Selling your business

Conducting short-term and long-range planning to maximize returns **Interviewed by Leslie Stevens-Huffman**

Should owners of closely held businesses plan for the ultimate sale of their business from the outset or as the sale date appears on the horizon? The answer: They should do both, says Peter G. Dolbee, corporate tax partner with Haskell & White LLP.

Dolbee says that both short-term and long-range planning are vital when it comes to achieving the optimal return from ownership and the subsequent sale of a closely held business. Planning should be an ongoing owner activity that starts before the business is launched and ends only after the business is sold and the final check is cashed. Along the way, there are strategies and supporting activities that can help owners achieve the maximum return on their business investment.

"The problem is that owners generally think about short-term tax-savings opportunities without considering the long-term consequences," says Dolbee. "Effective exit strategies are conceived from the outset, and they should be considered when the business is first formed. Very few owners do this well. I have seen sales transactions where we structured the sales strategy about 12 years before the business was sold, and it resulted in millions in tax benefits for the owners."

Smart Business talked to Dolbee about how owners can achieve maximum return by conducting short-range and long-term planning around the sale of their business.

How does the initial selection of the business entity impact return when the business is sold?

It's important to think long-term when planning for the sale of your business, and an important consideration when selecting the appropriate form of business entity is how long you intend to keep the business. Many owners think that if you're only going to keep the business short-term, it's best to structure as a C corporation, but that can be a bad strategy for closely held corporations because a sale or liquidation of the assets by a C corporation results in double taxation. Structuring as an S corporation or an LLC is a popular alternative because the tax consequences resulting from the sale of the business are more favorable than those resulting under a C entity. However, C corporations that convert to S status within 10 years of the sale may be subject to built-in tax gains at the highest corporate rate.

Peter G. Dolbee
Corporate tax partner
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Also, don't be ambiguous by structuring one component of your operations as a C and another as an S corporation. I've seen this before, and it makes no sense because you may not be getting the advantages of either type of entity. Last, keep your personal and real estate assets out of the business. If you wish to purchase such assets, do so in your own name and then lease them back to the company. Otherwise, when the business is sold, any assets will be taxed based upon their appreciated value.

What type of presale planning benefits business owners?

First, consider if you want to transfer the wealth resulting from the sale of your business to your heirs. Valuations of the business made in advance of the sale can be substantially less than at the time of the actual deal, and waiting until the sale is imminent imposes negative tax consequences. Anticipation and planning are vital, because when the gift is made well in advance of the sale, you can employ estate-planning techniques allowing you to transfer substantial value to your heirs at reduced gift-tax levels, and valuation principals decrease the amount of the gift.

Second, consider transferring a minority interest in your business to charity before the transaction to get the full benefit of the deduction without the taxable gain. You don't want to make a gift with after-tax dollars. Third, consider transferring ownership to your children before the transaction, which can save substantial taxes resulting from the sale.

What records are needed to complete the transaction?

Once the deal starts, things happen quickly, and the better organized the seller is, the more likely the deal is to close. Get a list of what records you need to keep and how long you need to keep them before you launch your business. Organize the files for easy access because recreating documentation is costly and delays can kill the deal.

Also, document all employee compensation agreements in writing. There can be substantial confusion as to what was promised once the deal is imminent, and having properly executed contracts in place will eliminate misunderstandings and ease the transaction

Where should owners go for advice?

Don't assume that your traditional advisers are the best ones to turn to when you need advice about selling your business. You want to select lawyers and accountants who specialize in mergers and acquisitions, and they should know the latest techniques. To select competent advisers, consider asking these questions:

- Should I do a stock sale or asset sale?
- Do you know what constitutes typical representations and warranties, indemnities, and sale provisions?
- Do you know what a basket, cap, clawback and antichurning mean?

Asking screening questions like these will assure business owners that they are selecting the right team when it comes time to sell their company.

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