



# Alternatives to an ESOP

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# Agenda

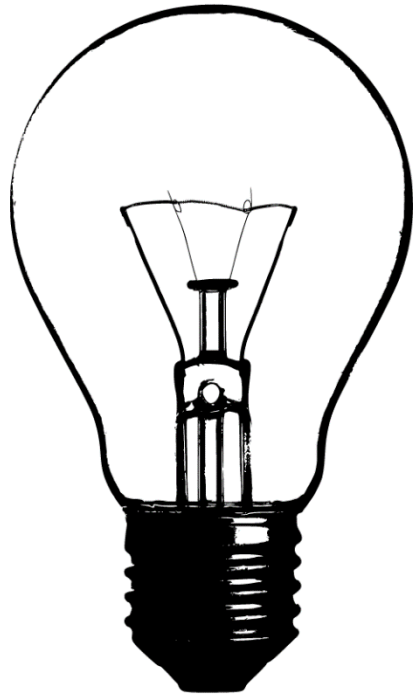
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- 8 Key Questions to Ask Yourself
- Determining Goals & Objectives
- Market Timing Considerations
- Ownership Transition Paths
- Corporate Governance
- Preparing the Business
- Sale Timelines
- Transaction Roles & Responsibilities
- Management Succession





# 8 Key Questions to Ask Yourself



- 1 Where do you see the ownership of your company in the next 5 to 10 years?
- 2 Are the exit timelines consistent?
- 3 What strategies are available that will meet these expectations?
- 4 How do you assess your choices in ownership transition?
- 5 Do you understand the tax consequences of various exit types?
- 6 How can you prepare yourself and the company for an exit in order to maximize value?
- 7 How will ownership transition impact your estate plan?
- 8 How do you identify management succession issues?



# Determining Goals & Objectives



## Reason for Sale

- Retirement / diversification
- Attractive M&A marketplace
- Industry forces
- Shareholder timing
- Lack of succession



## Your Requirements

- Value expectations
- Tax planning
- Continued employment
- Continued ownership
- Size of transaction



## Potential Deal Killers

- Minimum value
- Buyer fit
- Company legacy
- Employee welfare
- Intentions of acquirer

When selling a business, there are a number of factors, both economic and non-economic, that can impact the seller's decision



# Market Timing Considerations

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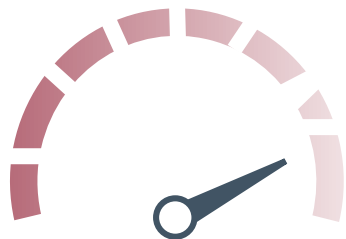
## Unique Situation of Company

- Seller Objectives
- Liquidity Needs
- Health Issues
- State of Preparation



## Industry & Company Dynamics

- Company performance
- Sector performance
- General economic performance
- Good performance → Good valuation



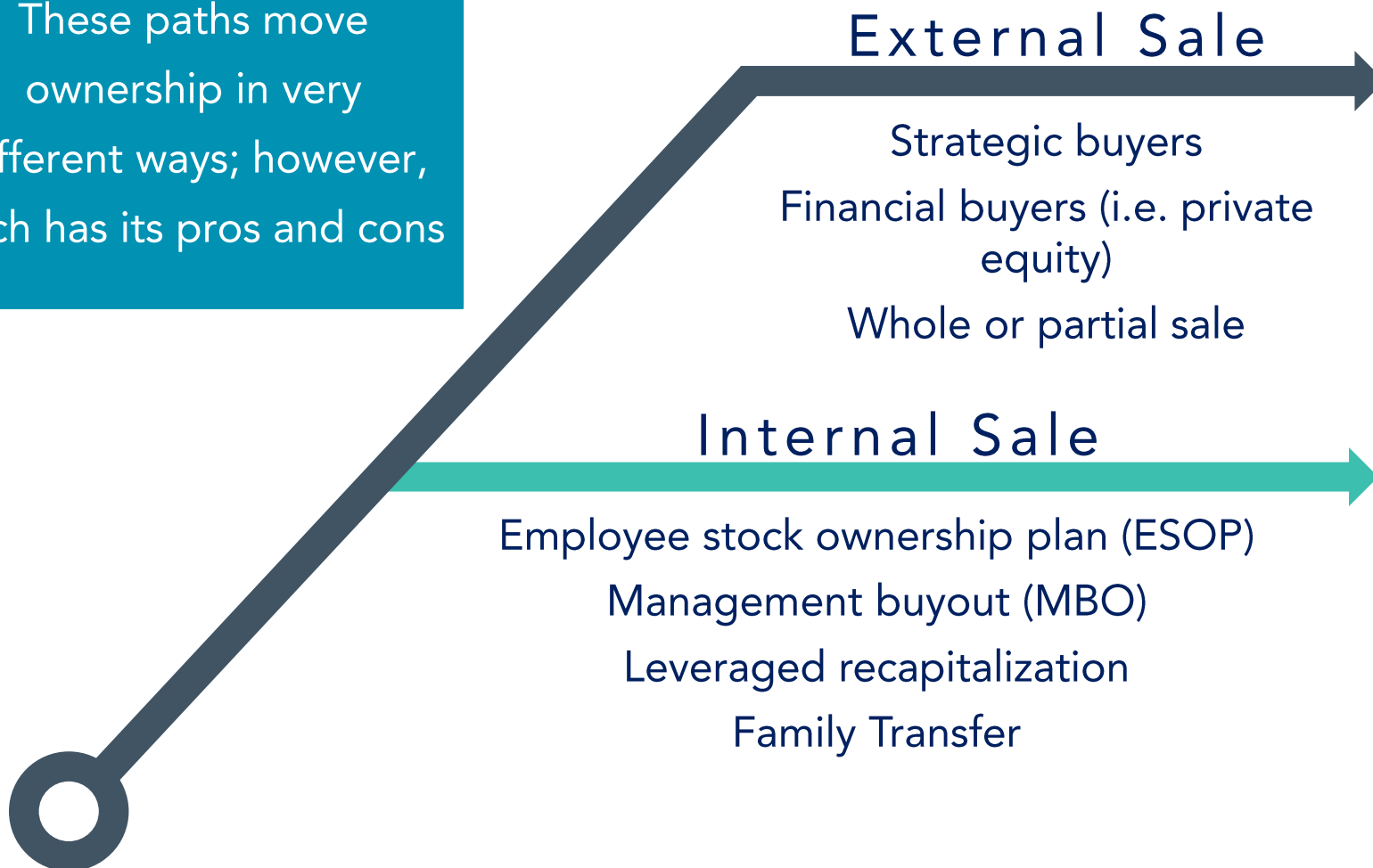
## Market Conditions

- Strategic acquirer activity
- Private equity appetite
- Bank lending conditions



# Ownership Transition Paths

These paths move ownership in very different ways; however, each has its pros and cons





# Ownership Transition Paths

## External Sale Pros & Cons

### Strategic Buyers

- ✔ Potential to maximize value
- ✔ Potential to maximize liquidity at close
- ✔ Potential opportunities for management
- ✔ Strong understanding of the business
- ✘ Consolidation motive may eliminate jobs
- ✘ Potential loss of legacy

### Private Equity

- ✔ Potential to maximize value
- ✔ May provide legacy protection
- ✔ Infusion of talent / expertise
- ✔ Opportunity for second liquidity event
- ✔ Possible management equity participation
- ✔ Owner may continue running the company
- ✘ Lack of in-depth business knowledge
- ✘ New owner / operator partner (partial sale)
- ✘ Investment rollover may be required



# Ownership Transition Paths

## Internal Sale Pros & Cons

### ESOP

- ✔ Tax – advantaged buyout
- ✔ Partial / total transaction
- ✔ Controllable transaction / structural flexibility
- ✔ Ability to continue to manage business
- ✔ Maintain legacy / employee-owned culture
- ✘ No strategic pricing
- ✘ Partial liquidity at close
- ✘ Administrative costs / regulatory oversight
- ✘ Non-productive debt
- ✘ Need succession planning

### MBO

- ✔ Business continuity
- ✔ Maintain legacy
- ✔ Opportunity for management to build wealth
- ✘ Lack of capital by management
- ✘ Negotiations can be adversarial
- ✘ Management motivations may change
- ✘ Need capable management team
- ✘ Non-productive debt







# Ownership Transition Paths

## Internal Sale Pros & Cons

### Recapitalization

- ✓ No loss of ownership
- ✓ Partial liquidity
- ✓ Controllable transaction
- ✓ Ability to continue to manage business
- ✓ Use for redemption of shareholder
- ✗ No transition
- ✗ Tax inefficient
- ✗ Non-productive debt
- ✗ Limiting financing (asset light businesses)

### Family Transfer

- ✓ Keep business in the family
- ✓ Provide future opportunities for family
- ✓ Opportunity for tax-efficient transfer
- ✗ Need capable management team
- ✗ Liquidity needs may not be met
- ✗ Value expectations may not be met
- ✗ No strategic value
- ✗ Family relationship complexities





# Ownership Transition Alternatives

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Sometimes, the best decision is to do nothing...

Really? Nothing?





# Ownership Transition Alternatives

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Holding on while building value may be an alternative

- Depending on shareholder objectives, not exiting at the current time may be the right alternative
  - Bigger payday; right timeline for the business; right timeline for potential buyers
  - While holding on, you should Focus on value drivers
  - Both internal and external

While holding on, you should **build value**

- Focus on value drivers
  - Both internal and external

You may not have control over drivers, and there are negative drivers to value!





# Preparing the Business

## Drivers of Company Value

An understanding of what drives value is critical to the decision to sell and the timing of a sales process. It's a balance of internal and external forces.

Value reflects the current characteristics of...

- The Company itself
- Its competitive marketplace
- The general economy and capital markets

## Adjustments to Earnings

The goal is to provide an accurate representation of the Company's ongoing earnings potential.

Adjustments may include:

- Income/expenses that are one-time in nature
- Expenses that are in excess of "normal" levels
- Expenses that will no longer continue in the future

## Getting Legal Affairs in order

- Corporate good standing, minutes, stock ownership records
- Continuity of key employees/stay bonuses
- Document important agreements with co-owners, joint venture partners, affiliates, customers and suppliers
- Intellectual property protection/infringement
- Other obstacles to closing? Environmental, non-competes, and third party consents to transactions
- Tax planning / Estate planning for sale

## Getting Financial Affairs in Order

- Identify financial statement problems
- Deal with pending and threatened claims
- Tax problems? Accuracy of tax returns?
- Insurance policies



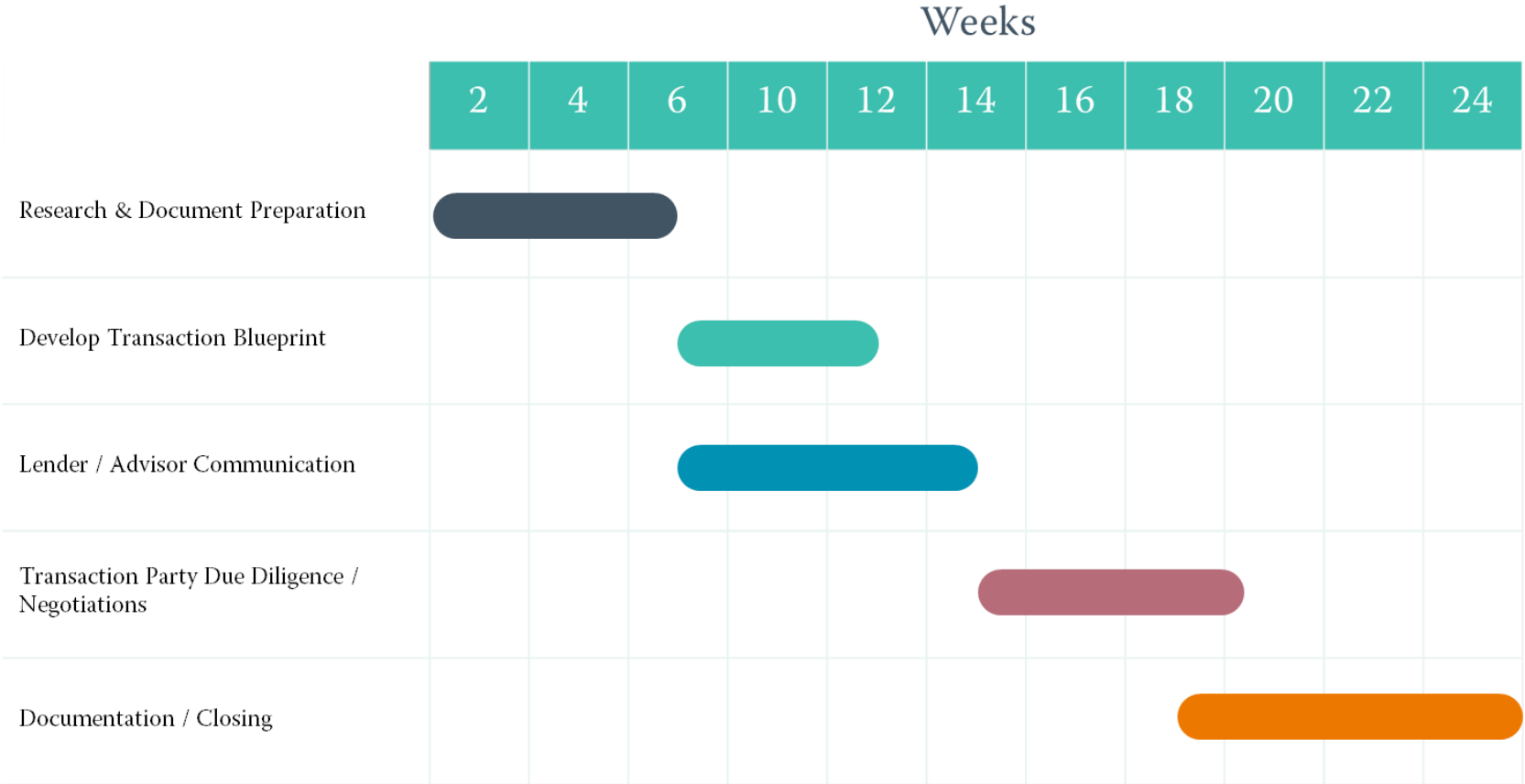


# External Sale Timeline





# Internal Sale Timeline





# Management Succession

## Assessing Skills & Development Timelines

You need the right people with the right skills at the right time

Is there ample time for developing bench strength?

## Identifying Gaps & Obstacles

Are there holes in the management structure?

Have you given thought for personal timelines?

## Internal Options for Succession

You need to make sure they are ready

... and, you need to keep them as employees

## External Options for Succession

You need to be able to compete for them in the marketplace

Are they proven? Are they a good cultural fit?

## Proper Compensation is Key

Real equity (stock, stock options)

Synthetic equity (stock appreciation rights, phantom stock)





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