Transitioning from Your Business

Your Next Great Challenge

Presented by:

David Looper
Consultant & Business Transition Advisor

(503) 804-5412
dlooper@omep.org
Ownership Transition

• 59% of company leaders anticipate or are considering transitioning out of their current positions within the next 5 years
  - Next Generation Manufacturing Study, 2011

• “65% to 75% of all small businesses will go up for sale in the next 5 to 10 years. Why? Retiring baby boomers.”
  - Inc Magazine
Reality Check:

Family-business transition success rates

- 2\textsuperscript{nd} generation success - 30%
- 3\textsuperscript{rd} generation success - 13%
- 4\textsuperscript{th} generation success - 3%

Selling your businesses is no better...

- 20% of business get sold to outside buyers that want to be sold
- The Future: Baby-boomer business glut will probably depress sales prices

Liquidation – 35-40% will use as Transition Exit
Most transitions fail because of...

- Insufficient planning horizon (time)
- Inadequate personal & financial planning
- Lack of successor leadership team preparation
- Mismanaged family communications and values
Studies bear this out

- 64% No exit/succession plan
- 63% No financial exit plan
- 62% Never had a business valuation
- 31% No estate plan beyond a will
- 30% No plans to retire, Effectively – “Dying in the chair”
- 48% Family-owned businesses collapse after the founder’s death.
Successful Exits Require Planning

Business Transition Planning is a Process
...It’s not an event that occurs one day.

- Self-discovery
- Planning
- Preparation
- Execution
Exit Strategy Development

- Exit Vision & Timing
- Financial Readiness/ Business Value
- Best Transition Options
- Exit Vision Review
- Contingency Plans
- Estate Planning
- Business & Personal Document Alignment
- Value/Business Enhancement
Exit Quadrant Chart
Adapted from Exiting your Business, Protecting your Wealth, by John Leonetti

**Transition Options**
- Internal Buyout
  - Management Team
  - Partners
  - Family Transition/Gifting
  - ESOP

**Transition Options**
- Sell to External Buyer
- Internal Buyout
- Family Transition/Gifting
- Professionally Managed
- ESOP

<table>
<thead>
<tr>
<th>Financial Readiness</th>
<th>Mental Readiness</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>High</strong></td>
<td><strong>Low</strong></td>
</tr>
<tr>
<td>Well off but chooses to work</td>
<td>Stay &amp; Grow</td>
</tr>
<tr>
<td>Rich and Ready to go</td>
<td>Get me out at highest price</td>
</tr>
</tbody>
</table>

**Transition Options**
- Grow Biz & Increase Savings
- Sell to Private Equity Group
- Family Transition upon inability to work or death
- Liquidation – upon inability to work or death

**Transition Options**
- Sell to highest price
  - External Buyer
  - Internal Buyer
  - Liquidation – no buyer
# Readiness & Timing Dictate Options

## Transition Options

<table>
<thead>
<tr>
<th>Internal</th>
<th>External</th>
<th>Other</th>
</tr>
</thead>
<tbody>
<tr>
<td>Family Transfer/Sale</td>
<td>Individual Buyer</td>
<td>Liquidation</td>
</tr>
<tr>
<td>Shareholder Sale</td>
<td>Strategic Buyer</td>
<td></td>
</tr>
<tr>
<td>Management Buyout</td>
<td>Financial Buyer</td>
<td></td>
</tr>
<tr>
<td>ESOP</td>
<td>Investor Group</td>
<td></td>
</tr>
<tr>
<td>≈ 30-40%</td>
<td>≈ 20-25%</td>
<td>≈ 35-40%</td>
</tr>
</tbody>
</table>
# Ownership Transfer Characteristics

<table>
<thead>
<tr>
<th>Internal Ownership Transfer</th>
<th>External Ownership Transfer</th>
</tr>
</thead>
<tbody>
<tr>
<td>• Buyer(s) have <strong>NO MONEY</strong></td>
<td>• Buyers bring cash/financing</td>
</tr>
<tr>
<td>• You finance buyout over 5-10 years</td>
<td>• Get paid immediately</td>
</tr>
<tr>
<td>• Increased risk - possible loan default</td>
<td>• No/low risk of default</td>
</tr>
<tr>
<td>• Low business value preferred</td>
<td>• High business value preferred</td>
</tr>
<tr>
<td>• Lower taxes and fees paid</td>
<td>• Highest taxes and fees paid</td>
</tr>
<tr>
<td>• Transition exit can be gradual</td>
<td>• Transition exit is immediately</td>
</tr>
<tr>
<td>• Maintain involvement &amp; control longer</td>
<td>• No future involvement or control</td>
</tr>
<tr>
<td>• Culture &amp; methods maintained</td>
<td>• Culture/methods will change</td>
</tr>
<tr>
<td>• Buyer(s) successors are known</td>
<td>• Buyer is stranger/competitor</td>
</tr>
<tr>
<td>• You can determine your successor</td>
<td>• New owners - new leadership</td>
</tr>
<tr>
<td>• Weak Leaders – <strong>BUSINESS WILL FAIL</strong></td>
<td>• Weak Leaders – <strong>NO SALE</strong></td>
</tr>
</tbody>
</table>
Sales Proceeds – What you keep

- **Business Proceeds**
  - **Net Proceeds**: 35%
  - **Taxes**: 5%
  - **Transaction costs**: 3%
  - **Intermediary**: 5%

- **Income Taxes** – Biggest amount goes to Uncle Sam;
  - Stock v. Asset Sale.
  - Best the seller can hope for is for capital gains on the sale of the business.
  - Combining the Feds and Oregon your rate is close to 35%.
  - Depreciation or ordinary income purchase price allocation may push the rate up.
  - Purchase price allocation – important tax implications.
  - C-Corporation entities are bad; some planning strategies exist.

- **Intermediary costs** or success fees rate from 3 to 7% of the selling price depending on the circumstances.

- **Other transactional costs** consist of legal, closing and other costs.
Create a “Turn-key Business”

Can your business run without your leadership?

The bigger question is...

Are you willing to let others lead?

Turn-key businesses are...

- Easier to sell, bring higher values
- Provide successor leadership a roadmap for success
- Answers the key question can the successor lead?
Contingency Plan

If you suddenly die or become incapacitated:

- Will your family continue to have an income?
- Who is capable of running the business?
- Who has the key customer, supplier, and bank relationships?
- Will key leadership and employees leave?

HAVE YOU TOLD ANYBODY YOU HAVE A PLAN?
Estate Planning

Tax efficiently directing your assets to your heirs

- Your Estate Tax Liability – Uncle Sam is waiting
- Federal Exemption $5.2 mil both you & spouse
- OR state Exemption $1.0 mil each / rate 10 – 16%
- Will your estate have the cash to pay in 9 months
- Tax liability impact to the business, will it survive?
Business Documents

Align your personal and business documents to support your exit strategy

- Business entity structure, C-corp, S-corp, LLC, etc
- Buy-sell or Operating Agreement language
- Estate Planning, wills, trusts, gifting plan, insurance
- Property ownership structure
Value/Business Enhancement

Drive business changes that close your personal WEALTH GAP

- Top line Sales growth
- Operational improvements
- Investments in business
- Leadership development

Identify targeted actions to be taken
Succession Planning – Build Bench Strength

Quality leadership adds to business value & increases your ability to sell the business

- Start early & get the right people on the bus!
- Identify successor skills & competency needs
- Develop OJT learning opportunities with clear roles, responsibilities and outcomes

Let them lead, let the succeed and let them fail – THIS IS HOW YOU LEARNED
You need an Advisory Team

---

# Business Advisor Team

The Experts You May Need and Their Roles

<table>
<thead>
<tr>
<th>Roles</th>
<th>CPA</th>
<th>Attorney</th>
<th>Valuation Professional</th>
<th>Intermediate / Broker</th>
<th>Consultant</th>
<th>Other</th>
</tr>
</thead>
<tbody>
<tr>
<td>Business Transition Advisor/Family Business Advisor</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Executive Coach</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Successor Leadership Coach</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Family Counseling - Broken/Stressed Family Unit</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Estate Planning</td>
<td>X</td>
<td>X</td>
<td>X</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>External &amp; Internal Transfer Options Analysis</td>
<td></td>
<td>X</td>
<td>X</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Contingency Planning &amp; Insurance Use</td>
<td></td>
<td></td>
<td></td>
<td>X</td>
<td>Insurance Broker</td>
<td></td>
</tr>
<tr>
<td>Business Value Enhancement</td>
<td></td>
<td></td>
<td></td>
<td>X</td>
<td>Financial Planner</td>
<td></td>
</tr>
<tr>
<td>Financial Planning/Wealth Management</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Advisory Board Members: X X

---

External Selling Process:

- NDA – Non-disclosure Agreement | X
- Buyer Identification
- Negotiation
- LOI – Letter of Intent | X
- Transaction Structure
- Tax Issues and Strategies – Max. Seller’s Proceeds | X
- Sale Document Generation | X

---

Special thanks to Mr. Tom Napier, Napier Business Advisors, for his help developing this information. Mr. Napier provides business valuation, intermediate services for selling businesses, and general business consulting. [www.bus-valx.com](http://www.bus-valx.com), (503) 670-8286

---

David Looper, Consultant
Cell: (503) 804-5412
Email: dlooper@omep.org
Thank You!

For more information, contact:

David Looper
OMEP
(503) 804-5412
dlooper@omep.org