6 CRITICAL STEPS
TO PLANNING YOUR BUSINESS OWNERSHIP TRANSITION

By Jane M. Johnson

As a business owner, you are unique—your situation, challenges, goals, and objectives are all specific to you. That's why when it's time to transfer the ownership of your business to someone else, the exit planning process should take all of this into account. An effective exit planning process will require you to create a written plan or roadmap showing where you are today and how you can achieve the life you want tomorrow. We call this a Business Ownership Transition Plan. We define this plan as a comprehensive written document that outlines how and when the ownership of a business will be transferred to others, either internally or externally, in order to achieve the owner's goals.

THE PROCESS OF CREATING AN OWNERSHIP TRANSITION PLAN CAN HAVE A PROFOUND EFFECT ON YOUR BUSINESS AND YOUR FUTURE. HERE IS A SIX-STEP PROCESS YOU MAY USE TO DEVELOP YOUR PLAN. WE HIGHLY RECOMMEND THAT YOU DO NOT CUT CORNERS OR SKIP ANY OF THESE CRITICAL STEPS.

STEP 1:
GETTING YOURSELF PREPARED

This step involves preparing yourself for the next phase of life. Whether you want to remain active with your company in your current capacity or a reduced capacity or wish to leave completely in a few years, you need to begin creating the life you want before you exit. Many owners think that life without their business will be great. They can't wait—no more worries, payroll, employees, or customers. But if owners don't complete this step and prepare themselves for the transition, it could lead to a feeling of emptiness and loss. Preferably you should craft a written plan. The plan should identify the ideal timing and your financial expectations and needs. This plan should be shared with key stakeholders and advisors, including your family, other owners, CPA, lawyer, board, and other key advisors and be synchronized with your business, including corporate bylaws, buy-sell agreement, and other organizing documents.

STEP 2:
COUNTING BEANS

You may not realize how much income you now derive from your business or how much income you will need in the future. It will be important to take stock of the assets you have outside of your business and quantify both the income and the other perks you get from your business, such as:

- Vehicle payments and expenses
- Health insurance
- Retirement contribution
- Club memberships
- Travel
- Entertainment
- Rental income payments if you own your property

Consider your lifestyle today and what you want it to be once you have transitioned out of your business. Most owners believe that their income needs will go down post-transfer but don't factor in new expenses they may take on in order to live life to the fullest. Once you are able to live the life you have imagined, your cost of living may actually increase. How much will you really need? This step answers that question and determines your Wealth Gap or how much money you will need to net (after taxes) out of your business to fund the rest of your life.

STEP 3:
BUILDING A BETTER BOX

Most owners will need to take steps to increase their business value before they can exit. A business that is dependent on the owner has less value than one that is run as an investment. Most owners believe that creating more value in their company is just a function of increasing sales and profit. While those two things are very important, there is so much more that can influence the value of privately held companies:

INTERNAL FACTORS

- A capable management team
- Lack of owner dependence
- Strong balance sheet
- Low customer concentration
- Written processes and procedures
- Overall size of the company

EXTERNAL

- State of the industry
- Cost of and availability of capital in the marketplace
- Cyclical Market forces

As owners, while we can exercise control over the internal factors, we have no control over the external factors, which can have a significant impact on business value. That's why owners cannot simply pick a target age for their transition. It will be important to stay vigilant, drive your business value, and stay aware of what is happening in your industry and the economy in order to determine the best possible time to transition your ownership to others. You don't want to transition when the value is dropping but rather as the value is increasing.

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STEP 4:
FOLLOW THE YELLOW BRICK ROAD

How should you exit your business? What are your exit options? In this step, we identify your options. There are two general categories of transition options: internal and external. “Internal” refers to selling or gifting the business to an insider, such as key employees, managers, or family members involved in the business. “External” refers to selling to an outsider, such as a competitor, customer, or investor. The process for identifying which one is best for you considers all of your goals, how much money you need, and the pros and cons of each option.

It is important to understand that different transfer options have different transfer values, as well as different fees and taxes. There are pros and cons to each type of transfer, and assessing the different options for suitability or how they will either accomplish or not accomplish your goals is a crucial step in planning your transition. The more time you give yourself to plan the exit from your business, the more options you will have.

STEP 5:
THE ART OF THE DEAL

Selling your business to a third party can be a minefield. This is a complex world of investment bankers, private equity groups, lenders, financial buyers, lawyers, and due diligence. Getting prepared for a possible transaction and minimizing taxes and fees takes time, preparation, and the assistance of a skilled advisory team. The art is in knowing how a buyer views your business and positioning it so you find the right buyer and negotiate the best possible deal. It will be important for you to understand how the deal process works and the landmines you will need to avoid in order to be successful.

STEP 6:
PAINT BY NUMBERS

Here is where all the hard work comes together. Based on what you have learned in each of the prior steps, you will be able to make an informed decision about which exit strategy is right for you. The step produces a unique roadmap for your business exit that will outline the steps you should take to successfully achieve your goals and ensure that your business continues.

Exit planning is a process, not an event. This planning should be done in a comprehensive, holistic, and integrated fashion to ensure that your needs are met and you reach your goals. For best results, we encourage owners to work with qualified, experienced exit planning professionals to guide them through these six important steps.

It is never too early to plan for your exit but may certainly be too late. Don’t let life events control your destiny. Take these steps well in advance of your desired exit to ensure that you have time to positively impact the outcome. As we know, it can take years to increase business value, groom your management team, and figure out what you are going to do in your next phase of life. Most owners will have one shot at monetizing the business they have worked so hard to build and achieving financial independence. Planning in advance will improve your chances for getting your deal of a lifetime! LC

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