Selling to the Team

A BUSINESS OWNER'S GUIDE TO ESOPS AS AN EXIT STRATEGY

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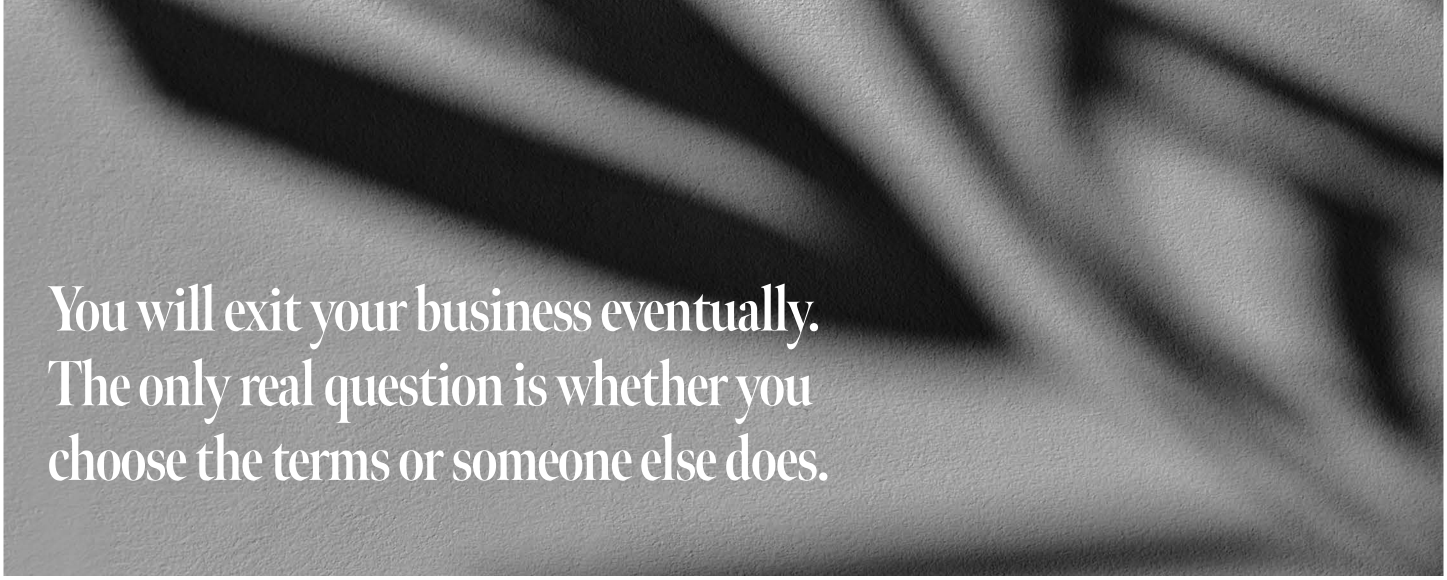

You will exit your business eventually. The only real question is whether you choose the terms or someone else does.

The scale of what's coming makes that question urgent. The Exit Planning Institute's most recent State of Owner Readiness research found that 75% of business owners intend to transition within the next ten years. That's as many as 4.5 million privately held businesses and roughly $14 trillion of wealth changing hands by 2033, the largest transfer of private business wealth in history. When that many owners head for the door in the same decade, the prepared ones set their terms. The rest take what's offered.

And you don't always get to pick your moment. We call them the five Ds. Death, Divorce, Disability, Distress, and Disagreement force sales every year, on timelines nobody chose and at prices nobody would have accepted with time to prepare. You can't schedule the five Ds. You can only decide whether one of them finds you with a plan or without one.

The cost of getting this wrong isn't just financial. Research cited by the Exit Planning Institute found that 75% of business owners profoundly regretted selling their company within a year of closing the deal. That's what happens when the sale gets planned and the life after it doesn't.

You've probably been told your options start and end with a family transition or a sale to private equity. Both are viable. This paper is about another path, selling to an ESOP, that gets far less attention, even though it touches more than six thousand companies nationwide. Selling to an ESOP isn't right for everyone. What it offers is control. Control over the timing, the terms, the confidentiality, and the legacy of your exit.

This whitepaper walks through what an ESOP is, whether your business fits the profile, what you stand to gain, and who you'll want around the table if you decide to take a closer look.

What an ESOP Actually Is

An ESOP is a qualified retirement plan, like a 401(k), except the plan invests in the stock of the company that sponsors it. In this case, yours. In other words, an ESOP is a tax-advantaged structure that allows your employees to become beneficial owners of the company over time. That doesn't mean employees are personally cutting you checks to buy the business. In most ESOP transactions, the company uses debt and future cash flow to fund the purchase of shares from you, the selling owner.

It helps to think about an ESOP in three ways at once, because it really is doing three jobs at the same time.

- **A transition tool.** It moves ownership from you to a trust. That trust steps in as a single buyer, which can be simpler than running a competitive auction with outside buyers. You retain board control throughout the transition.
- **A retirement plan for your employees.** Like a pension or profit-sharing plan, it is qualified, non-discriminatory, and grows tax-deferred for participants. Your employees pay nothing out of pocket to participate.
- **A leveraged buyout, structured for tax efficiency.** Most ESOP sales are financed with debt your company repays over time, similar in structure to a private equity buyout.

The tax treatment is a big part of the appeal. Sell at least 30% of a non-publicly traded C corporation to the ESOP, reinvest the proceeds in qualified replacement property, and Section 1042 of the tax code may let you defer the capital gain entirely. Hold that property until death, and the gain disappears for good through a stepped-up basis. If you own an S corporation, your benefit shows up on the company's tax return instead. The ESOP's share of the profits escapes federal income tax, and a company that becomes 100% ESOP-owned can result in significant tax advantages. Few other buyers can offer you any of that.

Is Your Business a Fit?

Certain ownership situations tend to line up especially well with an ESOP. See if any of these sound familiar.

- You want liquidity, partial or full, and you're willing to share ownership with the people who helped build the business.
- You have a management team capable of running the company without you in the room every day.
- You're not quite ready to fully step away and would rather sell in phases, or you've already stepped back, and management runs the day-to-day.
- You need to buy out a partner, or consolidate a shareholder base that has fragmented across too many family members and generations.
- Confidentiality matters to you, whether because you run a professional services or government-contracting firm or because you simply don't want the market knowing your company is for sale.

What You Gain

- Capital gains deferral and, potentially, elimination through a Section 1042 rollover.
- The ability to sell up to 100% of your company at fair market value, on your own timeline.
- The option to retain operational and board control through the transition period.
- Certainty of confidentiality that a broad market process simply cannot match.
- A way to reward the employees who built the company alongside you and preserve your legacy in the community.

The Trade-offs

- The ESOP can only pay fair market value. If a strategic buyer or a roll-up pays a premium above that, the ESOP may not be able to match it. However, your after-tax proceeds from a Section 1042 rollover may equal or exceed the proceeds from a taxable sale.
- You likely won't receive 100% of the purchase price in cash at closing. A seller note is common, which means part of your payout depends on the company's future performance.
- Your company takes on a repurchase obligation, the requirement to buy back shares from employees who retire or leave, which needs to be funded and planned for well in advance.
- An ESOP is regulated by both the IRS and the Department of Labor, and it is not a quick or simple structure to unwind once it is in place. Go in with your eyes open.
- It's not the right fit if your management bench is thin, since the business still needs to run, and run well, without you. But the payout stretches over a few years, so you get a built-in runway to develop the team that replaces you.

It Doesn't Have to Be All or Nothing

Nothing about an ESOP requires you to sell the whole company, and that opens up a strategy most owners never hear about. If your plan is to transition the majority of the business to your children, an ESOP can sit alongside that transition rather than compete with it. Your family keeps

control. The ESOP buys a minority stake. Your employees get an ownership stake in what they helped you build. The mechanics are appealing. You take chips off the table at a fair price without running a sale process. Your family inherits a company whose employees have a financial reason to stay through the transition, which is exactly when key people tend to walk. If your company is an S corporation, the ESOP's slice of the profits stops being taxed, which frees up cash to service the debt and fund the buyout. And you can sell additional tranches later, either to the ESOP or to the next generation, as everyone gets comfortable.

Who Sits at the Table

An ESOP transaction pulls together more advisors than a typical sale. An independent trustee, legally required to represent the ESOP and its participants, arrives with its own counsel and valuation advisor. Specialized ESOP counsel drafts the plan and ERISA documents. A plan administrator runs the plan after closing. Your CPA and corporate counsel handle diligence and tax structuring. Lenders fund the deal. And your personal wealth and estate advisors work through the Section 1042 rollover and how the sale fits your broader estate and tax plan.

None of these parties report to each other, and none of them owns the timeline. That's a lot of people at one table, and left to their own devices, they don't naturally align. Someone has to keep them connected and keep the process on track. At NewEdge Wealth, that's the role we play, and we built a practice around it. Onward is our wealth management offering designed for entrepreneurs at every stage of the business, from building it, to a liquidity event, to succession, and whatever comes after.

We're here to act as your quarterback. Not replacing your trustee, your attorney, or your lender. We make sure they're all working off the same plan and the same timeline. We keep the handoffs from getting dropped, chase down the open items, and keep every advisor pointed at the outcome you're after.

You've got a business to run. You shouldn't have to project manage a dozen specialists on top of it. We carry that coordination so you can stay focused on the decisions that matter.

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Where This Leaves You

If what you want is certainty of close, a tax-efficient path to liquidity, and a way to hand the company you built to the people who helped you build it, an ESOP deserves a seat at the table next to whatever offer eventually comes knocking.

The earlier you start exploring whether your business fits the ESOP profile, the more options you'll have when the timing is finally right. The result is simple: you choose the terms.

Sources

1. Exit Planning Institute, Certified Exit Planning Advisor Program, Module 16, ESOPs as an Exit Strategy.

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3. Exit Planning Institute, 2025 State of Owner Readiness Generational Report.

4. PricewaterhouseCoopers research on post-sale owner regret, cited in the 2025 State of Owner Readiness Generational Report.

5. ESOP.org, “What Is an ESOP (Employee Stock Ownership Plan)?,” esop.org.

6. Internal Revenue Code Section 1042, qualified replacement property and capital gains deferral provisions, as amended by the SECURE 2.0 Act of 2022, Section 114.

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