

ESOP Transaction Steps



Details of the activities in each step are outlined below. While the list is abbreviated, it provides an overview of ESOP Affiliates' involvement in each ESOP transaction.

1. Feasibility Study

- A. Interview & Data Request - Client management team is interviewed; financial and operational data is collected. Analyst performs due diligence and studies the issues affecting the company.
- B. Organizational Issues - Considers whether the management structure has the depth to continue operating as an autonomous, independent entity.
- C. Market Issues - Considers the company's market viability, and reviews the company's position in that market.
- D. Human Resource Issues - Evaluates management capability and continuity, in addition to the company's ability to fill new and replacement positions.
- E. Operations - Assesses the company's supply chain, management control systems, productivity, and quality control.
- F. Financial Analyses - Analyzes historical and prospective financial data, and determines if the payroll is adequate, in terms of IRC section 405 and 415, to support a buyout.
- G. Business Valuation - Develops a letter summary fair market valuation of the proposed shares being sold to the ESOP.
- H. Legal Issues - Identifies potential legal obstacles to an employee buyout, including pending litigation, environmental, pension, and corporate issues.
- I. Presentation - Written Feasibility Study is presented to client. Any negative findings are discussed, with plans made to address each.

2. Raise Financing

- A. Offering Memorandum - The Feasibility Study forms the basis of the Offering Memorandum for submission to ESOP funding sources.
- B. Lender Submission - Offering Memorandum and Financing Proposal is prepared, and application is made to select affiliated ESOP lenders.
- C. Negotiate Financing Terms - Buyout loan terms, including representations and warranties, are negotiated with lender on client's behalf.

3. Independent Valuation

- A. Engage Valuation Firm - Select and engage valuation firm with specific ESOP experience, and provide with information. Valuation firm must be independent to the transaction.
- B. Manage Business Valuation - Required standard of value is Fair Market Value as defined in IRS Revenue Ruling 59-60. Explain and negotiate valuation drivers with analyst.

4. Plan & Trust Development

- A. Establish ESOP Committee - The ESOP Committee may be composed of company management and staff personnel, although initially it includes only the seller(s).
- B. Plan & Trust Design - Plan and Trust Document drafts are prepared by ESOP Affiliates to minimize legal input and corresponding fees. SPD is prepared and reviewed.
- C. Engage Law Firm - Engage and manage affiliated law firm with specific ESOP experience.
- D. Establish Trust - Establish employee stock ownership trust to acquire client's stock. Trustee can be current company owner, management personnel, or third-party trust firm.
- E. Review Plan Document - Reviews Plan Document, making any changes to conform to current tax and labor law. Prepare stock sale agreement and other transaction documents.
- F. Determination Letter and Bank Documents- Send request for determination letter to the Internal Revenue Service. Review and negotiate loan documents with bank counsel.

5. Close

- A. Communicate Plan to Employees - Introduce conceptual framework to employees, and establish a strong communication channel to ensure comfort level.
- B. Close Transaction - The transaction is closed, with sales proceeds being disbursed accordingly. All transaction and loan documents are executed.
- C. Complete Plan Structure - Assign positions within the ESOP Committee, develop communication vehicles and frequencies.
- D. Hire Plan Administrator - Plan Administrator must be a specialist in ESOP administration.
- E. Education - Continue employee education process to ensure full understanding of ESOP benefits and the resulting increase in employee motivation.
- F. Repurchase Planning - Developing repurchase liability plan in years 2-3 through insurance or investment products.