such as Iowa, provide tax benefits and upfront costs to
6 businesses interested in employee ownership.

7 Further, the federal government has recognized the benefit broad-
8 based employee ownership structures provide to communities. The
9 American rescue plan act included \$10,000,000,000 for the state small
10 business credit initiative. Through that act congress also directed
11 the treasury department to allow state small business credit
12 initiative funding to be used for transitions to employee ownership,
13 when state small business credit initiative funding has not been
14 historically available for business transactions.

15 The legislature desires to provide a dedicated program to educate
16 businesses on employee ownership, assist both owners and workers in
17 navigating available resources, reduce barriers to transitioning to
18 employee-owned structures, and provide tax support for businesses
19 that transition to an employee ownership structure.

20 Therefore, it is the intent of the legislature to encourage the
21 growth of employee ownership structures through this expanding
22 employee ownership act.

23 NEW SECTION. **Sec. 2.** A new section is added to chapter 43.330
24 RCW to read as follows:

25 (1) The Washington employee ownership program is created to
26 support the efforts of businesses considering a sale to an employee
27 ownership structure. The Washington employee ownership program must
28 be administered by the department and overseen by the Washington
29 employee ownership commission established in section 3 of this act.

30 (2)(a) In implementing the Washington employee ownership program,
31 the director must:

32 (i) Create a network of technical support and service providers
33 for businesses considering employee ownership structures;

34 (ii) Work with state agencies whose regulations and programs
35 affect employee-owned businesses, and businesses with the potential
36 to become employee owned, to enhance opportunities and reduce
37 barriers;

38 (iii) Partner with relevant private, nonprofit, and public
39 organizations including, but not limited to, professional and trade

1 associations, financial institutions, unions, small business
2 development centers, economic and workforce development
3 organizations, and nonprofit entities to promote employee ownership
4 benefits and succession models;

5 (iv) Develop and make available materials regarding employee
6 ownership benefits and succession models;

7 (v) Provide a referral service to help qualified business owners
8 find appropriate legal, financial, and technical employee ownership
9 resources and services;

10 (vi) Work with the department of financial institutions and
11 appropriate state, private, and nonprofit entities to shape and
12 implement guidance on lending to broad-based employee ownership
13 vehicles;

14 (vii) Create an inventory of employee-owned businesses in the
15 state including employee stock ownership plans, worker cooperatives,
16 and employee ownership trusts; and

17 (viii) Subject to the successful award of federal funding for
18 this purpose, establish a revolving loan program to assist existing
19 small businesses to finance a transition to employee ownership.

20 (b) Loans offered by the revolving loan program must be used to
21 help facilitate the purchase of an interest in an employee stock
22 ownership plan or worker-owned cooperative from the owner or owners
23 of a qualified business, provided that:

24 (i) The transaction results in the employee stock ownership plan
25 or worker cooperative holding a majority interest in the business, on
26 a fully diluted basis; and

27 (ii) If used to assist in the purchase of an interest in an
28 employee stock ownership plan, the employee stock ownership plan: (A)
29 Has appointed an independent trustee; or (B) has, as a trustee,
30 person, or entity, completed education on best practices for employee
31 stock ownership plans.

32 (c) Loans financing the sale of an interest to a worker
33 cooperative shall be extended based on repayment ability and shall
34 not require a personal or entity guarantee. In meeting the
35 requirement in (b) of this subsection, lending guidelines must be
36 established for worker cooperatives not based on any personal or
37 entity guarantees provided by the member owners or the selling
38 business owner. These guidelines may include but are not limited to
39 cash flow-based underwriting, character-based lending, and reliance
40 on business assets.

1 (d) In order to support the revolving loan program, the director
2 or the director's designee must apply for federal funding
3 opportunities that:

4 (i) Support capitalization of state revolving loan programs; and

5 (ii) Support businesses that seek to transition to employee
6 ownership.

7 (e) Amounts from the repayment of loans offered by the revolving
8 loan program must be deposited in the employee ownership revolving
9 loan program account established in section 6 of this act.

10 (3) The director or the director's designee may contract with
11 consultants, agents, or advisors necessary to further the purposes of
12 this section.

13 (4) By December 1st each year, the department must submit a
14 report to the appropriate committees of the legislature on program
15 activities and the number of employee-owned businesses and employee-
16 owned trusts in the state, including recommendations for improvement
17 and barriers for businesses considering employee ownership structures
18 in Washington state. The first report must include rules and
19 guidelines for the administration of the program, as established by
20 the Washington employee ownership commission.

21 (5) For the purposes of this section:

22 (a) "Employee-owned business" means:

23 (i) An employee cooperative established under chapter 23.78,
24 23.86, 23.100, or 24.06 RCW that has at least 50 percent of its board
25 of directors consisting of, and elected by, its employees; or

26 (ii) An entity owned in whole or in part by employee stock
27 ownership plans as defined in 26 U.S.C. Sec. 4975(e)(7).

28 (b) "Qualified business" means a person subject to tax under
29 Title 82 RCW, including but not limited to a C corporation, S
30 corporation, limited liability company, partnership, limited
31 liability partnership, sole proprietorship, or other similar pass-
32 through entity, that is not owned in whole or in part by an employee
33 ownership trust, that does not have an employee stock ownership plan,
34 or that is not, in whole or in part, a worker-owned cooperative.

35 (6) Program support shall only be made available to businesses
36 headquartered in Washington state. For the purposes of this section,
37 "headquartered in Washington state" means that Washington state is
38 its principal place of business or the state where it is
39 incorporated.

1 (7) The director shall adopt rules as necessary to implement this
2 section.

3 NEW SECTION. **Sec. 3.** A new section is added to chapter 43.330
4 RCW to read as follows:

5 (1) The Washington employee ownership commission is hereby
6 created to exercise the powers in developing and supervising the
7 program created in section 2 of this act.

8 (2) The commission shall consist of:

9 (a) One member from each of the two major caucuses of the house
10 of representatives to be appointed by the speaker of the house and
11 one member from each of the two major caucuses of the senate to be
12 appointed by the president of the senate. The initial term shall be
13 two years; and

14 (b) The following members appointed by the governor:

15 (i) Five members who represent the private sector or professional
16 organizations as follows:

17 (A) One representative of a worker cooperative business. The
18 initial term shall be four years;

19 (B) One representative of an employee stock ownership plan
20 business. The initial term shall be four years;

21 (C) One representative from a statewide business association. The
22 initial term shall be two years;

23 (D) One economic development expert, from the private sector,
24 with employee ownership knowledge and experience. The initial term
25 shall be four years; and

26 (E) One representative from a financial institution with
27 expertise in assisting businesses transitioning into an employee
28 ownership structure. The initial term shall be two years; and

29 (ii) Two members who represent the public sector as follows:

30 (A) One economic development expert, from the public sector. The
31 initial term shall be four years; and

32 (B) One representative from the department of commerce, who will
33 chair the first meeting prior to the election of the chair. The
34 initial term shall be four years.

35 (3) After the initial term of appointment, all members shall
36 serve terms of four years and shall hold office until successors are
37 appointed.

38 (4) The commission shall be led by a chair selected and voted on
39 by members of the commission. The chair shall serve a one-year term

1 but may serve more than one term if selected to do so by members of
2 the commission.

3 (5) The commission shall develop, in consultation with the
4 director, rules and guidelines to administer the program. Rules and
5 guidelines for the administration of the program must be included in
6 the first report to the legislature required in section 2 of this
7 act.

8 (6) Before making any appointments to the commission, the
9 governor must seek nominations from recognized organizations that
10 represent the entities or interests identified in this section. The
11 governor must select appointees to represent private sector
12 industries from a list of three nominations provided by the trade
13 associations representing the industry, unless no names are put forth
14 by the trade associations.

15 (7) The commission shall conduct market research for the purposes
16 of, or to support, a future application to the federal government for
17 a program to assist in the purchase of an interest in an employee
18 stock ownership plan qualifying under section 401 of the internal
19 revenue code, worker cooperative, or related broad-based employee
20 ownership vehicle.

21 (8) For purposes of this section, a "professional organization"
22 includes an entity whose members are engaged in a particular lawful
23 vocation, occupation, or field of activity of a specialized nature
24 including, but not limited to, associations, boards, educational
25 institutions, and nonprofit organizations.

26 NEW SECTION. **Sec. 4.** (1) This section is the tax preference
27 performance statement for the tax preference contained in section 5,
28 chapter . . . , Laws of 2023 (section 5 of this act). This performance
29 statement is only intended to be used for subsequent evaluation of
30 the tax preference. It is not intended to create a private right of
31 action by any party or be used to determine eligibility for
32 preferential tax treatment.

33 (2) The legislature categorizes this tax preference as one
34 intended to induce certain designated behavior by taxpayers, as
35 indicated in RCW 82.32.808(2)(a).

36 (3) It is the legislature's specific public policy objective to
37 encourage business owners to create an employee stock ownership plan
38 or employee ownership trust, or to convert to a worker-owned

1 cooperative, that allows the company to share ownership with their
2 employees without requiring employees to invest their own money.

3 (4) If a review finds that the number of businesses in this state
4 offering employee stock ownership plans, employee ownership trusts,
5 or ones that have converted to a worker-owned cooperative, has
6 increased because of the tax credit under this act, then the
7 legislature intends for the legislative auditor to recommend
8 extending the expiration date of the tax preference.

9 (5) In order to obtain the data necessary to perform the review
10 in subsection (4) of this section, the joint legislative audit and
11 review committee may access and use any relevant data collected by
12 the state.

13 NEW SECTION. **Sec. 5.** A new section is added to chapter 82.04
14 RCW to read as follows:

15 (1) Beginning July 1, 2024, in computing the tax imposed under
16 this chapter, a credit is allowed for costs related to converting a
17 qualifying business to a worker-owned cooperative, employee ownership
18 trust, or an employee stock ownership plan, as provided in this
19 section.

20 (2) The credit is equal to:

21 (a) Up to 50 percent of the conversion costs, not to exceed
22 \$25,000, incurred by a qualified business for converting the
23 qualified business to a worker-owned cooperative or an employee
24 ownership trust; or

25 (b) Up to 50 percent of the conversion costs, not to exceed
26 \$100,000, incurred by a qualified business for converting the
27 qualified business to an employee stock ownership plan.

28 (3)(a) Credit under this section is earned, and claimed against
29 taxes due under this chapter, for the tax reporting period in which
30 the conversion to a worker-owned cooperative, employee ownership
31 trust, or an employee stock ownership plan is complete, or subsequent
32 tax reporting periods as provided in (c) of this subsection.

33 (b) The credit must not exceed the tax otherwise due under this
34 chapter for the tax reporting period.

35 (c) Unused credit may be carried over and used in subsequent tax
36 reporting periods, except that no credit may be claimed more than 12
37 months from the end of the tax reporting period in which the credit
38 was earned.

39 (d) No refunds may be granted for credits under this section.

1 (4) (a) The total amount of credits authorized under this section
2 may not exceed an annual statewide limit of \$2,000,000.

3 (b) Credits must be authorized on a first-in-time basis.

4 (c) No credit may be earned, during any calendar year, on or
5 after the last day of the calendar month immediately following the
6 month the department has determined that \$2,000,000 in credit has
7 been earned.

8 (5) (a) The department may require persons claiming a credit under
9 this section to provide appropriate documentation, in a manner as
10 determined by the department, for the purposes of determining
11 eligibility under this section.

12 (b) Every person claiming a credit under this section must
13 preserve, for a period of five years, any documentation to
14 substantiate the amount of credit claimed.

15 (6) For the purposes of this section:

16 (a) "Conversion costs" means professional services, including
17 accounting, legal, and business advisory services, as detailed in the
18 guidelines issued by the department, for: (i) A feasibility study or
19 other preliminary assessments regarding a transition of a business to
20 an employee stock ownership plan, a worker-owned cooperative, or an
21 employee ownership trust; or (ii) the transition of a business to an
22 employee stock ownership plan, a worker-owned cooperative, or an
23 employee ownership trust.

24 (b) "Employee ownership trust" means an indirect form of employee
25 ownership in which a trust holds a controlling stake in a qualified
26 business and benefits all employees on an equal basis.

27 (c) "Employee stock ownership plan" has the same meaning as set
28 forth in 26 U.S.C. Sec. 4975(e)(7), as of the effective date of this
29 section.

30 (d) "Qualified business" means a person subject to tax under this
31 chapter, including but not limited to a C corporation, S corporation,
32 limited liability company, partnership, limited liability
33 partnership, sole proprietorship, or other similar pass-through
34 entity, that is not owned in whole or in part by an employee
35 ownership trust, that does not have an employee stock ownership plan,
36 or that is not, in whole or in part, a worker-owned cooperative, and
37 that is approved by the department for the tax credit in this
38 section.

39 (e) "Worker-owned cooperative" has the same meaning as set forth
40 in 26 U.S.C. Sec. 1042(c)(2), as of the effective date of this

1 section, or such subsequent dates as may be provided by rule by the
2 department, consistent with the purposes of this section.

3 (7) Credits allowed under this section can be earned for tax
4 reporting periods starting on or before June 30, 2029. No credits can
5 be claimed on returns filed for tax periods starting on or after July
6 1, 2030.

7 (8) This section expires July 1, 2030.

8 NEW SECTION. **Sec. 6.** A new section is added to chapter 43.330
9 RCW to read as follows:

10 The employee ownership revolving loan program account is created
11 in the custody of the state treasury. All transfers and
12 appropriations by the legislature, repayments of loans, private
13 contributions, and all other sources must be deposited into the
14 account. Expenditures from the account may be used only for the
15 purposes of the Washington employee ownership program created in
16 section 2 of this act. Only the director or the director's designee
17 may authorize expenditures from the account. The account is subject
18 to allotment procedures under chapter 43.88 RCW, but an appropriation
19 is not required for expenditures.

20 NEW SECTION. **Sec. 7.** Sections 4 and 5 of this act take effect
21 July 1, 2024.

22 NEW SECTION. **Sec. 8.** This act may be known and cited as the
23 expanding employee ownership act.

Passed by the Senate April 19, 2023.
Passed by the House April 17, 2023.
Approved by the Governor May 9, 2023.
Filed in Office of Secretary of State May 10, 2023.

--- END ---

26 USC 280E: Expenditures in connection with the illegal sale of drugs

Text contains those laws in effect on March 26, 2024

From Title 26-INTERNAL REVENUE CODE

Subtitle A-Income Taxes

CHAPTER 1-NORMAL TAXES AND SURTAXES

Subchapter B-Computation of Taxable Income

PART IX-ITEMS NOT DEDUCTIBLE

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§280E. Expenditures in connection with the illegal sale of drugs

No deduction or credit shall be allowed for any amount paid or incurred during the taxable year in carrying on any trade or business if such trade or business (or the activities which comprise such trade or business) consists of trafficking in controlled substances (within the meaning of schedule I and II of the Controlled Substances Act) which is prohibited by Federal law or the law of any State in which such trade or business is conducted.

(Added Pub. L. 97-248, title III, §351(a), Sept. 3, 1982, 96 Stat. 640 .)

EDITORIAL NOTES**REFERENCES IN TEXT**

The Controlled Substances Act, referred to in text, is title II of Pub. L. 91-513, Oct. 27, 1970, 84 Stat. 1242, which is classified principally to subchapter I (§801 et seq.) of chapter 13 of Title 21, Food and Drugs. Schedules I and II are set out in section 812 of Title 21. For complete classification of this Act to the Code, see Short Title note set out under section 801 of Title 21 and Tables.

STATUTORY NOTES AND RELATED SUBSIDIARIES**EFFECTIVE DATE**

Pub. L. 97-248, title III, §351(c), Sept. 3, 1982, 96 Stat. 640, provided that: "The amendments made by this section [enacting this section] shall apply to amounts paid or incurred after the date of the enactment of this Act [Sept. 3, 1982] in taxable years ending after such date."

26 USC 4975: Tax on prohibited transactions

Text contains those laws in effect on January 2, 2001

From Title 26-INTERNAL REVENUE CODE

Subtitle D-Miscellaneous Excise Taxes

CHAPTER 43-QUALIFIED PENSION, ETC., PLANS

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§4975. Tax on prohibited transactions**(a) Initial taxes on disqualified person**

There is hereby imposed a tax on each prohibited transaction. The rate of tax shall be equal to 15 percent of the amount involved with respect to the prohibited transaction for each year (or part thereof) in the taxable period. The tax imposed by this subsection shall be paid by any disqualified person who participates in the prohibited transaction (other than a fiduciary acting only as such).

(b) Additional taxes on disqualified person

In any case in which an initial tax is imposed by subsection (a) on a prohibited transaction and the transaction is not corrected within the taxable period, there is hereby imposed a tax equal to 100 percent of the amount involved. The tax imposed by this subsection shall be paid by any disqualified person who participated in the prohibited transaction (other than a fiduciary acting only as such).

(c) Prohibited transaction**(1) General rule**

For purposes of this section, the term "prohibited transaction" means any direct or indirect-

(A) sale or exchange, or leasing, of any property between a plan and a disqualified person;

(B) lending of money or other extension of credit between a plan and a disqualified person;

(C) furnishing of goods, services, or facilities between a plan and a disqualified person;

(D) transfer to, or use by or for the benefit of, a disqualified person of the income or assets of a plan;

(E) act by a disqualified person who is a fiduciary whereby he deals with the income or assets of a plan in his own interests or for his own account; or

(F) receipt of any consideration for his own personal account by any disqualified person who is a fiduciary from any party dealing with the plan in connection with a transaction involving the income or assets of the plan.

(2) Special exemption

The Secretary shall establish an exemption procedure for purposes of this subsection. Pursuant to such procedure, he may grant a conditional or unconditional exemption of any disqualified person or transaction, orders of disqualified persons or transactions, from all or part of the restrictions imposed by paragraph (1) of this subsection. Action under this subparagraph may be taken only after consultation and coordination with the Secretary of Labor. The Secretary may not grant an exemption under this paragraph unless he finds that such exemption is-

(A) administratively feasible,

(B) in the interests of the plan and of its participants and beneficiaries, and

(C) protective of the rights of participants and beneficiaries of the plan.

Before granting an exemption under this paragraph, the Secretary shall require adequate notice to be given to interested persons and shall publish notice in the Federal Register of the pendency of such exemption and shall afford interested persons an opportunity to present views. No exemption may be granted under this paragraph with respect to a transaction described in subparagraph (E) or (F) of paragraph (1) unless the Secretary affords an opportunity for a hearing and makes a determination on the record with respect to the findings required under subparagraphs (A), (B), and (C) of this paragraph, except that in lieu of such hearing the Secretary may accept any record made by the Secretary of Labor with respect to an application for exemption under section 408(a) of title I of the Employee Retirement Income Security Act of 1974.

(3) Special rule for individual retirement accounts

An individual for whose benefit an individual retirement account is established and his beneficiaries shall be exempt from the tax imposed by this section with respect to any transaction concerning such account (which would

otherwise be taxable under this section) if, with respect to such transaction, the account ceases to be an individual retirement account by reason of the application of section 408(e)(2)(A) or if section 408(e)(4) applies to such account.

(4) Special rule for Archer MSAs

An individual for whose benefit an Archer MSA (within the meaning of section 220(d)) is established shall be exempt from the tax imposed by this section with respect to any transaction concerning such account (which would otherwise be taxable under this section) if section 220(e)(2) applies to such transaction.

(5) Special rule for education individual retirement accounts

An individual for whose benefit an education individual retirement account is established and any contributor to such account shall be exempt from the tax imposed by this section with respect to any transaction concerning such account (which would otherwise be taxable under this section) if section 530(d) applies with respect to such transaction.

(d) Exemptions

Except as provided in subsection (f)(6), the prohibitions provided in subsection (c) shall not apply to-

- (1) any loan made by the plan to a disqualified person who is a participant or beneficiary of the plan if such loan-
 - (A) is available to all such participants or beneficiaries on a reasonably equivalent basis,
 - (B) is not made available to highly compensated employees (within the meaning of section 414(q)) in an amount greater than the amount made available to other employees,
 - (C) is made in accordance with specific provisions regarding such loans set forth in the plan,
 - (D) bears a reasonable rate of interest, and
 - (E) is adequately secured;

- (2) any contract, or reasonable arrangement, made with a disqualified person for office space, or legal, accounting, or other services necessary for the establishment or operation of the plan, if no more than reasonable compensation is paid therefor;

- (3) any loan to an ¹ leveraged employee stock ownership plan (as defined in subsection (e)(7)), if-
 - (A) such loan is primarily for the benefit of participants and beneficiaries of the plan, and
 - (B) such loan is at a reasonable rate of interest, and any collateral which is given to a disqualified person by the plan consists only of qualifying employer securities (as defined in subsection (e)(8));

- (4) the investment of all or part of a plan's assets in deposits which bear a reasonable interest rate in a bank or similar financial institution supervised by the United States or a State, if such bank or other institution is a fiduciary of such plan and if-
 - (A) the plan covers only employees of such bank or other institution and employees of affiliates of such bank or other institution, or
 - (B) such investment is expressly authorized by a provision of the plan or by a fiduciary (other than such bank or institution or affiliates thereof) who is expressly empowered by the plan to so instruct the trustee with respect to such investment;

- (5) any contract for life insurance, health insurance, or annuities with one or more insurers which are qualified to do business in a State if the plan pays no more than adequate consideration, and if each such insurer or insurers is-
 - (A) the employer maintaining the plan, or
 - (B) a disqualified person which is wholly owned (directly or indirectly) by the employer establishing the plan, or by any person which is a disqualified person with respect to the plan, but only if the total premiums and annuity considerations written by such insurers for life insurance, health insurance, or annuities for all plans (and their employers) with respect to which such insurers are disqualified persons (not including premiums or annuity considerations written by the employer maintaining the plan) do not exceed 5 percent of the total premiums and annuity considerations written for all lines of insurance in that year by such insurers (not including premiums or annuity considerations written by the employer maintaining the plan);

- (6) the provision of any ancillary service by a bank or similar financial institution supervised by the United States or a State, if such service is provided at not more than reasonable compensation, if such bank or other institution is a fiduciary of such plan, and if-
 - (A) such bank or similar financial institution has adopted adequate internal safeguards which assure that the provision of such ancillary service is consistent with sound banking and financial practice, as determined by Federal or State supervisory authority, and
 - (B) the extent to which such ancillary service is provided is subject to specific guidelines issued by such bank or similar financial institution (as determined by the Secretary after consultation with Federal and State supervisory authority), and under such guidelines the bank or similar financial institution does not provide such ancillary service-
 - (i) in an excessive or unreasonable manner, and

(ii) in a manner that would be inconsistent with the best interests of participants and beneficiaries of employee benefit plans;

(7) the exercise of a privilege to convert securities, to the extent provided in regulations of the Secretary but only if the plan receives no less than adequate consideration pursuant to such conversion;

(8) any transaction between a plan and a common or collective trust fund or pooled investment fund maintained by a disqualified person which is a bank or trust company supervised by a State or Federal agency or between a plan and a pooled investment fund of an insurance company qualified to do business in a State if-

(A) the transaction is a sale or purchase of an interest in the fund,

(B) the bank, trust company, or insurance company receives not more than a reasonable compensation, and

(C) such transaction is expressly permitted by the instrument under which the plan is maintained, or by a fiduciary (other than the bank, trust company, or insurance company, or an affiliate thereof) who has authority to manage and control the assets of the plan;

(9) receipt by a disqualified person of any benefit to which he may be entitled as a participant or beneficiary in the plan, so long as the benefit is computed and paid on a basis which is consistent with the terms of the plan as applied to all other participants and beneficiaries;

(10) receipt by a disqualified person of any reasonable compensation for services rendered, or for the reimbursement of expenses properly and actually incurred, in the performance of his duties with the plan, but no person so serving who already receives full-time pay from an employer or an association of employers, whose employees are participants in the plan or from an employee organization whose members are participants in such plan shall receive compensation from such fund, except for reimbursement of expenses properly and actually incurred;

(11) service by a disqualified person as a fiduciary in addition to being an officer, employee, agent, or other representative of a disqualified person;

(12) the making by a fiduciary of a distribution of the assets of the trust in accordance with the terms of the plan if such assets are distributed in the same manner as provided under section 4044 of title IV of the Employee Retirement Income Security Act of 1974 (relating to allocation of assets);

(13) any transaction which is exempt from section 406 of such Act by reason of section 408(e) of such Act (or which would be so exempt if such section 406 applied to such transaction) or which is exempt from section 406 of such Act by reason of section 408(b)(12) of such Act;

(14) any transaction required or permitted under part 1 of subtitle E of title IV or section 4223 of the Employee Retirement Income Security Act of 1974, but this paragraph shall not apply with respect to the application of subsection (c)(1) (E) or (F); or

(15) a merger of multiemployer plans, or the transfer of assets or liabilities between multiemployer plans, determined by the Pension Benefit Guaranty Corporation to meet the requirements of section 4231 of such Act, but this paragraph shall not apply with respect to the application of subsection (c)(1) (E) or (F).

(e) Definitions

(1) Plan

For purposes of this section, the term "plan" means-

(A) a trust described in section 401(a) which forms a part of a plan, or a plan described in section 403(a), which trust or plan is exempt from tax under section 501(a),

(B) an individual retirement account described in section 408(a),

(C) an individual retirement annuity described in section 408(b),

(D) an Archer MSA described in section 220(d),

(E) an education individual retirement account described in section 530, or

(F) a trust, plan, account, or annuity which, at any time, has been determined by the Secretary to be described in any preceding subparagraph of this paragraph.

(2) Disqualified person

For purposes of this section, the term "disqualified person" means a person who is-

(A) a fiduciary;

(B) a person providing services to the plan;

(C) an employer any of whose employees are covered by the plan;

(D) an employee organization any of whose members are covered by the plan;

(E) an owner, direct or indirect, of 50 percent or more of-

(i) the combined voting power of all classes of stock entitled to vote or the total value of shares of all classes of stock of a corporation,

(ii) the capital interest or the profits interest of a partnership, or

(iii) the beneficial interest of a trust or unincorporated enterprise,

which is an employer or an employee organization described in subparagraph (C) or (D);

(F) a member of the family (as defined in paragraph (6)) of any individual described in subparagraph (A), (B), (C), or (E);

- (G) a corporation, partnership, or trust or estate of which (or in which) 50 percent or more of-
 - (i) the combined voting power of all classes of stock entitled to vote or the total value of shares of all classes of stock of such corporation,
 - (ii) the capital interest or profits interest of such partnership, or
 - (iii) the beneficial interest of such trust or estate,

is owned directly or indirectly, or held by persons described in subparagraph (A), (B), (C), (D), or (E);

(H) an officer, director (or an individual having powers or responsibilities similar to those of officers or directors), a 10 percent or more shareholder, or a highly compensated employee (earning 10 percent or more of the yearly wages of an employer) of a person described in subparagraph (C), (D), (E), or (G); or

(I) a 10 percent or more (in capital or profits) partner or joint venturer of a person described in subparagraph (C), (D), (E), or (G).

The Secretary, after consultation and coordination with the Secretary of Labor or his delegate, may by regulation prescribe a percentage lower than 50 percent for subparagraphs (E) and (G) and lower than 10 percent for subparagraphs (H) and (I).

(3) Fiduciary

For purposes of this section, the term "fiduciary" means any person who-

(A) exercises any discretionary authority or discretionary control respecting management of such plan or exercises any authority or control respecting management or disposition of its assets,

(B) renders investment advice for a fee or other compensation, direct or indirect, with respect to any moneys or other property of such plan, or has any authority or responsibility to do so, or

(C) has any discretionary authority or discretionary responsibility in the administration of such plan.

Such term includes any person designated under section 405(c)(1)(B) of the Employee Retirement Income Security Act of 1974.

(4) Stockholdings

For purposes of paragraphs (2)(E)(i) and (G)(i) there shall be taken into account indirect stockholdings which would be taken into account under section 267(c), except that, for purposes of this paragraph, section 267(c)(4) shall be treated as providing that the members of the family of an individual are the members within the meaning of paragraph (6).

(5) Partnerships; trusts

For purposes of paragraphs (2)(E)(ii) and (iii), (G)(ii) and (iii), and (I) the ownership of profits or beneficial interests shall be determined in accordance with the rules for constructive ownership of stock provided in section 267(c) (other than paragraph (3) thereof), except that section 267(c)(4) shall be treated as providing that the members of the family of an individual are the members within the meaning of paragraph (6).

(6) Member of family

For purposes of paragraph (2)(F), the family of any individual shall include his spouse, ancestor, lineal descendant, and any spouse of a lineal descendant.

(7) Employee stock ownership plan

The term "employee stock ownership plan" means a defined contribution plan-

(A) which is a stock bonus plan which is qualified, or a stock bonus and a money purchase plan both of which are qualified under section 401(a), and which are designed to invest primarily in qualifying employer securities; and

(B) which is otherwise defined in regulations prescribed by the Secretary.

A plan shall not be treated as an employee stock ownership plan unless it meets the requirements of section 409(h), section 409(o), and, if applicable, section 409(n) and section 664(g) and, if the employer has a registration-type class of securities (as defined in section 409(e)(4)), it meets the requirements of section 409(e).

(8) Qualifying employer security

The term "qualifying employer security" means any employer security within the meaning of section 409(l). If any moneys or other property of a plan are invested in shares of an investment company registered under the Investment Company Act of 1940, the investment shall not cause that investment company or that investment company's investment adviser or principal underwriter to be treated as a fiduciary or a disqualified person for purposes of this section, except when an investment company or its investment adviser or principal underwriter acts in connection with a plan covering employees of the investment company, its investment adviser, or its principal underwriter.

(9) Section made applicable to withdrawal liability payment funds

For purposes of this section-

(A) In general

The term "plan" includes a trust described in section 501(c)(22).

(B) Disqualified person

In the case of any trust to which this section applies by reason of subparagraph (A), the term "disqualified person" includes any person who is a disqualified person with respect to any plan to which such trust is permitted to make payments under section 4223 of the Employee Retirement Income Security Act of 1974.

(f) Other definitions and special rules

For purposes of this section-

(1) Joint and several liability

If more than one person is liable under subsection (a) or (b) with respect to any one prohibited transaction, all such persons shall be jointly and severally liable under such subsection with respect to such transaction.

(2) Taxable period

The term "taxable period" means, with respect to any prohibited transaction, the period beginning with the date on which the prohibited transaction occurs and ending on the earliest of-

- (A) the date of mailing a notice of deficiency with respect to the tax imposed by subsection (a) under section 6212,
- (B) the date on which the tax imposed by subsection (a) is assessed, or
- (C) the date on which correction of the prohibited transaction is completed.

(3) Sale or exchange; encumbered property

A transfer of real or personal property by a disqualified person to a plan shall be treated as a sale or exchange if the property is subject to a mortgage or similar lien which the plan assumes or if it is subject to a mortgage or similar lien which a disqualified person placed on the property within the 10-year period ending on the date of the transfer.

(4) Amount involved

The term "amount involved" means, with respect to a prohibited transaction, the greater of the amount of money and the fair market value of the other property given or the amount of money and the fair market value of the other property received; except that, in the case of services described in paragraphs (2) and (10) of subsection (d) the amount involved shall be only the excess compensation. For purposes of the preceding sentence, the fair market value-

- (A) in the case of the tax imposed by subsection (a), shall be determined as of the date on which the prohibited transaction occurs; and
- (B) in the case of the tax imposed by subsection (b), shall be the highest fair market value during the taxable period.

(5) Correction

The terms "correction" and "correct" mean, with respect to a prohibited transaction, undoing the transaction to the extent possible, but in any case placing the plan in a financial position not worse than that in which it would be if the disqualified person were acting under the highest fiduciary standards.

(6) Exemptions not to apply to certain transactions**(A) In general**

In the case of a trust described in section 401(a) which is part of a plan providing contributions or benefits for employees some or all of whom are owner-employees (as defined in section 401(c)(3)), the exemptions provided by subsection (d) (other than paragraphs (9) and (12)) shall not apply to a transaction in which the plan directly or indirectly-

- (i) lends any part of the corpus or income of the plan to,
- (ii) pays any compensation for personal services rendered to the plan to, or
- (iii) acquires for the plan any property from, or sells any property to,

any such owner-employee, a member of the family (as defined in section 267(c)(4)) of any such owner-employee, or any corporation in which any such owner-employee owns, directly or indirectly, 50 percent or more of the total combined voting power of all classes of stock entitled to vote or 50 percent or more of the total value of shares of all classes of stock of the corporation.

(B) Special rules for shareholder-employees, etc.**(i) In general**

For purposes of subparagraph (A), the following shall be treated as owner-employees:

- (I) A shareholder-employee.
- (II) A participant or beneficiary of an individual retirement plan (as defined in section 7701(a)(37)).
- (III) An employer or association of employees which establishes such an individual retirement plan under section 408(c).

(ii) Exception for certain transactions involving shareholder-employees

Subparagraph (A)(iii) shall not apply to a transaction which consists of a sale of employer securities to an employee stock ownership plan (as defined in subsection (e)(7)) by a shareholder-employee, a member of the family (as defined in section 267(c)(4)) of such shareholder-employee, or a corporation in which such a shareholder-employee owns stock representing a 50 percent or greater interest described in subparagraph (A).

(C) Shareholder-employee

For purposes of subparagraph (B), the term "shareholder-employee" means an employee or officer of an S corporation who owns (or is considered as owning within the meaning of section 318(a)(1)) more than 5 percent of the outstanding stock of the corporation on any day during the taxable year of such corporation.

(g) Application of section

This section shall not apply-

(1) in the case of a plan to which a guaranteed benefit policy (as defined in section 401(b)(2)(B) of the Employee Retirement Income Security Act of 1974) is issued, to any assets of the insurance company, insurance service, or insurance organization merely because of its issuance of such policy;

(2) to a governmental plan (within the meaning of section 414(d)); or

(3) to a church plan (within the meaning of section 414(e)) with respect to which the election provided by section 410(d) has not been made.

In the case of a plan which invests in any security issued by an investment company registered under the Investment Company Act of 1940, the assets of such plan shall be deemed to include such security but shall not, by reason of such investment, be deemed to include any assets of such company.

(h) Notification of Secretary of Labor

Before sending a notice of deficiency with respect to the tax imposed by subsection (a) or (b), the Secretary shall notify the Secretary of Labor and provide him a reasonable opportunity to obtain a correction of the prohibited transaction or to comment on the imposition of such tax.

(i) Cross reference

For provisions concerning coordination procedures between Secretary of Labor and Secretary of the Treasury with respect to application of tax imposed by this section and for authority to waive imposition of the tax imposed by subsection (b), see section 3003 of the Employee Retirement Income Security Act of 1974.

(Added Pub. L. 93-406, title II, §2003(a), Sept. 2, 1974, 88 Stat. 971 ; amended Pub. L. 94-455, title XIX, §1906(b)(13)(A), Oct. 4, 1976, 90 Stat. 1834 ; Pub. L. 95-600, title I, §141(f)(5), (6), Nov. 6, 1978, 92 Stat. 2795 ; Pub. L. 96-222, title I, §101(a)(7)(C), (K), (L)(iv)(III), (v)(XI), Apr. 1, 1980, 94 Stat. 198-201 ; Pub. L. 96-364, title II, §§208(b), 209(b), Sept. 26, 1980, 94 Stat. 1289 , 1290; Pub. L. 96-596, §2(a)(1)(K),(L), (2)(I), (3)(F), Dec. 24, 1980, 94 Stat. 3469 , 3471; Pub. L. 97-448, title III, §305(d)(5), Jan. 12, 1983, 96 Stat. 2400 ; Pub. L. 98-369, div. A, title IV, §491(d)(45), (46), (e)(7), (8), July 18, 1984, 98 Stat. 851-853 ; Pub. L. 99-514, title XI, §1114(b)(15)(A), title XVIII, §§1854(f)(3)(A), 1899A(51), Oct. 22, 1986, 100 Stat. 2452 , 2882, 2961; Pub. L. 101-508, title XI, §11701(m), Nov. 5, 1990, 104 Stat. 1388-513 ; Pub. L. 104-188, title I, §§1453(a), 1702(g)(3), Aug. 20, 1996, 110 Stat. 1817 , 1873; Pub. L. 104-191, title III, §301(f), Aug. 21, 1996, 110 Stat. 2051 ; Pub. L. 105-34, title II, §213(b), title X, §1074(a), title XV, §§1506(b)(1), 1530(c)(10), title XVI, §1602(a)(5), Aug. 5, 1997, 111 Stat. 816 , 949, 1065, 1079, 1094; Pub. L. 105-206, title VI, §6023(19), July 22, 1998, 112 Stat. 825 ; Pub. L. 106-554, §1(a)(7) [title II, §202(a)(7), (b)(7), (10)], Dec. 21, 2000, 114 Stat. 2763 , 2763A-628, 2763A-629.)

REFERENCES IN TEXT

The Employee Retirement Income Security Act of 1974, referred to in subsecs. (c)(2), (d)(12) to (15), (e)(3), (9)(B), (g)(1), and (i) is Pub. L. 93-406, [Sept. 2, 1974](#), 88 Stat. 829 , as amended. Part 1 of subtitle E of title IV of such Act is classified generally to part 1 (29 U.S.C. 1381 et seq.) of subtitle E of subchapter III of chapter 18 of Title 29, Labor. Sections 401, 405, 406, 408, 3003, 4044, 4223, and 4231 of such Act are classified to sections 1101, 1105, 1106, 1108, 1203, 1344, 1403, and 1411, respectively, of Title 29. For complete classification of this Act to the Code, see Short Title note set out under section 1001 of Title 29 and Tables.

The Investment Company Act of 1940, referred to in subsecs. (e)(8) and (g), is title I of act [Aug. 22, 1940](#), [ch. 686](#), 54 Stat. 789 , as amended, which is classified generally to subchapter I (§80a-1 et seq.) of chapter 2D of Title 15, Commerce and Trade. For complete classification of this Act to the Code, see section 80a-51 of Title 15 and Tables.

AMENDMENTS

2000-Subsec. (c)(4). Pub. L. 106-554, §1(a)(7) [title II, §202(b)(10)], substituted "an Archer" for "a Archer".

Pub. L. 106–554, §1(a)(7) [title II, §202(a)(7), (b)(7)], substituted "Archer MSAs" for "medical savings accounts" in heading and "Archer MSA" for "medical savings account" in text.

Subsec. (e)(1)(D). Pub. L. 106–554, §1(a)(7) [title II, §202(b)(10)], substituted "an Archer" for "a Archer".

Pub. L. 106–554, §1(a)(7) [title II, §202(a)(7)], substituted "Archer MSA" for "medical savings account".

1998-Subsec. (c)(3). Pub. L. 105–206, §6023(19)(A), substituted "exempt from the tax" for "exempt for the tax".

Subsec. (i). Pub. L. 105–206, §6023(19)(B), substituted "Secretary of the Treasury" for "Secretary of Treasury".

1997-Subsec. (a). Pub. L. 105–34, §1074(a), substituted "15 percent" for "10 percent".

Subsec. (c)(4). Pub. L. 105–34, §1602(a)(5), substituted "if section 220(e)(2) applies to such transaction." for "if, with respect to such transaction, the account ceases to be a medical savings account by reason of the application of section 220(e)(2) to such account."

Subsec. (c)(5). Pub. L. 105–34, §213(b)(2), added par. (5).

Subsec. (d). Pub. L. 105–34, §1506(b)(1)(B)(ii), struck out concluding provisions which read as follows: "The exemptions provided by this subsection (other than paragraphs (9) and (12)) shall not apply to any transaction with respect to a trust described in section 401(a) which is part of a plan providing contributions or benefits for employees some or all of whom are owner-employees (as defined in section 401(c)(3)) in which a plan directly or indirectly lends any part of the corpus or income of the plan to, pays any compensation for personal services rendered to the plan to, or acquires for the plan any property from or sells any property to, any such owner-employee, a member of the family (as defined in section 267(c)(4)) of any such owner-employee, or a corporation controlled by any such owner-employee through the ownership, directly or indirectly, of 50 percent or more of the total combined voting power of all classes of stock entitled to vote or 50 percent or more of the total value of shares of all classes of stock of the corporation. For purposes of the preceding sentence, a shareholder-employee (as defined in section 1379, as in effect on the day before the date of the enactment of the Subchapter S Revision Act of 1982), a participant or beneficiary of an individual retirement account or an individual retirement annuity (as defined in section 408), and an employer or association of employees which establishes such an account or annuity under section 408(c) shall be deemed to be an owner-employee."

Pub. L. 105–34, §1506(b)(1)(B)(i), substituted "Except as provided in subsection (f)(6), the prohibitions" for "The prohibitions" in introductory provisions.

Subsec. (e)(1)(D) to (F). Pub. L. 105–34, §213(b)(1), struck out "or" at end of subpar. (D), added subpar. (E), and redesignated former subpar. (E) as (F).

Subsec. (e)(7). Pub. L. 105–34, §1530(c)(10), inserted "and section 664(g)" after "section 409(n)" in concluding provisions.

Subsec. (f)(6). Pub. L. 105–34, §1506(b)(1)(A), added par. (6).

1996-Subsec. (a). Pub. L. 104–188, §1453(a), substituted "10 percent" for "5 percent".

Subsec. (c)(4). Pub. L. 104–191, §301(f)(1), added par. (4).

Subsec. (d)(13). Pub. L. 104–188, §1702(g)(3), substituted "408(b)(12)" for "408(b)".

Subsec. (e)(1). Pub. L. 104–191, §301(f)(2), reenacted heading without change and amended text generally. Prior to amendment, text read as follows: "For purposes of this section, the term 'plan' means a trust described in section 401(a) which forms a part of a plan, or a plan described in section 403(a), which trust or plan is exempt from tax under section 501(a), an individual retirement account described in section 408(a) or an individual retirement annuity described in section 408(b) (or a trust, plan, account, or annuity which, at any time, has been determined by the Secretary to be such a trust, plan, or account)."

1990-Subsec. (d)(13). Pub. L. 101–508 inserted before semicolon at end "or which is exempt from section 406 of such Act by reason of section 408(b) of such Act".

1986-Subsec. (d). Pub. L. 99–514, §1899A(51), inserted a closing parenthesis after "and (12)" in second sentence.

Subsec. (d)(1)(B). Pub. L. 99–514, §1114(b)(15)(A), substituted "highly compensated employees (within the meaning of section 414(q))" for "highly compensated employees, officers, or shareholders".

Subsec. (e)(7). Pub. L. 99–514, §1854(f)(3)(A), inserted ", section 409(o), and, if applicable, section 409(n)" in last sentence.

1984-Subsec. (d). Pub. L. 98–369, §491(d)(45), substituted in provision following par. (15) "or an individual retirement annuity (as defined in section 408)" for ", individual retirement annuity, or an individual retirement bond (as defined in section 408 or 409)".

Subsec. (e)(1). Pub. L. 98–369, §491(d)(46), struck out "or 405(a)" after "section 403(a)" and "or a retirement bond described in section 409" after "section 408(b)", and substituted "or annuity" for "annuity, or bond" and "or account" for "account, or bond".

Subsec. (e)(7). Pub. L. 98–369, §491(e)(7), substituted "section 409(h)" for "section 409A(h)", "section 409(e)(4)" for "section 409A(e)(4)", and "section 409(e)" for "section 409A(e)".

Subsec. (e)(8). Pub. L. 98–369, §491(e)(8), substituted "section 409(l)" for "section 409A(l)".

1983-Subsec. (d). Pub. L. 97-448 inserted ", as in effect on the day before the date of the enactment of the Subchapter S Revision Act of 1982" after "section 1379" in last sentence.

1980-Subsec. (b). Pub. L. 96-596, §2(a)(1)(K), substituted "taxable period" for "correction period".

Subsec. (d)(14), (15). Pub. L. 96-364, §208(b), added pars. (14) and (15).

Subsec. (e)(7). Pub. L. 96-222, §101(a)(7)(K), (L)(iv)(III), (v)(XI), substituted references to an employee stock ownership plan, for references to a leveraged employee stock ownership plan wherever appearing therein, and substituted provisions relating to treatment of a plan as an employee stock ownership plan, for provisions relating to treatment of a plan as a leveraged employee stock ownership plan.

Subsec. (e)(8). Pub. L. 96-222, §101(a)(7)(C), substituted provisions defining "qualifying employer security" within the meaning of section 409A(l), for provisions defining such term as stock, or otherwise an equity security, or within the meaning of section 503(e)(1) to (3).

Subsec. (e)(9). Pub. L. 96-364, §209(b), added par. (9).

Subsec. (f)(2)(B), (C). Pub. L. 96-596, §2(a)(2)(l), added subpar. (B) and redesignated former subpar. (B) as (C).

Subsec. (f)(4)(B). Pub. L. 96-596, §2(a)(1)(L), substituted "taxable period" for "correction period".

Subsec. (f)(6). Pub. L. 96-596, §2(a)(3)(F), struck out par. (6), which defined correction period, with respect to a prohibited transaction, as the period beginning on the date on which the prohibited transaction occurs and ending 90 days after the date of mailing of a notice of deficiency with respect to the tax imposed by subsec. (b) of this section under section 6212 of this title, extended by any period in which a deficiency cannot be assessed under section 6213(a) of this title and any other period which the Secretary determines is reasonable and necessary to bring about the correction of the prohibited transaction.

1978-Subsec. (d)(3). Pub. L. 95-600, §141(f)(6), substituted "leveraged employee" for "employee".

Subsec. (e)(7). Pub. L. 95-600, §141(f)(5), substituted in heading "Leveraged employee" for "Employee", and in text, "leveraged employee" for "employee" and inserted provision that a plan not be treated as a leveraged employee stock ownership plan unless it meet the requirements of section 409A(e) and (h).

1976-Subsecs. (c) to (f). Pub. L. 94-455 struck out "or his delegate" after "Secretary" wherever appearing.

EFFECTIVE DATE OF 1997 AMENDMENT

Amendment by section 213(b) of Pub. L. 105-34 applicable to taxable years beginning after Dec. 31, 1997, see section 213(f) of Pub. L. 105-34, set out as a note under section 26 of this title.

Section 1074(b) of Pub. L. 105-34 provided that: "The amendment made by this section [amending this section] shall apply to prohibited transactions occurring after the date of the enactment of this Act [Aug. 5, 1997]."

Amendment by section 1506(b)(1) of Pub. L. 105-34 applicable to taxable years beginning after Dec. 31, 1997, see section 1506(c) of Pub. L. 105-34, set out as a note under section 409 of this title.

Amendment by section 1530(c)(10) of Pub. L. 105-34 applicable to transfers made by trusts to, or for the use of, an employee stock ownership plan after Aug. 5, 1997, see section 1530(d) of Pub. L. 105-34, set out as a note under section 401 of this title.

Amendment by section 1602(a)(5) of Pub. L. 105-34 effective as if included in the provisions of the Health Insurance Portability and Accountability Act of 1996, Pub. L. 104-191, to which such amendment relates, see section 1602(i) of Pub. L. 105-34, set out as a note under section 26 of this title.

EFFECTIVE DATE OF 1996 AMENDMENTS

Amendment by Pub. L. 104-191 applicable to taxable years beginning after Dec. 31, 1996, see section 301(j) of Pub. L. 104-191, set out as a note under section 62 of this title.

Section 1453(b) of Pub. L. 104-188 provided that: "The amendment made by this section [amending this section] shall apply to prohibited transactions occurring after the date of the enactment of this Act [Aug. 20, 1996]."

Amendment by section 1702(g)(3) of Pub. L. 104-188 effective, except as otherwise expressly provided, as if included in the provision of the Revenue Reconciliation Act of 1990, Pub. L. 101-508, title XI, to which such amendment relates, see section 1702(i) of Pub. L. 104-188, set out as a note under section 38 of this title.

EFFECTIVE DATE OF 1990 AMENDMENT

Amendment by Pub. L. 101-508 effective, except as otherwise provided, as if included in the provision of the Revenue Reconciliation Act of 1989, Pub. L. 101-239, title VII, to which such amendment relates, see section 11701(n) of Pub. L. 101-508, set out as a note under section 42 of this title.

EFFECTIVE DATE OF 1986 AMENDMENT

Amendment by section 1114(b)(15)(A) of Pub. L. 99-514 applicable to years beginning after Dec. 31, 1988, see section 1114(c)(3) of Pub. L. 99-514, set out as a note under section 414 of this title.

Amendment by section 1854(f)(3)(A) of Pub. L. 99-514 effective Oct. 22, 1986, see section 1854(f)(4)(A) of Pub. L. 99-514, set out as a note under section 409 of this title.

EFFECTIVE DATE OF 1984 AMENDMENT

Amendment by section 491(d)(45), (46) of Pub. L. 98-369 applicable to obligations issued after Dec. 31, 1983, see section 491(f)(1) of Pub. L. 98-369, set out as a note under section 62 of this title.

Amendment by section 491(e)(7), (8) of Pub. L. 98-369 effective Jan. 1, 1984, see section 491(f)(3) of Pub. L. 98-369, set out as a note under section 401 of this title.

EFFECTIVE DATE OF 1983 AMENDMENT

Amendment by Pub. L. 97-448 effective on date of enactment of Subchapter S Revision Act of 1982 [Oct. 19, 1982], see section 311(c)(4) of Pub. L. 97-448, set out as a note under section 1368 of this title.

EFFECTIVE DATE OF 1980 AMENDMENTS

For effective date of amendment by Pub. L. 96-596 with respect to any first tier tax and to any second tier tax, see section 2(d) of Pub. L. 96-596, set out as an Effective Date note under section 4961 of this title.

Amendment by section 208(b) of Pub. L. 96-364 effective Sept. 26, 1980, see section 210(a) of Pub. L. 96-364, set out as an Effective Date note under section 418 of this title.

Amendment by section 209(b) of Pub. L. 96-364 applicable to taxable years ending after Sept. 26, 1980, see section 210(c) of Pub. L. 96-364, set out as an Effective Date note under section 418 of this title.

Section 101(b)(1)(C) of Pub. L. 96-222 provided that: "The amendment made by subparagraph (C) of subsection (a)(6) [probably should be '(a)(7)', which amended this section] shall apply to stock acquired after December 31, 1979."

Amendment by section 101(a)(7)(K), (L)(iv)(III), (v)(XI) of Pub. L. 96-222 effective, except as otherwise provided, as if it had been included in the provision of the Revenue Act of 1978, Pub. L. 95-600, to which such amendment relates, see section 201 of Pub. L. 96-222, set out as a note under section 32 of this title.

EFFECTIVE DATE OF 1978 AMENDMENT

Section 141(h) of Pub. L. 95-600, as added by Pub. L. 96-222, [title I, §101\(a\)\(7\)\(B\), Apr. 1, 1980](#), 94 Stat. 197 ; Pub. L. 99-514, [§2, Oct. 22, 1986](#), 100 Stat. 2095 , provided that: "Paragraphs (5) and (6) of subsection (f) [section 141(f)(5), (6) of Pub. L. 95-600] shall apply-

"(1) insofar as they make the requirements of subsections (e) and (h)(1)(B) of section 409A [now section 409] of the Internal Revenue Code of 1986 [formerly I.R.C. 1954] applicable to section 4975 of such Code, to stock acquired after December 31, 1979, and

"(2) insofar as they make paragraphs (1)(A) and (2) of section 409A(h) [now section 409(h)] of such Code applicable to such section 4975, to distributions after December 31, 1978."

EFFECTIVE DATE; SAVINGS PROVISION

Section 2003(c) of Pub. L. 93-406, as amended by Pub. L. 99-514, [§2, Oct. 22, 1986](#), 100 Stat. 2095 , provided that:

"(1)(A) The amendments made by this section [enacting this section and amending section 503 of this title] shall take effect on January 1, 1975.

"(B) If, before the amendments made by this section [enacting this section and amending section 503 of this title] take effect, an organization described in section 401(a) of the Internal Revenue Code of 1986 [formerly I.R.C. 1954] is denied exemption under section 501(a) of such Code by reason of section 503 of such Code, the denial of such exemption shall not apply if the disqualified person elects (in such manner and at such time as the Secretary or his delegate shall by regulations prescribe) to pay, with respect to the prohibited transaction (within the meaning of section 503(b) or (g)) which resulted in such denial of exemption, a tax in the amount and in the manner provided with respect to the tax imposed under section 4975 of such Code. An election made under this subparagraph, once made, shall be irrevocable. The Secretary of the Treasury or his delegate shall prescribe such regulations as may be necessary to carry out the purposes of this subparagraph.

"(2) Section 4975 of the Internal Revenue Code of 1986 (relating to tax on prohibited transactions) shall not apply to-

"(A) a loan of money or other extension of credit between a plan and a disqualified person under a binding contract in effect on July 1, 1974 (or pursuant to renewals of such a contract), until June 30, 1984, if such loan or other extension of credit remains at least as favorable to the plan as an arm's-length transaction with an unrelated party would be, and if the execution of the contract, the making of

the loan, or the extension of credit was not, at the time of such execution, making, or extension, a prohibited transaction (within the meaning of section 503(b) of such Code) or the corresponding provisions of prior law);

"(B) a lease of joint use of property involving the plan and a disqualified person pursuant to a binding contract in effect on July 1, 1974 (or pursuant to renewals of such a contract), until June 30, 1984, if such lease or joint use remains at least as favorable to the plan as an arm's-length transaction with an unrelated party would be and if the execution of the contract was not, at the time of such execution, a prohibited transaction (within the meaning of section 503(b) of such Code) or the corresponding provisions of prior law;

"(C) the sale, exchange, or other disposition of property described in subparagraph (B) between a plan and a disqualified person before June 30, 1984, if-

"(i) in the case of a sale, exchange, or other disposition of the property by the plan to the disqualified person, the plan receives an amount which is not less than the fair market value of the property at the time of such disposition; and

"(ii) in the case of the acquisition of the property by the plan, the plan pays an amount which is not in excess of the fair market value of the property at the time of such acquisition:

"(D) Until June 30, 1977, the provision of services to which subparagraphs (A), (B), and (C) do not apply between a plan and a disqualified person (i) under a binding contract in effect on July 1, 1974 (or pursuant to renewals of such contract), or (ii) if the disqualified person ordinarily and customarily furnished such services on June 30, 1974, if such provision of services remains at least as favorable to the plan as an arm's-length transaction with an unrelated party would be and if the provision of services was not, at the time of such provision, a prohibited transaction (within the meaning of section 503(b) of such Code) or the corresponding provisions of prior law; or

"(E) the sale, exchange, or other disposition of property which is owned by a plan on June 30, 1974, and all times thereafter, to a disqualified person, if such plan is required to dispose of such property in order to comply with the provisions of section 407(a)(2)(A) (relating to the prohibition against holding excess employer securities and employer real property) of the Employee Retirement Income Security Act of 1974 [29 U.S.C. 1107(a)(2)] and if the plan receives not less than adequate consideration.

For the purposes of this paragraph, the term 'disqualified person' has the meaning provided by section 4975(e)(2) of the Internal Revenue Code of 1986."

REGULATIONS

Secretary of the Treasury or his delegate to issue before Feb. 1, 1988, final regulations to carry out amendments made by section 1114 of Pub. L. 99-514, see section 1141 of Pub. L. 99-514, set out as a note under section 401 of this title.

PLAN AMENDMENTS NOT REQUIRED UNTIL JANUARY 1, 1998

For provisions directing that if any amendments made by subtitle D [§§1401-1465] of title I of Pub. L. 104-188 require an amendment to any plan or annuity contract, such amendment shall not be required to be made before the first day of the first plan year beginning on or after Jan. 1, 1998, see section 1465 of Pub. L. 104-188, set out as a note under section 401 of this title.

PLAN AMENDMENTS NOT REQUIRED UNTIL JANUARY 1, 1989

For provisions directing that if any amendments made by subtitle A or subtitle C of title XI [§§1101-1147 and 1171-1177] or title XVIII [§§1800-1899A] of Pub. L. 99-514 require an amendment to any plan, such plan amendment shall not be required to be made before the first plan year beginning on or after Jan. 1, 1989, see section 1140 of Pub. L. 99-514, as amended, set out as a note under section 401 of this title.

INTENT OF CONGRESS CONCERNING EMPLOYEE STOCK OWNERSHIP PLANS

Section 803(h) of Pub. L. 94-455 provided that: "The Congress, in a series of laws (the Regional Rail Reorganization Act of 1973, the Employee Retirement Income Security Act of 1974, the Trade Act of 1974, and the Tax Reduction Act of 1975) and this Act has made clear its interest in encouraging employee stock ownership plans as a bold and innovative method of strengthening the free private enterprise system which will solve the dual problems of securing capital funds for necessary capital growth and of bringing about stock ownership by all corporate employees. The Congress is deeply concerned that the objectives sought by this series of laws will be made unattainable by regulations and rulings which treat employee stock ownership plans as conventional retirement plans, which reduce the freedom of the employee trusts and employers to take the necessary steps to implement the plans, and which otherwise block the establishment and success of these plans. Because of the special purposes for

which employee stock ownership plans are established, it is consistent with the intent of Congress to permit these plans (whether structured as pension, stock bonus, or profit-sharing plans) to distribute income on employer securities currently."

SECTION REFERRED TO IN OTHER SECTIONS

This section is referred to in sections 401, 404, 408, 409, 411, 414, 415, 420, 503, 512, 514, 664, 674, 856, 1042, 2056, 4943, 4947, 4963, 4978, 4980, 6213, 6501, 6503, 6511, 7422 of this title; title 5 section 8477; title 15 section 632; title 19 sections 2345, 2373; title 29 sections 1054, 1055, 1056, 1101, 1107, 1132, 1203, 1342, 1403; title 45 section 726.

¹ So in original. Probably should be "a".

RCW 69.50.325 Cannabis producer's license, cannabis processor's license, cannabis retailer's license. (1) There shall be a cannabis producer's license regulated by the board and subject to annual renewal. The licensee is authorized to produce: (a) Cannabis for sale at wholesale to cannabis processors and other cannabis producers; (b) immature plants or clones and seeds for sale to cooperatives as described under RCW 69.51A.250; and (c) immature plants or clones and seeds for sale to qualifying patients and designated providers as provided under RCW 69.51A.310. The production, possession, delivery, distribution, and sale of cannabis in accordance with the provisions of this chapter and the rules adopted to implement and enforce it, by a validly licensed cannabis producer, shall not be a criminal or civil offense under Washington state law. Every cannabis producer's license shall be issued in the name of the applicant, shall specify the location at which the cannabis producer intends to operate, which must be within the state of Washington, and the holder thereof shall not allow any other person to use the license. The application fee for a cannabis producer's license shall be two hundred fifty dollars. The annual fee for issuance and renewal of a cannabis producer's license shall be one thousand three hundred eighty-one dollars. A separate license shall be required for each location at which a cannabis producer intends to produce cannabis.

(2) There shall be a cannabis processor's license to process, package, and label cannabis concentrates, useable cannabis, and cannabis-infused products for sale at wholesale to cannabis processors and cannabis retailers, regulated by the board and subject to annual renewal. The processing, packaging, possession, delivery, distribution, and sale of cannabis, useable cannabis, cannabis-infused products, and cannabis concentrates in accordance with the provisions of this chapter and chapter 69.51A RCW and the rules adopted to implement and enforce these chapters, by a validly licensed cannabis processor, shall not be a criminal or civil offense under Washington state law. Every cannabis processor's license shall be issued in the name of the applicant, shall specify the location at which the licensee intends to operate, which must be within the state of Washington, and the holder thereof shall not allow any other person to use the license. The application fee for a cannabis processor's license shall be two hundred fifty dollars. The annual fee for issuance and renewal of a cannabis processor's license shall be one thousand three hundred eighty-one dollars. A separate license shall be required for each location at which a cannabis processor intends to process cannabis.

(3) (a) There shall be a cannabis retailer's license to sell cannabis concentrates, useable cannabis, and cannabis-infused products at retail in retail outlets, regulated by the board and subject to annual renewal. The possession, delivery, distribution, and sale of cannabis concentrates, useable cannabis, and cannabis-infused products in accordance with the provisions of this chapter and the rules adopted to implement and enforce it, by a validly licensed cannabis retailer, shall not be a criminal or civil offense under Washington state law. Every cannabis retailer's license shall be issued in the name of the applicant, shall specify the location of the retail outlet the licensee intends to operate, which must be within the state of Washington, and the holder thereof shall not allow any other person to use the license. The application fee for a cannabis retailer's license shall be two hundred fifty dollars. The annual fee for issuance and renewal of a cannabis retailer's license shall be one thousand three

hundred eighty-one dollars. A separate license shall be required for each location at which a cannabis retailer intends to sell cannabis concentrates, useable cannabis, and cannabis-infused products.

(b) An individual retail licensee and all other persons or entities with a financial or other ownership interest in the business operating under the license are limited, in the aggregate, to holding a collective total of not more than five retail cannabis licenses.

(c)(i) A cannabis retailer's license is subject to forfeiture in accordance with rules adopted by the board pursuant to this section.

(ii) The board shall adopt rules to establish a license forfeiture process for a licensed cannabis retailer that is not fully operational and open to the public within a specified period from the date of license issuance, as established by the board, subject to the following restrictions:

(A) No cannabis retailer's license may be subject to forfeiture within the first nine months of license issuance; and

(B) The board must require license forfeiture on or before twenty-four calendar months of license issuance if a cannabis retailer is not fully operational and open to the public, unless the board determines that circumstances out of the licensee's control are preventing the licensee from becoming fully operational and that, in the board's discretion, the circumstances warrant extending the forfeiture period beyond twenty-four calendar months.

(iii) The board has discretion in adopting rules under this subsection (3)(c).

(iv) This subsection (3)(c) applies to cannabis retailer's licenses issued before and after July 23, 2017. However, no license of a cannabis retailer that otherwise meets the conditions for license forfeiture established pursuant to this subsection (3)(c) may be subject to forfeiture within the first nine calendar months of July 23, 2017.

(v) The board may not require license forfeiture if the licensee has been incapable of opening a fully operational retail cannabis business due to actions by the city, town, or county with jurisdiction over the licensee that include any of the following:

(A) The adoption of a ban or moratorium that prohibits the opening of a retail cannabis business; or

(B) The adoption of an ordinance or regulation related to zoning, business licensing, land use, or other regulatory measure that has the effect of preventing a licensee from receiving an occupancy permit from the jurisdiction or which otherwise prevents a licensed cannabis retailer from becoming operational.

(d) The board may issue cannabis retailer licenses pursuant to this chapter and RCW 69.50.335. [2022 c 16 § 54; 2020 c 236 § 6; 2018 c 132 § 3. Prior: 2017 c 317 § 1; 2017 c 316 § 2; 2016 c 170 § 1; 2015 c 70 § 5; 2014 c 192 § 2; 2013 c 3 § 4 (Initiative Measure No. 502, approved November 6, 2012).]

Intent—Finding—2022 c 16: See note following RCW 69.50.101.

Findings—Intent—2020 c 236: See note following RCW 69.50.335.

Effective date—2018 c 132 § 3: "Section 3 of this act takes effect July 1, 2018." [2018 c 132 § 4.]

Findings—2017 c 317: "The legislature finds that protecting the state's children, youth, and young adults under the legal age to purchase and consume marijuana [cannabis], by establishing limited restrictions on the advertising of marijuana [cannabis] and marijuana [cannabis] products, is necessary to assist the state's efforts to discourage and prevent underage consumption and the potential risks associated with underage consumption. The legislature finds that these restrictions assist the state in maintaining a strong and effective regulatory and enforcement system as specified by the federal government. The legislature finds this act leaves ample opportunities for licensed marijuana [cannabis] businesses to market their products to those who are of legal age to purchase them, without infringing on the free speech rights of business owners. Finally, the legislature finds that the state has a substantial and compelling interest in enacting this act aimed at protecting Washington's children, youth, and young adults." [2017 c 317 § 12.]

Application—2017 c 317: "This act applies prospectively only and not retroactively. It applies only to causes of action that arise (if change is substantive) or that are commenced (if change is procedural) on or after July 23, 2017." [2017 c 317 § 25.]

Effective date—2017 c 316 §§ 2 and 3: "Sections 2 and 3 of this act take effect July 1, 2018." [2017 c 316 § 4.]

Effective date—2016 c 170: "This act takes effect July 1, 2016." [2016 c 170 § 3.]

Short title—Findings—Intent—References to Washington state liquor control board—Draft legislation—2015 c 70: See notes following RCW 66.08.012.

Intent—2013 c 3 (Initiative Measure No. 502): See note following RCW 69.50.101.

RCW 69.50.328 Cannabis producers, processors—No direct or indirect financial interest in licensed cannabis retailers. Neither a licensed cannabis producer nor a licensed cannabis processor shall have a direct or indirect financial interest in a licensed cannabis retailer. [2022 c 16 § 57; 2013 c 3 § 5 (Initiative Measure No. 502, approved November 6, 2012).]

Intent—Finding—2022 c 16: See note following RCW 69.50.101.

Intent—2013 c 3 (Initiative Measure No. 502): See note following RCW 69.50.101.

RCW 69.50.339 Transfer of license to produce, process, or sell cannabis—Reporting of proposed sales of outstanding or issued stock of a corporation. (1) If the board approves, a license to produce, process, or sell cannabis may be transferred, without charge, to the surviving spouse or domestic partner of a deceased licensee if the license was issued in the names of one or both of the parties. For the purpose of considering the qualifications of the surviving party to receive a cannabis producer's, cannabis processor's, or cannabis retailer's license, the board may require a criminal history record information check. The board may submit the criminal history record information check to the Washington state patrol and to the identification division of the federal bureau of investigation in order that these agencies may search their records for prior arrests and convictions of the individual or individuals who filled out the forms. The board shall require fingerprinting of any applicant whose criminal history record information check is submitted to the federal bureau of investigation.

(2) The proposed sale of more than ten percent of the outstanding or issued stock of a corporation licensed under chapter 3, Laws of 2013, or any proposed change in the officers of such a corporation, must be reported to the board, and board approval must be obtained before the changes are made. A fee of seventy-five dollars will be charged for the processing of the change of stock ownership or corporate officers. [2022 c 16 § 62; 2013 c 3 § 8 (Initiative Measure No. 502, approved November 6, 2012).]

Intent—Finding—2022 c 16: See note following RCW 69.50.101.

Intent—2013 c 3 (Initiative Measure No. 502): See note following RCW 69.50.101.

RCW 69.50.342 State liquor and cannabis board—Rules. (1) For the purpose of carrying into effect the provisions of chapter 3, Laws of 2013 according to their true intent or of supplying any deficiency therein, the board may adopt rules not inconsistent with the spirit of chapter 3, Laws of 2013 as are deemed necessary or advisable. Without limiting the generality of the preceding sentence, the board is empowered to adopt rules regarding the following:

(a) The equipment and management of retail outlets and premises where cannabis is produced or processed, and inspection of the retail outlets and premises where cannabis is produced or processed;

(b) The books and records to be created and maintained by licensees, the reports to be made thereon to the board, and inspection of the books and records;

(c) Methods of producing, processing, and packaging cannabis, useable cannabis, cannabis concentrates, and cannabis-infused products; conditions of sanitation; safe handling requirements; approved pesticides and pesticide testing requirements; and standards of ingredients, quality, and identity of cannabis, useable cannabis, cannabis concentrates, and cannabis-infused products produced, processed, packaged, or sold by licensees;

(d) Security requirements for retail outlets and premises where cannabis is produced or processed, and safety protocols for licensees and their employees;

(e) Screening, hiring, training, and supervising employees of licensees;

(f) Retail outlet locations and hours of operation;

(g) Labeling requirements and restrictions on advertisement of cannabis, useable cannabis, cannabis concentrates, cannabis health and beauty aids, and cannabis-infused products for sale in retail outlets;

(h) Forms to be used for purposes of this chapter and chapter 69.51A RCW or the rules adopted to implement and enforce these chapters, the terms and conditions to be contained in licenses issued under this chapter and chapter 69.51A RCW, and the qualifications for receiving a license issued under this chapter and chapter 69.51A RCW, including a criminal history record information check. The board may submit any criminal history record information check to the Washington state patrol and to the identification division of the federal bureau of investigation in order that these agencies may search their records for prior arrests and convictions of the individual or individuals who filled out the forms. The board must require fingerprinting of any applicant whose criminal history record information check is submitted to the federal bureau of investigation;

(i) Application, reinstatement, and renewal fees for licenses issued under this chapter and chapter 69.51A RCW, and fees for anything done or permitted to be done under the rules adopted to implement and enforce this chapter and chapter 69.51A RCW;

(j) The manner of giving and serving notices required by this chapter and chapter 69.51A RCW or rules adopted to implement or enforce these chapters;

(k) Times and periods when, and the manner, methods, and means by which, licensees transport and deliver cannabis, cannabis concentrates, useable cannabis, and cannabis-infused products within the state;

(l) Identification, seizure, confiscation, destruction, or donation to law enforcement for training purposes of all cannabis, cannabis concentrates, useable cannabis, and cannabis-infused products

produced, processed, sold, or offered for sale within this state which do not conform in all respects to the standards prescribed by this chapter or chapter 69.51A RCW or the rules adopted to implement and enforce these chapters;

(m) The prohibition of any type of device used in conjunction with a cannabis vapor product and the prohibition of the use of any type of additive, solvent, ingredient, or compound in the production and processing of cannabis products, including cannabis vapor products, when the board determines, following consultation with the department of health or any other authority the board deems appropriate, that the device, additive, solvent, ingredient, or compound may pose a risk to public health or youth access; and

(n) Requirements for processors to submit under oath to the department of health a complete list of all constituent substances and the amount and sources thereof in each cannabis vapor product, including all additives, thickening agents, preservatives, compounds, and any other substance used in the production and processing of each cannabis vapor product.

(2) Rules adopted on retail outlets holding medical cannabis endorsements must be adopted in coordination and consultation with the department.

(3) The board must adopt rules to perfect and expand existing programs for compliance education for licensed cannabis businesses and their employees. The rules must include a voluntary compliance program created in consultation with licensed cannabis businesses and their employees. The voluntary compliance program must include recommendations on abating violations of this chapter and rules adopted under this chapter. [2022 c 16 § 63; 2020 c 133 § 3; 2019 c 394 § 4; 2015 2nd sp.s. c 4 § 1601; 2015 c 70 § 7; 2013 c 3 § 9 (Initiative Measure No. 502, approved November 6, 2012).]

Intent—Finding—2022 c 16: See note following RCW 69.50.101.

Findings—2020 c 133: "The legislature finds that recent reports of lung illnesses associated with vapor products demand serious attention by the state in the interest of protecting public health and preventing youth access. While state law grants the liquor and cannabis board broad authority to regulate vapor products containing marijuana [cannabis], the legislature finds that risks to public health and youth access can be mitigated by clarifying that the board is granted specific authority to prohibit the use of any additive, solvent, ingredient, or compound in marijuana [cannabis] vapor product production and processing and to prohibit any device used in conjunction with a marijuana [cannabis] vapor product." [2020 c 133 § 1.]

Effective date—2020 c 133: "This act is necessary for the immediate preservation of the public peace, health, or safety, or support of the state government and its existing public institutions, and takes effect immediately [March 25, 2020]." [2020 c 133 § 5.]

Findings—2019 c 394: See note following RCW 69.50.563.

Findings—Intent—Effective dates—2015 2nd sp.s. c 4: See notes following RCW 69.50.334.

Short title—Findings—Intent—References to Washington state liquor control board—Draft legislation—2015 c 70: See notes following RCW 66.08.012.

Intent—2013 c 3 (Initiative Measure No. 502): See note following RCW 69.50.101.

RCW 82.04.4488 Credit—Conversion to worker-owned cooperative, employee ownership trust, or employee stock ownership plan. (Effective July 1, 2024, until July 1, 2030.) (1) Beginning July 1, 2024, in computing the tax imposed under this chapter, a credit is allowed for costs related to converting a qualifying business to a worker-owned cooperative, employee ownership trust, or an employee stock ownership plan, as provided in this section.

(2) The credit is equal to:

(a) Up to 50 percent of the conversion costs, not to exceed \$25,000, incurred by a qualified business for converting the qualified business to a worker-owned cooperative or an employee ownership trust; or

(b) Up to 50 percent of the conversion costs, not to exceed \$100,000, incurred by a qualified business for converting the qualified business to an employee stock ownership plan.

(3)(a) Credit under this section is earned, and claimed against taxes due under this chapter, for the tax reporting period in which the conversion to a worker-owned cooperative, employee ownership trust, or an employee stock ownership plan is complete, or subsequent tax reporting periods as provided in (c) of this subsection.

(b) The credit must not exceed the tax otherwise due under this chapter for the tax reporting period.

(c) Unused credit may be carried over and used in subsequent tax reporting periods, except that no credit may be claimed more than 12 months from the end of the tax reporting period in which the credit was earned.

(d) No refunds may be granted for credits under this section.

(4)(a) The total amount of credits authorized under this section may not exceed an annual statewide limit of \$2,000,000.

(b) Credits must be authorized on a first-in-time basis.

(c) No credit may be earned, during any calendar year, on or after the last day of the calendar month immediately following the month the department has determined that \$2,000,000 in credit has been earned.

(5)(a) The department may require persons claiming a credit under this section to provide appropriate documentation, in a manner as determined by the department, for the purposes of determining eligibility under this section.

(b) Every person claiming a credit under this section must preserve, for a period of five years, any documentation to substantiate the amount of credit claimed.

(6) For the purposes of this section:

(a) "Conversion costs" means professional services, including accounting, legal, and business advisory services, as detailed in the guidelines issued by the department, for: (i) A feasibility study or other preliminary assessments regarding a transition of a business to an employee stock ownership plan, a worker-owned cooperative, or an employee ownership trust; or (ii) the transition of a business to an employee stock ownership plan, a worker-owned cooperative, or an employee ownership trust.

(b) "Employee ownership trust" means an indirect form of employee ownership in which a trust holds a controlling stake in a qualified business and benefits all employees on an equal basis.

(c) "Employee stock ownership plan" has the same meaning as set forth in 26 U.S.C. Sec. 4975(e)(7), as of July 1, 2024.

(d) "Qualified business" means a person subject to tax under this chapter, including but not limited to a C corporation, S corporation, limited liability company, partnership, limited liability partnership, sole proprietorship, or other similar pass-through entity, that is not owned in whole or in part by an employee ownership trust, that does not have an employee stock ownership plan, or that is not, in whole or in part, a worker-owned cooperative, and that is approved by the department for the tax credit in this section.

(e) "Worker-owned cooperative" has the same meaning as set forth in 26 U.S.C. Sec. 1042(c)(2), as of July 1, 2024, or such subsequent dates as may be provided by rule by the department, consistent with the purposes of this section.

(7) Credits allowed under this section can be earned for tax reporting periods starting on or before June 30, 2029. No credits can be claimed on returns filed for tax periods starting on or after July 1, 2030.

(8) This section expires July 1, 2030. [2023 c 392 § 5.]

Tax preference performance statement—2023 c 392 § 5: "(1) This section is the tax preference performance statement for the tax preference contained in section 5, chapter 392, Laws of 2023. This performance statement is only intended to be used for subsequent evaluation of the tax preference. It is not intended to create a private right of action by any party or be used to determine eligibility for preferential tax treatment.

(2) The legislature categorizes this tax preference as one intended to induce certain designated behavior by taxpayers, as indicated in RCW 82.32.808(2)(a).

(3) It is the legislature's specific public policy objective to encourage business owners to create an employee stock ownership plan or employee ownership trust, or to convert to a worker-owned cooperative, that allows the company to share ownership with their employees without requiring employees to invest their own money.

(4) If a review finds that the number of businesses in this state offering employee stock ownership plans, employee ownership trusts, or ones that have converted to a worker-owned cooperative, has increased because of the tax credit under this act, then the legislature intends for the legislative auditor to recommend extending the expiration date of the tax preference.

(5) In order to obtain the data necessary to perform the review in subsection (4) of this section, the joint legislative audit and review committee may access and use any relevant data collected by the state." [2023 c 392 § 4.]

Effective date—2023 c 392 §§ 4 and 5: "Sections 4 and 5 of this act take effect July 1, 2024." [2023 c 392 § 7.]

Findings—Intent—Short title—2023 c 392: See notes following RCW 43.330.590.

WAC 314-07-035 What persons or entities have to qualify for a liquor license? Per RCW 66.24.010(1), a liquor license must be issued in the name(s) of the true party(ies) of interest.

(1) **True parties of interest** - For purposes of this title, "true party of interest" means:

True party of interest	Persons to be qualified
Sole proprietorship	Sole proprietor and spouse.
General partnership	All partners and spouses.
Limited partnership, limited liability partnership, or limited liability limited partnership	<ul style="list-style-type: none"> • All general partners and spouses; • All limited partners that have more than 10% interest in the partnership and their spouses.
Limited liability company	<ul style="list-style-type: none"> • All members (or persons with equivalent title) with more than 10% interest in the LLC and spouses. (Note: In order for the liquor control board to identify the persons to be qualified, we will need to know all parties that have an interest in the limited liability company or have a pending interest.) • All managers (or persons with equivalent title) and their spouses.
Privately held corporation	<ul style="list-style-type: none"> • All corporate officers (or persons with equivalent title) and their spouses. • All stockholders (or persons with equivalent title) and their spouses who hold more than 10% of the issued or outstanding stock. (Note: In order for the liquor control board to identify the persons to be qualified, we will need to know all parties who have been issued or will be issued corporate stock.)
Publicly held corporation	All corporate officers (or persons with equivalent title).
Multi-level ownership structures	The liquor control board will review each entity to determine which individuals are to qualify according to the guidelines in this rule.
Any entity	Any person who is in receipt of, or has the right to receive, more than ten percent of the gross or net sales from the licensed business during any full or partial calendar or fiscal year. For the purposes of this chapter:

True party of interest	Persons to be qualified
	<ul style="list-style-type: none"> • "Gross sales" includes the entire gross receipts from all sales and services made in, upon, or from the licensed business. • "Net sales" means gross sales minus cost of goods sold.

(2) For purposes of this section, "true party of interest" does not mean:

(a) A person or entity receiving reasonable payment for rent (as determined by the board) on a fixed or percentage basis under a bona fide lease or rental obligation, unless the lessor or property manager exercises control over or participates in the management of the business.

(b) A person who receives a bonus as an employee, if: The employee is on a fixed wage or salary and the bonus is not more than twenty-five percent of the employee's prebonus annual compensation; or the bonus is based on a written incentive/bonus program that is not out of the ordinary for the services rendered.

(c) A person or entity contracting with the applicant(s) to sell the property, unless the contract holder exercises control over or participates in the management of the licensed business.

(d) A person or entity receiving payment of franchise fees on a fixed or percentage basis under a bona fide franchise agreement, unless the person or entity receiving payment of franchise fees exercises control over or participates in the management of the licensed business.

(e) A 401K, IRA, or nonfamilial trust.

(3) **Financiers** - The board may conduct a financial investigation of financiers.

(4) **Persons who exercise control of business** - The board may conduct an investigation of any person or entity who exercises any control over the applicant's business operations.

In cases where there is an entity who is in control of the day-to-day business operation (other than the owner) because of an agreement between the owner and the operator, the operating party becomes a true party of interest. The operator must meet all the qualifications of any other true party of interest and if approved, must be the licensee. The owner may be required to be named on the license as a party of interest based on the terms of the agreement, but will not normally be required to meet all the qualifications of a true party of interest.

(5) The board reserves the right to investigate any person or entity in a liquor license application or current liquor license where hidden ownership or misrepresentation of fact is suspected.

(6) For purposes of this section, a person or entity who takes more than ten percent of the profits and/or exercises control over the licensed business in a given agreement may be named on the license as a party of interest per this rule. Examples of this are lease, operating plan, concession or management agreement.

[Statutory Authority: RCW 66.08.030. WSR 17-12-030, § 314-07-035, filed 5/31/17, effective 7/1/17. Statutory Authority: RCW 66.08.030 and 66.24.010. WSR 15-11-106, § 314-07-035, filed 5/20/15, effective 6/20/15; WSR 10-10-126, § 314-07-035, filed 5/5/10, effective 6/5/10.

Statutory Authority: RCW 66.08.030, 66.24.010, 66.24.015, and 66.24.025. WSR 05-07-012, § 314-07-035, filed 3/4/05, effective 4/4/05.]

WAC 314-55-035 Qualifying for a cannabis license. A cannabis license must be issued in the name(s) of the true party(ies) of interest. The board may conduct an investigation of any true party of interest who exercises control over the applicant's business operations. This may include financial and criminal background investigations.

(1) **True parties of interest.** True parties of interest must qualify to be listed on the license, and meet residency requirements consistent with this chapter. For purposes of this title, "true party of interest" means:

Entity	True party(ies) of interest
Sole proprietorship	Sole proprietor
General partnership	All partners
Limited partnership, limited liability partnership, or limited liability limited partnership	All general partners All limited partners
Limited liability company (LLC)	All LLC members All LLC managers
Privately held corporation	All corporate officers and directors (or persons with equivalent title) All stockholders
Multilevel ownership structures	All persons and entities that make up the ownership structure
Any entity(ies) or person(s) with a right to receive revenue, gross profit, or net profit, or exercising control over a licensed business	Any entity(ies) or person(s) with a right to receive some or all of the revenue, gross profit, or net profit from the licensed business during any full or partial calendar or fiscal year Any entity(ies) or person(s) who exercise(s) control over the licensed business
Nonprofit corporations	All individuals and entities having membership rights in accordance with the provisions of the articles of incorporation or bylaws

(2) A married couple may not be a true party of interest in more than five retail cannabis licenses, more than three producer licenses, or more than three processor licenses. A married couple may not be a true party of interest in a cannabis retailer license and a cannabis producer license or a cannabis retailer license and a cannabis processor license.

(3) The following definitions apply to this chapter unless the context clearly indicates otherwise:

(a) "Control" means the power to independently order, or direct the management, managers, or policies of a licensed business.

(b) "Financial institution" means any bank, mutual savings bank, consumer loan company, credit union, savings and loan association, trust company, or other lending institution under the jurisdiction of the department of financial institutions.

(c) "Gross profit" means sales minus the cost of goods sold.

(d) "Net profit" means profits minus all other expenses of the business.

(e) "Revenue" means the income generated from the sale of goods and services associated with the main operations of business before any costs or expenses are deducted.

(4) For purposes of this chapter, "true party of interest" does not include (this is a nonexclusive list):

(a) A person or entity receiving payment for rent on a fixed basis under a lease or rental agreement. Notwithstanding, if there is a common ownership interest between the applicant or licensee, and the entity that owns the real property, the board may investigate all funds associated with the landlord to determine if a financier relationship exists. The board may also investigate a landlord in situations where a rental payment has been waived or deferred.

(b) A person who receives a bonus or commission based on their sales, so long as the commission does not exceed 10 percent of their sales in any given bonus or commission period. Commission-based compensation agreements must be in writing.

(c) A person or entity contracting with the licensee(s) to receive a commission for the sale of the business or real property.

(d) A consultant receiving a flat or hourly rate compensation under a written contractual agreement.

(e) A person with an option to purchase the applied for or licensed business, so long as no money has been paid to the licensee under an option contract or agreement for the purchase or sale of the licensed business, or a business that is applying for a license.

(f) Any business or individual with a contract or agreement for services with a licensed business, such as a branding or staffing company, will not be considered a true party of interest, as long as the licensee retains the right to and controls the business.

(g) A financial institution.

(5) **Notification.**

(a) Except as provided in this subsection (4)(a)(i), (ii), and (iii), after licensure the licensee must continue to disclose the source of all funds to be invested in the licensed business, including all funds obtained from financiers, prior to investing the funds into the licensed business.

(i) Revenues of the licensed cannabis business that are reinvested in the business do not require notification or vetting by the board.

(ii) Proceeds of a revolving loan where such loan has been approved by the board within the three previous years do not need to be vetted by the board, unless the source of the funds has changed or the approved loan amount has increased.

(iii) If the source of funds is an identified true party of interest on the license, or a previously approved financier associated with the license, or a previously approved revolving loan, the board will allow these funds to be used upon receipt of an application to use such funds. The board will then investigate the source of funds. If the board cannot verify the source of funds after reasonable inquiry, or the board determines that the funds were obtained in a manner in violation of the law, the board may take actions consistent with the provisions of this chapter.

(b) Licensees must receive board approval before making any ownership changes consistent with WAC 314-55-120.

(c) Noncompliance with the requirements of this section may result in action consistent with this chapter.

(6) **Disclosure agreements and intellectual property.**

(a) Licensed cannabis businesses may enter into agreements consistent with the provisions of RCW 69.50.395.

(b) Notwithstanding the foregoing, no producer or processors may enter into an intellectual property agreement with a retailer.

(7) **Financiers.**

(a) Consistent with WAC 314-55-010(11), a financier is any person or entity, other than a financial institution or a government entity, that provides money as a gift, a grant, or loans money to an applicant, business, or both, and expects to be paid back the amount of the loan, with or without reasonable interest.

(b) A financier may not receive an ownership interest, control of the business, a share of revenue, gross profits or net profits, a profit sharing interest, or a percentage of the profits in exchange for a loan or gift of funds, unless the financier, if directly involved in the loaning of funds, receives board approval and has qualified on the license as a true party of interest.

(c) Washington state residency requirements do not apply to financiers who are not also a true party of interest, but all financiers must reside within the United States.

(d) The board will conduct a financial and criminal background investigation on all financiers.

[Statutory Authority: RCW 69.50.342 and 2022 c 16 § 168. WSR 22-14-111, § 314-55-035, filed 7/6/22, effective 8/6/22. Statutory Authority: RCW 69.50.342, 69.50.345, 69.50.395 and 2019 c 380. WSR 20-18-099, § 314-55-035, filed 9/2/20, effective 10/3/20. Statutory Authority: RCW 69.50.342 and 69.50.345. WSR 16-11-110, § 314-55-035, filed 5/18/16, effective 6/18/16. Statutory Authority: RCW 69.50.325, 69.50.331, 69.50.342, 69.50.345. WSR 13-21-104, § 314-55-035, filed 10/21/13, effective 11/21/13.]