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Taylor Guitars: A San Diego Success Story – Owners Leave Legacy in the Hands of Employees

■ By MATT HANSEN, CFP®, CEPA®

By most every measure, Taylor Guitars is a great American success story. Bob Taylor built his first guitar when he was just a junior in high school, guided by a book about how classical guitars were manufactured, and with oversight from his high school woodshop teacher. Taylor's business partner of nearly 50 years, Kurt Listug, says Taylor's initial motivation was that he was a kid who wanted a guitar but didn't have the money to buy one.



Bob Taylor

"Bob's a do it yourself," says Listug, who serves as Taylor Guitars' CEO. "He's the kind of guy who, if you couldn't afford to buy something, you'd figure out how to make it." In 1974, Taylor and Listug bought a small guitar store in Lemon Grove, and Bob started honing his skills as a guitar maker. In the nearly 50 years since the two established Taylor Guitars, the brand has grown to be a highly respected name in the music industry, and their guitars are played by prominent professional musicians as well as recreational players worldwide. With their roots still firmly planted in San Diego County, their primary manufacturing facility in El Cajon and another in Tecate, Mexico, the firm now employs more than 1400 people, and their guitars are sold all over the globe. Coming off a year in which the pandemic

affected both their manufacturing capacity and consequently their revenue, Kurt Listug says the company is now projecting 30% year-over-year growth for 2021. He describes the surging demand as "staggering" and says the team at Taylor is now manufacturing nearly a thousand guitars a day.

After enjoying the success they may only have dreamed of when they bought that first shop in Lemon Grove, Bob Taylor and Kurt Listug started turning their attention to-

ward options for an exit strategy and succession plan several years ago. Eventually, every business owner comes to a crossroads in their career when they'll contemplate what to do with the company when they're ready to step down or scale back their commitment. For thousands of business owners in America, including Taylor and Listug, the path they chose after making the decision to sell the company was to create an Employee Stock Ownership Plan, or ESOP. Simply put, an ESOP allows shares of a

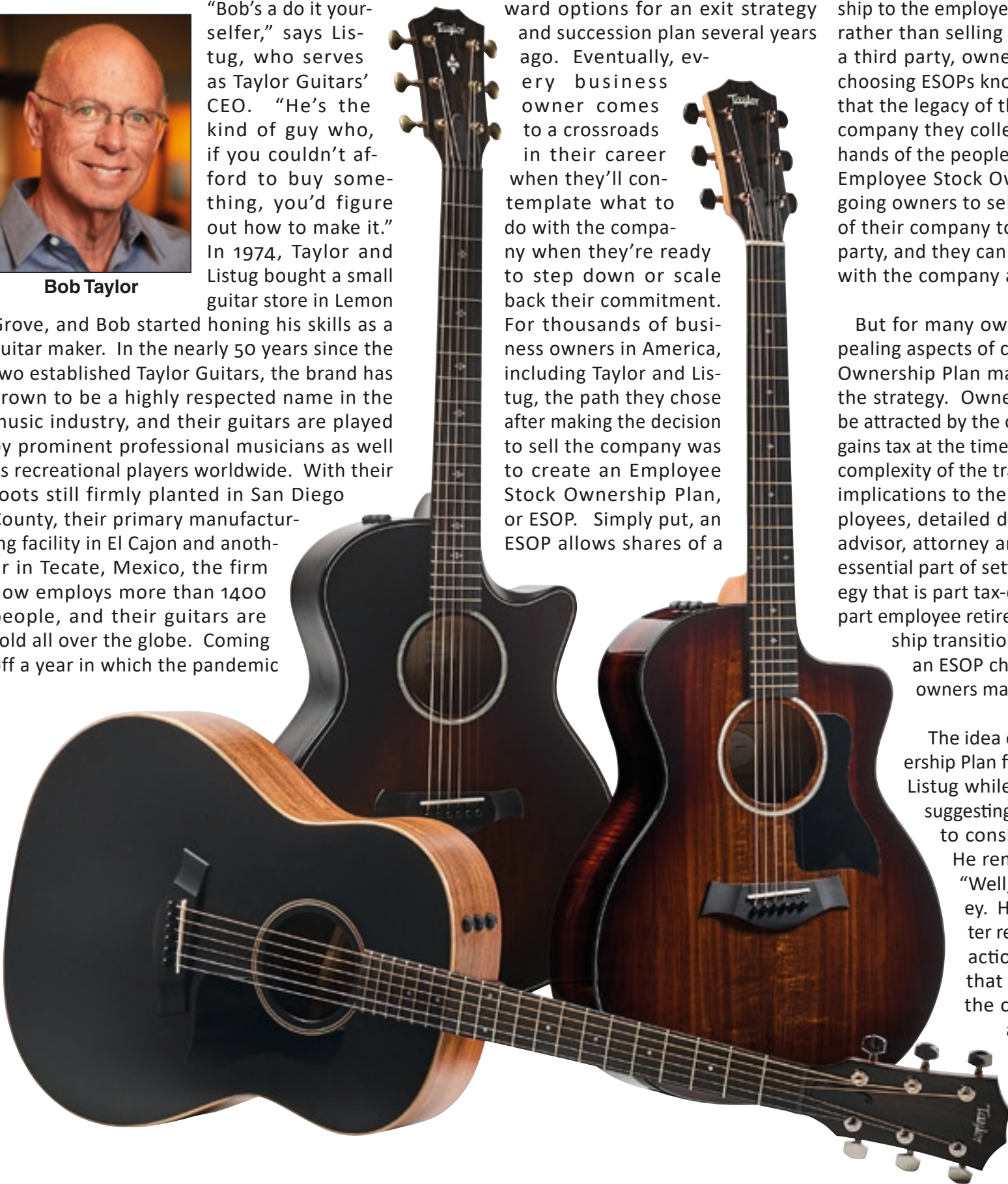
company to be sold to the employees of the business. It gives them the potential to enjoy future appreciation of the company's value in a qualified retirement plan, at no expense to the workers. Employee ownership also gives a business owner the opportunity to reward their staffs for their dedication and loyalty to the company. By handing off ownership to the employees rather than selling to a third party, owners choosing ESOPs know that the legacy of the company they collectively built will be in the hands of the people responsible for its growth. Employee Stock Ownership Plans allow outgoing owners to sell a portion or the entirety of their company to the employees or a third party, and they can still choose to be involved with the company after a full or partial sale.



Kurt Listug

But for many owners, one of the most appealing aspects of creating an Employee Stock Ownership Plan may be the tax efficiency of the strategy. Owners considering ESOPs may be attracted by the opportunity to defer capital gains tax at the time of the sale. Because of the complexity of the transaction and potential tax implications to the owner, company and employees, detailed discussions with a financial advisor, attorney and a tax consultant are an essential part of setting up an ESOP. As a strategy that is part tax-efficient leveraged buyout, part employee retirement plan and part ownership transition tool, the idea of creating an ESOP checks off many of the boxes owners may desire for an exit strategy.

The idea of an Employee Stock Ownership Plan first struck a chord with Kurt Listug while he was reading an article suggesting business owners may want to consider selling to employees. He remembers joking to himself, "Well, they don't have any money. How would we do that?" After researching how such a transaction functions, he concluded that an ESOP may fit well with the culture of the company he and Bob Taylor built. "This could be pretty amazing with some of the benefits," he remembers thinking at the time. But Kurt Listug and Bob Taylor





were­n't primarily motivated by what the tax deferral would mean to them, but by what it would mean to their employees, and how it would help preserve the legacy of the brand they built over nearly half a century. Listug says the opportunity for employees to participate in an ESOP was a far greater consideration. He says, "We've already made good money. People will always

talk about it's better to give than receive, and anyone will agree to that, but when it comes down to selling your company, how many people are actually going to practice that?" By creating a retirement plan that provided shares in a company with solid sales and high demand for their product, the owners of Taylor Guitars knew they were affording their employees a chance to

grow their retirement assets in an alternative to a traditional retirement plan. "We thought this would be a good opportunity for employees to build wealth through ownership of the company in a way they would never be able to otherwise," Listug said, recognizing this was a way to address wealth inequality.

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Exit planning strategies including Employee Stock Ownership Plans



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As the doors opened to employee ownership, it provided a way for middle-class workers to close the wealth gap. “People have so few opportunities to increase their wealth because really the odds are stacked against the average person and family. So many people just get left out.” It should be noted that the ESOP was constructed to include all employees, including those in the United States and Mexico, with a comparable benefit program for its employees in Europe, in accordance with different benefit laws. The company still offers U.S. workers a traditional 401(k) plan. Tim O’Brien is the Vice President of Marketing for Taylor Guitars, and he reflected on what employee ownership means to the men and women he has worked with for the past eight years. “People feel excited when they come to work every day and see a sign that says, ‘Welcome employee owners’ and that makes them feel great,” he says. “It reinforced the culture that Bob and Kurt had already established. If it were some short-term windfall, that isn’t actually the culture we have. It was a nice consistent, continuation of the company they made.”

Leslie Lauer is a Managing Director and Private Wealth Advisor at UBS Financial Services and is experienced in Employee Stock Ownership Plans. She and her team, The ESOP Group, worked closely with Kurt Listug following Taylor Guitars’ transition to 100% employee ownership as part of a broader, comprehensive exit planning and wealth management strategy that was designed for him. Lauer talked about the advantages of ESOPs for all parties involved. “Both the management and the employees are getting a benefit. Under certain circumstances, as long as you meet the criteria, it allows business owners to defer or possibly avoid capital gains tax. For the employees, they’re getting a benefit that they’re not paying for, which helps build culture and motivation.” She describes the ESOP as not unlike a 401(k) plan for employees, where the shares they will hold may continue to grow tax-free until the employee retires, then he or she pays the applicable tax when drawing money out in retirement.

Lauer has guided companies through the ESOP process for nearly 30 years and works with a group that has assisted the sellers on nearly 800 such transactions. She stresses the importance of collaborating with an experienced firm when establishing an ESOP, because of the complex elements involved in the process: “There’s tax planning, there’s philanthropy, there’s a lending component, there’s an insurance component sometimes... all these different disciplines come together.” She says

there are “a lot of moving parts, and there are many players involved, but the structure may create an outcome that is more in line with the owners’ goals.”



Leslie Lauer

Ted Margarit is a Managing Director at Chartwell Financial Advisory who served as the investment banker to Taylor Guitars, and thoroughly evaluated all their transition and liquidity options. He then worked with them over the course of seven years to establish their ESOP, and acknowledges what Taylor was able to do for its staff when they became the owners was amazing. “They wanted their employees to be able to build wealth in a meaningful way. There’s no way anyone working in the shop making \$60,000 a year was ever going to save enough money to have as meaningful of a retirement nest egg,” he said, reiterating the tax advantages to Taylor and Listug were a secondary consideration. “The tax benefits followed here. They were not the driver. They were the icing on the cake.” Lastly, the tax benefits for the company are significant. As a 100% ESOP owned company, Taylor Guitars no longer pays federal tax, and in most states, also pays no state tax. The company is then able to use the tax savings to repay the debt the company took on to buy Taylor and Listug’s shares. Margarit says, “An ESOP is often referred to as the most tax-efficient corporate structure.”

Having invested nearly fifty years of his life to Taylor Guitars, Kurt Listug was concerned that the brand could be diluted if they sold to a company that might prioritize profit at the expense of product quality. He saw the possibility of overseas operations, inferior manufacturing, and overproduction as being credible threats to the brand they built if the business was sold to an outside entity. “We wouldn’t want any of those things to happen,” Listug says. “Those are against our core values.” In addition to the advantages of capital gains tax deferral and allowing employees ownership of the company, Listug also liked the flexibility ESOPs allowed for continued involvement after the sale. “It’s a great option if you love the business and love the employees,” he said. “The ESOP was really going to be the custodian of the business, and we could still stay involved.”

Now in his late 60s and describing himself as “semi-retired,” though he still serves as Taylor’s CEO, Kurt Listug reflects on the legacy he knows he and Bob Taylor will leave behind. “We feel that we’ve put the company in the hands of the best people that we possibly could,” he notes. “Those people are all spending their lives helping you with your mission, and they’re the ones doing the work every day. So, it’s a really good feeling to give back to them to recognize what they’ve been doing for you all along and help them get to a better place in life, too.”

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