Business Succession Planning

GRANT COUNTY EXTENSION

LANCASTER, WI

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Succession Options

Leadership Succession

Merger or Acquisition

Employee ownership can be accomplished in a variety of ways.

- Buy stock directly
- Given it as a bonus
- Receive stock options
- Obtain stock through a profit sharing plan
- Become owners through worker cooperatives
- Employee Stock Ownership Plan (ESOP)

Becoming an entity

- Sole proprietorships or partnership
  - End upon the death of an owner
  - No limitation of liability
- Limited liability company and corporations
  - Membership units transfer like other assets
  - The company continues
  - New member or shareholder steps into the shoes of the deceased
  - Can sell some or all of the ownership interest
  - Limits liability

Leadership Succession

- Strategic Planning
- Target and train
  - Can be employees or family members
- Transfer of interests
  - Can be all at once or over a number of years
  - Purchase
  - Gift

Mergers & Acquisitions

Mergers and acquisitions are not just for large corporations

Transfer of ownership

Can be a part of leadership succession or an unrelated third party

Merger

Essentially, a merger occurs when two businesses join together to form a single, new business entity.

Exchange of ownership interests

Acquisition

Ownership interests

- New owners of business, same company
- Liabilities stay with company, new owners assume them
- Corporations = Stock
- LLC = Membership Interests

Asset sale

- New company owns assets, old company often dissolves
- Liabilities usually remain with old company

Ownership Interest Sale

The buyer purchases the selling shareholders' ownership interests directly and, in doing so, obtains an ownership interest in the seller's legal entity.

- The buyer steps into the shoes of the seller.

In General, Sellers Prefer Stock Sales

- May be an opportunity for the seller to "walk away" from the business (and its future liabilities).
- All the proceeds are taxed at a lower capital gains tax rate and with C corporations, the corporate level taxes are bypassed.
- Buyers lose the ability to gain a stepped up basis in the assets.
  - The basis of the assets at the time of the sale (book value) sets the depreciation basis for the new owner.

Asset Sale

Asset acquisitions involve the sale or purchase of the tangible (e.g. equipment) and intangible (e.g. intellectual property) assets of a business.

The result is that the buyer will own the assets of the seller. The seller will retain possession of the selling entity.

In General, Buyers Prefer Asset Sales

- Asset sales allow buyers to “step-up” the company’s depreciable basis in its assets.
  - By allocating a higher value for assets that depreciate quickly (equipment with a typical 3-7 year life) and by allocating lower values on assets that amortize slowly (goodwill with a 15 year life), the buyer can gain additional tax benefits.
  - This allocation reduces taxes sooner and improves the company’s cash flow for the first few years.
- Asset sales allow buyers to more easily avoid inheriting potential liabilities.
- Certain assets may need third-party approval to be assigned (e.g. contracts, leases, etc.) and can cause some hold-ups in the transaction.

ESOP

The most common form of employee ownership in the U.S. is the ESOP, or employee stock ownership plan.

By 2014, 7,000 companies had ESOPs covering 13.5 million employees

- Public companies account for about 5% of the plans and about 40% of the plan participants

ESOPs are most commonly used for a variety of reasons

- to provide a market for the shares of departing owners of successful closely held companies
- to motivate and reward employees
- to take advantage of incentives to borrow money for acquiring new assets in pretax dollars

https://www.nceo.org

Before Jumping In

Make the business case

Get the facts straight

Make sure the company cultures mesh

Think the unthinkable

Avoid crucial mistakes

Sellers' Considerations

Engage expert assistance

Get your corporate books in order

Grow your business to sell it

Evaluate the impact of external factors

Value your business

Maximize your selling price (e.g. core competency focus; reduce customer concentration)

Know your buyer

Plan for management succession

Understand your goals for the sale (price, post-sale plans, etc.)

Value of Business Varies with Buyer

	Highest Enterprise Value
9	Strategically Positioned Businesses
8	Diversifying Businesses
7	Competing Businesses
6	ESOPs
5	Outside Investors/Managers
4	Insider Management Group
3	Diversified Passive Investors
2	Investor/Job Seeker
1	Undiversified Passive Investors
	Lowest Enterprise Value

Questions?

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Thank you!