YOUR MONEY: RETIREMENT PLANNING

Dear Business Owner: Your exit is inevitable

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Unfortunately, too many business owners do not consider or plan their eventual exit from their business. Like Benjamin Franklin's famous quote, "in this world, nothing is certain except death and taxes," thus all business owners will eventually exit their business. For many owners, their business is their largest asset, but they often neglect effective estate planning.

Preparing for your business transition may come up in an estate planning meeting, discussion of whether a family member will step in to run the company, or how to best take care of loyal employees, and/or in the context of addressing the Illinois or federal death tax. Further, senior company leadership may have discussed this concern in a strategic planning meeting, or perhaps a discussion related to a business broker's unsolicited offer to buy the company. Many owners acknowledge business transition is important, but they move on to the more urgent matters of the day, leaving the transition planning to another time when it may be too late to implement the most effective transition plan.

Clearly, deciding when and how to exit a business is intensely personal and complex. The decision to exit usually has many implications for the business itself, the management team, the employees and their families, the customers, and the community. If those considerations were not enough, the business owner has to balance the potential impact for their family and lifestyle. These factors can directly conflict and cause the business owner to put off the pre-transition planning. According to Lauren Randazzo, CPA, PFS, CFP®, CEPA®, Wealth Management Advisor, at Archford, "personal finances are often overlooked during the transition process – this is where we begin and bring our client's significant value."

Just how important is pre-transition planning? Many organizations have conducted surveys of business owners asking this question providing insight to one general reality: Business transition is more successful for all parties, if the owner has done pre-transition planning. Although many business owners have no current plans to exit the business, they should recognize that exiting the business is inevitable. Should something happen to the business owner prior to a planned exit, the unexpected transition will likely lead to less than optimum results. A major factor will be who is in charge of the transition and what is their readiness to manage the transition as indicated by the various circumstances listed below:

If incapacity causes the transition, then it may be up to the named agent under a financial power of attorney.

If the business is owned by the business owner's revocable trust, then in the case of incapacity or death, the successor trustee will be left to follow the instructions set forth in the trust agreement.

If the business owner dies owning the company in their individual name, then a probate estate will have to be commenced to facilitate the transition of the business from the deceased owner to the beneficiaries of their Will or under state law.

If the business owner becomes disabled owning the company in their individual name and without a durable power of attorney, then a conservatorship will have to be commenced to facilitate the operation and potential transition of the business.

Many exit planning professionals will tell you that too often the estate planning documents are not designed to handle the complexities of a forced business transition. The lack of specificity around the business frequently leaves the family with inadequate direction on how to best handle the business as a significant asset of the estate.

Business owners who begin the process of putting a transition plan into place must first consider all options. Those options include a transition within the family, a transition to employees sometimes as an Employee Stock Ownership Plan (ESOP), a strategic transition to a similar business, or an outright sale to a third party or private equity. When business owners state that their goal is to transition leadership to their children, the difficult issues are identifying at least one child who is both capable of running the business and truly wants to step into that role and then determining how to transition the business to that family member. Considerations include tax savings, cash flow for the business, and cash flow for the parent.

Once the business owners get past this hurdle, they then have to grapple with what they need to do, if anything, for the other children to keep things "fair." The issue of fairness has the potential to not only derail a transition of the business, but also to cause disharmony inside the family if the issue is not dealt with head on. Often through a skilled family coach open resolution and family harmony can be achieved by giving everyone an opportunity to be heard and allow the business owner to feel confident that the transition plan will leave family harmony intact.

If the owner decides a family transition just does not work, they must then decide which outside buyer to consider. The strategic buyer would likely be more beneficial to the leadership team and the customers, but may not generate the multiples on valuation a financial buyer would offer. If maintaining the business culture and rewarding the employees for the success of the business, then an ESOP may be a possible consideration.

So how does a business owner start the process? Regardless of the planned transition, the business owner should put in place a specific estate plan that is designed to allow the family to transition the business in a way that will maximize value and preserve family harmony. Once the business owner has created a path in the event of a forced transition, they can step back and begin to formalize a strategy for a planned transition. For entrepreneurs who specialize in creating value, they should recognize the value maximization available by doing pre-transition planning. At Archford Capital Strategies, we stand ready to help business owners with business transition planning and valuation activities and look forward to speaking with owners today to help them through this important process.