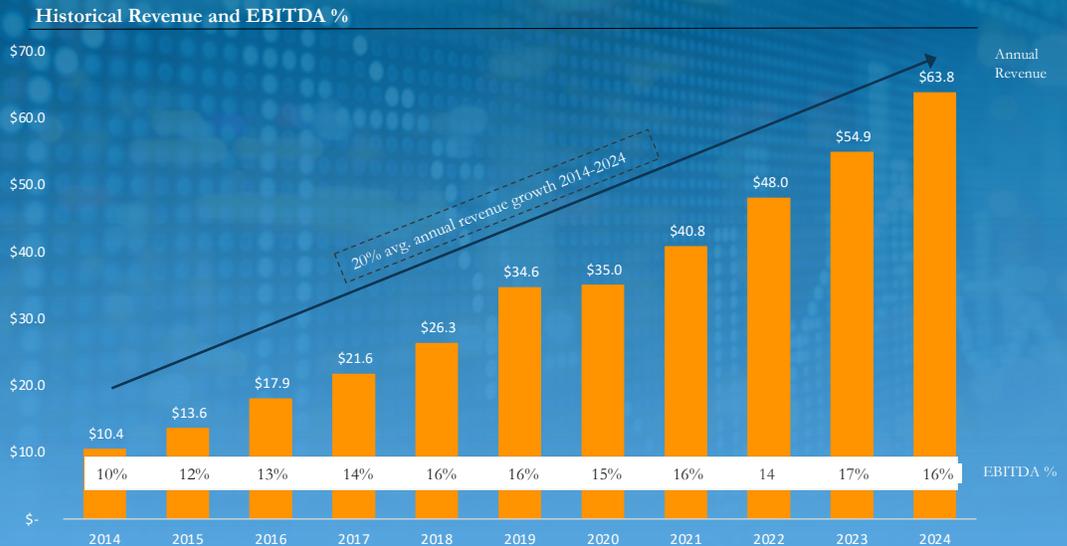


Owner Liquidity:

Taking chips off the table without selling your business



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Owner Liquidity

Corporate Finance
for Entrepreneurs

Executive Summary

Many business owners face a growing dilemma: how to access the value they have built in their company without giving up control or selling outright. This white paper explores owner liquidity as a powerful strategy to de-risk, diversify, and achieve key financial goals while continuing to lead the company through its next phase of growth.

Introduction

Conventional business exit planning typically presents owners with two options: sell the business or 'let it all ride.' Owner liquidity offers a third option and is gaining popularity among owners who want to de-risk and diversify their holdings while continuing to grow a business they enjoy. Interestingly, this strategy of 'taking chips off the table', has long been used by private equity firms, yet many business owners never consider it. This paper explains what owner liquidity is, how owners can achieve it, and reasons why it's been an attractive strategy for other business owners.

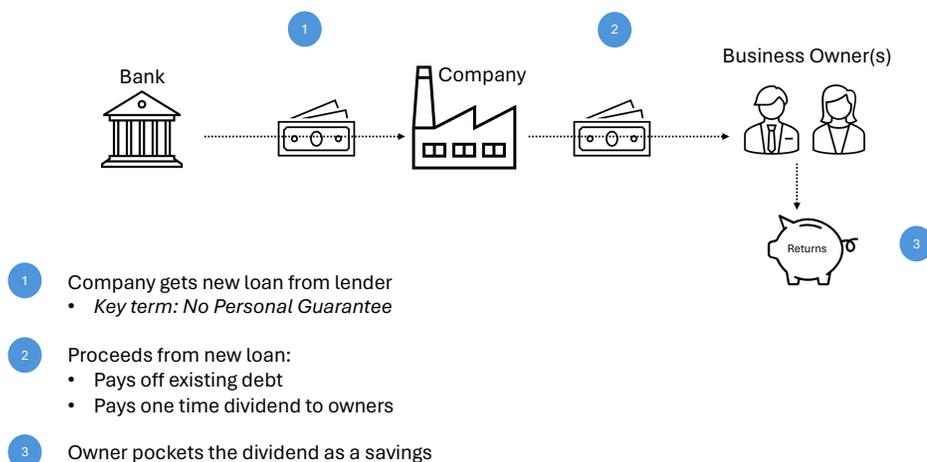


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Defining Owner Liquidity

Owner liquidity is achieved when a company provides its owner capital without requiring a full sale of the business. This can involve various owner liquidity transactions, such as securing a loan or attracting an equity investor. As part of this transaction, the company may also pay off or refinance existing debt. A simple diagram illustrating owner liquidity transaction using bank debt is shown below:

Simple Illustration: Owner Liquidity Transaction



- 1** Company gets new loan from lender
 - *Key term: No Personal Guarantee*
- 2** Proceeds from new loan:
 - Pays off existing debt
 - Pays one time dividend to owners
- 3** Owner pockets the dividend as a savings

The Rise of Owner Liquidity Transactions by Private Equity

In the PE world owner liquidity transactions are commonly called Dividend Recapitalizations (or dividend recaps). In 2024, dividend recaps by private equity firms rose by **5 (x) times** the amount of the prior year to reach **\$80 billion**. Levels in 2025 remained high as well. This growth is notable given bank interest rates have been higher during this period than in prior years.

Several factors, explain why private equity firms continue to pursue dividend recaps despite higher borrowing costs:

1. A slowdown in M&A activity, making it harder to find new acquisition targets.
2. A slower market for selling existing portfolio companies.
3. Increasing demand from investors for the return of capital.

A dividend recap allows a private equity fund to return a portion of investor capital even if it plans to hold the business for additional years. The timing of these capital returns is critical, as private equity firms raise new funds by marketing their historical rates of return. Returning capital earlier can materially improve internal rates of return due to the time value of money.

Reasons to Seek Owner Liquidity

While dividend recaps are common for private equity funds, owner liquidity transactions are attractive to business owners but different reasons which include:

1. **De-risk and Greater Peace of Mind** – One of the primary benefits of owner liquidity is the ability to de-risk your investment and gain more peace of mind. While it may seem counterintuitive, using owner liquidity to take a distribution can enhance financial security by providing readily available capital. This allows owners to diversify assets and avoid having all their wealth tied to the business. Although this may not initially feel like true diversification, it is important to note that owner liquidity transactions using debt typically do not require a personal guarantee. So, if the company defaults on the loan, the owner isn't personally obligated to pay it back, creating financial liquidity that's independent of the business.
2. **Avoid Regret of Selling Too Soon** - While the risk of a business shutting down is low, a more subtle but common risk is the regret of selling too early. **One study found that 76% of business owners profoundly regretted selling their business one year after the sale.** As the business grows more valuable, the pressure to sell often intensifies to realize a life changing financial event. Taking a dividend allows owners to secure a portion of the financial future while continuing to enjoy growing the business. A useful exercise is working with a personal financial advisor to estimate the capital required to support retirement and family needs. Taking liquidity in that amount allows owners to focus on long-term growth without feeling forced to sell prematurely.
3. **An Alternative to Selling at a Low Valuation** - If a company receives a purchase offer at a low EBITDA multiple and carries little debt, the owner may be able to obtain owner liquidity in an amount close to the proposed sale price while retaining ownership and continuing to grow the companies value.
4. **Improved Investment, Tax, and Estate Planning** - Increased owner liquidity creates opportunities for estate planning and investment in long term assets that preserve and grow wealth. Taking a dividend allows owners to gain experience investing in financial assets focused on capital preservation. Gaining this experience can be valuable prior to selling the business in the future at a much greater amount. There are also numerous tax-advantaged strategies available for estate planning, business succession, and maximizing after tax income, including family trust, donor advised funds, ESOPs, and deferred compensation plans. In some cases, dividends may be treated as a partial sale of the business allowing owners to capture lower capital gains rates or potentially qualify for tax-free treatment, such as AAA earnings for S corporations. A dividend recap creates an opportunity to evaluate these strategies in the context of the owners' long-term goals.
5. **Buyout Exiting Partner or Rebalance Ownership** - A common scenario arises when one owner wants to exit while another owner wants to continue growing the business. Owner liquidity can provide a solution by offering liquidity without selling the business outright. These transactions have been used to rebalance equity ownership interests in the Company.
6. **Invest in Other Ventures** - Entrepreneurs have used dividend recaps to free up capital to invest in other businesses.

Helpful Exercise:
Estimate the capital
you would need to
support a comfortable
retirement.

Challenges to Owner Liquidity Transactions

- **Not Popular with All Lenders** - While owner liquidity can be a powerful tool, securing financing for this purpose may be challenging. Some lenders are hesitant due to perceived increases in risk. However, not all lenders share this view and many routinely approve similar transactions for equity-backed companies. As a result, owners may need to approach many capital sources.
- **Not Always Encouraged by Investment Bankers** - Investment bankers typically earn fees based on a percentage of a company's sale value or capital raise. Selling a business is often their most lucrative transaction, while securing debt financing or minority equity investment generates smaller fees. As a result, bankers may emphasize selling the business and downplay the benefits of taking chips off the table.

Other Key Considerations

- **Range of Financing Options** - Capital for owner liquidity is available from a variety of debt and equity providers, including commercial banks, mezzanine funds, subordinated debt funds, private funds, and family offices. Some capital providers often blended structures combining debt and equity tailored to the owner's control, leverage, and ownership objectives.
- **Cost of Capital** - The cost of capital for owner liquidity or dividend recaps can range from relatively low bank rates (currently less than 7%) to 12% or more depending on the provider. While higher rates may seem expensive to owners accustomed to traditional bank financing, debt interest is tax deductible, and the cost is partially offset by income earned from investing the proceeds. Additionally, interest expense does not typically reduce enterprise value, as most businesses are valued based on a multiple of EBITDA. Any outstanding principle at the time of sale would generally be repaid from sale proceeds, but the principal represents value the owner already accessed to diversify and de-risk.
- **An Opportune Time to Reward Key Management** - Owner liquidity transactions can be an ideal time to reward key employees. Many owners promise equity to employees without formalizing it, which can complicate a future sale. Providing equity or bonuses during an owner liquidity transaction can reward contributions, strengthen retention, and solidify management commitment. Companies where management has a meaningful ownership stake are also attractive to investors and lenders and usually well-positioned for a future management buyout. Incentives can include cash bonuses, stock grants, or ownership that vests over time.

Real World Examples / Case Studies

Over the past year, we have helped clients complete owner liquidity transactions of varying sizes. One client completed \$150 million dividend recap, with up to \$75 million available for distributions to its founders. Part of their motivation for doing this was the business shut down for two months during the Covid pandemic. As part of the transaction, the owners also awarded a substantial one-time cash bonus to key managers. The investment capital was structured as debt with an additional up to 10% ownership interest for the capital provider. Thus, the owners retained at least 90% of the equity while remaining focused on long-term growth.

In another transaction, a client obtained a \$5 million bank loan after bootstrapping the company's growth and earning a spot on the Inc 5000 list. The owner sought liquidity to reduce reliance on his personal capital and build personal liquidity outside the business. After evaluating multiple bank and non-bank lenders, the owner selected a financing structure with a 4-year term, limited personal guarantee and a floating interest rate slightly below 7%.

Exploring owner liquidity options

If you would like to explore owner liquidity options for your business, contact Lantern Advisors. We can provide insight into potential owner liquidity strategies based on your company's financial profile and your personal goals. Owner liquidity transactions can be a powerful way to de-risk, diversify, and achieve key financial objectives while continuing to lead your company toward future growth.



Lantern Capital Advisors

Lantern Capital Advisors provides corporate financial consulting to growing entrepreneur-owned companies typically with revenues of \$10 million to \$150 million. Many accomplished entrepreneurs lack knowledge of corporate finance and miss opportunities to realize even greater value in their business. Lantern helps educate clients on this topic and ways to apply it to grow and build more value - often without giving up control or ownership of the business. Common corporate finance strategies include:

- fund faster growth
- acquire other businesses
- shareholder or management buyouts
- obtaining owner liquidity

Lantern provides its services on an hourly consulting basis similar to accountants and lawyers and receives no commissions or success fees related to a clients' financing. This structure allows us to uniquely serve as trusted advisors and often at a fraction of the cost of comparable services offered by investment banks.

About Chris Risey

Chris is the founder and president of Lantern Capital Advisors. For over 20 years Chris has worked with growing entrepreneurial companies to develop and finance strategies that drive growth, increase enterprise value and achieve important business objectives. In addition to his role at Lantern Capital Advisors, Chris has served as a managing director of a \$600 million private credit fund that provides capital to high growth companies. Chris began his career as a CPA for Arthur Anderson in New Orleans, LA. Chris is active in business civic and faith communities and held volunteer and leadership roles with Rotary International, Financial Executives International, the Association for Corporate Growth, and the Knights of Columbus. Chris is a frequent writer and experienced speaker to entrepreneurs around the country through Vistage International. Chris earned a Bachelor of Science in Finance from the University of South Florida where he was a member of the men's basketball team. His team won a conference championship in 1990 and earned the school's first ever appearance in the NCAA March madness basketball tournament.