

# Financing the EO Model



# Capital for Colleagues



Advice Investment Growth

# Why employee ownership?



**EMPLOYEE OWNED  
BUSINESSES GREW SALES BY**

**11.1%**  
**IN THE RECESSION  
COMPARED TO  
NON-EMPLOYEE  
OWNED BUSINESSES  
WHICH ONLY GREW  
BY 0.6%**



\*Cass Business School, 2014

**OPERATING  
PROFITS  
OF THE TOP 50  
EMPLOYEE OWNED  
BUSINESSES  
INCREASED  
25.5%**

\*Capital Strategies 2014



**PRODUCTIVITY\*  
INCREASED  
4.5%  
YEAR-ON-YEAR  
IN EMPLOYEE-OWNED BUSINESSES  
PRODUCTIVITY  
IN THE UK ECONOMY  
AS A WHOLE IS FLAT**

\* Value added per employee = Operating profit plus salaries, wages and payroll expenses divided by the average number of employees.

Source:  
Cass Business School  
Capital Strategies

# Why employee ownership?

**EMPLOYEE  
NUMBERS  
INCREASED BY  
3.3%  
YEAR-ON-YEAR  
IN EMPLOYEE-OWNED BUSINESSES**



\*Capital Strategies 2014

**THE NUMBER OF  
EMPLOYEE OWNED  
BUSINESSES IS  
GROWING AT AN  
ANNUAL RATE  
OF JUST UNDER  
10%**



**80% OF  
EMPLOYEE OWNERS  
ARE HAPPY TO  
RECOMMEND THEIR  
ORGANISATION  
AS A PLACE  
TO WORK**



\*Edinburgh Napier University, 2012

**80% OF  
EMPLOYEE OWNERS  
EXPERIENCE  
A SENSE OF  
ACHIEVEMENT  
FROM THEIR JOBS**

\*Edinburgh Napier University, 2012

Source:  
Capital Strategies  
Edinburgh Napier University

# EOB project



## PROJECT MANAGEMENT

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### Options

- Trade sale
- MBO/BI
- Listing
- EOB
- ...

### First steps

- People motivation
- Owners' wishes
- Share ownership structure

### Bring to life

- Project team
- Engage Directors & managers
- Price agreed
- Legal work
- Articles of Association
- ET, Options, SIP
- Tax advice
- ...
- Plan for launch
- Event

### Funding

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- Price
- Funding model
- Funding partners
- Financial due diligence
- Business due diligence

### Engaging employees

#### Governance

- Employee elected Director
- Appoint Trustees
- Training
- Monthly, quarterly, annual meetings

### Make it work

#### Employee engagement

- Rights, responsibilities
- Communicate
- Employee councils
- Change behaviour
- Grow EO culture

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# Ownership structures



- **Direct ownership** – employees hold shares directly or through a tax advantaged share plan 
- **Indirect ownership** – shares held collectively on behalf of employees through an Employee Trust 
- **Combination** – direct and indirect ownership 



# Background to C4C involvement with TPS



- **WTB Group (TPS former parent & former EOB)**
- **C4C (founded by WTB directors and shareholders)**
- **TPS**
- **TPS Transition to EOB Independence**
- **TPS Ongoing EOB funding considerations**
- **Lessons Learned**



- **Core business founded 1929 in Birmingham UK – specialist distributor of civil engineering products**
- **Early 1980's following death of founder shares gifted to charitable trust with balance to management**
- **1983 one of the first UK tax qualifying all employee share schemes established. Direct holdings for all employees**
- **1984-2008 Turnover growth from £24m-£350m employees 100 - 1200**
- **2008 £15m returned to initial management and employee shareholders funded by RBS and HBOS....**
- **2012 core business sold to USA based Wolseley PLC and balance of Group placed in administration by directors following EU restrictions on Wolseley deal.**



- **Conceived in 2008 by WTB in partnership with Castlefield Capital Ltd (EOB & professional investors and advisors to the WTB charitable trust) as a result of difficulties in funding the buyout of WTB employee shareholders**
- **Initially capitalised by way of investment from WTB Employee Benefit Trust and some WTB shareholders in conjunction with High Net Worth clients of Castlefield**
- **Floated on UK ISDX market in 2013 and has subsequently made a series of loans and equity investments in former WTB EOB's and other SME's and raised further crowd finance**
- **Current Market Cap c £5m with investments in 12 companies across 20 sites in the UK and Ireland with 350 colleague employees**



- **Former Irish sister company to WTB's UK core and theoretical beneficiaries of WTB's EBT**
- **Mini Group under ROI holding company with NI and ROI subsidiaries both well established and historically profitable but heavily loss-making through GFC 2008-2012**
- **Historic revenues in excess of £15m and > 40 employees reduced by over half by 2012**
- **No interest from Wolseley who had just pulled out of the Irish market.**
- **No confidence from any advisor, funder or WTB administrator (D&P) in the future of the market or the company at that time in the absence of WTB funding**
- **D&P required a break up value for the companies assets £300k > than the security value of those assets in the event a funder could be found**
- **As it turned out, no confidence from over half the company's management team either who progressively departed through 2013 as negotiations with D&P and funders took place !**
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# TPS – Transition



- **Fortunately, the residual management and colleagues remained totally committed, there was insider cause for optimism (Irish Water) and C4C retained confidence through historic connection.**
- **The company's depot in Cork was closed and a compromise reached with the landlord. One of the two depots at Newtownabbey in Northern Ireland was consolidated into the other at Lisburn. Interim**
- **A debt settlement was ultimately agreed with D&P and concluded in Dec 2013 in which the company's property in Clondalkin was sold to a customer and an element leased back on favourable terms and following rejection from Bank of Ireland Bibby provided Invoice Discount Finance in what was then their largest deal in Ireland**
- **C4C provided £300k of mezzanine finance with all ordinary equity acquired by management and employees at nominal value.**
- **Market conditions have subsequently improved and TPS has secured a leading position in a number of niches returning to profitability and repaying £100k of C4C funding. 20 jobs were saved.**
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# TPS – Ongoing EOB funding considerations



- **The current ordinary share ownership structure is 80% shared between a management team of three and a 20% Employee Ownership Trust in favour of the other approx 20 employees**
- **The company is now entitled to redeem the remaining £200k of C4C preference capital, is close to having the capacity to do so and the double digit coupon set to cover initial risk provides further incentive to redeem.**
- **However, whilst not ruling out the prospect of a future trade exit, management's current preference is to develop the business with the further support of C4C in the form of both capital and management input with a view to ultimately realising their investment through sale or partial sale to the EOT with the support of C4C**
- **A new investment agreement is currently being finalised which incorporates an ongoing valuation model of the ordinary equity on an EBITDA multiple less debt and comprises the basis on which C4C will hold a new class of participating share and also provide a market in the ordinary equity and either buy or sell accordingly or fund the EOT through loans to do the same.**

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# TPS – Ongoing EOB funding considerations



- **A commitment is being made to pay 20% of annual profit after tax to all employees on a pro rata basis and further provision is being made for up to one third of profits to be paid by way of dividend or bonus to ordinary shareholders at the option of the board**
- **There remains a longer term option for the company to redeem C4C's equity on the basis of the valuation model from which the cumulative value of any dividends received in the meantime will be deducted**
- **C4C also receive a management fee for the ongoing input of a mutually agreed Associate to support the ongoing development of the business. That fee is index linked to the average remuneration of all employees including bonus**
- **The business plan (which involves going back to Cork and re-purchasing a property !) indicates that the average employee bonus could rise from 6 - 14% of remuneration over the next five years and that the value of the EOT holding will be of the order of £400k. C4C will earn a healthy overall return albeit subordinated to other stakeholders**

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# Lessons Learned (personal)



- **Its easier to establish and sustain an EO culture in smaller entrepreneurial businesses than large bureaucratic ones (Its also comparatively easy for small entrepreneurial business to quite quickly become large bureaucratic ones !)**
- **It is crucial for the interests of all stakeholders to be aligned for a long term EOB to be sustainable. It's structurally easier to achieve that under a 100% indirect model but not necessarily easy to get there or appropriate to do so**
- **Where direct shareholdings by individuals are involved, there is an inevitable need for long term funding partners (who may be those shareholders but that can be quite limiting)**
- **Cultural and structural considerations are far more important than tax incentives (which can nevertheless be helpful not least in attracting the interest of professional advisors)**
- **EO is potentially a very attractive exit route for many more businesses than are either aware of it or fully appreciate why. It need not require an act of great selflessness by a business owner but rather a series of actions of enlightened self interest**
- **The business performance and quality of life benefits which come from getting it right are unquestionable but its also quite possible to get it wrong. There is a huge opportunity here for the business advisory community**



**Thank you**

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