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WEALTH MANAGEMENT

Top Five Things to Consider Before Selling a Business

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To call oneself an entrepreneur is one thing; to truly be one is another. Those fortunate enough to find success eventually encounter an inevitable crossroad: Is it time to sell my business? This can become an incredibly difficult decision when blood, sweat, and tears were poured into the business over the course of decades, and the idea of relinquishing control and moving on to the next chapter can create numerous questions – many of which have not been contemplated before.

Owners who are new to the process should consider not only the financial ramifications of selling their business but also how it can affect their life after the sale has finished. Here are five important things to think about before selling your business:

What financial means do I need to support my current lifestyle?

Many entrepreneurs are accustomed to living on the cash flow from their business, as they distribute most, if not all, of it annually. This cash flow is a byproduct of a successful business but also attracts potential buyers. It is important to fully understand whether the after-tax proceeds from the sale of your business can support your accustomed lifestyle plus any aspirations you may have, such as private aviation, additional residences, increased travel, etc.

In my experience, fully assessing an entrepreneur's needs and goals before selling their business has proven to be a fruitful exercise and time well spent. Through this process, some entrepreneurs realize they need to grow their business a little more before they sell and experience liquidity, while others have realized they do not need as large of a sale price to support their needs as they originally thought. The latter has proved helpful in negotiation efforts.

Should I do any estate planning before I sell my business?

Tax planning is one of the most common topics raised by entrepreneurs when deciding whether to sell their business. Engaging in wealth-transfer strategies is often a very powerful tax planning strategy. For closely held businesses, often when a third-party valuation is completed, the company receives a marketability and/or minority interest discount. Through the gifting of company interests or engaging in other wealth-transfer strategies, the ability to pass on a discounted value to the next generation before someone makes an offer to buy the company (generally at a higher price than the valuation) allows the entrepreneur to maximize the use of their lifetime exemption and reduce their future estate tax bill.

It is imperative, however, to consider how much is transferred to the next generation. A common mistake entrepreneurs make is focusing too much on tax savings by transferring an excess to the next generation, leaving the business owner deficient in their ability to meet their lifestyle needs. To thoughtfully complete estate planning before a potential sale, consider starting the process at least six to 12 months before the desired transaction date.

If philanthropy is important to me, is there anything I can do to fulfill this interest before selling my business?

In addition to the wealth planning techniques discussed above, philanthropically motivated entrepreneurs have a unique opportunity to establish a family legacy and receive tax benefits on their business sale. We have found that pre-transaction planning serves to bring a family closer together and better align their values for navigating decisions about wealth created after the transaction. It is commonly believed that a private foundation is the best vehicle to accomplish this planning, but a donor-advised fund capable of handling closely held businesses may be preferable. It is vital that the business owner begin planning and understanding what is needed to maintain their lifestyle before making large contributions to either of these options.

If I sell my business, what will that mean for my family? My children? My grandchildren?

Selling a business may open doors and provide opportunities to the family that were unavailable before the sale. The influx of liquid assets from the sale enables the family to fulfill aspirational lifestyle goals. With this freedom, it is important to think about how the family values and perceptions of the next generation are affected by such an event, especially in cases where the day-to-day lifestyle becomes more lavish with vacation homes, private aviation, yachts, etc.

Without time dedicated to working through family governance and learning, the next generation can tend to feel self-conscious around their peers or even lose their own drive for success, believing wealth will always be there to support them.

If my staff has handled my family's personal affairs, how will I transition that upon a sale?

In many closely held businesses, it is common for the CFO or other trusted employees to also handle personal affairs for the family. Potential buyers of the business will want these personal responsibilities separated from day-to-day operations. This is when the consideration of a single-family office or engaging the strategic oversight of a multi-family office occurs. This is often a big decision for a family because it relates to cost, succession planning, cybersecurity, and whether they want to run another business. Business owners should think carefully about this transition and how to navigate the path ahead before the transaction date.

When you find yourself at the crossroads of selling a business, be mindful of your current and projected lifestyle goals and how your cash flow may be impacted. Explore the possibilities of how estate planning may influence your family for generations. Consider philanthropic activities that fit within the framework of your family values. Don't lose sight of the necessary education and family learning opportunities that can help ensure the successful transfer of wealth for your family. Lastly, be sure to fully evaluate the day-to-day resources your family enterprise needs now and long into the future.

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