5 Ways To Prepare For A Business Exit Or Sale

Exiting or selling your business is a complex process that requires careful consideration. The financial returns loom large and there are a vast amount of personal implications to consider as well.

While it may be a daunting endeavor, a business exit can be an opportunity for you to build generational wealth for your family, pursue new business ventures, achieve a great work-life balance, and more.

Pennington works with many entrepreneurs who have either sold businesses in the past or may consider a sale in the future. There are a myriad of best practices for business owners to consider and adopt prior to an exit, and this whitepaper highlights the most important ones, based on our experience working with successfully exited entrepreneurs.

1. *Reduce your tax burden through income and estate tax minimization strategies*

There are numerous strategies that may enable you to reduce the tax burden of your exit and thus, maximize your gains. These include estate planning strategies such as:

- Family limited partnerships and grantor annuity trusts (GRATs), or a combination of the two, which allow for the transfer of appreciated assets to other family members at a low tax basis.
- A change in personal residency, as there are numerous states that have very low or no taxes.
- A change in corporate structure from a flow-through entity to a C Corp or vice versa.
- Employing rollovers and exclusions, such as Section 1202 treatment, which provides investors an opportunity to exclude some or all of the gain realized from the sale of qualified small business stock (QSBS) held for more than five years.
- Reinvesting the gains in an Opportunity Zone Fund or an Opportunity Zone Business, which would allow for deferral of the gain on sale as well as tax free treatment on the new investment if held for 10 years.
- Specialized investment strategies that accelerate capital losses or ordinary income losses to shelter or protect income.

2. *Partner with an investment banker to maximize your business valuation*

Hiring an investment banker with knowledge and experience in the sector will help to drive a professional but competitive sale process. There are numerous options for an exit that need to be considered, including:

- Sale to employees through an ESOP
- Sale to a strategic buyer
- Partial or majority sale to a private equity investor
- An IPO
- A debt-financed recapitalization that can lower cost of capital and allow owners to retain control.

Selecting the right investment banker and aligning and negotiating the right terms can be overwhelming. In our experience working with exited founders, many described partnering with an investment banker as 'invaluable' or 'challenging' like working with many professional advisors. Choosing the right partner and creating alignment up-front often yields a better outcome adding value at a multiple of their fees.

3. *Take financial and legal preparations*

Planning ahead and conferring with experienced legal counsel and tax advisors is absolutely critical. Not only will this facilitate a smoother transaction process, but it also has the possibility of driving higher offers from buyers. Some preparations you can take are:

- Getting your books and records in order (consider audits for the past year or two)
- Make sure your tax filings are up to date
- Clean up any pending litigation

4. *Formulate your post-exit plan*

Creating a post-exit plan can contribute to a greater level of satisfaction and fulfillment following a sale. Determine how involved you wish to be in the business after you sell, as this decision will impact deal structure (up-front cash vs. earnouts, etc.) and the next phase of your professional life. If you do not wish to stay involved in company operations post-sale, there are a number of possibilities for you, such as:

- Pursuing new business ventures
- Serving on an advisory board or in an operating partner role at a private equity firm
- Providing guidance to others through consultancy or mentorship
- Investing time and resources into philanthropic causes or social impact initiatives

In a market study performed by the Exit planning Institute, 'The State of Owner Readiness' report, approximately 3 out of 4 business owners said they experienced regret over the sale of their business due to poor or no post-exit planning. This is because of the emotional link many entrepreneurs place on their identity and their business. Once that link is severed by a sale, a sense of loss often comes with it. This underscores the importance of creating a post-exit roadmap, to enable you to create and reach new personal and professional goals, empowering you for the next phase of your life.

> Advice from a successfully exited entrepreneur:
>
> ***Know not only why you're selling, but what you will be doing post-sale. Have a purpose around what is next.***

5. *Ensure your financial legacy and have a plan to protect your wealth for generations*

Major liquidity events inevitably lead to increased wealth management challenges as finances become more complex post-sale. Growing and maintaining your wealth requires sophisticated strategies that go beyond traditional wealth management. While most entrepreneurs will pass wealth onto the next generation, familial wealth often dissipates by the third generation without proper planning and management. To avoid a potentially negative outcome and to protect your legacy, consider creating a family office or partnering with a multi-family office. Taking this step will allow you access to experts who can craft a bespoke strategy to preserve your wealth, your values, and your legacy for generations to come.

Conclusion

Closing on the sale of your business can feel like a major victory – all the work you put into building your business, the time, energy, and passion you invested, has finally come to fruition. Letting go of that chapter of your life to pave the way for new opportunities, requires careful planning and an understanding of the tax, legal, and financial preparations that are crucial for a smooth business exit and life transition. While it may be overwhelming, we have created a community of previously exited entrepreneurs at Pennington and an infrastructure to guide and support you in this transitory stage and plan for your next chapter, both financially and personally.

Pennington Partners is an award winning multi-family office whose mission is to elevate the lives of highly successful entrepreneurial founders in their families. Pennington was founded by entrepreneurs, for entrepreneurs, and because of this, understands the challenges that entrepreneurs face in making and maintaining their wealth.

Ready to start planning for your liquidity event?
Speak with our founder.

Pennington Partners & Co.