



1234 SW Nowhere Street • Portland, OR 97777 • (503) 222-2222 • www.yourcompany.com

When You Might Consider Selling Your Business

For the past 20 years you have built your business, and your company has become part of your identity, just as you have become part of its identity. Even when you are not at “the office,” you are working, thinking, planning. You probably never stop. If you sell your business, you will be leaving behind much more than a job. In this article we discuss some signs that might indicate that it is time to exit your business.

Major Capital Investment Required.

You are supposed to be diversifying your assets, not concentrating them even further. Think about a simple payback analysis: does that extend beyond your estimated retirement date? You want to be able to defend that investment with the energy and intensity you devoted when you were originally growing your business. Maybe it is time to bring in an equity partner with smart money, an industry buyer with the management depth, infrastructure, or distribution network to protect that investment. It might be time to consider selling with, say, a three year employment contract, and let the new owner defend the required capital investment.

A Large Competitor is Taking Market Share Away from You.

Believe me, the news is not going to get better. As an investor you would probably sell the stock in a company you owned if Microsoft or GE decided to assume a presence in that market. Business owners often struggle with objectivity when a similar event takes place in their own company's industry.

Your Legacy Systems have been "Leap Frogged" by a Nimble Entrepreneurial Firm.

This can cause an erosion of your customer base. Your inertia will sustain you for a while, but eventually you will begin to experience customer defections. You can either rewrite, acquire or sell. If you decide to sell, do so early.

A Giant Company in a Related Industry Just Acquired One of Your Major Competitors.

You know they did not make this acquisition to maintain status quo. They want to grow their market share. They will be coming after your clients. The good news is that, as a defensive measure, one or more of

Volume 1, Issue 1

Newsletter SPOTLIGHT

When you might consider selling your business:

- Major capital investment required
- Competitor is taking market share away from you
- Your Legacy Systems have been “leap frogged” by a nimble entrepreneurial firm
- A giant company in a related industry just acquired one of your major competitors
- You’ve lost a major client or key employee
- And more...

Continued to next page...

their competitors will be compelled to make a similar acquisition. Is it best to be aggressively ahead of the curve and present yourself as an attractive acquisition candidate (your CPA can help you do this) while the market is hot and prices are being bid upwards?

Your Fire to Compete at the Highest Level is Not as Bright as I Once Was.

Y o u r competition was already tough when you were at your best. Is your current emotional, energy and financial commitment enough to protect your family's net worth?

Your Kids are Not Interested In or Perhaps Aren't Well Suited To Continuing the Business.

Your original plan was to turn your business over to your children. You do have alternatives. It may well be the greatest legacy you can leave to your kids is to convert your company into a diversified portfolio of financial assets that are far less risky than turning the company over to inexperienced or disinterested managers.

You Have Had a Health Scare.

You start thinking of all the sacrifices you made and all the things you want to do before it was too late. Your list of goals is immediately changed from financial in nature to family, friends, travel, experiences, philanthropy, etc. You might want to listen to your heart this time.

You Have Lost a Major Client or a Key Employee.

Such a loss can be a real blow to a business. By nature, you are optimistic and believe that the lost business will soon be replaced, and you might hesitate to ratchet down the expense level to match this new sales level. If you did cut, did you do it fast enough and deep enough? Maybe it is time to seek a buyer that could replace that business before your company's value is severely impaired as your profits erode.

The Market is Hot and You Decide to Take Some Chips Off the Table for Diversification.

You may be thinking of retiring in four years, but a consolidation is occurring in your industry and valuations are up 20%. Perhaps you can sell at the top and sign a four year employment or consulting contract. (On the average, it takes a business owner and his Exit Strategy team three

years to ready a company for sale. Schedule a valuation meeting with your CPA as early as possible in the process to make sure you are in position

to take advantage of a "hot" market.)

You Can Exit Your Business in an Orderly Fashion and from a Position of Strength.

This is what you intended to do all along. You need an Exit Strategy team to evaluate competitive forces in the market and the relative strength or weakness in valuation multiples, and then to help you prepare your business to be attractive to a strategic buyer. **

What the Current Capital Gains Rate Means to You, The Small Business Owner

Thinking of selling your business?

If you have planned it correctly, most of your transaction proceeds should be long term capital gains. Given the current political climate and the stated direction from the White House, capital gains taxes will come under attack. If you are a business owner and are thinking of selling your business within the next 5 years, you may want to consider moving up your exit timeframe.

The reduced 15% tax rate on capital gains has

“Your competition was already tough when you were at your best.”

been extended through 2010 as a result of the Tax Reconciliation Act signed into law by President Bush on May 17, 2006. In 2011 these reduced tax rates will revert to the rates in effect before 2003, which were generally around 20% (33% MORE tax!).

Here's a very possible scenario (ask your CPA to help you calculate the impact of these possible developments on your business). The Alternative Minimum Tax (AMT) is currently targeted by some for elimination. The revenue shortfall will be made up by raising taxes elsewhere, and the capital gains tax, the "owner of capital" tax, is the most vulnerable for a sizeable increase.

Don't be surprised if the long term capital gain tax rate will be moved to an upper limit of 28% by late 2010 for the high end income bracket.

Key point: The business seller is going to take a big hit on his after tax proceeds if his business sale is concluded after November 1, 2010. Example: A 63-year-old man started a business 25 years ago and now sells it for \$5 million. His initial investment was for equipment, and that has fully depreciated, so his basis is approximately \$0. Ignoring selling costs, under current tax laws he would have a \$5 million capital gain from the sale of his business, and his after tax proceeds would total \$4,250,000.

If he were to sell after the projected increase in the capital gains tax, the same sale would net him \$3,600,000. Additionally, if the business owner waits until the actual change is voted into law, there will be an unusually high number of businesses to be for sale as owners try to beat the increase. That add unwanted supply and demand pressures on the selling price.

The most important tax issue, however, for the business seller continues to be the corporate structure (C Corp, S Corp, or LLC) and whether the business sale is an asset sale or a stock sale. Unless you are planning on going public or have hundreds of stockholders, you probably do not want a C Corp to begin with. Ask your CPA about an S Corp or an LLC. If you are currently are a C Corp, ask about the advantages of converting to an S Corp.

Here is what happens when there is an asset sale of a C Corp. The assets that are sold are compared to their depreciated basis and the difference is treated as ordinary income to the C Corp. Any goodwill is considered a 100% gain and also is treated as ordinary income. This new income drives up your corporate tax rate, often to the maximum rate of around 34%. You are not done yet. The corporation pays this tax bill and then there is a distribution of the remaining funds to the shareholders. They are taxed a second time at their long term capital gains rate.

Compare this to a C Corp stock sale. The stock is sold and there is no tax to the corporation. The distribution is made to the shareholders and they pay only their long term capital gain on

“ This anticipated change to the capital gains tax rates will certainly add to the complexity of selling a business. ”

the change in value over their basis. The difference can be hundreds of thousands of dollars.

This anticipated change to the capital gains tax rates will certainly add

to the complexity of selling a business. It cannot be stressed how important a factor taxes will be in your successful business exit, and how important it is to have your CPA lead the Exit Strategy team you assemble. Here is a summary checklist:

Continued to next page...

Tax Consideration Checklist

- Get Good Advice on Original Corporate Structure
- If C Corp - Retain Ownership of all Appreciating Assets Outside Corporation, i.e. Real Estate, Patents, Franchise Rights: avoid double taxation
- Look at Deal Economics First, Taxes Second
- Make Sure Your Transaction Support Team has Deal Experience
- Before You Go To Market, Work With Your Team to Understand Deal Structure vs. After Tax Proceeds
- You Have the Right to Pursue the Minimum Payment of Taxes; Exercise Your Rights
- Planning is more effective as a fore thought than an afterthought

Professional advisors can match your desired outcomes with the right tools. Be aggressive in

your tax positioning of the sale of your business, both with the buyer in your negotiations and with your filings with the IRS. The various deal structure options are very important issues that need to be understood from a tax impact perspective. Remember that a deal term that is favorable to the buyer for tax treatment is correspondingly unfavorable to the seller. You can bet that the buyer's team of advisors is well versed on this topic. Make sure that your team of advisors is equally well versed or you could end up with a much less than you thought in after tax proceeds. **

©2010. No part of this newsletter may be reproduced or redistributed without the express written permission of the copyright holder. Although the information in this newsletter is believed to be reliable, we do not guarantee its accuracy, and such information may be condensed or incomplete. This newsletter is intended for information purposes only, and it is not intended as financial, investment, legal or consulting advice.



Menden & Menden
1234 SW Nowhere Street
Portland, OR 97777