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Graceful Exit

North Carolina builder-developer Ashley Turner takes an unconventional approach in planning to sell his companies to his employees.

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ASHLEY TURNER'S TENOR NORTH Carolina voice quivers with excitement. He has just rolled out a new profit-sharing deal for his 30 employees—who he describes as the “greatest, grandest people”—and he can't wait to talk about it. “Each month the team meets their sales quota,” he says. “Each individual on the team gets $5,000 per month in addition to their salary. They get more if they go over 100 percent of quota. The program makes no difference between the receptionist and the senior vice president. They all get the bonus.”

Turner likes rewarding the people whose hard work have helped his business grow, and he's probably written out a lot of bonus checks since he started out. He's already in his second career as a land developer and home builder. His first career in the industry began in 1989 and ended in 1994 when he sold out and retired at the age of 42. But he didn't stay idle long. Turner built a shopping center, started and sold a corporate appliance store, and founded and sold yet another development company before launching Ashley Turner Enterprises, which became the parent company for Columbus Real Estate and a group of home building, development, and building supply companies bearing the Ashley Turner name.

THINKING AHEAD: Ashley Turner hasn't retired yet, but his dream is to turn his company over to those who helped him build it. This year, his companies will develop 440 lots and build and sell 760 homes for about $113 million, making Turner the fifth-largest builder in the Raleigh-Durham area. From his base of operations in Johnston County, N.C.—which includes Raleigh and Garner—Turner has rapidly expanded into four more ocean-side locations in North and South Carolina, including Myrtle Beach. He's also planning to expand into one or two venues each in both Florida and Virginia.

However, once the expansions succeed, Turner says he will retire again—only this time, instead of selling out, he wants to sell “in” to his employees. Turner's exit strategy reflects a lot about him as an individual. His plans say as much about his unconventional approach to business as they do about his graciousness toward those who've helped him succeed.

An owner in Turner's position usually has three standard options for retiring from a successful business: sell out entirely to a national builder; sell out partially; or sell to employees via an employee stock ownership plan (ESOP). But Turner won't take those conventional paths. He's set on selling to his employees, but without an ESOP. He's intent on doing things differently—the way he always has.

Loyalty, Loyalty, Loyalty One thing that distinguishes Turner in these times of rightsizing, outsourcing, and off-shoring is his loyalty to his employees. Even across a phone line, a listener can tell Turner's smiling when he discusses them. “For 30 people to do the amount of business I've done in the last roughly 20 years is unheard of. Most companies my size have around 100 employees,” he says. “My people have devoted much of their lives to the company. They know how to run it.”

TURNER'S TEAM: In front, left to right, are Laura Taylor, Chaz Elam, and Debbie Johnson. In the back, left to right, are Steve Kornegay, Jackie Gross, and Charlie Crocker. Empowering his people and helping them succeed has bred deep-rooted loyalties to Turner, say current and former employees. Paul Smith, who began as the sole agent at Turner's real estate agency, Columbus Realty, just finished buying the company from his former boss. Smith now has 14 agents working for him and just signed a franchise agreement with Weichert Realtors to open four more offices in the next two years. Smith says, “I never envisioned myself being an owner. I never saw how big I could think until I got around a big [picture] thinker” like Turner. Although Smith doesn't work for Turner any-more, he still sells most of Turner's homes. And he's relocating to South Carolina for up to a year to help make Turner's expansion into the state a success, adding, “I won't leave until I have the right people in place.”

Torri Rockwell was a prize-winning custom builder in her own right before joining Turner's company three years ago. She's now a regional vice president heading up Turner's expansion efforts in Myrtle Beach, S.C. She recalls: “[Turner's] been talking about selling to the employees ever since I've known him. The main reason is that he's a self-made person, and he wants to make sure the people around him are successful. He does lots of charity work, and he wants his community to be successful, too.”

Debbie Johnson, vice president for the Piedmont region operations, has worked with Turner on and off for the past 20 years. “He's given me opportunities as a single mother that no other man, especially in the South, would have given me,” she says. “He's very fair to women. He looks at us all as individuals.”

Turner, for his part, is emphatic that it's his employees who really built his business and created his success. That's why he rejected two offers during the past seven years to sell out. “It would have been very lucrative for me, but I chose not to do that because of the loyalty of my employees and their possible displacement,” he says. “No one was willing to commit to five- or 10-year contracts with my employees, and I wouldn't sell under those circumstances.”

Turner's unwavering loyalty to his employees, however, doesn't solve the dilemma of how to make employee ownership a reality. As other business owners have discovered, employees, individually or as a group, are hard pressed to come up with the tens of millions of dollars it would take to buy them out. Home equity loans just don't cover it.

GROWTH MOMENTUM Experts Weigh In Why doesn't Turner choose to take the conventional ESOP route? It worked for Holiday Builders, of Melbourne, Fla., whose founder, Larry Sietsma, used the structure to reward his employees for their loyalty to him. Holiday Builders' CEO Richard Hawkes, who was Sietsma's vice president, initially opposed an ESOP and thought his boss ought to sell out. “Then I changed my mind and decided it was a very good thing,” he says. Today, the company is highly successful and undergoing a wave of expansion.

Tony Avila, managing director for JMP Securities of San Francisco, “heavily” advises Turner to use an ESOP for its tax advantages. Neither ESOPs nor their owners pay income taxes until the owners cash out. Theoretically that doesn't happen until retirement, so it's easy for ESOP companies to accumulate capital quickly. The seller may also reap tax advantages, he adds.

But home building merger and acquisition expert Michael Kahn of Michael P. Kahn & Associates, which is based in Ponte Vedra Beach, Fla., disdains ESOPs. Pension rules govern the plans, and reporting requirements are strict. Kahn says that “ESOPs are a wonderful way for starting out when everyone's goals are aligned. But after 15 or 20 years, goals change." If an owner wants to cash out of the ESOP before retirement to spend more time with family or pursue a lifelong dream, he or she will pay hefty tax penalties. Strict ESOP rules also make it tough to sell the company. Still, Kahn acknowledges that in those rare cases where employees do buy out an owner, most use an ESOP.

It's the ESOP restrictions that Turner dislikes. He doesn't want his employees straight-jacketed by their ownership. Instead, he says he's developed a multiphase plan that starts with "downsizing" his large companies by breaking them up into smaller units. The break-up is driving the recent expansion into new areas; the new, smaller companies must separate from the parent. "This makes the companies smaller and thus more affordable for the employees," Turner says. It's a move that nets approval from Avila and Kahn, who agree that this kind of downsizing makes it easier for employees to buy. But Kahn says Turner's approach "is quite unconventional."

Still, there's the issue of financing the sale. Turner says he will leave his equity in the business, finance its book value, and agree to be paid 10 percent to 15 percent of each small company's net earnings. "The essence is that the employees pay interest as if they had a loan on the book value, but the principal is paid off from net earnings," he says. "This is the 'magic' of the arrangement." Turner says he expects full pay off in eight to 10 years.

This is where the financial analysts start shaking their heads. "I would have brought somebody in to let Turner take some of the cash out at closing rather than put all his hopes in his employees," says Kahn. "It's totally a trust issue."

"Turner continues to be subject to the risks of the business instead of getting his capital out," says Avila. Another M&A specialist, Nick Beare, managing director and head for Matrix Capital Markets Group, based in Charlotte, N.C., thinks that having Turner's equity in the companies could hinder growth. "There is only so much cash flow to service debt," he says. "For a bank lender, the cash flow of the company is less than it would otherwise be because of the necessity of paying Turner."

Turner's Math Turner, of course, sees it differently. He believes that his equity—which will be subordinate to other debts—will serve as collateral for the bank loans that are essential to growth. "It is unusual," Turner acknowledges, "but I know what my employees can do. I'll stay on as a consultant as long as my money is in the business, so I'll know what's going on."

Turner's company valuation method raised eyebrows, too. First, he added up the average profit margin for the average number of units sold for the past three years. Then he did the same for the current and next two years. For three years beyond that, he estimated the value of each company as 25 percent of the average value of the past and present three-year periods, not counting earnings. "The likelihood is that in the future, the value will be much more than 25 percent," Turner says. Finally, he took the book—not retail—value of actual holdings, such as lots and houses, and subtracted outstanding debt. Adding up all four elements yields the total dollar value. "I'm being very conservative in my estimates," Turner says. "People will say I'm leaving money on the table, but I don't think so. And if bad things happen, this gives the employees room to address them."

Kahn says he's never seen a valuation done this way. "The common way is to value the company on the open market and then figure out a mechanism for the employees to buy," he says. "My hat's off to Ashley Turner, and I hope it works for him. Most people aren't that nice to their employees. They're a little more selfish, and that's not necessarily a bad thing."

Turner doesn't worry about the issues the analysts raise. There's his consulting role, for one thing. But far more important is his certainty about his employees. "I'm very, very confident that my employees will do well. They will do the job. They're doing it now," he says. What greater reward could he offer his employees than the bonus of ownership?

Selling To Employees Merger and acquisition specialists Tony Avila, managing director of JMP Securities, and Michael Kahn, of Michael Kahn and Associates, offer different views on the best approach for owners who want to sell their companies to their employees. But owners would be wise to keep the following in mind:

- Find out what the real value of the company is before talking to the employees.
- Retain financial advisers, one for employees and one for the owner, to ensure fair treatment for both sides.
- Take some of your money out at closing.
- Make sure enough capital is left behind for growth.
- Stay away from ESOPs because of their complexities. If you do sell to an ESOP, try not to have everything riding on it. Invite employees to decide whether or not they want an ESOP.
- Ensure that all management issues are handled. It is especially important to decide who's going to take over.