



Exit Planning In a Pandemic



Janet Chase, ASA, CPA/ABV
Managing Director

3241 E. Shea Blvd, #196
Phoenix, AZ 85028

480.608.4919
jchase@southparkval.com

The global pandemic has caused many Americans to think more about their own mortality and the importance of planning for contingencies. If you are a business owner, now is a good time to think about exit planning. Exit planning involves four key considerations:

- Considering your objectives;
- Establishing business value;
- Determining what will increase value, and
- Evaluating your alternatives for a buyer.

Looking For a Buyer

In terms of a buyer, each business owner has several alternatives. If there are other owners in the business, one option worth exploring is selling your share to these other owners. Similarly, selling to existing managers can sometimes be a viable option, either through a partial sale or in a management buy-out. Business owners quite often also explore selling to a third party or transferring to existing company employees. There are many complexities involved with each of these alternatives, but in general there are four top things to consider:

- Value,
- Taxes,
- Extent of Involvement after the Sale, and
- Impact on Your Employees.

Value

When selling your business, who you sell to can greatly impact value. For example, if you own a small clothing shop and sell to a national retail clothing chain, who can then use existing distribution channels for your designs, the price they're willing to pay will usually not be based on the earnings you were able to achieve at your shop alone. Instead, the price will be based upon the national retailer's projections of the profit they can make selling your designs at all their stores (usually a higher value). So, selling to a third party may produce a higher value if there are synergies involved.



Exit Planning in a Pandemic (continued)

Taxes

If you get a high value, that's good news, right? Like any other type of income, if you make money on the sale of your business there will usually be tax implications. If you sell to an outside party, whether the money you make on the sale is considered ordinary income or capital gain usually depends upon the details of the transaction. Also important is whether the sale is structured as an asset sale or a stock sale. On the other hand, if you sell to your employees (referred to as an Employee Stock Ownership Plan, or "ESOP") instead of to a third party, tax benefits can be significant.

Extent of Involvement After the Sale

Although financial considerations like value and taxes are important, business involvement after the sale is another key consideration. To many business owners, the thought of staying involved in the business after the sale is very appealing. It is difficult to give up the reins all at once. Some business owners stay involved after the sale to a third party, but sometimes this is not an option. The buyer may require the business owner to retire and sign a non-compete agreement. Here the type of transaction is also very important because many business owners find that significant involvement after the sale is a more probable outcome with an ESOP transaction.

Impact on Your Employees

And if the business owner wants to keep his or her job, what about the employees? A final question to ask is "What's going to happen to my employees after I sell my business?" To many business owners who are concerned about employees keeping their jobs after the transaction, an ESOP can be very appealing. When the company is sold to an outside party, there are no guarantees that employees will keep their jobs. Often the acquiring company prefers to bring in their own management team. Also, back office operations such as accounting may be consolidated into the acquiring company's operations, with the resulting positions being eliminated. In contrast, in an ESOP transaction the employees are the owners after the sale, so they determine their own fate.

Should I Stay or Should I Go?

Many small business owners are finding that, now that the pandemic is upon us, they are giving greater thought to "What is next?". There is no better time than the present to evaluate your alternatives and plan for the future.