SELLING YOUR BUSINESS; HARMING YOUR FAMILY?

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Planning an Exit

So you've concluded that it's finally time to sell the business and move on. Surely this was not an easy decision. After all, it's been central to your life for so many years. The company is where you made your mark, achieved respect, and made a comfortable living. These are results that are not easily duplicated, so leaving this behind is not something done lightly. But chances are you've been well advised by people experienced in the exit planning, mergers and acquisitions, and investment banking fields. They've been able to get the business "lean and mean," systems working well, and the management team geared for the challenges ahead. With this solid foundation, the team believes they'll be able to realize the full value of the company in a competitive bidding environment they intend to use to attract qualified buyers. So you've worked hard to get ready and you can now see the day when you no longer have to be responsible for this enterprise. Hopefully, this vision is one that pleases you for the new opportunities you'll have for the future.

Or does it? Perhaps you've already adjusted to the idea of others being in charge and not earning the same measures of respect you received in the past. But the company also provided for a comfortable lifestyle that will have to be replaced. And this new endeavor will be challenged by taxes, lower investment returns, unforeseen events, and other risks. Are you worried that in *selling your business, you may be harming your family?*

"Thanks for Your Support" – Uncle Sam

Your kids and spouse aren't the only family members counting on your support. The other dependent is your "favorite uncle" – Uncle Sam. He'll come looking for you just as soon as you close your sale and realize the product of your life's work. If you started your business some time ago, you likely have a low tax basis (consult with your CPA), which means the consideration received in cash (or the cash realized upon the subsequent sale of exchanged stock received from the acquirer) is nearly all a capital gain. Though long-term capital gains are more favorably taxed than ordinary income (from wages, business income, interest income, etc.), this tax along with the Medicare Tax may mean that nearly a quarter of your sales price will be shared with the government (Ouch!). And don't forget about state taxes that might take even more. So, how well do you think you'll live on reinvesting 70 to 80 cents on the dollar realized from your company?

"What Happened to My Share?" – Kids

If you're over 50, your children are likely adults, and may even work for your company (or have in the past). So they likely have a pretty good idea of the success and value of the business (they may even be part of the management team preparing for the upcoming sale). So, if the Merger & Acquisition team is talking about a multi-million dollar sale, the children most likely can fairly accurately estimate the family's net worth. And from there, they can also start planning on what they believe their respective inheritances should be. Now you may have other ideas about sharing wealth with your children (the many various consequences of doing so, or not, is a very good subject to analyze at another time), but that won't stop them from planning ahead, thinking about their own plans and opportunities, and even approaching you about "lifetime gifting opportunities" to get control of their share while you're still around! And whether you engage in such a discussion post-sale, or defer that subject for the estate settlement process, children often forget that Uncle Sam jumped to the head of the line to take his share, leaving considerably less for them.

More for Loved Ones, Less for Uncle

But do you have to settle for such a reduction of your net worth and future life-style as the price for realizing the value of your hard work over so many years? Does selling your company have to have such a negative impact on your family?

With the right pre-sale planning, the answer is, not necessarily. One effective strategy is to create a Charitable Remainder Trust – a legal entity benefiting both the creator's family as well as one or more worthy charitable organization(s) of the creator's choice. The business owner may transfer (donate) part of the company's equity to such a charitable trust prior to any agreement to sell the business (consult with counsel on rules and restrictions on such qualifying transfers) in order to generate a number of benefits. Assuming a sale will be consummated in the not too distant future, the first benefit is that the sale of the business equity from the trust avoids capital gains taxation. The next benefit is that the value of the equity transferred to the trust creates an immediate charitable tax deduction (consult with your tax professional to determine the size of the deduction and how to apply these deductions) resulting in substantial tax savings. Finally, without capital gains taxes to pay, the trust will be able to reinvest 100% of its sale proceeds to create income and growth, some of which will be distributed regularly to the donor (and his/her family) to help meet expenses for the lifetimes of these family members.

At the end of the trust's income beneficiaries' lives, the remaining trust property (corpus) will go to the named charitable beneficiaries (another very large benefit in terms of fulfilling your plans for achieving lifetime significance). This, of course, means this property is similarly not going to the children. Does this thwart the intended goal of keeping more of your net worth for your family? Again, with the right planning, the answer is, not necessarily. One solution is to use a portion of the income from the trust – or the tax savings from the charitable deduction mentioned earlier – to purchase a life insurance policy on the lives of the donors to replace the assets that the trust will provide the charities.

So, it is feasible to make this change to the second half of life without doing as much harm to the family's future. Appropriate financial, tax, and estate planning advice and strategies may help save taxes, increase future income, and help the family for years to come while also serving the important needs of the community and our society.