



SUCCESSION PLANNING AND EMPLOYEE OWNERSHIP

A workbook for business owners

Prepared by The ICA Group for the City of Cambridge

www.icagroup.org

What is exit planning?

- Based on premise that at some point, every business owner will leave their business
- Includes: owner's target departure date, owner's financial needs, succession plan, preliminary valuation,



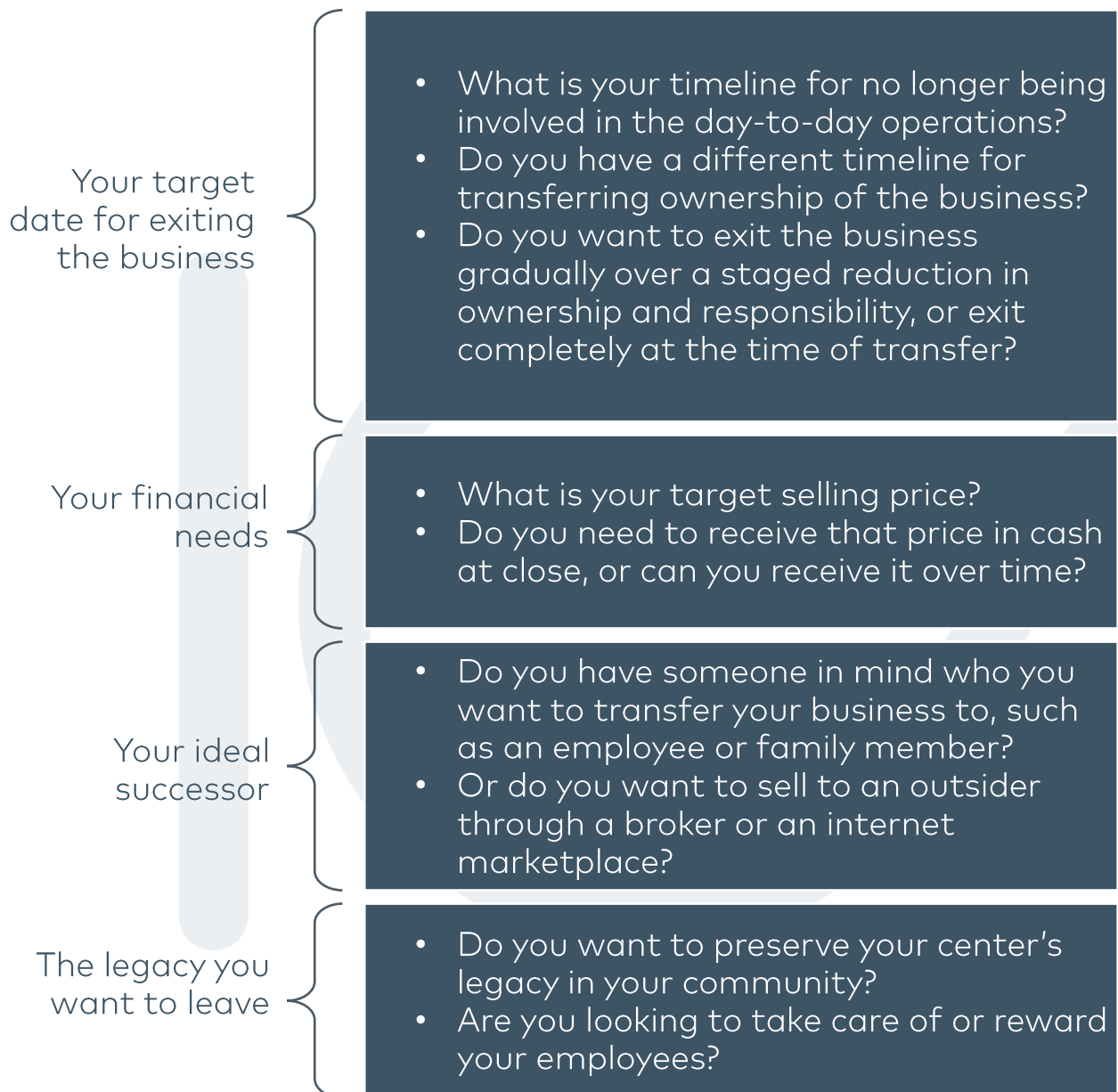
By creating and executing an exit plan, business owners can transfer ownership while assuring that their goals can be achieved during the transaction



A successful exit plan...

- Maximizes the value of your business at the time of ownership transfer
- Minimizes the risk for the owner and the business
- Serves as a tool to maintain owner control throughout the transition process

Identify your goals for exiting your business



Your Succession Options

As you begin to explore an exit plan for your business, it is wise to know what your options are. Below are four common options available to business owners considering their plans for retirement.

Third Party Sale

Using a Broker or Investment Banker

Advantages	Challenges	Your Notes
<ul style="list-style-type: none"> • The buyer can typically finance the purchase of the sale leading to more cash up front. • Owners can typically exit on a faster timeline • Often generate the most money for the selling owner 	<ul style="list-style-type: none"> • Buyers are often selective about the businesses they'll consider (only about 20% of businesses listed with brokers sell) • Could result in changes to the culture and "feel" of the company • Typically results in the selling owner having no control or connection to the business post-sale 	

Management Buyout

Selling to a trusted employee

Advantages	Challenges	Your Notes
<ul style="list-style-type: none"> • Buyers can maintain what is working well with operations and culture • Buyers are more likely to know how the business works • Buyers have pre-existing relationships to staff and customers 	<ul style="list-style-type: none"> • Sellers may not receive as much money as in a sale to a third party • Sales typically require seller financing, leading to less cash up front 	

Family Transfer

Selling or gifting the company to an heir

Advantages	Challenges	Your Notes
<ul style="list-style-type: none"> • Maintains or creates a family legacy • Meaningful for the owner to see their family members take the reigns • Buyers are more likely to know how the business works and have relationships with customers and vendors 	<ul style="list-style-type: none"> • Often not sustainable for numerous generations (our kids don't always <i>want</i> to own our businesses) • Mixing business and family can be complicated • Likely requires seller financing leading to less cash at close 	

Selling to Employees

Broad Based Employee Ownership (Cooperative, ESOP, or Employee Ownership Trust)

Advantages	Challenges	Your Notes
<ul style="list-style-type: none"> • Can preserve the legacy and values of the company • Rewards employees for years of service • Sale can happen gradually, at the chosen pace of the seller • Employees already have relationships with customers and vendors 	<ul style="list-style-type: none"> • May not receive as much money as in a sale to a third party • Likely requires seller financing 	

Worker Ownership

What does it mean for your business?

What is a worker cooperative?

A worker cooperative is a business that is owned and controlled by its workers.

Employee cooperatives are almost always for-profit businesses. They sell a product or service to customers, with the goal of generating a profit for the business and its owners. Like conventional businesses, worker cooperatives incorporate with the state, secure appropriate business licenses, pay taxes, and hire employees.

What does it mean for workers to own a business?

"Ownership" of a business gives owners the right to business profits and decision-making about how the business is run. In a worker cooperative, workers can purchase a membership share to become an owner of the business.

- **Profits:** Worker-owners are entitled to a portion of the money the business makes after expenses. This surplus is distributed to workers based on hours worked.
- **Decision-making:** A membership share also grants workers a decision-making vote in the business. Each worker can only own one membership share, and when the cooperative holds elections, they do so on a one person, one vote basis. Worker control can take many forms, but at a minimum, worker-owners elect the company's Board of Directors and receive information about how the business operates and how it is performing.

How are worker cooperatives started?

Some businesses are started as worker-owned cooperatives, but many start out as conventional companies. Owners decide to convert their business to worker ownership to preserve their legacy, retain community jobs, reward employees, or simply because it offers a profitable and flexible pathway to sell the business. Often this process occurs as the owner retires or moves on from the business. Other owners choose to continue to work at the business while sharing the risks and rewards of ownership with their employees.

Who is buying the business? Who pays for it?

The business typically takes out a loan to purchase the shares from the selling owner and then pays off the loan using its profits. In other words, workers are not expected to find enough money to purchase the full value of the company out of their own personal finances; most of the money to finance the transaction comes from the company's cash flow.

Generally, a small portion of the purchase price is funded by the workers, who purchase a membership share to become worker-owners. Each cooperative sets its share price in proportion to the profits the worker is expected to receive for owning a share. Typically, this translates to a cost of roughly \$1,000 to \$5,000 per share.

Is this the same as a management buy-out?

No. In a conversion to worker ownership, the shares of the business are transferred from the existing owners to a broad base of employees. All workers who meet certain basic eligibility requirements (such as length of time at the company or hours worked) can become owners, not just management or a small group of workers. In the future, as new workers join the business and meet eligibility requirements, they too will have the opportunity to become owners.

How does the conversion to worker ownership work?

The ICA Group works with business owners of all types to convert their firm to a worker cooperative. We provide simple, straightforward tools designed to ensure that the interests of all parties are addressed. Every business is unique, and so are the objectives of the owners who wish to sell their business. We'll walk you through the three basic phases of transferring your business to your employees:

1. **Owner Planning** – ICA works one-on-one with the owner to determine whether a conversion to worker ownership will work for their business and meet their personal and financial goals.
2. **Worker Engagement** – Through a series of presentations and trainings, ICA supports workers in learning about worker ownership, developing the skills needed to take over the business, and structuring the new entity.
3. **Transaction Execution** – ICA supports both workers and owners in completing the legal and financial transaction.

Who makes the decision to convert the business?

Many decisions are made during the process of converting the business to worker ownership by many stakeholders. Rather than one yes or no decision, conversions are a structured, staged process of information sharing and decision making.

- **The Owner:** Typically, it is the selling owner who decides to start exploring worker ownership. The owner also decides what conditions need to be met in order to sell to the workers, including selling price, any seller financing, and transaction timeline.

- **The Staff:** Once the owner is certain that they want to pursue conversion to worker ownership, workers are presented with the opportunity and given a chance to shape what the converted business will look like. Generally, a steering committee of interested workers, with the support of the owner and the ICA Group, works to develop new organizational policies. This committee gathers input and feedback from all workers throughout the process to ensure that a number of workers will pursue ownership.
- **Individual Workers:** As the transaction structure and new organizational policies are finalized, each individual worker decides whether to purchase a member-share and become an owner.

For both owners and workers, these decisions can be challenging and emotional. Building trust and sharing information throughout the process are necessary for a conversion to succeed.

How long does it take?

In general, the process takes about a year, depending on an owner's goals, the health of the business, and financing needs. The ICA Group can provide post-conversion support to worker-owners as they develop their ownership culture and learn to successfully run the business. This support can range from a short training series to multi-year partnerships, depending on business needs and interests and funding sources.

What does The ICA Group do?

The ICA Group is a nonprofit business consulting and development firm that has helped convert over 50 businesses to worker ownership. Our staff help support all phases of the process including business valuation, access to financing, worker training, and more. To begin exploring this process, we start with a free owner consultation.

Succession Planning for Business Owners

Preliminary Exit Planning Worksheet

Background:

Your Business's Name: _____ Entity Type: _____
 Your Name: _____ % Ownership: _____

Timeline:

When do you need to end your involvement in day-to-day operations? _____
 How long could you continue to own stock in, or stay involved? _____

Non-Financial Goals:

Besides proceeds from the sale, what else do you wish to achieve from exiting the business?

- Give back to community; be charitable: _____
- Maintain company culture: _____
- Preserve business legacy: _____
- Provide for employees: _____
- Start new venture: _____
- Other? _____

Potential Successors:

Please indicate which options you would consider when exiting the business. Rank your preferences.

- Third-party open-market sale: _____
- Management buyout: _____
- Broad-based employee ownership (i.e., worker coop, ESOP): _____
- Family member: _____
- Liquidation and closure: _____

Financial Goals:

Have you had a business valuation, or know what your business is worth? _____

What is your financial goal for the sale of the business? _____

Of this amount, how much would you need in cash at closing? _____

Is there a gap between the business' value today, and your financial goals? _____

Your Personal Goals:

- What goals do you have regarding the sale of the business, and the future of the business after you exit?

- How much longer do you want to work in or be involved in the business?

- To whom have you considered selling or transferring the business?

- What are your short- and long-term personal financial goals?

Business Situation:

- Is your business profitable?

- What are the biggest challenges and opportunities facing the business?

- How much cash do you need immediately from the sale or transfer of your business (vs. payment in a seller's note payable over a period of years)?

Ownership Culture:

- To what extent do employees learn how things work and help make decisions?
- To what extent do employees share in business outcomes like profits and recognition?

Business Financials:

- In what state are your financial records, and have they been reviewed for accuracy or cleaned up by any third party?
- How would you describe the effectiveness of your accounting systems in collecting payments and managing books overall?
- Regarding your customers, how would relationships with them be affected by a transfer?
- Do you have any clauses in contracts and/or licensing requirements limiting transferability?
- Do you have any recurring revenues or long-term contracts?
- Do you have a plan to strengthen or grow your company?

People & Operations:

- Regarding any key employees, do you have incentive plans to ensure they stay on before, during, and after a sale?

- To what extent have operational processes been documented, and are transferable?

- How would you describe your organizational culture?
 - To what extent do employees learn how things work and help make decisions?
 - To what extent do employees share in the business outcomes like profits and recognition?

Industry Strategy:

- What competitive advantages does your company have compared to others in the same industry/market? Any competitive disadvantages?

- What are the biggest challenges and opportunities facing the business?

Next Steps Toward Employee Ownership

Once you've completed the Preliminary Exit Planning Worksheet and are ready to explore a transition to employee ownership, use the checklist below to help guide your next steps:

- ❑ Organize your financial records – Gather and compile your company's financial statements for review. Include profit and loss statements and balance sheets from the last three to five years, as well as year-to-date statements.
- ❑ Identify personal and non-recurring expenses – Create a list of any personal expenses currently run through the business, as well as any one-time or unusual expenses.
- ❑ Document your current role – Outline your responsibilities in the company. Consider what you handle on a daily, weekly, monthly, and annual basis. Write a job description for your current role.
- ❑ Ensure current policies and practices of the company are well documented – employee handbooks, policy handbooks, procedural documents, and job descriptions should all be updated.
- ❑ Consult a financial advisor – Discuss your long-term financial goals and retirement needs with a qualified advisor.
- ❑ Engage with an employee ownership specialist – Connect with a professional who can guide you through the specifics of transitioning to employee ownership.

Contact the ICA Group for more information and to schedule a free consultation.

Phone: 617-232-8765

Email: info@icagroup.org

Learn more: www.icagroup.org