

ENTERPRISE
Family Business

Family business must consider various exit strategies

Mike Cohn

You've built a successful company and now it's time for someone else to take over.

How can you get fair value for what you have built? Can family members buy out other family members and still spend holidays together?

Or, maybe there's a competent family member in the business who is a willing buyer, but you worry about getting paid.

What if they don't succeed? Or, worse, what if, without you, they succeed beyond your wildest expectations. What options do you have?

Although most family businesses are closely held and not readily marketable, here are some options you may want to explore when it's time to sell the business.

But first, understand the current value of your business. A business valuation firm or your CPA can be helpful with this first step.

Next, evaluate your business as a potential buyer would.

While historical earnings are informative, a buyer will want to understand what the future earnings might be, along with future opportunities and risks.

Third, be sure that a realistic sales price meets your needs for financial independence after the salary stops.

Sale to a third party

There may be strategic buyers in your industry interested in



synergy and market opportunities with your company.

Sometimes your commercial banker can put you in touch with qualified local, or national, financial buyers interested in a well-run, closely held company with growth potential and a solid earnings history.

In either case, having a competent management team who will stay on will add value to the transaction.

Sale to key employees

Key employees or family members may be the best buyers, especially if they work as a team and can take on the responsibilities of ownership.

After all, they already know the company.

They can often get financing for a complete or partial purchase.

For example, buying operating assets now, with non-operating assets, such as real estate, to be purchased at a later date.

Structuring the transaction to include consulting and other consideration for the seller can make this a win-win for both parties.

Sale to an ESOP

An employee stock ownership plan can provide attractive tax benefits to both a seller and buyer.

The seller may defer the capital gains taxes normally due on sale, and the buyer, through the ESOP, can deduct some or all of the purchase price.

The income tax benefits of the ESOP (for both buyer and seller) can often help bridge the gap between the two sides.

Sometimes, a leveraged ESOP transaction can be successfully combined with a sale to key executives.

Stock redemptions

Don't overlook having the company buy back the seller's stock.

Properly structured, a sale to the company will have capital gain tax treatment.

To protect the company, the sale can be part cash, part installment note. Sometimes a gift or the sale of a few shares to a family member, or key employee, followed by a complete redemption of the remaining shares, can be a viable strategy.

If family members also are shareholders, it will be important to follow the IRS' attribution rules to get favorable capital gain tax treatment.

Coordination with charities

Entities such as charitable trusts are another option. A charitable remainder trust can create favorable income tax treatment along with a retirement benefit for a withdrawing owner.

If the business is a C corporation, shares of the company can be gifted to the trust, and then sold to a third party or back to the company -- if the company purchases the shares for cash.

Proceeds from the sale of stock by the charitable remainder trust are not taxed since the trust is a charitable entity.

The trust invests the sales proceeds and then pays the grantor a retirement benefit.

There are numerous ways to structure charitable trusts to meet individual objectives.

Identifying the proper exit strategy is only one part of the puzzle.

A well-thought-out succession plan takes time and effort, both on the part of the seller and the buyer or buyers in order to make sure the business remains healthy after the transition.

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