This booklet helps business owners evaluate employee ownership. It shows how selling to your employees can mean flexibility and fair market value for you, security for your workforce and community, and the deep satisfaction of knowing the people responsible for your company’s success after you have left.
Why do some business owners sell their companies to their employees?

As a business owner, you will someday have to decide who should own your business after you. Some people sell to family members, to investors or to other businesses. But over the past four decades, thousands of owners have decided to make their employees the next owners of their companies.

The most common path to employee ownership in the United States is an employee stock ownership plan, or ESOP. In an ESOP transaction, you sell your shares at fair market value to a trust, and the trust holds the shares for the benefit of your company’s employees. Across every state and nearly every economic sector, 6,000 privately held companies have ESOPs. Though the motivation varies, over 90% of respondents to our ESOP transaction survey reported being satisfied with their ESOP.

Another form of broad-based employee ownership, worker cooperatives are fast gaining in popularity. Often favored for their simplicity and democratic approach, worker coops number in the hundreds in the US with many more found overseas, including the world’s worker coop, the Mondragon Corporation, located in Spain’s Basque region.

The decision you make affects you, your family, your community, the people your company does business with, and your workforce. Striking the right balance is hard, and no one can understand that challenge better than people who were in your situation.

Why sell to an ESOP?

Joe Motz  
Founder and CEO, The Motz Group

I founded Motz Environmental Maintenance in 1977, becoming an established landscape maintenance and commercial grounds care presence in our Cincinnati community and beyond. I soon found myself in the position to sell our lawn care division to a large group in our industry who promised that they would look after our employees and our valued customers.

The promises weren’t kept. Sure, I received value in the end, but seeing a part of the company I built change only to the detriment of those who helped build it caused me a lot of pain, turning what should have been a joyous occasion into something altogether less gratifying. I wanted it done a better way.

I felt I found that better way in 2015, when I made the internal decision to sell the company “in” verses selling “out.” In the spring of 2018 I sold 20% of the company to the ESOP in a self-financed transaction without warrants. I’m thankful that we had been practicing financial literacy and transparency before the ESOP. This puts us in the best possible position for the employees to understand the significance of the ESOP and to make sure that it keeps the Motz Group going well into the future, for the benefit of those who helped build it and who we serve.

Holly Saltzman  
Founder and President, Imagine Early Learning Centers

Imagine Early Learning Centers’ reputation for building and operating top quality, multi-site, boutique early learning centers has always made us attractive to bigger companies. Perhaps the primary reason we have been so sought after is the strength of our staff. So when it became time for me to assess my options for transitioning out of the business, I looked at strategic buyers. However, for me to go through with selling the company, I wanted a guarantee that all Imagine employees would be given contracts—not just the executive team, but the assistant teachers, the bookkeepers—everybody. After getting very close to finalizing a deal, it became apparent that the buyer would not make this guarantee. I then realized that selling to a strategic buyer was not the right move for Imagine.

Since my hang-up with any potential buyer was protecting my employees, I decided to Google “employee-owned” and started reading. After reading about stock options and alternative business structures, I finally came to ESOPs. The information seemed daunting at first and there were times I thought my head might explode. But with repetition the process eventually began to make sense. It doesn’t seem that complicated anymore.

I’m proud to say that Imagine’s employees now own nearly 33% of the company. The plan is to sell the remainder to them in the next few years. Imagine has always been a team, and the employees are crucial to that team. In my view, they deserve to be rewarded both for their excellent work and for sticking with the company over the years.

“I imagine has always been a team, and the employees are crucial to that team. In my view, they deserve to be rewarded both for their excellent work and for sticking with the company over the years.” — Holly Saltzman
The National Center for Employee Ownership (NCEO) talk with owners at all stages of the transaction, and some of their most common questions are…

Q. How much will an ESOP pay?
A. The ESOP buys the stock at fair market value, as determined by an independent appraiser. ESOPs can also provide you tax benefits in the form of a deferral of capital gains. Third-party strategic buyers may pay fair market value up front, but owners who sold to an ESOP often find that their after-tax take-home is higher in an ESOP sale.

Q. Do employees pay for their shares?
A. It’s possible but rare. Generally, company contributions to the ESOP support the buyout of the selling owner’s shares while also providing a benefit to employees.

Q. What will my role be in the company?
A. It’s flexible. Some sellers stop working the day the sale is completed, or even before. Others provide for a long-term, orderly transition, and some remain as CEO or board member.

Q. Does employee ownership make a difference?
A. Typical ESOP companies outperform competitors and provide above-average compensation, benefits, and employment security.

Q. Do I have to sell 100% of my shares?
A. You can sell all or some of your shares. Unlike most other buyers, an ESOP can buy a portion of your shares or can buy in stages.

Q. Are ESOPs complicated?
A. No matter what anyone tells you, there is no simple, hassle-free way to sell your business. ESOP transactions require the support of experienced advisors because an ESOP is an employee retirement plan subject to substantial federal regulation. They also give sellers more control over the inherent risks of a business sale, and they may cost less and close more quickly than a sale to the third party.

See page 6 for information on the structure, price, and process of the sales transaction.
Shawn Burcham
Founder and President, PFSbrands

When I started researching my options for selling my company, I knew I wanted two things: I wanted the flexibility to stay involved in the business, and I knew I wanted PFSbrands to remain a thriving and vital part of central Missouri. This essentially ruled out third-party and private equity sales, because there are too many horror stories of those resulting in a business moving, massive layoffs, or closing.

I was familiar with the ESOP model from various supermarkets we distribute to, so we started exploring that around 2008, getting more serious about it in 2012. After assembling an awesome senior leadership team and examining our options, we decided that selling 100% of our S corporation was the best for all involved—doing so gave the company all the tax benefits possible while also demonstrating to the employees that I’m serious about giving them a stake in the outcome and seeing them make PFSbrands as successful as they possibly can.

So in 2017 we set up a long-term leveraged transaction which involved senior debt, seller financing, and seller warrants. Now the community and our employee-owners know these jobs aren’t going anywhere. And the proof is in the pudding—in the first year since the sale, our stock price is up 488%.

“Now the community and our employee-owners know these jobs aren’t going anywhere. And the proof is in the pudding—in the first year since the sale, our stock price is up 488%.” — Shawn Burcham

ESOP companies OUTPERFORM

- ESOP companies generate 2.5% more new jobs per year than these same companies would have generated if they did not have an ESOP.
- Employee-owners are one-third to one-quarter as likely to lose their jobs compared to non-employee-owners, according to the General Social Survey.
- ESOP companies default on their loans at a rate of 0.2% per year.
- Companies with ESOPs were 75% more likely to stay in business, according to research looking at the last two recessions.

ESOPs create GOOD JOBS

Among workers ages 30 to 36, employee-owners do better than non-employee owners:

- 90% higher or nearly 2 times the median household wealth at age 30
- 22% higher median income from wages
- 46% longer median job tenure

The relationships between employee ownership and improved economic outcomes for workers largely persist over time and when controlling for demographic factors.
ESOP SALES: Structure, price, and process

ESOP sales range from small and simple to complex M&A transactions.

In the simplest kind of transaction, the company buys shares from the selling owner and contributes those shares to the ESOP, which allocates them to employee accounts. Employees gradually build up an ownership interest as the owner sells more and more shares.

The most common structure is that an ESOP trust borrows money from an outside funder on standard commercial terms and uses that money to buy shares from the selling shareholders. The company makes annual contributions to cover the repayment of the loan. Common variations include seller financing, buying out the owner or owners in stages, and conversions between S and C corporation status.

ESOP transaction main steps
1. Complete a feasibility study and determining an initial valuation range
2. Hire the team of advisors
3. Develop the transaction structure
4. Conduct due diligence
5. Establish the trust and appoint the trustee.
6. Determine fair market value by the trustee and independent appraiser
7. Negotiate the transaction terms and conditions
8. Close the transaction and communicating to employee-owners.

Valuation
ESOPs are financial buyers and cannot pay a strategic price. An independent appraisal firm values the shares being purchased by the ESOP at fair market value. If the ESOP is buying a minority interest the price will likely include a minority interest discount. Most ESOP valuations also include a small discount for lack of marketability.

Governing the transaction
The ESOP trustee, generally an outside institution or an individual with specific expertise in ESOPs, ensures that the ESOP transaction meets all the legal requirements and that the ESOP does not pay more than fair market value. The trustee is obligated to work solely in the interest of plan participants.
Roger Ryberg  
**Former Owner and CEO, Windings**

I know I’m mortal. So I started exploring my exit options in 1990, only seven years after I bought the company from its founder, JW McKinney.

That’s 28 years before I exited the company in full. I loved working at Windings, I love the company and its people and I’d love to still be working there to this day, but the reality of the situation is you can’t live forever.

I was drawn to the ESOP idea because I knew that I wanted to see Windings continue to benefit its employees and its community in New Ulm, Minnesota. Employee ownership seemed like a win-win-win: a win for the owner, the employees, and for the community. Private equity or a third-party sale would take away our independence without the employees reaping potential reward.

So a little over 10 years after I started exploring my options, I began selling Windings to its employees through an ESOP. I sold the company piece by piece, with my wife and me financing all but the last transaction without warrants. I sold 13% at a time until the ESOP reached majority ownership, then sold two 15% tranches. At this point I wanted to sell the rest of the company in a transaction that was financed with a local bank.

When I acquired Windings in 1983, it was a $700,000 per year business. By the time I sold my last portion to the ESOP, it was a $25 million business and financially strong such that the local bank that financed the final transaction didn’t even ask my wife and me to cosign the loan! And it’s only grown stronger since then, doubling in share value in the time since I left in 2008.

Exiting over time allowed me to continue steering the ship through the transition. What’s more, as the share value grew, so did the value of my retirement, as both an ESOP participant and as the majority owner. Most of all, I’m proud to say that our company is still a thriving and important part of the community, one that is owned by all the people who continue to make it great.

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Kevin Mauger  
**President, NCC Automated Systems**

I didn’t strongly consider anything but the ESOP, which now owns 42% of the shares. I plan on selling off the remainder of my shares at some point, either all at once or in tranches along the way, but I’m not exiting NCC Automated Systems yet and I have no desire to work elsewhere.

At the core of this is me asking myself, “How do we take the next step as a company?” To have a thriving environment, you have to have really strong players whom you challenge and to whom you provide opportunity. In order to further that environment and to leave a lasting impact for all of these great people in my life, it starts with growth. One of the foundational ways of encouraging that growth is by providing a stake in the game through an ESOP.

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Curt Curry  
**Manager of IT Support and employee-owner, Cape Air**

It’s life-changing to be a part of a company that’s employee-owned. As an employee-owner, every decision I make is not only for myself but for everyone around me and every other department around me. There’s a real connection. There’s a real desire to take things to another level and to be a part in making the best possible decisions, not just around personnel but also equipment issues and issues of fiscal responsibility. So I think it truly transforms your relationship with your company.

“It’s life-changing to be a part of a company that’s employee-owned.”

— Curt Curry
ESOPs aren’t the only way to implement broad-based employee ownership at your company. Worker cooperatives are fast gaining in popularity thanks to their simplicity and democratic principles.

**What is a worker cooperative?**

A worker cooperative is a values-driven business that puts worker and community benefit at the core of its purpose. The two central characteristics of worker cooperatives are:

- Workers own the business and they participate in its financial success on the basis of their labor contribution to the cooperative
- Workers have representation on and vote for the board of directors, adhering to the principle of one worker, one vote

In addition to their economic and governance participation, worker-owners often manage the day-to-day operations through various management structures.

At a worker cooperative, workers have financial equity that allows them to share the real risk and reward of small business ownership. Workers also have meaningful participation in business decisions, including the ability to voice their desires and improve their work life. A worker cooperative is owned and controlled by its workers.
A brief history of worker cooperatives in the United States

Though we don’t yet have comprehensive data on the nature and scope of worker cooperatives in the U.S., our research has verified 465 worker cooperatives in the United States. These democratic workplaces employ around 7,000 people and generate over $550 million in annual revenues. The number of worker cooperatives has grown steadily over the past 20 years, and is made up of both well-established businesses and new, growing ones, increasingly including some businesses that have been sold to their employees by their owners.

Any business can be a worker-owned and -controlled business. In the U.S., worker cooperatives tend to be concentrated in the service and retail sectors. Common industries include:

- Accommodation and food service
- Health care
- Manufacturing and engineering
- Technology
- Design

Many of the worker cooperatives in existence today were inspired by the Mondragon Cooperatives in Spain, which enabled the Basques to lift themselves out of poverty and build what is today Spain’s 7th largest corporation, a worker cooperative.

Worker cooperatives are currently experiencing a surge in popularity, marked by industry and sector concentrations and the growth of a support infrastructure that includes financing, technical assistance providers and trade associations at the local, regional and national levels. Interest in worker cooperatives as a job creation and wealth-building strategy is also on the rise, with community organizations, cities, and small business advocates seeing potential in the form to build a more inclusive economy.

This recent growth in the worker cooperative sector can be traced back to the 1970s and 1980s, when all of today’s largest worker cooperatives were founded, as part of an explosion in alternative economic forms. Those cooperatives that survived have thrived, and have helped seed new growth through investment of capital and expertise in a second wave of worker cooperative development starting in the late 1990s. By 2000, several worker cooperative development organizations had begun to have success using the form as means to create good jobs for low- and moderate-income workforces, from home care to housecleaning.

WORKER COOPERATIVE FACTS AND FIGURES

- Number of worker cooperatives in the United States: 465-800
- Total number of people working at worker cooperatives in the United States: 7,000
- Total annual revenues generated by worker cooperatives: $550 million
- Average size of a worker cooperative: 50 people (the median is 10 people)
- Largest worker co-op: Cooperative Home Care Associates (CHCA) with more than 2,000 workers
- Number of worker cooperatives formed since the start of the 21st century: over 150
- Percentage of worker cooperatives that began as traditional for-profit enterprises: 26%
- Percentage of worker cooperatives that have annual revenues over $1 million: 31%
- Average annual profit margin for a worker cooperative: 6.4%
- Worker cooperatives structures: 46% incorporate under cooperative statutes, 26% operate as LLCs and the remainder are C-corporations, partnerships, and other.
The transition process for worker cooperatives

The process takes an investment of resources and professional assistance to ensure success and long-term benefits. While unique for each business, the process generally has five stages. Durations can vary widely, depending on the complexity and readiness.

**EXPLORE** (timeframe varies) — the business owner studies worker ownership and decides if it is an idea worth pursuing

**ASSESS** (3-6 months) — the business owner works with experienced professionals to affirm an ownership transition is feasible

**STRUCTURE** (6-12 months) — a transition team establishes the sale terms and leadership changes

**EXECUTE** (3-6 months) — the transaction is financed with lender support and the company legally changes hands. In most cases, employees will require outside or seller financing to make the purchase.

**SUPPORT** (timeframe varies) — leadership and operational gaps are addressed with ongoing training for staff in new roles with new responsibilities.

### What are the differences between ESOPs and Worker Cooperatives?

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<tr>
<th>ESOPs</th>
<th>Worker Cooperatives</th>
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<td>Stock owned by trust, employees own indirectly</td>
<td>Direct ownership of stock, one vote per shareholder</td>
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<td>Better option for larger companies (minimum 20 employees)</td>
<td>Good option for companies of all sizes (minimum 5-6 employees)</td>
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<tr>
<td>Significantly more expensive to set up and maintain</td>
<td>Affordable to set up, even from very beginning</td>
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<td>Strong tax benefits</td>
<td>Modest tax benefits</td>
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<td>Can have democratic structure but up to board and founders</td>
<td>Inherently democratic</td>
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<td>Can take on most kinds of financing</td>
<td>More limited financing options (though getting better)</td>
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Why form a worker cooperative?

Carolyn Edsell-Vetter
A Yard and a Half

A Yard and a Half was founded by Eileen Michaels in 1998. It is a landscaping company located in Massachusetts. She planned to retire and decided to sell the company to her employees. The cooperative was formed to preserve and continue to develop a locally-owned, safe, and democratic workplace in an industry where workers often face exploitation, wage theft, and hazardous working conditions.

Our former boss really just found good people and then found a way to make them fit, and she really grew the company based on the strengths of the people that she had working for her.

One of the challenges for an owner thinking about co-op conversion is becoming conscious of all of the hats that they wear as a sole owner. When the time came to sell to the employees, Eileen developed a management team where five of us started meeting with her on a regular basis and she started being more transparent about what it takes to run a business.

“From a business perspective, worker-owned companies tend to be substantially more profitable and productive.”

Matthias Scheiblehner
Metis Construction

Any small business owner knows what goes into running a small business—the lack of sleep, a lot of stress—and to be able to work with a group of people that you really like to work with, to share that risk and to share that stress makes working through stress and crises something that draws everybody together and actually is really rewarding.

From a business perspective, worker-owned companies tend to be substantially more profitable and productive.

For our worker-owners, there’s a lot of advantages that come with this. They participate, they share in the profits. The best way I can describe it is a community, being a part of something that is bigger than me but connects me to the work we do in a way I wasn’t connected to it before. It’s a pretty amazing experience to walk into work every day knowing you’re doing some small thing to make the world a more just and equitable place. And I wouldn’t have it any other way.

“One of the challenges for an owner thinking about co-op conversion is becoming conscious of all of the hats that they wear as a sole owner.”
How you can learn more

As the leading source of information on ESOPs and employee ownership, the NCEO is committed to helping businesses make informed decisions. We’re happy to help guide you through the process of figuring out if an ESOP is right for you.

Start with the essentials: Our ESOP Essentials (nceo.org/esop-essentials) membership offers six months of exclusive educational content with curated resources for selling business owners.

Speak with an employee-owned company in your state or industry: We can connect you with an NCEO member in your area or industry to learn about their experience and better decide whether an ESOP will suit your succession needs. Contact Timothy Garbinsky at 510-208-1310 or TGarbinsky@nceo.org to get started.

Become an NCEO member: As an NCEO member, you can call us anytime with questions at 510-208-1300.

Interested in worker-cooperatives? Learn how to get started with the Democracy at Work Institute at institute.coop/conversion.

THE NATIONAL CENTER FOR EMPLOYEE OWNERSHIP (NCEO) is a nonprofit membership organization established in 1981 to provide practical resources and objective, reliable information about employee ownership to businesses, employees, and the public. We have more than 3,000 members, from companies and the professional advisors who assist them to academics, government officials, and others.

The NCEO holds meetings, such as our annual conference (with 1,800-plus attendees); conducts weekly webinars; is the main publisher in the field, with more than 60 publications; conducts employee surveys and compiles and distributes data on ESOP companies; and provides speaking and introductory consulting services. Our work also includes assistance to academics and extensive contacts with the media, both through interviews and through writing articles.

We do not lobby or provide ongoing consulting services. We are qualified as a 501(c)(3) charitable nonprofit.

National Center for Employee Ownership
1629 Telegraph Ave., Suite 200, Oakland, CA 94612
(510) 208-1300 | nceo.org

THE DEMOCRACY AT WORK INSTITUTE (DAWI) was founded by the US Federation of Worker Cooperatives as the only national think-and do-tank expanding the promise of worker ownership to communities locked out of good jobs and business ownership opportunities, especially for BIPOC, immigrant, and low-wage workers. Through research, innovation, government relations, and education, DAWI supports worker ownership as the superior business model for creating jobs with dignity, fair compensation, and opportunities for wealth and skill-building.

DAWI brings both a birds-eye view of the national stage and an experiential on-the-ground understanding of cooperative business, making sure that the growth of the cooperative movement is both rooted in worker cooperatives themselves and branches out to reach new communities of worker-owners.

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