

6 Frequently Asked ESOP Questions Answered



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1 WHAT TYPES OF BUSINESSES ARE BEST SUITED FOR AN ESOP?

Any type of business can be an ESOP. There are ESOPs of nearly every size in very diverse industries across the country. There are no specific size requirements to form an ESOP. A feasibility study can help business owners decide if an ESOP will work for them. Of note, numerous studies have shown that ESOPs often become more competitive in the marketplace due to changes in tax structure, improved employee recruitment and retention, and changes in culture. ESOPs also offer owners a liquidity solution that does not require them to sell all of their company; allowing them to take some "chips off the table" while still working in the business.

2 DO ESOPS REQUIRE EMPLOYEE OWNERS TO PUT "ALL THEIR RETIREMENT EGGS IN ONE BASKET"?

ESOPs do not require employees to use their own retirement savings or any of their earnings to participate. ESOPs are designed to supplement normal retirement savings, potentially creating more retirement savings than may be available to employees otherwise. A study done by the NCEO shows that 95% of companies with ESOPs also offer a 401(k) plan.

3 WILL I RECEIVE THE SAME AMOUNT SELLING TO AN ESOP AS I WOULD SELLING TO OTHER POTENTIAL BUYERS?

The value received by selling shareholdings is similar to what can be received when selling to any financial buyer such as private equity, Strategic buyers, those buyers who can benefit from synergies created post acquisitions such as staff reductions, can sometimes pay more. However, tax advantages and transaction structures can offset some or all of any differences in value. Advisors can help quantify this difference.

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4 I HAVE BEEN TOLD BY AN ADVISOR THAT ESOPS ARE TOO COMPLEX AND EXPENSIVE TO CONSIDER AS AN OPTION IN SELLING MY BUSINESS, IS THIS TRUE?

Many advisors do not have a lot of experience with ESOPs. Due to this lack of experience many advisors will view ESOP transactions as too complex. That is simply not the case. Like with any transaction, experience is important and there are a number of advisors who specialize in ESOP transactions. Generally speaking, the fees associated with an ESOP transaction are similar to or less than those that would be incurred in a non-ESOP transaction.

5 ARE THERE TAX ADVANTAGES WHEN SELLING MY COMPANY TO ANY ESOP?

There are numerous tax advantages available to the company and seller. Some advantage include:

- Shareholders who decided to sell at least 30% of their company to an ESOP may qualify to defer tax related to the sale.
- The Company may be able to deduct contributions to the plan.
- 100% S-corporation ESOPs can eliminate all corporate income taxes.

Advisors can help quantify these advantages and help structure transactions to take advantage of tax incentives and deductions.

6 AFTER AN ESOP IS PUT IN PLACE, DO THE EMPLOYEE OWNERS TAKE CONTROL OF THE BUSINESS AND HAVE ACCESS TO FINANCIAL STATEMENTS AND OTHER INFORMATION?

No. Roles and responsibilities within the Company do not change after becoming an ESOP and employee owners do not have the right to review any financial information. However, many ESOP companies share some data as part of the ESOP educational process.

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