Exit Planning Strategies

Thinking about retirement or selling your business? Avoid disaster with these exit planning strategies.

Over the past thirty years, over five million closely-held, small and middle market businesses were founded. Most of the owners of these businesses are now in their 50's or older and are beginning to think about retirement. This transition is difficult for most but it can be much more overwhelming for a closely-held business owner. In addition to the normal fears surrounding retirement, a closely-held business owner often feels responsible for the business, the employees, customers and vendors. In addition, a large portion of the owner's net worth may be trapped in the business and children and other family may be employed there as well.

Recent studies by PriceWaterhouseCoopers, MassMutual and Marquette University showed that one out of two businesses will change hands between 2006 and 2016. The American Family Business Survey sponsored by MassMutual showed that approximately 30% of these owners plan to sell their business to a third-party buyer. Another 30% plan to sell to a family member, while another 18% plan to sell in some manner to current employees. The remainder plan to close and liquidate the business.

For those business owners who intend to sell to a third-party, it will become increasingly important that they position their business to sell successfully in an increasingly competitive market. With one out of every two business owners looking to sell over the next 15 years, there will be a glut of businesses on the market. Now, more than ever, it will be important that a business owner focus on doing everything he or she can to increase the attractiveness, value, and salability of the business.

Tragically, the Price-WaterhouseCoopers study showed that approximately 75% of private business owners have no strategic exit plans in place. In fact, 25% have done little or no estate planning. This presents the potential for disaster that must be addressed as soon as possible.

An exit plan is a comprehensive, integrated plan that asks and answers all of the personal, business, legal, financial, tax and estate issues that are involved in exiting from a privately owned business. This plan shows business owners how to begin positioning themselves and their businesses so that the owners accomplish all of their personal, financial and business goals when they exit.

It is best to begin this process early, even though no exit is planned. Given the number of companies coming to market, business owners will need to focus on improving profitability, building a management team, and growing revenue in order to make their companies more attractive and maximize the proceeds they receive at the time of exit. This is true whether the ultimate buyer is a third-party, family members, or existing management employees.

Exit planning delivers tangible results for business owners. It is not uncommon for companies that have invested the time and effort to prepare themselves for sale to sell for a significant premium over companies that come to market unprepared. In addition, with good planning, business owners are often able to reduce the taxes due at the time of sale with a dramatic increase in the after-tax net proceeds that the owner retains.

Equally important, proactively addressing these issues and having a plan to reach goals provides peace of mind for the business owner who has previously been waiting passively to let the future take care of itself — after all, deciding how and when to exit a privately owned business is perhaps the single most important financial and personal decision in a business owner's lifetime. ◆

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THE EXIT PLANNING PROCESS

- GOAL SETTING - Designed to determine the owner's overall needs and goals. What is the ideal timing of an exit? Who is the ideal buyer? What are the owner's plans after the transaction? What are the owner and family's financial needs after the transaction?
- INITIAL REVIEW - Analysis of the current situation. Is a contingency plan in place to deal with a crisis before the overall plan is complete? Has the owner done appropriate estate planning? Is the company's tax structure appropriate for the upcoming transaction? What is the current estimated value of the business? What value drivers are bringing value down that can be manipulated to drive value higher? What value drivers are positively affecting value that need to be maintained? Are the owner's financial goals realistic based on the current situation and time frame? Has the owner and his family thought through life after retirement?
- ACTION PLANS - Recommend specific steps to be taken to improve the likelihood of meeting the established goals. Common areas that action plans address include establishing a contingency plan in case of death, disability, divorce, or business distress before the exit can be completed, updated estate planning, building business value through manipulation of the appropriate value drivers, and refining investment strategy.

TOP REASONS TO BEGIN EXIT PLANNING NOW

- ❑ The baby boomers, born from 1945 through 1961 are reaching retirement age and generally tend to have done minimal planning.
- ❑ By 2009, the number of business owners wanting to sell their businesses each year will have increased fivefold over 2004. This trend is expected to continue for the next decade or more.
- ❑ It takes approximately two years of focused activity to get yourself and your business ready to sell at a reasonable price.
- ❑ Being ready to sell when the economy is expanding and we are entering a strong economic cycle, your industry is actively consolidating, or you are approached by a strategic acquirer, will allow you to make thoughtful decisions and take advantage of potential opportunities.
- ❑ Planning in advance can ease the burden created by a personal or business crisis.
- ❑ Taking advantage of favorable tax laws can require longer term planning to be most effective.