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What to know when selling your business

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There comes a time when a successful business owner realizes it's time to move on. Sometimes it is the result of age or health concerns, and other times it's because the owner wants to do something new.

In either instance, the common theme is that the owner starts to consider the implications of this decision too late. Typically, advisers will tell a client to start preparing for the sale of a business about 5 to 10 years in advance. This is due to the complexity of the process and the time involved in developing the groundwork to ensure a smooth transition.

One of the first considerations should be how to prepare the business entity for the eventual sale. This encompasses the following five fundamental elements:

- Cleaning up the books and records;
- Increasing the cash flow of the business;
- Creating long-term stability;
- Determining an estimated business value, and
- Choosing an ideal buyer type.

Buyers want to be confident in their purchase and therefore prefer 3-5 years of financial information that has been reviewed or audited by a reputable accounting firm. Furthermore, a buyer will want to see that revenue and profits have consistently increased, giving them confidence that this trend will continue after the sale. In some cases, this can be accomplished by developing long-term contracts and implementing incentives for key officers to stay with the company after the sale, either through vesting bonuses or offering small ownership percentages.

The final pieces of the preparation process is to determine the target buyer and an approximate value of your company.

These two decisions are interrelated. Many owners who sell to employees or family members look to determine a fair and affordable value, whereas owners who sell to competitors or public companies look to maximize value.

A qualified valuation analyst can determine a fair market value of your business as well as sale prices based on the targeted buyers.

The key advisers

In addition to a valuation analyst, there are a number of key advisers who should be conferred with when preparing for a sale. It is generally suggested that a seller retain an attorney to navigate the legal process of the sale and to work hand in hand with an accountant to determine the tax and cash flow implications.

Additionally, many sellers prefer to work with a business broker or investment banker, depending on the size of the company, to market, negotiate and develop the structure of the sale. Finally, a wealth management adviser should be consulted to provide financial options after the sale is completed, but also to assist owners in determining what net sales price is needed in order to meet their on-going lifestyle needs.

The sale process is always the biggest surprise to first-time sellers. It is not uncommon for the sale of a company to take from eight months to over a year to culminate with multiple deals falling through. Additionally, deal structure is much more complex than the price paid. Negotiations will typically include stock versus asset sales, personal goodwill, employment agreements, the value of fixed assets, and potential earn outs. Each of these substantially impacts a seller's legal liability, taxes, and net sales price.

Complicating the issue are the emotions of an owner who sacrificed throughout the years for the business. Although it is difficult for an owner to emotionally detach from the deal points, it is necessary and is one of the main advantages of using a broker to negotiate these terms.

For owners, it is worth asking an adviser about each element of deal structure, as it is uncommon to receive the full sales price at once and the associated costs can vary. At a minimum, an owner should consider the sales price net of taxes and advisory fees as well as any additional income related to non-compete and employment agreements.

Emotional impact

After much due diligence, negotiations and contemplation, selling a business may be the right exit strategy for an owner. While an owner may have laboriously considered every intricate financial and legal detail, there is often one area that is overlooked when preparing a business for the marketplace – the emotional impact of selling a business.

For many owners, their company has become part of their identity. It provided purpose and, in many regards, meaning. It is critical for owners to have a post-sale plan for the next phase of their lives.

Far too many owners look back and regret the sale of their business due to poor planning. It is important for an owner to have an idea of what their lives will look like once there isn't a business to take care of. Owners often consider the objectives of relaxation and retirement, increased time to spend with family members, philanthropy, new business ventures, part-time work, volunteering and teaching in order to give back and share experiences.

Regardless of the intentions for selling a business, a plan is crucial for owners to help think through what they are REALLY going to do with the rest of their lives.

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Financial changes

With the sale of a business, an owner's financial situation often significantly changes.

There are numerous pre-sale and post-sale financial planning and wealth management considerations that must be addressed. Before a company is sold, an owner must determine if the sale price is adequate to meet future financial requirements and lifestyle continuation. To do so mandates a comprehensive financial plan addressing key areas such as: health insurance, retirement needs, taxes and estate planning.

A holistic financial plan requires an owner's honest look at expenses and personal cash flow. Any expenses that the business has been paying for must be added back into one's personal obligation.

These include items such as: vehicle payments, insurance premiums, dining, cell phones, gas mileage and auto repairs. After significant financial planning work has been completed, and an owner decides to exit the business, sale proceeds must be properly and prudently invested to preserve wealth and maintain financial independence.

Once you believe you are financially secure, it is a good idea to discuss effective methods and timing of transferring assets to the beneficiaries of your estate with an accountant, attorney, and wealth management adviser. Many people decide to hold on to their assets and allow them to flow into their estate. However, if you have amassed enough wealth for your estate to be considered taxable, it may be worth enacting some tax-saving measures.

Individuals are able to gift approximately $5.45 million in assets, which is the lifetime exemption. As a result, trusts and family limited liability companies are good options to transfer assets while continuing to build wealth. Additionally, once a financial plan is in place, gifting to a favorite charity might be an option as well. Discussing these alternatives with qualified professionals will help to secure the financial future for both you and your family.

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