# Planning Your Exit: Five Questions On Optimizing Results

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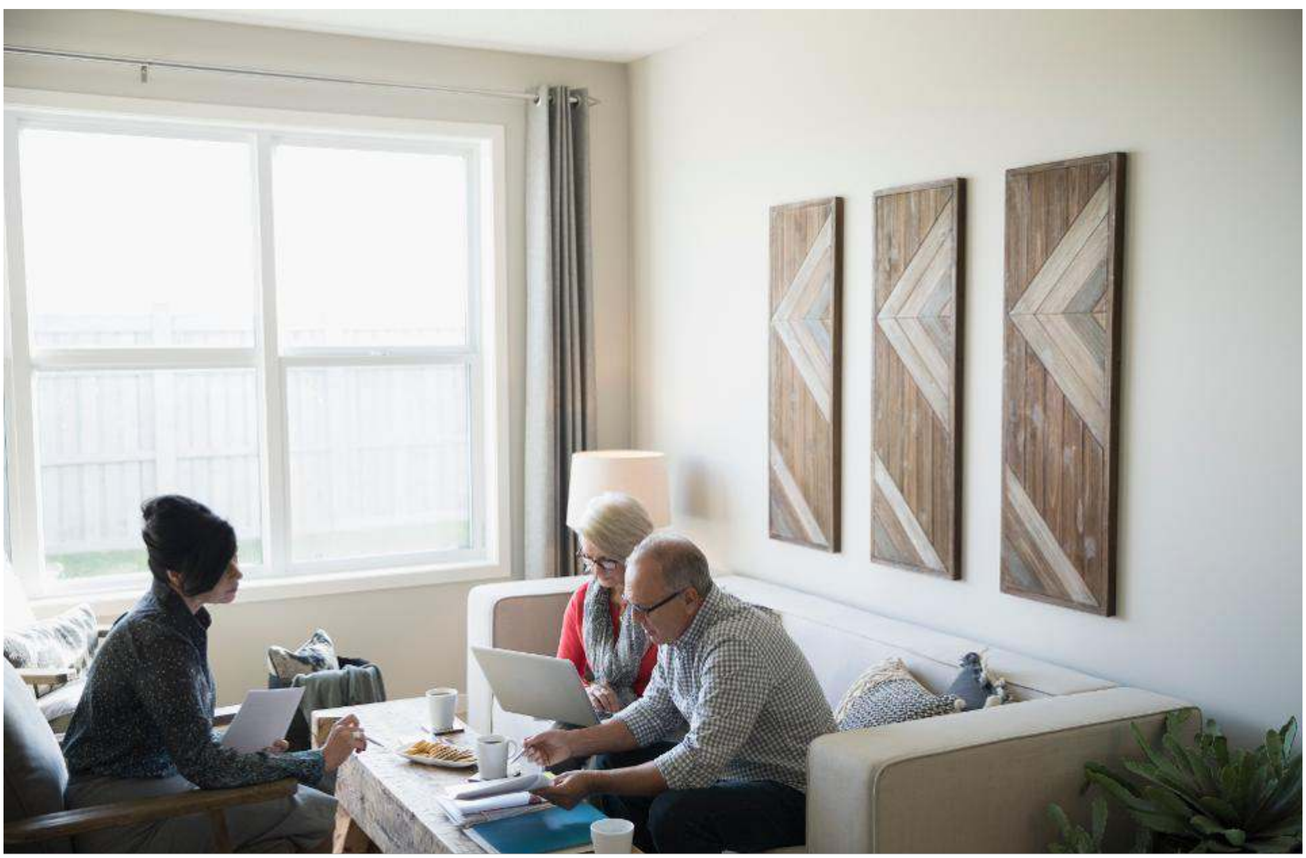
Forbes Insights research shows that over half of today's high-net-worth investors generated or obtained the lion's share of their wealth either exclusively (22%) or to some degree (31%) through a family-run business. This highlights the essential art of exit planning—prepping the family and the business for its future once today's stewards hand over the reins.



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To gain deeper insight into the issue, Forbes Insights spoke with Thomas J. Frank Jr., Executive Vice President, Northern California Regional Manager for Whittier Trust. Below he responds to five questions relating to effective exit planning.

**1. What forms of exits are available in which circumstances?**

Whole books are written on the myriad ways business owners can extract value when exiting their companies. But in general, depending upon the ownership structure and whether there are family members set to inherit, there are a variety of tools that may be employed. These can include outright gifts of ownership interests, recapitalizations, partial or complete sales of the business, sales to ESOPs, just to name a few. And each has its advantages to be evaluated against specific circumstances.

But the important thing is for a business owner to step back from the business and ask, "What do I envision for this company long after I'm gone?" The answer to that will drive many of the decisions that need to be made. For example, has the owner extracted enough cash out of the business to live comfortably in retirement? If so, then maybe gifting ownership interests to heirs is the way to go. Does the owner need to take cash out at the exit? In this case, a sale or partial sale may be the right answer. There is certainly not a one-size-fits-all solution here.

**2. How long before retirement should owners begin thinking about their exits?**

Generally speaking, a hallmark of any well-run business is a good succession plan. If it's a family business, meaning that there is a hope and expectation that younger family members will step up to take the reins, then planning several years in advance is essential.

The details of such a plan will again depend on many circumstances such as the size of the business, whether it's an LLC, partnership or corporation, the complexity of the business and the ownership structure. Steps to consider include preparing future generation(s) by encouraging them to take an interest in the industry, perhaps giving them a role in the business or have them go to work at another business in the same industry. It's also a good idea to set up some mechanism of family governance so that family member shareholders have access to information about the business even if they're not involved in running it day to day.

Overall, it will be important to work closely with the family's lawyers and tax advisors to efficiently and effectively transfer ownership interests, paying particularly close attention to estate tax planning. And if by chance family members will not be running the business in the future, then it becomes critical to make sure there is a team of skilled managers in place to keep the business running.

**3. Are there any steps that should be taken to optimize valuation and transition?**

Get an early start to the planning. Engage the next generation of management, be they family or non-family executives, and prepare them for the transition so the business retains its value and its ability to grow. Also, make sure there is sufficient capital left in the business post-exit to allow for rough patches in the business cycle. Don't burden the company with excessive debt in order to take cash out. If the goal is to transfer ownership over time to heirs, make use of downturns in the business cycle to gift ownership interests at low valuations to take advantage of gift tax exclusion amounts.

Also, consider hiring business valuation experts to perform regular valuations so there aren't any surprises. This is critical when making gifts of ownership interests to family members.

**4. What if you're certain a big part of your exit is going to be a sale or even a partial sale? Are there any sorts of steps you should be taking, and if so, when?**

The business owner will want to position the company for peak valuation to occur at the time the deal is struck. Steps to take might include lightening up on debt, strengthening strategic partnerships, locking in low cost rents/equipment and similar moves.

One thing to consider here is that many family-owned and run businesses may run certain expenses through the business—things like company cars, planes, etc. The acquiring owners are probably not going to want to foot the bill for these things going forward, so the exiting owner should make sure to have enough cash or cash flow post-sale to pay for things like this.

I've seen many situations where the acquirer wants the current owner to stay on in some capacity. In the best of circumstances, this is a short-term arrangement of a couple of years. I've also seen a complete and immediate exit of the selling owner from the business. Exiting owners should really think about what they're willing to actually commit to, as few entrepreneurs are going to truly enjoy working for someone else.

**5. Any advice on structuring such deals?**

In terms of deal structure and tax planning, owners should bring in their tax and legal advisors very early on. Once a letter of intent is signed, there isn't a lot of room for planning. So when thinking about pre-sale tax planning, don't focus solely on income tax planning. Think about gift and estate tax planning as well. Again, before the letter of intent, there may be some excellent opportunities to transfer ownership interests to younger generation family members or to trusts for their benefit. But this kind of planning needs to start early.

In my experience, sales to a strategic buyer are often more effective at keeping the business intact, while sales to a financial buyer usually mean there will be some dislocation of existing resources. Private equity firms often consolidate core functions from the underlying portfolio companies they acquire. Preserving as much of the business as possible may or may not be important to the seller/retiree, but if it is, be certain to seek out a strategic buyer.

Planning to exit a business can be almost as much of a full-time job as running the business. Early and consistent planning is the key to success and will help avoid surprises. Whatever you do, it shouldn't be to put this off until the last minute and certainly not before the business owner passes away. Don't leave this to others to unravel. Failure to plan now will imperil the next generation's opportunities to retain and grow the company after the business owner is gone.

To learn more, read "Reality Check: High-Net-Worth Investors Face Trends Of Lackluster Service and Performance."



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