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NEWSLETTER

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FIRM NEWS:

MMPPH Attorney, Judy Bae, was recently named as a 2012 Top Attorney Finalist by the San Diego Daily Transcript (SDDT). Ms. Bae is a litigation attorney, specializing in disputes relating to trusts and estates, as well as employment. Ms. Bae was recognized by her San Diego peers for her exceptional legal skills.

In this Issue:

TO WHOM DO YOU SELL THE BUSINESS? AND WHEN?

Bradford N. Dewan

"To whom do I sell my business? When should I sell my business?" These will likely be the initial questions that a business owner will be asking himself or herself as he or she begins to contemplate one of the most significant events in the life of a business owner and in the life of the business itself. Often the initial answer is either "I will wait until someone comes knocking on my door and makes a good offer," or, "I will search (may be with the assistance of a business broker) for that third-party buyer who will make me the best offer when the time is right."

But once these options are analyzed, the business owner may then determine that instead of looking externally for a buyer, the best option is actually to look internally and to sell or transfer the business either to a family member (e.g. son or daughter) or to a key employee (or to several key members of the management team).

Certainly analyzing the options for selecting or determining who will be the successor is important. But it is likely not the first set of "questions" that should be addressed. Rather, the first questions that every owner must answer when considering the transition away from the business include the following:

1. When do I want to leave the business? Or, to incorporate more flexibility, when do I want to have <u>the option</u> of leaving the business?
2. What will I do with my life (i.e. how will I spend my time) after I leave the business?
3. How much money will I need (or want) to support my new life?
4. Knowing how much money I need (or want), how much of that can come from my personal assets and investments?
5. How much money will need to come from my company if my personal assets and investments are likely to be insufficient to support the life I want?
6. What do I want to do for the key employees as I plan to leave the company in three years? five years? seven years?
7. Is one of my children interested in, and capable of, becoming the next "leader" of the company?
8. Does my estate plan support, complement and sustain my vision?

When do you plan on leaving your company? One of the key personal transition goals for a business owner is deciding on when he or she will leave the company. There are several methods that owners can use in deciding on a departure date:

1. Choose a specific year when you want to leave (realistically, in order to have the best results from the "departure," that "year" will likely have to be at least three to five years in the future).
2. Selecting your age when you want to leave.
3. The year in which the company achieves a specific level of sales.
4. The projected time it will take to have fully implemented the business transition strategy (e.g. evaluating and then enhancing the management team)(typically 3-5 years).
5. The projected time it will take to increase the value of the business so that a sale of the business will provide the funds needed in addition to the owner's personal assets and investments.

Opening up this discussion about a departure date with the spouse or other family members can be quite important. They may well have their own ideas about when the owner should transition away from being the owner of the company and towards that new life and passion.

Of course, it is important for the owner to keep in mind that he or she can always change the projected departure date to a later date, or maybe an earlier date, if circumstances change. But it is quite important to select a specific departure date now since this will provide a firm goal to aim toward and will likely make the rest of the planning and implementation process more solid and real.

Determining Future Financial Needs Post Departure. One of the very key issues that needs to be addressed initially is what level of income will be needed in the "post-transition" life after leaving the company. Having a clear and comprehensive vision and plan for the new life of the owner is very essential for determining how much money will be needed for this new life. After having designed the plan for that "post-transition" life, it then becomes important to meet with a personal financial planner/wealth management advisor and show them the plan. This will allow the professional financial advisors to determine how much money and assets will be needed for this future life.

These personal financial goals may well include other financial intentions that one may have for the future in addition to supporting the owner's future lifestyle. For example, the owner may want to help pay for the grandchildren's college education, make a philanthropic donation to a favorite community or charitable organization or to the owner's *alma mater*.

How much money can come from personal assets and investments? Once the financial advisors have completed their analysis and determined how much money will be needed, they can then determine if the personal assets and investments, based upon reasonable growth projections to the date of the projected departure, will provide enough income to support that desired life style.

If sufficient personal assets already exist to support the future life style plans, or if sufficient assets are anticipated based on some reasonable growth assumptions, then the owner is definitely fortunate. Not only can the owner live the envisioned new personal future more successfully, the ability to support the new life style from personal assets will likely give the owner far more flexibility in designing and implementing the business transition plan, i.e. the plan for "transitioning" the business so that it will continue on its path of success after the owner has departed.

However, if the analysis shows that the current personal assets and investments combined with reasonable growth assumptions will not provide financial security and support during the planned new future and life, then this clearly means that there is a "financial gap." Maybe the financial advisors will be able to redesign the investment strategies in order to close the "financial gap" and thus provide a high level of certainty the future income will be at the level desired.

But the income from new, but appropriate (from a risk level perspective), strategies may still not be enough.

In this scenario, the business owner must now look to how much will be needed from the company.

How much will be needed from the company? If the financial analysis shows that there is a "financial gap," then part of the owner's future income may need to come from the money the owner will get from transferring the company to new owners. This is the point at which the business owner will need to develop and begin implementing a "business transition process."

The likely first step in this “business transition process” is to have a business valuation done for the company in order to determine how much money the company is currently worth to potential new owners. This business valuation will also likely reveal what parts of the business should be, or can be, improved upon or, maybe more importantly, can be improved resulting in a direct positive impact on the valuation of the business, thus resulting in a higher sales price.

This analysis will also impact the owner’s perspective of who will be the best “buyer” of the business. For example, the owner may have initially wanted to transfer the business to the management team. But rather than pursue that particular path immediately, it will be critical for the owner to step back to see if that type of transfer would satisfy the “transition” goals and objectives. For example, would a transfer to the management team allow the owner to leave on his or her timetable? Would such a transfer yield the amount of cash the owner would need to fill that “financial gap” described above and attain financial security? If the answer is “no,” then are there other paths that would allow the owner to leave at or before the chosen departure date, with more money, or perhaps, greater benefit for the owner’s family? These fundamental questions (and certainly other more specific questions) require the owner’s careful consideration before rushing down any particular path.

In conclusion, the primary purpose of the above discussion was to emphasize that the first step most business owners should consider taking in order to have a successful transition away from the business that they have worked so hard to develop and grow is to focus on, and to the extent possible, decide on, what will be their “life” after transitioning away from the business. Clearly for many business owners this will not be an easy task. But once the owner becomes engaged in looking at what that “post-transition” life may be, a passion for that new life may appear much sooner than expected.

Future articles will continue the exploration of a successful transition process. For a more in-depth discussion of these issues, see the excellent book “Finding Your New Owner: For Your Business, For Your Life” by Jack Beauregard.

LEGISLATIVE UPDATE: Deadlock Continues

With elections barely 3 months away, the window of opportunity for Congress to compromise on tax legislation is closing fast. Disagreements remain regarding extending the Bush Era tax cuts, with both parties promising to allow them to expire for all Americans rather than compromise. Senate Democrats introduced the Middle Class Tax Relief Act in mid-July to extend certain tax cuts and benefits for middle class taxpayers (i.e., individuals earning less than $200,000 and couples earning less than $250,000), through 2013, including the AMT patch. Senate Republicans have introduced a competing bill that would extend the Bush Tax Cuts to all tax brackets, and extend the AMT patch through 2014. Neither bill is expected to pass. In mid-July, Federal Chairman Ben Bernanke warned Congress that their failure to reach agreement on the tax bill was threatening the fragile recovery, and again urged Congress to work together to provide long term stability to the marketplace. It now appears less likely that tax legislation will be agreed upon before the November elections.

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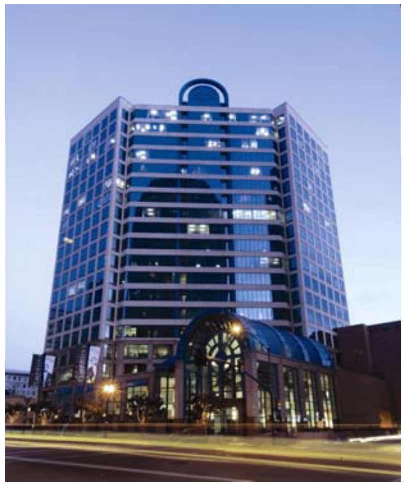

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