

Planning an Exit Strategy for Your Business

The Importance of a Transition Plan and Steps to Move Forward



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A lot has changed in five years.

Before 2016, business pundits noted that baby boomers owned an unprecedented number of small businesses, and the number of sold or dissolved businesses was likely to increase dramatically between 2015-2025 as baby boomers retired and exited the workforce. Additionally, research reports estimated the percent of U.S. businesses that would not sell during this period at 75% to 90%.

Enter the novel Coronavirus in early 2020.

While plenty of small businesses were hit hard by the pandemic, many boomer businesses have used the pandemic and record low-interest rates as an opportunity to expand.

In his article *Baby Boomer-Owned Businesses Can Help Resuscitate Urban Economies*, The Hill.com, September 12, 2020, Jerry Haar notes that 3.5 million Boomer-owned/operated businesses in the U.S. employ an estimated 72 million full-time workers and are valued between \$13-15 trillion. Further, he points out that Boomer-owned companies drive local economies, representing at least 40 percent of a city's economy. Because such a significant portion of local economies is tied to Boomer-businesses, the successful transition of these businesses cannot be overstated.

However, according to Haar, while approximately 2.4 million boomer owners are poised to transition by 2027, less than three out of 10 owners have a transition plan in place, and only six in 10 have a contingency plan prepared should they die unexpectedly or become disabled.

As attorneys, accountants, and wealth management advisors guide their business clients through this unprecedented economic situation, the answers lie in creating a sound exit strategy.



What is an Exit Strategy?

It is a blueprint that enables the small business owner to plan for ownership transition either to another company, individual, or investor. Exit strategies include selling the company or turning it over to another individual via succession. And while it might not be about making money, business owners often have other goals they want to accomplish, such as establishing a legacy, ensuring that the business remains in the family, or continuing to have a say in what happens in the business.

Getting your clients to plan for next week can be a challenge, let alone plan for retirement. Common responses to the "why don't we put a plan in place for your future" question include:

"I'm too busy running the company";
"There's plenty of time for that";
"I know what my business is worth";
"My business is my retirement" and, of course,
"That'll never happen to me."

The information below is not new, nor is it rocket science; it is, however, necessary for your clients to consider. As trusted professionals, the onus is on us to bring these topics to our client's attention and revisit them regularly.

Steps for Success

1. Set Financial Goals. The first step in creating a viable transition plan and strategy is to determine the owner's long-term income needs and retirement goals. From this, the owner will be able to determine how much money the sale of the business must generate to retire comfortably.
2. Quantify the Value of the Business. Once your client's long-term financial goals have been determined, the next step is to figure out the current fair market value of the business. The current value will then dictate whether or not #4below (building business value) is necessary and, in turn, the approximate time frame for the owner's exit from the business.
3. Request a Business Valuation. An accurate valuation is an essential tool for a business owner to assess opportunities and opportunity costs as they plan for future growth and eventual transition. Additionally, it is an excellent tool to help identify problem areas and/or areas of concern in the business.



4. Build Business Value. If the value of the business is what the owner expected, then the owner's exit will likely fall in line with the financial goals established. If, however, the value of the business is not as much as the owner expected, then it is likely the owner will need to stay active in the company for a more extended period to bring the value of the business up to a level that will allow him to exit comfortably.

There are several ways to improve the overall financial condition of the business.

- a. Eliminate worthless inventory and debtors. No one wants a business with out-of-date stock or long-term non-payers. If the plan is to sell the company, have your client get rid of both.
 - b. Prepare the management team. Encourage your client to share critical knowledge with management and establish a succession team for the business—document daily operation procedures. A few simple how-to manuals can help in a transition. Videos would work as well.
 - c. Clean up the financial statements. Are there personal expenses included in the company books? Put an end to that practice. Is there real estate or a portfolio of marketable securities in the company that is no longer vital to the business's operations? Move them to a separate entity.
5. Strengthen Legal and Contractual Affairs. Many legal questions arise when selling a business. Be certain the ownership and structure of the business are in order. Has your client been compliant with the regulators, if applicable? What contracts are in place with customers and vendors? Are those contracts up-to-date?
 6. Create a Contingency Plan. Even with a comprehensive transition plan in place, things can go wrong. For example, the owner can become physically or mentally disabled, an essential employee could leave or die, or a fire or hurricane could destroy the business. Planning for these and other types of unexpected situations should be built into every business exit plan. Things the owner should consider as part of a contingency plan include a buy-sell agreement, essential employee incentive programs, and purchasing business, disability, and/or life insurances.

Bottom line, if your client wants to sell his business for a maximum profit later, then you need to help him prepare his transition plan today.

Conclusion

Many moving parts can impact a company's valuation. As a trusted advisor, helping your client develop an exit strategy begins with proactive planning and targeted conversations about their long-term goals. Recommending a business evaluation is an important first step in assessing opportunities and opportunity costs as the business owner plans for future growth and eventual transition.